

FLORIDA PUBLIC SERVICE COMMISSION

Fletcher Building  
101 East Gaines Street  
Tallahassee, Florida 32399-0850

MEMORANDUM

August 30, 1990

TO : DIRECTOR, DIVISION OF RECORDS AND REPORTING

FROM : DIVISION OF APPEALS (MILLER) *ew*  
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (CAUSSEAU) *APC*  
DIVISION OF COMMUNICATIONS (MAILHOT) *dm*  
DIVISION OF ELECTRIC AND GAS (McCORMICK, SLEMKEWICZ) *JS*  
DIVISION OF RESEARCH (HOPPE, HEWITT) *ghd*  
DIVISION OF WATER AND SEWER (HILL, LOWE) *at bl*

RE : DOCKET NO.: 891278-PU, PROPOSED REVISION OF RULE 25-14.003, F.A.C., PERTAINING TO CORPORATE INCOME TAX EXPENSE ADJUSTMENTS: MIDPOINT AND ADDITIONAL CHANGES

AGENDA: 9/11/90 - CONTROVERSIAL AGENDA - PARTIES MAY NOT PARTICIPATE

CRITICAL DATES: NONE

RULE STATUS: ADOPTION CAN BE DEFERRED

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BACKGROUND

The Commission voted on May 15 to withdraw its current rule proposal and initiate a new rulemaking on repeal language to Rule 25-14.003, F.A.C., which would have the effect of repealing the existing cumbersome mechanism. It replaces such a rule with the existing Commission practice of an ongoing earnings review, limited proceedings and rate cases and states the method by which the Commission will address 1989 tax savings. The rule revision, as published in the Florida Administrative Weekly, mandates that the Commission monitor the impact of any corporate income tax expense changes on the regulated companies' overall earnings through the Commission's ongoing earnings review program. The Commission could address such a change in earnings through a limited proceeding or through a full rate case. It also states that the Commission will address the 1989 tax savings under the rule in effect at 12/31/89.

DOCUMENT NUMBER-DATE

07835 AUG 30 1990

FPSC-RECORDS/REPORTING

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The rule proposed was published in the Florida Administrative Weekly. No hearing was requested. Thus, final Commission action is now possible.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission take final action to repeal all of Rule 25-14.003, F.A.C.?

PRIMARY RECOMMENDATION: Yes. The best way to address the concerns with the rule is to repeal the language altogether. (Attachment A).

ALTERNATIVE 1: If the Commission chooses to maintain some rule language specifically addressing corporate tax law changes, the language which reflects the Commission practices after a repeal should be adopted through final action. This language, which was proposed by the Commission on May 15, is set forth in Attachment B, with some minor technical changes.

ALTERNATIVE 2: If the Commission chooses to retain some language to address only a concern about pre-1990 tax rate changes, the language in Attachment C would satisfy this concern.

STAFF ANALYSIS:

Primary Recommendation

After reviewing this rule recommendation again in light of comments received by participants, we believe actual repeal of the tax rule in toto is superior to adopting language which is intended to reflect Commission practice after a repeal. In other words, we recommended to the Commission on May 15 that if there were lingering concerns about 1989 tax savings, then some language reflecting total repeal could be placed in the rule to replace the existing cumbersome mechanism. We presented some draft language at Agenda which was then amended by the Commission to initiate a new rulemaking.

However, several commenters have raised concerns with that language, which leads us to recommend instead that the Commission proceed with a total repeal of the rule. The primary reason is that placing any language in the rule leads to varying interpretations in this complex area, no matter how hard we attempt to use precise wording to reflect the intended practice. The written comments received from Southern Bell and Florida Power & Light Company (FPL), as well as the verbal concerns expressed

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by the Division of Water and Sewer staff and other members of staff, illustrate the potential problems in our language as proposed.

Both FPL and Southern Bell, in their comments, acknowledged that the proposed rule merely reflects existing practices of the Commission absent some mechanism in Rule 25-14.003. Southern Bell stated, "In general, Southern Bell believes that the proposed rule simply restates that powers granted to the Commission elsewhere can be exercised specifically with respect to income tax expense changes . . ." FPL referred to its comments as "intended to assist the Commission in its attempt to repeal the existing cumbersome mechanism for corporate income tax adjustments." FPL agreed that the existing language should be repealed.

However, then Southern Bell spells out concerns with the use of phrases "change in tax expense" and "income tax adjustments." In addition, Southern Bell objects to the Summary of the Estimate of Economic Impact which states that, "Following rule revision, the Commission may conduct limited proceedings regarding any change in earnings due to tax rate changes or may address such earnings change through full rate cases." Southern Bell states:

The summary implies that the rule encompasses only "tax rate changes" rather than all tax law changes affecting the company's income tax expense, as provided in the rule itself.

This evidence of confusion regarding repeal language leads us to recommend total repeal of any language.

This total repeal is equivalent to the policy and intention of the language in the FAW proposal and in the EIS. Therefore, we do not believe a new rulemaking process needs to be initiated. The Commission has already adopted the policy of repeal: only the mechanics are in need of debate. Repeal of the tax rule, as discussed in the last recommendation, is entirely consistent with case law. Tax expenses are to be treated in the same manner as other expenses.

The Division of Water and Sewer is also concerned that the language, as proposed, may not--in reality--equal repeal. The rule language--no matter what the Commission's intention--could be turned into a cumbersome process or a vehicle to address other issues.

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Alternative 1

If the Commission chooses to maintain some rule language specifically addressing corporate income tax expense adjustments, the language proposed by the Commission reflecting the Commission practices absent the current mechanism should be adopted through final action. This language, which was proposed by the Commission May 15, is set forth in Attachment B, with some technical changes.

FPL, in its comments relating to the proposal suggested adding the phrase "to effect the change in base rates prospectively" so that the sentence would read:

The Commission may conduct a limited proceeding regarding such a change in tax expense to effect the change in base rates prospectively or may address income tax expense adjustments in a full rate case.

This language is somewhat unclear and subject to varying interpretation. FPL states that the purpose is to "conform with the Commission's objective to effect changes in tax expense in base rates on a prospective basis." If the Commission wishes to incorporate FPL's change, we suggest instead inserting: "Resulting revenue requirement changes shall be prospective."

As discussed above, Southern Bell raised the concern that the summary should be clarified to state that the rule encompasses all tax law changes affecting the company's income tax expense. Staff agrees and believes that the rule itself can more clearly state that intent. Therefore, staff has added the phrase "caused by changes in federal or state income tax laws" to the term "income tax expense changes."

Southern Bell suggested that the rule would be easier to understand if it was stated that "Pre-1990 tax savings will continue to be treated in accord with the rule as it existed on January 1, 1990," rather than the earlier rule language. It stated, "The repeal of existing language shall apply to tax savings for the tax year 1990 and thereafter." We followed Southern Bell's suggestion, yet used the December 31, 1989, date to avoid any confusion about the emergency rule.

In addition, Joint Administrative Procedures Committee staff suggested that the language which stated, "The repeal of existing language shall not apply to pending cases" was unnecessary. We agree and therefore have deleted it from the rule proposal.

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Alternative 2

If the Commission chooses only to retain some language to address concerns about pre-1990 tax rate changes, the language in Attachment C would satisfy this concern. It merely states, "Pre-1990 income tax expense changes will continue to be treated in accord with Rule 25-14.003, Florida Administrative Code, as it existed on December 31, 1989."

ISSUE 2: After this rule revision has been filed with the Department of State and becomes effective, should this docket be closed?

RECOMMENDATION: Yes. The Commission should be able to proceed to final revisions without re-opening this process.

While there are some arguments to the contrary, we believe the Commission may choose any of the above options and proceed for final adoption of such revision. Throughout this lengthy rulemaking, participants have had full opportunity to discuss every conceivable angle of this revision--outright repeal, alternative mechanism, etc. Also, the water and wastewater utilities were already exempted from the existing rule; thus, it has already been operating under a "repeal" umbrella. Thus, we believe the above points in this recommendation lend support to any of these final approaches. While no commenter to the May 15 proposal actually recommended outright repeal, the comments indicate sufficient ambiguity and confusion regarding the repeal language in the proposal to warrant outright deletion of any rule language.

CBM:prl  
Attachment  
0034G

REPEALED

1 25-14.003 Corporate Income Tax Expense Adjustments.

2 (1) This rule shall not apply to water and wastewater  
3 utilities, as defined in Chapter 367, Florida Statutes.

4 (2) Definitions. For the purposes of this rule, the  
5 following definitions shall apply:

6 (a) "Tax Savings." The difference between the tax expenses  
7 for a utility calculated under the previously effective corporate  
8 income tax rates and those calculated under newly effective,  
9 reduced corporate income tax rates.

10 (b) "Tax Deficiency." The difference between the tax  
11 expenses for a utility calculated under newly effective, higher  
12 corporate income tax rates and those calculated under the  
13 previously effective corporate income tax rates.

14 (c) "Associated Revenues." Those revenues resulting from the  
15 application of a utility's revenue expansion factor to a tax  
16 savings or tax deficiency.

17 (d) "Previously Effective." Refers to the corporate income  
18 tax rate used in a utility's last rate case or show cause  
19 proceeding, or used in the last tax expense adjustment by the  
20 Commission, whichever occurred most recently.

21 (e) "Tax Rate." The statutory tax rates, both federal and  
22 state, applicable to utility income, including any surcharges,  
23 minimum taxes, and other adjustments to the basic percentage tax  
24 rates.

25 (f) "Midpoint." The midpoint of the range of return approved

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1 by the Commission in the utility's last rate case, adjusted for  
2 the cost of any debt issued subsequent to the rate case and prior  
3 to the commencement of a tax savings refund or tax deficiency  
4 collection.

5 (3) Tax Savings Refunds. In accordance with subsection (6)  
6 of this rule and using a calendar year as the basis of the  
7 calculation:

8 (a) When, during the reporting period described in paragraph  
9 (6)(a) below, a utility is earning a rate of return which is at or  
10 above the midpoint of its authorized range computed without  
11 consideration of a tax rate reduction, the utility shall refund  
12 all associated revenues as described in paragraph 6(c).

13 (b) When, during the reporting period described in paragraph  
14 6(a) below, a utility is earning a rate of return which is below  
15 the midpoint of its authorized range computed without  
16 consideration of a tax rate reduction, the utility shall refund  
17 only those associated revenues which cause the utility to earn in  
18 excess of that midpoint, as described in paragraph 6(c).

19 (4) Tax Deficiency Collections. In accordance with  
20 subsection (6) of this rule and using a calendar year as the basis  
21 of the calculation:

22 (a) When, during the reporting period described in 6(a)  
23 below, a utility is earning a rate of return which is at or below  
24 the midpoint of its authorized range computed without  
25 consideration of a tax rate increase, the utility shall collect

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1 all associated revenues, as described in paragraph 6(c).

2 (b) When, during the reporting period described in 6(a)  
3 below, a utility is earning a rate of return which is above the  
4 midpoint of its authorized range computed without consideration of  
5 a tax rate increase, the utility shall collect only those revenues  
6 which cause the utility to earn below that midpoint, as described  
7 in paragraph 6(c).

8 (5) Reporting Requirements. Fifteen days after the due date,  
9 including authorized extensions, of the annual report, of every  
10 year following a tax rate change, each utility shall furnish a  
11 final report, in the form prescribed by the Commission. The  
12 report shall cover only the prior calendar year during which the  
13 tax rate change was effective.

14 (6) Procedures.

15 (a) Refunds or collections shall be calculated from the  
16 effective date of any tax rate change through the end of the  
17 calendar year. If the tax rate change is in effect for only part  
18 of a tax year, the refund or collection shall be calculated in  
19 accordance with the utility's customary accounting treatment as  
20 authorized by the federal or state taxing authority for tax rate  
21 changes which occur during a tax year.

22 (b) A further change in the tax rate shall end one period of  
23 compliance and initiate a new period but shall not affect any  
24 refund or collection already in progress pursuant to this rule.

25 (c) Together with the final report described in subsection

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1 (5) of this rule, each utility shall file a petition containing a  
2 calculation of and the method for refunding or collecting any tax  
3 savings or deficiency for the tax year of the report. The  
4 Commission will review the petition and either approve it, approve  
5 it with modification, or deny it; an opportunity for a hearing on  
6 the Commission's decision will then be provided, if requested.  
7 Thereafter, the utility shall either make the refund to or collect  
8 the deficiency from its existing customers in accordance with  
9 paragraphs (e) and (f) of this subsection.

10 (d) Upon its own or other motion, the Commission may  
11 determine that a refund or collection for a particular year is  
12 impractical because its amount will not warrant the expense of  
13 making the refund or collecting the deficiency. In such an event,  
14 no refund or collection will be made for that year.

15 (e) The utility may make any refund or collection either as a  
16 lump sum payment or billing or in monthly installments not to  
17 exceed twelve (12) months. Such refunds or collections shall be  
18 made to or from current customers of the utility at the time that  
19 such refunds or collections are to be effected. In either event,  
20 the utility shall refund or collect the amount with interest  
21 accruing on any outstanding balance from the date of  
22 overcollection or underpayment. Interest shall be set by the  
23 Commission.

24 (f) An electric utility shall determine each customer's share  
25 of refund or collection on a kilowatt hour basis. A telephone

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1 company shall determine each customer's share of refund or  
2 collection based on existing general residence and business local  
3 rate relationships. Other utilities shall determine each  
4 customer's share of refund or collection based on consumption or  
5 any other reasonable basis specified in the utility's petition and  
6 approved by the Commission.

7 (7) Effect of Rate Case or Show Cause Proceeding. A tax  
8 savings refund or tax deficiency collection shall be consistent  
9 with this rule except that:

10 (a) The issue of a tax savings refund or tax deficiency  
11 collection shall be decided in the course of rate cases and show  
12 cause proceedings that are pending when a tax rate change becomes  
13 law, or that commence prior to the close of the tax year in which  
14 a tax rate change becomes effective.

15 (b) Nothing in this subsection shall be construed as limiting  
16 the operation of the tax expense adjustment process under this  
17 rule either in completing a tax savings refund or tax deficiency  
18 collection for any tax years prior to the year in which a rate  
19 case or show cause is initiated. It shall also not prohibit a tax  
20 savings refund or tax deficiency collection for any tax year or  
21 portion thereof ending prior to the final order in a rate case or  
22 show cause proceeding.

23 Specific Authority: 364.01, 366.05, 367.121, F.S.

24 Law Implemented: 364.01, 366.05, 367.121, F.S.

25 History: New 6/22/82, formerly 25-14.03, Amended 1/1/90.

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1 (Substantial rewording of Rule 25-14.003. See Florida  
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3 25-14.003 Corporate Income Tax Expense Adjustments.  
4 The Commission shall monitor the impact of any corporate  
5 income tax expense changes caused by changes in federal or state  
6 income tax laws upon the regulated companies' overall earnings  
7 through the Commission's ongoing earnings review program. The  
8 Commission may conduct a limited proceeding regarding such a  
9 change in income tax expense or the Commission may address changes  
10 in income tax expense in a full rate case. Pre-1990 income tax  
11 expense changes will continue to be treated in accord with Rule  
12 25-14.003, Florida Administrative Code, as it existed on December  
13 31, 1989.

14 Specific Authority: 350.127(2), 364.01, 366.05, 366.06(3),  
15 367.121, F.S.

16 Law Implemented: 364.01, 364.035, 364.05, 366.05, 366.06,  
17 366.076, 367.121, 367.081, 367.0822, F.S.

18 History: New 6/22/82, formerly 25-14.03, Amended 1/1/90, \_\_\_\_\_.

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