

M E M O R A N D U M

March 3, 1998

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9:05
FPSC - Records/Reporting

TO: DIVISION OF RECORDS AND REPORTING
FROM: DIVISION OF LEGAL SERVICES (JAEGEN) *JAEGEN*
RE: DOCKET NO. 980178-SU - DISPOSITION OF GROSS-UP FUNDS
COLLECTED BY EAGLE RIDGE UTILITIES, INC. IN LEE COUNTY.

98-0370-FDF-SU

Attached is a NOTICE OF PROPOSED AGENCY ACTION ORDER ACCEPTING SETTLEMENT OFFER, REQUIRING NO REFUNDS FOR THE YEAR 1996, AND CLOSING DOCKET, to be issued in the above-referenced docket.

(Number of pages in order - 8)

RRJ/lw

Attachment

cc: Division of Water and Wastewater (Gilchrist)
Division of Auditing and Financial Analysis (Causseaux)

I:980178or.rrj

See 4

RAK.
2 - wanted
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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Disposition of gross-up
funds collected by Eagle Ridge
Utilities, Inc. In Lee County.

DOCKET NO. 980178-SU
ORDER NO. PSC-98-0370-FOF-00
ISSUED: March 6, 1998

The following Commissioners participated in the disposition of
this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.

NOTICE OF PROPOSED AGENCY ACTION ORDER ACCEPTING SETTLEMENT
OFFER, REQUIRING NO REFUNDS FOR THE YEAR 1996, AND CLOSING DOCKET

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service
Commission that the action discussed herein is preliminary in
nature and will become final unless a person whose interests are
substantially affected files a petition for a formal proceeding,
pursuant to Rule 25-22.029, Florida Administrative Code.

BACKGROUND

Eagle Ridge Utilities, Inc. (Eagle Ridge or utility) is a
Class "B" wastewater utility providing service to 606 customers in
Lee County. According to its 1996 annual report, the utility
reported operating revenues of \$374,953 and net operating income of
\$15,030.

As a result of the repeal of Section 118(b) of the Internal
Revenue Code, contributions-in-aid-of-construction (CIAC) became
gross income and were depreciable for federal tax purposes. In
Order No. 16971, issued December 18, 1986, we authorized corporate
utilities to collect the gross-up on CIAC in order to meet the tax
impact resulting from the inclusion of CIAC as gross income.

DOCUMENT NO.
02934-98

ORDER NO. PSC-98-0370-FOF-SU
DOCKET NO. 980178-SU
PAGE 2

Orders Nos. 16971 and 23541, issued December 18, 1986 and October 1, 1990, respectively, require that utilities annually file information which would be used to determine the actual state and federal income tax liability directly attributable to the CIAC, and whether a refund of the gross-up is appropriate for any given year for which gross-up was in effect. These orders also required that all gross-up collections for a tax year which are in excess of a utility's actual tax liability for the same year resulting from its collection of CIAC should be refunded on a pro rata basis to those persons who contributed the taxes.

In Order No. 23541, we determined that any water and wastewater utility already collecting the gross-up on CIAC and wishing to continue collecting the gross-up, had to file a petition for approval with us on or before October 29, 1990. Eagle Ridge filed for authority to continue to gross-up on December 11, 1990. By Order No. 25436, issued December 4, 1991, Eagle Ridge was granted authority to continue to gross-up using the full gross-up formula.

On September 9, 1992, we issued Proposed Agency Action (PAA) Order No. PSC-92-0961-FOF-WS, which clarified the provisions of Orders Nos. 16971 and 23541 for the calculation of refunds of gross-up of CIAC. On September 14, 1992, we issued PAA Order No. PSC-92-0961A-FOF-WS, which included Attachment A which reflects the generic calculation form. No protests were filed, and these Orders became final.

On March 29, 1996, Docket No. 960397-WS was opened to review our policy concerning the collection and refund of CIAC gross-up. Workshops were held and comments and proposals were received from the industry and other interested parties. By Order No. PSC-96-0686-FOF-WS, issued May 24, 1996, we directed our staff to continue processing CIAC gross-up and refund cases pursuant to Orders Nos. 16971 and 23541; however, we also directed our staff to make a recommendation to us concerning whether our policy regarding the collection and refund of CIAC should be changed upon staff's completion of its review of the proposals and comments offered by the workshop participants. In addition, we directed our staff to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up.

However, on August 1, 1996, The Small Business Job Protection Act of 1996 (The Act) passed Congress and became law on August 20, 1996. The Act provided for the non-taxability of CIAC collected by water and wastewater utilities effective retroactively for amounts received after June 12, 1996. As a result, on September 20, 1996, in Docket No. 960965-WS, we issued Order No. PSC-96-1180-FOF-WS revoking the authority of utilities to collect gross-up of CIAC and cancelling the respective tariffs unless, within 30 days of the issuance of the order, affected utilities requested a variance. Based on the above, there was no longer a need to review our policy to determine any changes, and, on October 8, 1996, we issued Order No. PSC-96-1253-FOF-WS closing Docket No. 960397-WS. However, as established in Order No. PSC-96-0686-FOF-WS, all pending CIAC gross-up refund cases are being processed pursuant to Orders Nos. 16971 and 23541. The disposition of gross-up funds collected by the utility in 1995 was handled in Docket No. 970121-SU and we issued Order No. PSC-97-0329-FOF-SU accordingly. The purpose of this Order is to address the disposition of gross-up funds collected by the utility in 1996 and to address the utility's proposal that 50 percent of its legal and accounting costs be offset against the refund amount. This Order addresses the settlement offer and the appropriate disposition of excess gross-up funds collected for the year 1996.

REFUND REQUIREMENT FOR 1996

In compliance with Orders Nos. 16971 and 23541, Eagle Ridge filed its 1996 annual CIAC report regarding its collection of gross-up. The utility calculated its above-the-line income to be \$69,395. Our Staff adjusted the utility's above-the-line income by \$604 to reflect first year's depreciation as above the line. As a result, our staff calculated above the-line-income to be \$68,791. By letter dated January 12, 1998, our staff submitted preliminary refund calculation numbers to the utility. By letter dated January 23, 1998, the utility stated that while they did not agree with our staff's calculation of above-the-line taxable income, it did not intend to raise that issue since the adjustment made by staff did not affect the proposed refund amount.

We have calculated the gross-up required to pay the tax liability resulting from the collection of taxable CIAC by grossing-up the net taxable CIAC amount, in accordance with the

ORDER NO. PSC-98-0370-FOF-SU
DOCKET NO. 980178-SU
PAGE 4

method adopted in Order No. PSC-92-0961-FOF-WS. Our calculations, taken from the information provided by the utility in its gross-up report, are reflected on Schedule No. 1 attached to this Order. A summary of the refund calculation follows.

The utility's 1996 CIAC report indicates that the utility was in a taxable position on an above-the-line basis prior to the inclusion of taxable CIAC and gross-up. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$22,498 in taxable CIAC was received, with \$604 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rate as provided in the 1996 CIAC Report to calculate the tax effect, we calculated the income tax effect to be \$8,239. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$13,210. The utility collected \$13,571 of gross-up monies. Therefore, the utility collected \$361 more in gross-up than was required to pay the tax impact.

However, the utility provided documentation requesting legal and accounting fees of \$5,436. A review of these costs shows that \$5,237 of the legal and accounting fees submitted by the utility are directly associated with preparing the required reports and calculating the tax effect. The utility has requested that it be allowed to offset fifty percent of these costs against any refund requirement. Fifty percent of this amount is \$2,619. However, the utility only overcollected in the amount of \$361. Therefore, only, \$361 of the legal and accounting fees is necessary to completely offset any overcollection.

We have considered on several occasions the question of whether such an offset should be allowed pursuant to the orders governing CIAC gross-up. In Order No. PSC-97-0647-FOF-SU, issued June 6, 1997, in Docket No. 961077-SU; Order No. PSC-97-0657-AS-WS, issued June 9, 1997 in Docket No. 961076-WS; and Order No. PSC-97-0816-FOF-WS, issued July 7, 1997 in Docket No. 970275-WS, we accepted the utilities' settlement proposals that 50 percent of the legal and accounting costs be offset against the refund amount.

As in the other cases referenced above, we find that acceptance of the settlement proposal would avoid the substantial

ORDER NO. PSC-98-0370-FOF-SU
DOCKET NO. 980178-SU
PAGE 5

cost associated with a hearing, which may in fact exceed the amount of the legal and accounting costs to be recovered. We further note that the actual costs associated with making the refunds have not been included in these calculations and will be absorbed by the utility. Moreover, we believe the utility's settlement proposal is a reasonable "middle ground". Therefore, while not adopting the utility's position, we find it appropriate to accept the utility's settlement proposal. When the legal and accounting fees of \$361 are offset against the overcollection of \$361, there is no refund required for 1996.

CLOSING OF DOCKET

Upon expiration of the protest period, if a timely protest is not received from a substantially affected person, this docket shall be closed.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the request of Eagle Ridge Utilities, Inc., to offset fifty percent of the legal and accounting fees against any overcollections is approved as set forth in the body of this Order. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective unless an appropriate petition, in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" attached hereto. It is further

ORDERED that no refunds for overcollection of gross-up on contributions-in-aid-of-construction for the year 1996 is required. It is further

ORDERED that the schedule attached to this Order is incorporated into and made a part of this Order. It is further

ORDERED that in the event this Order becomes final, this Docket shall be closed.

ORDER NO. PSC-98-0370-FOF-SU
DOCKET NO. 980178-SU
PAGE 6

By ORDER of the Florida Public Service Commission this 6th
day of March, 1998.

BLANCA S. BAYÓ, Director
Division of Records and Reporting

By: Kay Flynn
Kay Flynn, Chief
Bureau of Records

(S E A L)

RRJ

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by

ORDER NO. PSC-98-0370-FOF-SU
DOCKET NO. 980178-SU
PAGE 7

Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on March 27, 1998.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

COMMISSION CALCULATED GROSS-UP REFUND

Eagle Ridge Utilities, Inc.
 SOURCE: (Line references are from CIAC Reports)

		1996
1 Form 1120, Line 30 (Line 15)	\$	68,791
2 Less CIAC (Line 7)		(22,498)
3 Less Gross-up collected (Line 19)		(13,571)
4 Add First Year's Depr on CIAC (Line 8)		604
5 Add/Less Other Effects (Lines 20 & 21)		(68)
6		-
7 Adjusted Income Before CIAC and Gross-up	\$	33,258
8		
9 Taxable CIAC (Line 7)	\$	22,498
10 Less first years depr. (Line 8)	\$	(604)
11		-
12 Adjusted Income After CIAC	\$	55,152
13 Less: NOL Carry Forward	\$	0
14		-
15 Net Taxable CIAC	\$	21,894
16 Combined Marginal state & federal tax rates		37.63%
17		-
18 Net Income tax on CIAC	\$	8,239
19 Less ITC Realized		0
20		-
21 Net Income Tax	\$	8,239
22 Expansion Factor for gross-up taxes		1.6033349466667
23		-
24 Gross-up Required to pay tax effect	\$	13,210
25 Less CIAC Gross-up collected (Line 19)		(13,571)
26		-
27 (OVER) OR UNDER COLLECTION	\$	(361)
28		-
29 TOTAL YEARLY REFUND	\$	(361)
30 Offset of Legal and Accounting Fees	\$	361
31		---
32 PROPOSED REFUND (excluding interest)	\$	0
33		---