

MEMORANDUM

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FPSC - Records/Reporting

TO: DIVISION OF RECORDS AND REPORTING
FROM: DIVISION OF LEGAL SERVICES (JAEGER)
RE: DOCKET NO. 971529-WS - DISPOSITION OF CONTRIBUTION-IN-AID-OF-CONSTRUCTION GROSS-UP FUNDS COLLECTED BY ALOHA UTILITIES, INC. IN PASCO COUNTY

98-0319-AS-WS

Attached is an NOTICE OF PROPOSED AGENCY ACTION ORDER ACCEPTING SETTLEMENT OFFER AND REQUIRING NO REFUNDS FOR THE YEARS 1993 THROUGH 1996, to be issued in the above-referenced docket.

(Number of pages in order - 10)

RRJ/lw

Attachment

cc: Division of Water and Wastewater (Gilchrist)

I:971529or.rrj

See 1

2/0.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Disposition of
contribution-in-aid-of-
construction gross-up funds
collected by Aloha Utilities,
Inc. In Pasco County.

DOCKET NO. 971529-WS
ORDER NO. PSC-98-0319-AS-WS
ISSUED: February 23, 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
AND REQUIRING NO REFUNDS FOR THE YEARS 1993 THROUGH 1996

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

Aloha Utilities, Inc. (Aloha or utility) is a Class A utility
providing service to approximately 11,038 water and 10,554
wastewater customers in Pasco County. According to its 1996 annual
report, operating revenues were \$1,885,752 for water and \$2,811,605
for wastewater. The utility reported net operating income of
\$94,254 for the water system and \$407,422 for the wastewater
system.

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

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utilities to collect the gross-up on CIAC in order to meet the tax impact resulting from the inclusion of CIAC as gross income.

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. The information would also determine whether refunds of gross-up would be appropriate. 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, should be refunded on a pro rata basis to those persons who contributed the taxes.

In Order No. 23541, we required any water and wastewater utility already collecting the gross-up on CIAC and wishing to continue, to file a petition for approval with the Commission on or before October 29, 1990. Aloha filed for authority to continue to gross-up on December 28, 1990. By Order No. 25526, issued December 24, 1991, we granted Aloha's petition for continued gross-up authority using the full gross-up formula.

On September 9, 1992, we issued Proposed Agency Action Order (PAA) 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, PAA Order No. PSC-92-0961A-FOF-WS was issued. This order included Attachment A which reflects the generic calculation form. No protests were filed, and these Orders became final.

On March 29, 1996, we opened Docket No. 960397-WS 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 review the proposals and comments offered by the workshop participants and make a recommendation concerning whether our policy regarding the collection and refund of CIAC should be changed. In addition, we directed our staff to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up. Pending this review, we directed our staff to continue processing CIAC gross-up refund cases pursuant to Orders Nos. 16971 and 23541.

However, the Small Business Job Protection Act of 1996 (The Act) was signed into 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 canceling the respective tariffs unless, within 30 days of the issuance of the order, affected utilities requested a variance.

Since there was no longer a need to review our policy on the gross-up of CIAC, we closed Docket No. 960397-WS, by Order No. PSC-96-1253-FOF-WS, issued October 8, 1996. 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 1990-1992 was handled in Docket No. 940156-WS and Order No. PSC-94-0444-FOF-WS was issued accordingly. The purpose of this docket is to address the disposition of gross-up funds collected by the utility from 1993 to 1996, and to address the utility's proposal that 50 percent of its legal and accounting costs be offset against the refund amount.

REFUND REQUIREMENT

In compliance with Orders Nos. 16971 and 23541, Aloha filed its 1993 through 1996 annual CIAC reports regarding its collection of gross-up for each year. By letter dated November 14, 1997, our staff submitted preliminary refund calculation numbers to the utility. By letter dated December 22, 1997, the utility stated that while they do not agree with staff's above-the-line classification of officers' salaries, they accepted the staff's refund calculations for 1993-1996.

Our refund calculations are based on the method adopted in Order No. PSC-92-0961-FOF-WS. The adjustments have been explained in the body of this Order and are reflected on the schedule attached to this Order. A summary of each year's refund calculation follows.

1993

The utility proposes that no refund is appropriate. We agree that a refund of gross-up collections for 1993 is not appropriate.

The 1993 CIAC report indicates 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 \$553,643 in taxable CIAC was received, with \$7,651 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rates as provided in the 1993 CIAC report, we calculate net income taxes to be \$205,457. 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 \$329,416.

In December, 1992, Aloha received and booked \$24,010 of property CIAC from Heritage Lake Development. Such CIAC was included as income on the 1992 tax return and the 1992 gross-up refund report filed with the Commission. However, the related gross-up of \$13,927 was not received and booked until January, 1993. Therefore, the gross-up amount collected in 1993 has been adjusted to properly match 1993 CIAC with the related 1993 gross-up collections. As a result, the amount of gross-up collected by the utility in 1993 is \$327,570. The utility required more in gross-up to pay the tax impact than the utility collected; therefore, no refund is necessary.

1994

The utility proposes that no refund is appropriate. We agree that a refund of gross-up collections for 1994 is not appropriate.

The 1994 CIAC report indicates 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 \$1,301,370 in taxable CIAC was received, with \$15,192 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rates as provided in the 1994 CIAC report, we calculate net income taxes to be

\$483,989. 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 \$775,996. The utility collected \$762,413 of gross-up monies. The utility required more in gross-up to pay the tax impact than the utility collected; therefore, no refund is necessary.

1995

The utility proposes that no refund is appropriate. We agree that a refund of gross-up collections for 1995 is not appropriate.

The 1995 CIAC report indicates 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 \$401,761 in taxable CIAC was received, with \$7,043 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rates as provided in the 1995 CIAC report, we calculate net income taxes to be \$148,532. 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 \$238,147. The utility collected \$235,421 of gross-up monies. The utility required more in gross-up to pay the tax impact than the utility collected; therefore, no refund is necessary.

1996

The utility proposes that no refund is appropriate. We agree.

The 1996 CIAC report indicates 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 \$454,632 in taxable CIAC was received, with \$17,065 being deducted for the first year's depreciation. Using the 37.63 percent combined marginal federal and state tax rates as provided in the 1996 CIAC report, we calculate net income taxes to be \$164,656. 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 \$263,999. The utility collected \$266,858 of

gross-up monies. Therefore, the utility collected \$2,859 more in gross-up than was required to pay the tax impact.

However, the utility provided documentation for legal and accounting fees of \$6,100, and requested that 50 percent of these fees be offset against any over collection. A review of these costs shows that all of the legal and accounting fees submitted by the utility are directly associated with preparing the required reports and calculating the tax effect, and, thus, are legitimate expenses. Fifty percent of this amount is \$3,050. We have considered on several occasions the question of whether such an offset should be allowed pursuant to the orders governing CIAC gross-up. See: Order No. PSC-97-0647-FOF-SU, issued June 7, 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. In these orders, we accepted the utility's 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 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 Aloha's settlement proposal.

Although 50 percent of the utility's legal and accounting fees equals \$3,050, only \$2,859 of this amount is necessary to offset the overcollection of \$2,859. When the legal and accounting fees of \$2,859 is offset against the overcollection of \$2,859, there is nothing left to refund, and no refund is required for 1996.

Based on all the above, no refund is required for the years 1993 through 1996.

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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 Aloha Utilities, Inc., to offset fifty percent of the legal and accounting fees against any overcollections is accepted. 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

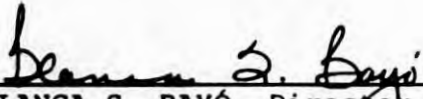
ORDERED that no refunds are required for the collection of gross-up on Contributions-in-Aid-of-Construction for the years 1993 through 1996. It is further

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.

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By ORDER of the Florida Public Service Commission this 23rd
day of February, 1998.



BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

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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 Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and

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Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on March 16, 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

Aloha Utilities, Inc.
SOURCE: (Line references are from CIAC

	1993	1994	1995	1996
1 Form 1120, Line 30 (Line 15)	\$ 1,117,308	\$ 2,130,594	\$ 869,363	\$ 1,530,948
2 Less CIAC (Line 7)	(553,643)	(1,301,370)	(401,761)	(454,632)
3 Less Gross-up Collected (Line 10)	(341,497)	(762,413)	(235,421)	(266,858)
4 Add First Year's Depr on CIAC (Line 8)	7,651	15,192	7,043	17,065
5 Add/Less Other Effects (Lines 20 & 21)	(1,779)	(1,455)	(968)	(1,055)
6	-	-	-	-
7 Adjusted Income Before CIAC and Gross-up	\$ 228,040	\$ 80,548	\$ 238,256	\$ 825,468
8	-	-	-	-
9 Taxable CIAC (Line 7)	\$ 553,643	\$ 1,301,370	\$ 401,761	\$ 454,632
10 Less first years depr. (Line 8)	\$ (7,651)	\$ (15,192)	\$ (7,043)	\$ (17,065)
11	-	-	-	-
12 Adjusted Income After CIAC	\$ 774,032	\$ 1,366,726	\$ 632,974	\$ 1,263,035
13 Less: NOL Carry Forward	\$ 0	\$ 0	\$ 0	\$ 0
14	-	-	-	-
15 Net Taxable CIAC	\$ 545,992	\$ 1,286,178	\$ 394,718	\$ 437,567
16 Combined Marginal state & federal tax	37.63%	37.63%	37.63%	37.63%
17	-	-	-	-
18 Net Income tax on CIAC	\$ 205,457	\$ 483,989	\$ 148,532	\$ 164,656
19 Less ITC Realized	0	0	0	0
20	-	-	-	-
21 Net Income Tax	\$ 205,457	\$ 483,989	\$ 148,532	\$ 164,656
22 Expansion Factor for gross-up taxes	1.6033349366	1.6033349366	1.6033349366	1.6033349366
23	-	-	-	-
24 Gross-up Required to pay tax effect	\$ 329,416	\$ 775,996	\$ 238,147	\$ 263,999
25 Less CIAC Gross-up Collected (Line 19)	(341,497)	(762,413)	(235,421)	(266,858)
Less 1992 Gross-up Collected in 1993	13,927			
Adjusted 1993 Gross-up Collected	(327,570)			
26	-	-	-	-
27 (OVER) OR UNDER COLLECTION	\$ 1,846	\$ 13,583	\$ 2,726	\$ (2,859)
28	-	-	-	-
29 TOTAL YEARLY REFUND	\$ 0	\$ 0	\$ 0	\$ (2,859)
30 Offset of Legal and Accounting Fees				
31	-	-	-	-
32 PROPOSED REFUND (excluding interest)	\$ 0	\$ 0	\$ 0	\$ 0