

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Review of Florida Public ) DOCKET NO. 960397-WS  
Service Commission's policy ) ORDER NO. PSC-96-0686-FOF-WS  
concerning collection and refund ) ISSUED: May 24, 1996  
of contributions-in-aid-of- )  
construction (CIAC) gross-up. )

The following Commissioners participated in the disposition of this matter:

SUSAN F. CLARK, Chairman  
J. TERRY DEASON  
JOE GARCIA  
JULIA L. JOHNSON  
DIANE K. KIESLING

NOTICE OF PROPOSED AGENCY ACTION ORDER ON PROCESSING OF CONTRIBUTIONS-IN-AID-OF-CONSTRUCTION GROSS-UP CASES

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

The Passage of the Tax Reform Act of 1986 (Act), effective January 1, 1987, made Contributions-in-Aid-of-Construction (CIAC) taxable income. To address this change, we issued several orders. In Proposed Agency Action (PAA) Order No. 16971, issued on December 18, 1986, we granted the Florida Waterworks Association's (FWWA's) application for emergency approval of amended service availability policies with modifications. That order, among other things, allowed utilities to collect from contributors an amount equal to the tax impact of CIAC, set forth a gross-up formula, required filing of annual CIAC tax impact reports, and required a refund of excess monies collected.

By PAA Order No. 21266, issued May 22, 1989, we proposed to establish guidelines to control the collection of the gross-up. However, on June 12, 1989, Order No. 21266 was protested by FWWA and 14 water and wastewater utilities. Also, by PAA Order No. 21436, we proposed to require a number of utilities to refund

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amounts of the gross-up collected or make adjustments to their depreciation reserves. This order was also protested.

Those protests were combined and a formal hearing was held on April 27 and 30, 1990. As a result of that formal hearing, we issued Order No. 23541 on October 1, 1990. In the ordering paragraphs, the Order stated:

Ordered that any gross-up amounts collected in excess of a utility's actual tax liability resulting from its collection of CIAC, as set forth in the body of this Order shall be refunded on a pro rata basis to the contributors of those amounts.

In the body of the order, we recognized that above-the-line Net Operating Losses (NOLs) and Investment Tax Credits (ITCs) shall be used to calculate the actual tax liability. Then, consistently after that, the authorization to continue gross-up of CIAC was made contingent upon compliance with Order No. 16971, issued December 18, 1986, and Order No. 23541, issued October 1, 1990. Further, in subsequent orders authorizing gross-up, the matters discussed in Orders Nos. 16971 and 23541 were expressly incorporated therein by reference.

For the last year, several applications for gross-up authority and refund calculations have been held up pending the outcome of the Commission Workshop on CIAC Gross-up. At the Commission Workshop on November 29, 1995, the utilities proposed an alternate plan for the treatment of CIAC Gross-up, and we are now considering this plan.

#### CHANGE IN HANDLING OF CIAC GROSS-UP

As stated previously, Order No. 16971 authorized water and wastewater utilities to amend their service availability policies to meet the tax impact on CIAC resulting from the amendment of Section 118(b) of the Internal Revenue Code. This order also contained a gross-up formula.

Order No. 23541, issued October 1, 1990, after a formal hearing, ordered utilities currently grossing-up CIAC to file a petition for continued authority to gross-up and also ordered that no utility may gross-up CIAC without first obtaining our approval. The order stated that at a minimum, each utility should be able to demonstrate that a tax liability existed and that sources of funds were not available at a reasonable cost. Further, the order stated that a utility may demonstrate such need by filing the following

information: (1) Demonstration of an actual tax liability on a regulated, above-the-line basis, (2) Cash flow statement, (3) Statement of Interest Coverage, (4) Statement of Alternative Financing, (5) Justification for Gross-up, (6) Gross-up Method Selected (full gross-up or net present value) and (7) Proposed Tariffs.

Order No. 23541 also modified the gross-up formula contained in Order No. 16971. Both orders prescribed the accounting and regulatory treatments for the gross-up and ordered that CIAC tax impact monies received during the tax year that were in excess of the actual amount of tax expense that was attributable to the receipt of the CIAC, together with interest earned on such excess monies held in the CIAC Tax Impact Account, must be refunded on a pro rata basis to the parties which made the contribution and paid the tax impact amounts during the tax year. In addition, Order No. PSC-92-0961-FOF-WS, issued September 9, 1992, clarified the provisions in Orders Nos. 16971 and 23541 for the calculation of refunds of gross-up of CIAC.

Although our staff attempted to process applications for gross-up authority and refund calculations in accordance with the provisions of Orders Nos. 23541 and PSC-92-0961-FOF-WS, Canal Utilities, Inc., in Docket No. 941083-WS, raised the question of whether or not staff's method of calculating refunds was contrary to the requirements of Order No. 23541 and the Commission's previous practice. Specifically at issue was the treatment of depreciation of CIAC after the first year; i.e., whether subsequent years' depreciation should be included above-the-line or below-the-line. Staff had included subsequent years' depreciation on CIAC above-the-line; however, the utility contended that in previous CIAC gross-up refund dockets, subsequent years' depreciation had been included below-the-line. Thus, the utility contended that staff's refund calculation was contrary to the provisions of Order No. 23541 and the Commission's previous practice. Also at issue was the appropriate level of review necessary to grant authority or process a refund, offsetting of above-the-line NOLs and ITCs with CIAC income, the requirement of refunds of excess collections of CIAC gross-up, and the differing interpretations given to our past decisions.

As a result of these issues, among others, we directed our staff to hold workshops to discuss the current practices of the Commission employed in dealing with the taxability of CIAC and to discuss viable alternatives. We also directed our staff to consider the need, if any, to change the Commission's current policy. The processing of CIAC gross-up dockets has been held in abeyance pending resolution of these issues.

The first workshop was held on August 30, 1995, with staff, industry representatives and other interested parties attending. Staff compiled a list of relevant questions for discussion at the workshop and solicited responses from the industry. A subsequent workshop was held on November 29, 1995 before the full Commission, in which the responses received in the first workshop were presented and discussed. Also provided at that workshop was a summary of the responses and positions taken at the August 30, 1995, workshop. While most participants tend to agree that a gross-up of CIAC is necessary, opinions differed as to its application.

Mr. Paul Freeman of Southwest Florida Capital Corporation, a developer, believes that if a gross-up is allowed, the net present value method should be used because the ratepayer is whole and the developer is paying the actual cost of the contribution. Mr. Robert Nixon, on behalf of the Florida Waterworks Association and several utilities currently utilizing or interested in the Commission's policy on gross-up of CIAC submitted a proposal in which the full gross-up method is used. This proposal is currently under review by our staff.

Under this proposal, refunds to contributors, annual reporting, and the gross-up escrow account (all of which are required by Order No. 23541) are eliminated. In addition, the proposal provides that applications to gross-up should be liberally granted; that 100% of gross-up is returned to the general body of ratepayers; and that a method of accounting be adopted which does the following: (1) amortizes contributed taxes to above-the-line income as a direct benefit to ratepayers (Contributed tax amortization increases operating income and decreases revenues); (2) has no impact on rate base, balance sheet, or income statement over the useful life of contributed assets; (3) equalizes the tax benefits to the utility to the benefits given back to the ratepayers; and (4) treats the deferred tax liability as zero cost capital.

We believe that, consistent with the purpose of Orders Nos. 16971 and 23541, any gross-up method employed should enable utilities to meet the tax impact resulting from the inclusion of CIAC in gross income. The majority of the workshop participants believe that, while each utility should make its own decision on whether to gross-up and the method to use (full gross-up or net present value gross-up), full gross-up would best enable utilities to meet the tax impact of CIAC. However, because of differing interpretations of Orders Nos. 16971 and 23541 and their application, if gross-up is allowed, one of the major issues to be resolved is what accounting and regulatory treatment for the gross-

up would achieve the purpose of Orders Nos. 16971 and 23541. More importantly, if a tax liability is created, it should be determined what adjustments are made to income to calculate the tax liability (offsetting of above-the-line NOLs and ITCs with CIAC income) and, also, if refunds of excess collections of gross-up should be required.

Based on the above, we find that our policy concerning the collection and refund of CIAC gross-up should be revisited to determine what changes, if any, should be made to accomplish the intended purpose of CIAC gross-up as established in Orders Nos. 16971 and 23541. In addition, our staff shall consider ways to simplify the process and whether there are viable alternatives to the gross-up. Upon staff's completion of its review of the proposals and comments offered by the workshop participants, our staff shall make a recommendation to us concerning whether our current policy regarding the collection and refund of CIAC gross-up should be changed.

#### CONTINUED PROCESSING OF CIAC GROSS-UP CASES

Order No. 23541 was issued October 1, 1990, after a formal hearing. That Order concluded that gross-up amounts collected in excess of a utility's actual tax liability resulting from its collection of CIAC shall be refunded on a pro rata basis to the contributors of those amounts. In the body of the order, actual tax liability was to be calculated using above-the-line net operating losses (NOLs) and investment tax credits (ITCs). All orders granting the authorization for gross-up expressly refer to Orders Nos. 16971 (this order referred to actual tax amount of tax expense) and 23541, and all matters in these two orders were expressly incorporated therein in any orders granting gross-up authority.

We do not have a rule on the appropriate method to calculate gross-up of CIAC, a rule on how to determine if gross-up authority is warranted, nor a rule to determine how refund of gross-up should be calculated. We have, however, developed incipient policy for all of these determinations by the issuance of the above-referenced orders. In Southern Bell Telephone and Telegraph Co. v. Florida Public Service Commission, 443 So. 2d 92 (Fla. 1983), the Florida Supreme Court considered the emerging policy of the Commission as to whether to allow charitable contributions as expenses and noted that there was some inconsistency between 1977 and 1981. However, the Court concluded that although rulemaking might have been better, the Commission is not required to institute a rulemaking proceeding every time a new policy is developed, and that the change in policy did not amount to an arbitrary or capricious act.

Also, Subsections 120.535(1)(a)1. and 2., Florida Statutes, recognize that where the agency has not had sufficient time to acquire the knowledge and experience reasonably necessary to address a statement by rulemaking, or where matters are not sufficiently resolved to enable the agency to address a statement by rulemaking, then rulemaking may not be "feasible and practicable." By our issuance of Orders Nos. 16971 (issued December 18, 1986), 23541 (issued October 1, 1990), and PSC-92-0961-FOF-WS (issued September 9, 1992), and many other orders, and, also, through the workshops held on August 30, 1995 (a staff workshop), and November 29, 1995 (a full Commission workshop), we have shown that, up to now, matters were neither sufficiently resolved, nor had we gathered sufficient knowledge and experience to address the issue of CIAC gross-up in rulemaking. We now believe that we have gathered such knowledge and experience.

However, pending the final outcome of any rulemaking process, we must determine how to process the current CIAC gross-up cases that are either already filed or will be filed prior to the issuance of any rule. For the collection of any gross-up of CIAC to date, Orders Nos. 16971 and 23541 were and still are in effect, and specifically require that all gross-up in excess of the liability related to the collection of CIAC be refunded. Pursuant to the principle of administrative finality, orders of administrative agencies, like the courts, must eventually pass out of the agency's control and become final and no longer subject to modification. However, the courts have recognized that administrative agencies do have inherent power to reconsider final orders which are still under their control, but such inherent authority to modify is a limited one. See, Peoples Gas System v. Mason, 187 So. 2d 335, (Fla. 1966). The Florida courts do recognize that administrative agencies decide issues according to a public interest that often changes with time and so do allow the agencies a very limited ability to modify based on this public interest. However, Orders Nos. 16971 and 23541 were issued over five years ago, and have long since passed from our control (in Peoples Gas, four years was too long).

Also, while rules may be given retroactive effect in some circumstances, it is generally allowed only where the rule embodies previously established policy. See, Upjohn Healthcare Services, Inc. v. Dept. of Health and Rehabilitation Services, 496 So. 2d 147 (Fla. 1st DCA 1986); and, Jordan v. Dept. of Professional Regulation, 422 S. 2d 450 (Fla. 1st DCA 1988). In the case at hand, we have stated that the funds collected over and above the actual tax liability shall be refunded. Therefore, until the policy is established otherwise, any new rule should be applied prospectively only.

Although we may change our policy, any change from the procedures set out in Order No. 23541 shall be prospective only. To now change the policies, and allow the utility to keep all of the CIAC gross-up without regard to the effect of the above-the-line NOLs and ITCs would be in contradiction of Order No. 23541. When the contributors made their contributions, Order No. 23541 was in effect and any payment or contribution of gross-up was made with those restrictions and requirements validly in place. Therefore, it would not appear to make any difference whether the order requiring refunds for any particular utility has already been issued. Orders Nos. 16971 and 23541 affect all those that have applied (and will continue to affect any future applications) until the policy of offsetting the tax effect with above-the-line NOLs and ITCs is officially changed - whether by order or adoption of a rule.

Based on all of the above, until we indicate our change in policy, the requirements of Orders Nos. 16971 and 23541 shall be met in the collection of CIAC gross-up and the ordering of refunds. Although we may change this policy, any such change shall be made prospectively only. Therefore, all pending CIAC gross-up cases, and any such cases filed prior to any change in policy, if there is a change, should continue to be processed pursuant to Orders Nos. 16971 and 23541. Any change, if and when finally approved, shall be effective for cases filed from that point forward.

#### CLOSING OF DOCKET

Pending our staff's review of our policy on the collection and refund of CIAC gross-up in conjunction with proposals and comments received at the workshops, staff's recommendation concerning any change in policy, and our final determination in this matter, this docket shall remain open.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that our policy concerning the collection and refund of Contributions-in-aid-of-Construction gross-up shall be revisited. It is further

ORDERED that pending a change in policy, if any, all current Contributions-in-aid-of-Construction gross-up cases, or any Contributions-in-aid-of-Construction gross-up cases filed prior to any change in policy, shall be processed under the provisions of Orders Nos. 16791 and 23541. It is further

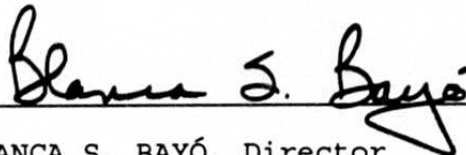
ORDERED that each of the findings made in the body of this Order is hereby approved in every respect. It is further

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ORDERED that the provisions of this Order are issued as proposed agency action and shall become final, unless an appropriate petition in the form provided by Rule 25-22.029, Florida Administrative Code, is received by the Director of the Division of Records and Reporting at 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the date set forth in the Notice of Further Proceedings below. It is further

Ordered that this docket shall remain open.

By ORDER of the Florida Public Service Commission, this 24th day of May, 1996.



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 120.59(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.

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



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Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on June 14, 1996.

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.