

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Request by FLORIDA WATERWORKS)	DOCKET NO. 860184-PU
ASSOCIATION for investigation of)	
proposed repeal of Section 118(b),)	ORDER NO. 24413
Internal Revenue Code (Contributions-)	
in-aid-of-construction)	ISSUED: 4/22/91
)	

The following Commissioners participated in the disposition of this matter:

BETTY EASLEY
 GERALD L. GUNTER
 MICHAEL MCK. WILSON

ORDER DENYING MOTIONS FOR RECONSIDERATION
AND GRANTING MOTION FOR CLARIFICATION

BY THE COMMISSION:

CASE BACKGROUND

As a result of the repeal of Section 118(b), Internal Revenue Code, under the Tax Reform Act of 1986, on January 1, 1987, contributions-in-aid-of-construction (CIAC) became includible in a utility's gross income for federal tax purposes. Accordingly, by Order No. 16971, issued December 18, 1986, this Commission authorized corporate utilities subject to its jurisdiction to amend their service availability policies to "gross-up" CIAC, in order to meet the resulting tax impact. Since then, 44 water and/or wastewater utilities have elected to implement the gross-up. Of these, only 37 remain subject to the Commission's jurisdiction.

By Order No. 21266, issued May 22, 1989, we proposed to establish certain guidelines to control the collection of the gross-up. On June 12, 1989, Order No. 21266 was protested by the Florida Waterworks Association (FWWA) and 14 water and/or wastewater utilities.

By Order No. 21436, issued June 26, 1989, we also proposed to require a number of utilities to refund amounts of the gross-up collected or to make adjustments to their depreciation reserves. On or about June 17, 1989, Order No. 21436 was protested by six water and/or wastewater utilities.

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Based upon the protests of Orders No. 21266 and No. 21436, a formal hearing was held on April 27 and 30, 1990. By Order No. 23541, issued October 1, 1990, this Commission authorized the continuation of the gross-up, prescribed regulatory and accounting treatments therefor, and required that certain refunds be made.

On October 16, 1990, Aloha Utilities, Inc. (Aloha), one of the petitioners in this proceeding, filed a motion for reconsideration of Order No. 23541. Aloha also filed a request for oral argument on its motion for reconsideration, and a motion for a stay pending our decision on its motion for reconsideration. Also on October 16, 1990, Palm Coast Utility Corporation (PCUC) filed a motion for reconsideration or clarification of the order. We granted Aloha's motion for a stay by Order No. 23936, issued December 24, 1990. Oral argument was held on January 3, 1991.

ALOHA'S MOTION FOR RECONSIDERATION

By Order No. 23541, we found that, for purposes of determining whether any refund of the gross-up is appropriate, we would offset net operating losses (NOLs), NOL carryforwards, and investment tax credits (ITCs). However, we also held that, to the extent a utility could demonstrate that its NOLs or ITCs were "below-the-line", we would not require such an offset.

In its motion for reconsideration, Aloha cites our decision in Docket No. 890277-WS, the application of Palm Coast Utility Corporation for increased rates in Flagler County, as reflected by Order No. 22843, issued April 23, 1990. In that case, we imputed certain ITCs to PCUC's capital structure, and explained our adjustment as follows:

Since it was through its own error that the utility did not realize the benefits of the ITCs, we do not believe that the ratepayers should bear additional costs. We find, therefore, that the ITCs should be imputed to PCUC's capital structure.

Aloha argues that the above-quoted passage indicates that the benefits of ITCs should in all cases be preserved for the ratepayers. According to Aloha, our decision to offset even above-the-line ITCs will mean that the contributors, and not the

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ratepayers, will receive the benefits of the ITCs. Aloha further contends that our failure to explicate our "deviation" from prior Commission practice is violative of Section 120.68(12), Florida Statutes, which states, in part:

- (12) The court shall remand the case to the agency if it finds the agency's exercise of discretion to be:
- (c) Inconsistent with an officially stated agency policy or a prior agency practice, if deviation therefrom is not explained by the agency ...

We do not believe that we have deviated from our prior practice whatsoever. We imputed ITC's in PCUC's rate case because it was PCUC's fault that they were not taken, and we did not believe that PCUC's customers should suffer due to the utility's mistake. In this case, we have also preserved the benefits of the ITCs for utility customers. The benefits are flowed back to the customers over time through normalization. Normalization is required by the Internal Revenue Code. As discussed by witness Jackson at the hearing, through normalization, ITCs are considered either zero cost capital with amortization below-the-line or a capital component with a weighted cost rate and amortization above-the-line.

The treatment that we found to be appropriate in Order No. 23541 is also that which will naturally occur. As we stated in that Order:

According to Witness Causseaux, however, utilities will use their ITCs to reduce taxable income from any source, including the receipt of CIAC or contributed taxes, without regard to the outcome of this docket, in order to minimize their actual tax liabilities. As we have already stated, until there is an actual tax liability, we do not believe that there is any tax burden created by the collection of CIAC or contributed taxes. Our treatment will simply recognize what is actually transpiring.

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Based upon the discussion above, we find that our decision in this case is consistent with the prior practice of this Commission. Accordingly, Aloha's motion for reconsideration is denied.

PCUC'S MOTION FOR RECONSIDERATION OR CLARIFICATION

In Order No. 23541, we also discussed the information that should be filed in a petition in order for the Commission to evaluate whether a utility should be authorized to collect a gross-up. We specifically listed seven items that would be required in such a filing: the demonstration of an actual tax liability, a cash flow statement, a statement of interest coverage, a statement of alternative financing, justification for the gross-up, the gross-up method selected, and proposed tariffs.

In its motion, PCUC requests that we reconsider or clarify some of the filing requirements. First, PCUC requests that, in our determinations of need for a gross-up, we place more emphasis on the impact to a utility's ratepayers. We believe that PCUC's concern is appropriate. We never meant the criteria enumerated in Order No. 23541 to be either exclusive or exhaustive. They are simply guidelines. If a utility is able to demonstrate that without a gross-up its ratepayers will be harmed, we will, of course, take that into consideration. In fact, we encourage utilities to submit whatever information they believe will justify their collection of the gross-up. Any special concerns should be addressed under the "justification for gross-up" criterion. Accordingly, PCUC's motion for clarification of this issue is granted.

Next, PCUC requests that we reconsider our decision to require a utility to demonstrate not only a tax liability resulting from the collection of the gross-up, but that alternative funds are not available at a reasonable cost. PCUC takes this to mean that cash flow is a threshold consideration. We did not intend this to be the case. In fact, we specifically stated, at page 4 of Order No. 23541, that "[a]lthough we believe that cash flow is a consideration in the overall gross-up picture, it is only one of many." At page 11 of Order No. 23541, we also stated that "the need for a gross-up should be determined on a case-by-case basis, based upon the facts and circumstances peculiar to each utility." We believe that if a utility has requested a gross-up, it should be able to demonstrate that it has explored alternatives to the gross-

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up and that reasonable alternatives are not available. PCUC's motion for reconsideration of this issue is, therefore, denied.

PCUC also requests that the cash flow statements required in the criteria be on a prospective basis. Although Order No. 23541 is silent as to whether the cash flow statement should be on a prospective or an historic basis, we believe that prospective cash flow statements are, in fact, more relevant to a prospective gross-up. However, we realize that putting this kind of information together can be expensive for small utilities. Accordingly, although we would prefer the information on a prospective basis, if a utility is unable to provide prospective cash flow statements due to budget considerations, we will allow the information to be provided on an historic basis. Accordingly, PCUC's motion for clarification of this issue is granted.

Finally, PCUC asks that we reconsider our decision to offset debit deferred taxes associated with CIAC against credit deferred taxes in the capital structure. In Order No. 23541, we stated that, "[i]n Florida, the norm is to offset debit deferred taxes against credit deferred taxes in the capital structure. If the net of the credit and debit deferred taxes amounts is a debit, the amount is included in rate base." We also noted that IRS Notice 87-82 requires utilities to follow the treatment afforded by the Commission for debit deferred taxes associated with CIAC.

PCUC disputes whether the capital structure treatment is the norm for debit deferred taxes. PCUC references Orders Nos. 22843 and 21265, wherein debit deferred taxes associated with CIAC were allowed rate base treatment. Witness Causseaux, on behalf of Staff, testified that "this Commission treats credit balance deferred taxes as zero cost capital in the capital structure, the IRS would expect to find the debit balance deferred taxes used to offset the credit balance or zero cost deferred taxes in the capital structure." This testimony was not disputed at the hearing. Although PCUC has presented two cases wherein debit deferred taxes were treated in rate base, two cases are not sufficient to prove the "norm" of this Commission.

PCUC also argues that we based our decision in this regard, at least in part, upon a misstatement of Witness Elliott's testimony. PCUC quotes Order No. 23541, in part, as follows:

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Notwithstanding the above, Witness Causseaux stated that a more simplistic approach would be to recognize the full debit deferred tax balance in rate base. Witness Elliott, however, argued that the accounting treatment should follow the regulatory treatment, and not vice-versa. We agree. Although the proposed rate base treatment would be easier to administer, we believe that the appropriate method of normalization is the capital structure method. This would keep the treatment in total compliance with Notice 87-82.

In his testimony, Mr. Elliott proposed rate base treatment for the deferred taxes. His statement about accounting treatment following the regulatory treatment was made in reference to alternatives available for the taxes associated with the CIAC. Mr. Elliott also testified that Notice 87-82 requires that, "to the extent that a utility treats deferred taxes as zero cost capital, any prepayment of CIAC will result in the decrease of the amount of zero cost capital in the capital structure." We believe that this supports our decision to afford capital structure treatment for the debit deferred taxes.

Our decision in this case, as reflected by Order No. 23541, was designed to deal with a problem common to many utilities in as generic a fashion as possible. If conditions exist where the debit deferred taxes warrant rate base treatment, those conditions can be presented to the Commission on a case-by-case basis during a rate proceeding. Since PCUC has presented no evidence that has not already been considered by this Commission, its motion for reconsideration of this issue is denied.

It is, therefore,

ORDERED by the Florida Public Service Commission that Aloha Utilities, Inc.'s motion for reconsideration of Order No. 23541 is hereby denied, as set forth in the body of this Order. It is further

ORDERED that Palm Coast Utility Corporation's motion for reconsideration of Order No. 23541 is hereby denied, as set forth in the body of this Order. It is further

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ORDERED that Palm Coast Utility Corporation's request for clarification of Order No. 23541 is hereby granted, as set forth in the body of this Order. It is further

ORDERED that Docket No. 860184-PU be and is hereby closed.

By ORDER of the Florida Public Service Commission, this
22nd day of APRIL, 1991.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

RJP

by: Kay Flynn
Chief, Bureau of Records

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NOTICE OF JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), 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.

Any party adversely affected by the Commission's final action in this matter may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer 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 after the issuance 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.