**FLORIDA PUBLIC SERVICE COMMISSION**

**Fletcher Building**

**101 East Gaines Street**

**Tallahassee, Florida 32399-0850**

**M E M O R A N D U M**

**January 20, 1994**

**TO : DIRECTOR, DIVISION OF RECORDS AND REPORTING**

**FROM : DIVISION OF WATER AND WASTEWATER (MEADOR)**

**DIVISION OF AUDIT AND FINANCIAL ANALYSIS (HICKS) DIVISION OF LEGAL SERVICES (JABER)**

**RE :UTILITY: FLORIDA CITIES WATER COMPANY**

**DOCKET NO.: 921240-WS**

**COUNTIES: BREVARD, COLLIER AND LEE**

**CASE: DISPOSITION OF GROSS-UP FUNDS COLLECTED**

**AGENDA : FEBRUARY 1, 1994 - REGULAR - POST HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF**

**CRITICAL DATES: NONE**

**SPECIAL INSTRUCTIONS:ISSUES A AND B SHOULD BE VOTED ON FIRST, ISSUES 2 AND 3 SHOULD BE VOTED ON PRIOR TO ISSUE 1**

**RECOMMENDATION FILE NAME: I:\WP\WAW\921240B.RCM WAW**

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**CASE BACKGROUND**

Orders Nos. 16971 and 23541, issued December 18, 1986, and October 1, 1990, respectively, require that utilities annually file information to be used to determine the actual state and federal income tax liability directly attributable to contributions-in-aid-of-construction (CIAC), and whether a refund of the gross-up is appropriate for any given year for which gross-up was in effect.

Order No. PSC-92-0961-FOF-WS, issued September 9, 1992, clarified the provisions of Orders Nos. 16971 and 23541 for the calculation of refunds of gross-up of CIAC. On September 14, 1992, Order No. PSC-92-0961A-FOF-WS, was issued. That Order included the generic calculation form.

In accordance with Order No. 16971, Florida Cities Water Company (Florida Cities or utility) filed its 1987 through 1990 annual CIAC reports regarding its collection of gross-up each year. By Proposed Agency Action Order No. PSC-93-0389-FOF-WS, issued March 15, 1993, the Commission proposed that the utility refund excess CIAC gross-up collections for the years 1987 through 1990. The proposed refund amounts were $30,478 for 1987, $95,341 for 1988, $86,097 for 1989, and $70,121 for 1990.

On April 2, 1993, Florida Cities timely filed a protest to Order No. PSC-93-0389-FOF-WS. A hearing on this matter was held on November 4, 1993, in Tallahassee, Florida.

On November 16, 1993, Florida Cities filed a Motion for the Commission to Accept Late-filed Exhibit No. 9. On November 29, 1993, Florida Cities filed a Motion for Extension of time to file its post-hearing brief. These motions will be addressed in Issues A and B, respectively.

**DISCUSSION OF ISSUES**

**ISSUE A:** Should Florida Cities Water Company's Motion for the Commission to Accept Late-Filed Exhibit No. 9 be granted?

**RECOMMENDATION:** Yes. (JABER)

**STAFF ANALYSIS:** On November 16, 1993, Florida Cities filed a Motion for the Commission to Accept Late-Filed Exhibit No. 9, which, in its belief, shows the correct amount of CIAC tax refund as is contemplated by the Staff's method. In support of its motion, Florida Cities states the following:

1. The CIAC reports filed by Florida Cities for the years 1987   
   through 1990 included in the depreciation on line 8, the   
   first year's depreciation on the CIAC property and cash   
   received by Florida Cities;
2. Those reports were identified as Exhibit 6 at   
   the hearing.
3. Florida Cities learned at the hearing that Staff had   
   intended to consider depreciation on property and not   
   depreciation on cash.

Late-Filed Exhibit No. 9 consists of an explanation of the exhibit, revised CIAC reports for the years 1987 through 1990, a calculation of the gross-up refund, and a schedule of the first year's tax depreciation on contributed property for the years 1987 through 1990.

Staff believes that the contents of this exhibit should be given whatever weight the Commission deems appropriate in reaching its final decision in this docket. Therefore, Staff recommends that the Motion to Accept Late-Filed Exhibit No. 9 should be granted.

**ISSUE B:** Should Florida Cities Water Company's Motion for Extension of Time to file its post hearing brief be granted?

**RECOMMENDATION:** Yes. (JABER)

**STAFF ANALYSIS:** On November 29, 1993, the utility requested a three-day extension of time to file its post-hearing brief. Staff had no objection to this request. Staff believes the motion should be granted because there was no prejudice to either Staff nor the party, nor was there any impediment to the preparation of this recommendation. Florida Cities filed its Brief on December 1, 1993. Therefore, staff recommends that the Motion for Extension of Time be granted.

**ISSUE 1:** Should Florida Cities Water Company be required to refund excess gross-up collections of $30,478 for 1987; $95,341 for 1988; $86,097 for 1989; and $70,121 for 1990, for a total of $282,037 plus accrued interest through the date of refund?

**RECOMMENDATION:** Yes, the utility should be required to refund a total of $282,037 ($30,478 for 1987; $95,341 for 1988; $86,097 for 1989; and $70,121 for 1990), plus accrued interest through the date of refund, for gross-up collections in excess of the actual tax liability resulting from the collection of CIAC. No gross-up was collected in 1991, therefore, no refund for 1991 is appropriate. The refunds should be completed within 6 months. The utility should submit copies of cancelled checks, credits applied to monthly bills, or other evidence which verifies that the refunds have been made, within 30 days from the date of the refund. (MEADOR)

**POSITION OF THE PARTIES**

**UTILITY:** Florida Cities properly calculated tax expense attributable to the receipt of CIAC in accordance with Order No. 16971 and approved tariffs. Under such calculations, no refund is due. Alternatively, any refund calculation should be limited to recognize first year depreciation on contributed property (not cash), with any resulting balance credited to CIAC.

**STAFF ANALYSIS:** The determination of whether the first year's depreciation is used to reduce taxable CIAC (Issue 2) and whether the refund calculation adopted by the Commission in Orders Nos. PSC-92-0961 and 92-0961A-FOF-WS will be used prospectively (Issue 3), will have an effect on the refund calculation addressed in this issue.

The utility's position is that it properly calculated the tax expense attributable to the receipt of CIAC in accordance with Order No. 16971 and approved tariffs. Utility Witness Werle testified that the utility made the appropriate calculations and has complied with Order No. 16971, Staff Advisory Bulletin No. 25 and the tariffs approved by the PSC issued under that Order; and therefore, no refund is appropriate (TR 14). Witness Schifano testified that the tariffs, approved by the PSC set forth the same formula for calculation of the gross-up as provided by Order No. 16971 (TR 50-51). The utility provided no testimony as to actual numbers for the refund calculation.

Staff believes the record is clear that both Orders Nos. 16971 and 23541 are consistent in their reference to a utility's actual tax expense or tax liability (TR 71, EXH 1, JBW-2, Page 15 of 17, Order No. 23541, Page 24). Witness Causseaux testified that the gross-up required was to be calculated on the actual liability of the utility -- contributions received less depreciation taken multiplied by the applicable tax rate. That required gross-up was to then be compared to the actual gross-up collected (TR 72). Witness Causseaux further testified that the Commission, by issuance of Order No. PSC-92-0961-FOF-WS, provided that refunds should no longer be calculated by including the taxes on the gross-up. Staff Witness Causseaux testified that in the future, the actual tax liability was to be grossed-up for comparison with the amount of gross-up actually collected. (TR 74) Order No. PSC-92-0961-FOF-WS was not protested (TR 72).

Composite Exhibit No. 6, APC-4, Page 7 of 7 reflects the Commission's proposed refund calculations for the years 1987 through 1990. The balances were taken from the jurisdictional amounts in the revised reports as filed by the utility. (Composite EXH 6, APC-3, Pages 7, 8, 9, 10 and 11) Order No. 23541, Page 18, requires that above-the-line net operating losses (NOLs) be used to offset CIAC income. Order No. 23541 further states that, until a tax liability is incurred, there is no additional tax burden. By requiring utilities to offset CIAC income with NOLs, the Commission is only recognizing what utilities are actually doing on their tax returns. In each year, the tax returns (Composite Exh 3) and the annual gross-up reports (Composite Exh 6) indicate above-the-line taxable income prior to the collection of taxable CIAC. As a result, staff recommends the full amount of taxable CIAC collected be used as taxable income. The full amount of taxable CIAC less the first year's depreciation claimed by the utility in its federal and state income tax returns determines the amount of net taxable CIAC. The reduction for first year's depreciation is consistent with staff's recommendation in Issue No. 2. The following method of calculating the "required gross-up" is consistent with the method established by Orders Nos. PSC-92-0961 and PSC-92-0961A-FOF-WS. It is the utility's position that the refund calculation found in Order No. 92-0961 should be applied prospectively.

Consistent with staff's recommendation in Issue No. 2, the calculation established in Order No. PSC-92-0961A-FOF-WS was used. The net taxable amount was multiplied by the combined federal and state tax rate for each year to arrive at net income taxes associated with the collection of taxable CIAC. The net income taxes were then grossed-up to reflect the taxes associated with collection of that amount of "required gross-up". The amount of refund is determined by comparing the required gross-up with the amount of gross-up collected for each year. (TR 74) The calculation is reflected in Schedule No. 1 attached to the recommendation.

Staff recommends that the utility be required to refund a total of $282,037 ($30,478 for 1987; $95,341 for 1988; $86,097 for 1989; and $70,121 for 1990), plus accrued interest through the date of refund, for gross-up collections in excess of the actual tax liability resulting from the collection of CIAC. No gross-up was collected in 1991, therefore, no refund for 1991 is appropriate (TR 54, 60-61). The refunds should be completed within 6 months. The utility should submit copies of cancelled checks, credits applied to monthly bills, or other evidence which verifies that the refunds have been made, within 30 days from the date of the refund.

**ISSUE 2:** Should the first year's depreciation on CIAC be deducted from taxable CIAC in calculating the refund of excess gross-up collections on CIAC?

**RECOMMENDATION:** Yes. Depreciation is an allowable deduction for federal tax purposes, which the utility claimed on its federal tax returns in determining taxable income. Depreciation is an integral part of the determination of taxable income, which should be calculated by reducing the amount of taxable CIAC collected in each year by the amount of first year's depreciation deduction taken by the utility. (MEADOR, HICKS)

**POSITION OF THE PARTIES**

**UTILITY:** No. Prior to October, 1990, there was no reasonable basis to believe that the Florida Public Service Commission intended to authorize the collection of that which would necessarily be refunded. The first year's depreciation should be treated no differently than subsequent years' depreciation.

**STAFF ANALYSIS:** The utility's position is that the first year's depreciation on CIAC should not be deducted from taxable CIAC in calculating the refund of excess gross-up collections on CIAC. Witness Werle testified there was no reasonable basis to believe the Commission intended to authorize the collection of that which would necessarily be refunded. Mr. Werle testified that overcharging customers is not a sound business practice and is frowned on by the Commission. (TR 106) He argued that if the Commission really intended that the benefit from first year depreciation was to ultimately reduce the amount of gross-up, why would the utility be allowed to collect an excess amount from the developer for which a refund was guaranteed at the point of time of collection (TR 15, 106). Both Witnesses Werle and Schifano argue that the utility collected the gross-up as allowed by its approved tariffs which were consistent with the formula presented in Order No. 16971 (TR 17, 50-52). Witnesses Werle and Schifano testified that the issuance of Order No. 23541 was the first indication that first year tax benefit of depreciation of CIAC should be passed on to contributors paying the tax impact on CIAC (TR 14-17, 54-55). Witness Werle further argued that what is pertinent to this proceeding, is that all the Tax Reform Act of 1986 actually did was make CIAC not subject to the general provisions of Section 118, which had formerly exempted it from income tax (TR 24).

Staff disagrees with Messrs. Werle and Schifano regarding the collection of depreciation which would necessarily be refunded. First, Witnesses Schifano and Causseaux both testified that the issuance of Order No. 16971 granting authority to gross-up was due to the emergency nature of the change in the tax code (TR 57, 87, Order No. 16971, Page 4). Witness Schifano testified that the purpose of gross-up was to pass on the tax impact (TR 60) and Witness Causseaux testified that the purpose was intended to keep the utility whole and not provide it with a windfall (TR 70). Witness Causseaux went on to testify that Order No. 16971 was issued to provide absolutely the maximum amount of taxes that could possibly be required (TR 81, 88). The amounts collected were subject to refund (Order No. 16971, Page 3), which protects the customer or developer who pays the gross-up (TR 81). In addition, by collecting the maximum amount the utility may possibly owe, the utility is protected from undercollection. Witness Causseaux testified that it would not be very easy to go back in the past and collect something that was not previously collected that was needed (TR 81). Staff agrees.

Upon subsequent examination, Witness Werle agreed that if an undercollection existed and a utility would not be allowed to go back and collect it, the utility would be better off to overcollect and allow a refund (TR 39-40). While staff agrees with the utility that generally overcharging customers is not a sound business practice and is frowned on by the Commission, staff notes that **all** gross-up collections are made subject to refund, pending a final determination of the gross-up required. Therefore, staff does not believe the utility's argument involving overcollection is persuasive. Staff believes that if a utility collects the maximum amount that could possibly be due, subject to refund, both parties are protected.

The utility's second argument that gross-up was collected consistent with the formula contained in Order No. 16971 and therefore, no refund is necessary, is also not persuasive. First, the formula presented in Order No. 16971 and the utility's tariff calculates the amount of gross-up to collect and does not address refunds (TR 76, 80, 84). As Witness Causseaux testified, Order No. 16971 was issued to allow utilities the opportunity to collect the maximum amount of taxes that could possibly be required (TR 81, 88) and does not calculate refunds. Staff does not dispute that the utility collected gross-up in accordance with its tariff and intent of Order No. 16971; however, the formula which determines the amount of gross-up to collect does not calculate the amount to be refunded (TR 80). Florida Cities has provided no evidence in the record which indicates that if the utility calculates and collects the gross-up according to its tariff, then no refund is due. The tariff reiterates what is found in Order No. 16971 (TR 6-7, 50-51, 86-87). The refund determination should be based upon what the utility does on its tax return (Order No. 23541, Page 18). The collection of gross-up and the refund determination are two separate calculations and have different functions.

Finally, both Witnesses Werle and Schifano argue that first year's depreciation did not emerge until October, 1990, with the issuance of Order No. 23541. Depreciation is and has been an element used in determining the actual tax liability of the utility (TR 30-31, 62-64, 75). The determination of a utility's actual tax liability has been referenced in both Orders Nos. 16971 and 23541, and therefore, should be included in calculating each year's refund of excess gross-up collections (TR 19-22; 71; Composite Exh 1, JBW-2, Page 15 of 17; Composite Exh 6, APC-1, Page 2 of 7; Order No. 23541, Page 24). Staff believes that the utility's arguments regarding the "prospective application" (Issue 3) of the refund calculation and the lack of specific reference to depreciation in the tariff and formula granting a utility gross-up authority ignore completely the basic fact that depreciation is an integral part of the calculation of the utility's actual tax liability (TR 75).

Order No. 16971 on page 3, paragraph (4)(c) states:

Annually, following the preparation and filing of the utility's annual Federal and State income tax returns, a determination shall be made as to the **actual Federal and State income tax expense** that is directly attributable to the inclusion of CIAC in taxable income for the tax year. CIAC tax impact monies received during the tax year that are in excess of the actual amount of tax expense that is attributable to the receipt of 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. (emphasis added)

On page 23 of Order No. 23541, the Commission states its intent regarding the language contained in Order 16971 as:

This could be interpreted to mean that we will look at the receipt of CIAC as an isolated tax event, or that a tax liability must be incurred on the overall jurisdictional return. However, since the taxation of CIAC in isolation can only produce a tax liability, the former interpretation makes no sense because there is no way that a refund could occur. **Accordingly, we believe that the intent was to consider the entire tax picture.** (emphasis added)

Order No. 23541 goes on to say on page 24:

Based upon the evidence of record and our discussion above, we find that all gross-up amounts in excess of **a utility's actual tax liability** resulting from its collection of CIAC should be refunded on a pro rata basis to those persons who contributed the taxes. (emphasis added)

The record is clear that both orders are and have been consistent in their reference to a utility's actual tax expense or tax liability (TR 19-22; 71; Composite Exh 1, JBW-2, Page 15 of 17; Composite Exh 6, APC-1, Page 2 of 7; Order No. 23541, Page 24). In addition, both utility witnesses Werle and Schifano testified that depreciation expense is an allowable deduction in calculating actual tax expense (TR 31, 63-64). Staff is not persuaded by the utility's argument that depreciation was not raised as an issue in connection with gross-up until the issuance of Order No. 23541. While depreciation was not specifically delineated as a component to be used in determining actual tax liability, the record is sufficiently clear that the Commission intended to analyze the entire tax picture (Order No. 23541, Page 23), which by definition and by the utility's own admission, includes depreciation (TR 31, 63-64, 75).

Witness Causseaux testified that depreciation is an integral part of the calculation of the utility's actual tax liability and reduces the revenues from the collection or receipt of CIAC (TR 75). All three witnesses agree that depreciation is a component in the calculation of actual tax liability (TR 31, 63-64, 75). In staff's opinion, it is not relevant whether the orders, tariffs or the gross-up formula itself specifically refer to depreciation expense or not. Staff believes the orders clearly indicate the intent of the Commission has always been to determine that amount of gross-up to be retained based upon the utility's actual tax liability, which would include a deduction to CIAC revenue for depreciation.

Witness Causseaux testified depreciation reduces the revenues from the collection or receipt of CIAC (TR 75). If depreciation is excluded from the calculation of actual tax liability, it appears to staff, that the utility will collect more in taxes than it actually pays on its federal tax return, which would result in a windfall of cash to the utilities. Witness Causseaux further testified that gross-up was intended to keep the utility whole and not provide it with a windfall (TR 70, 76). Witness Werle testified that the purpose of gross-up was to keep the utilities whole because of the tax change (TR 33) and Witness Schifano testified that the purpose of gross-up is to allow the utility to pass through the tax impact of CIAC that became taxable because of the amendments to 118 of the code (TR 61-62). Staff believes the exclusion of depreciation would violate the stated intent of gross-up.

As discussed in Issue A, the utility filed Late-Filed Exhibit No. 9. Late-Filed Exhibit No. 9 indicates that no cash CIAC received in any year was converted into property and all associated depreciation should be removed. Based upon our discussion and recommendation in Issue A, staff has reviewed the exhibit. On a basic and bottom line review, the late-filed exhibit appears to revise the Commission required gross-up reports and remove ALL depreciation associated with its collection of cash CIAC. It appears inconsistent with the utility's response in Interrogatory No. 1, Composite Exhibit No. 2. In Composite Exh No. 2, the utility acknowledged that it included the depreciation on its tax return (TR 25). The utility does not mention in Late-Filed Exhibit No. 9 that amended tax returns will be filed which remove the depreciation deduction associated with the cash CIAC.

We cannot rely on Late-Filed Exhibit No. 9 for several reasons. First, as a part of the exhibit, the utility included a portion of the hearing transcript where Witness Causseaux testified that staff had not intended to include depreciation on cash CIAC unless converted into property in the year of receipt. Also included was a portion of the hearing transcript wherein Witness Causseaux discusses netting the amount of property added in a year with the amount of cash received as a basis of determining whether cash CIAC has been converted, and therefore depreciable, in lieu of detailed records which attempt to trace the cash received (TR 95). Exhibit No. 9 fails to include any supporting numbers. It appears to be a bold blanket statement that no cash was converted with no supporting documentation. The company did not even perform the netting of property additions and cash that Witness Causseaux suggested be done. Second, if such a netting is done, it indicates that some if not all of the cash had to have been converted to property in each year.

The following analysis was determined from the tax returns which are Composite Exhibit No. 3 and Exhibit No. 7. Staff was not able to make the netting calculation for 1987 because beginning year amounts are not available in the 1987 tax return. The analysis could be performed from the financial annual reports, however, those annual reports are not part of the record.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| YEAR | (A)  Beg. Depr Assets  Per 1120  Exh 3 | (B)  End. Depr  Assets  Per 1120  Exh 3 | (C)  Increase in Depr Assets  (B) - (A) | (D)  Less  Property  CIAC  Exh 7 | (E)  Net  Additions  After Prop. CIAC  (C) - (D) | (F)  Less  Cash  CIAC  Exh 7 | (G)  Net Assets  In Excess  of Cash and Prop  (E) - (F) |
| 1988 | 101,426,885 | 106,443,239 | 5,016,354 | 2,452,777 | 2,563,577 | 1,941,892 | 621,685 |
| 1989 | 106,443,239 | 117,234,646 | 10,791,407 | 1,896,478 | 8,894,929 | 2,162,635 | 6,732,294 |
| 1990 | 117,234,646 | 123,195,940 | 5,961,294 | 1,931,389 | 4,029,905 | 1,290,861 | 2,739,044 |

Staff has taken the beginning and ending depreciable plant balance from the balance sheet included in each year's 1120 tax return (Composite Exh 3) to determine the annual additions of depreciable plant. Staff then removed the amount of property CIAC received in each year as detailed in Exhibit No. 7 to arrive at the amount of net additions after property CIAC. Staff then removed the amount of cash CIAC collected (Composite Exhibit No. 7) to determine if the amount of property additions exceeded both the amount of cash and property CIAC received.

Based upon this analysis, it appears that the utility had plant additions for each year 1988 through 1990 far in excess of the amount of property and cash CIAC collections. Staff believes the utility has failed to support its position that no cash was converted into property and that the depreciation the utility indicates in its response to Interrogatory No. 1, Composite Exh No. 2 took on its tax returns should be excluded from the refund calculation.

Rule 25-30.515(3), Florida Administrative Code defines CIAC as:

any amount or item of money, services, or property received by a utility, from any person or governmental agency, any portion of which is provided at no cost to the utility, which represents an addition or transfer to the capital of the utility, and **which is utilized to offset the acquisition, improvement, or construction costs of the utility's property, facilities, or equipment used to provide utility services to the public**. The term includes system capacity charges, main extension charges and customer connection charges. (Emphasis added)

By definition, CIAC charges are intended for plant and are to be utilized for the acquisition, or construction of utility property, and therefore, staff believes they will be converted into property and will be depreciated. The problem is when will the conversion be made, and not whether they will be converted into property.

As stated earlier, Orders Nos. 16971 and 23541 refer to an annual determination of a utility's actual tax liability; which as testified to, includes a reduction to revenue for depreciation (TR 31, 63-64, 75). In an effort to keep utilities whole, staff believes the orders have also clearly shown the intent has always been to look at **all** of the actual components the utility included on their tax returns relating to the collection of taxable CIAC and determine the amount of gross-up required. The amount of gross-up collected in excess of the amount of gross-up required would be refunded.

Based upon the above discussion, staff recommends that the first year's depreciation on CIAC should be deducted from taxable CIAC in calculating the refund of excess gross-up collection on CIAC.

**ISSUE 3:** Should the refund formula in Order No. PSC-92-0961-FOF-WS be used in calculating the refund of excess gross-up collections for 1987 through 1990?

**RECOMMENDATION:** Yes, the purpose of Order No. PSC-92-0961-FOF-WS was to clarify the calculation of the refund only. It is consistent with the stated intent of both Orders Nos. 16971 and 23541, and therefore, should be applied to the calculation of refunds for 1987 through 1990. (JABER, MEADOR, HICKS)

**POSITION OF THE PARTIES**

**UTILITY:** No. The Florida Public Service Commission should exercise its power to clarify, modify or supersede Order No. 16971 prospectively. To do otherwise would violate the doctrines of administrative finality and the prohibition against retroactive ratemaking.

**STAFF ANALYSIS:** It is the utility's position that Order No. PSC-92-0961-FOF-WS should be applied to prospective years. The utility argues that to apply the order to the years 1987 through 1990 would constitute retroactive ratemaking. (BR 13). In support of its position, the utility cites to Southern Bell Telephone and Telegraph Company v. PSC, 453 So 2d 780 (Fla. 1984) and Sunshine Utilities v. PSC, 577 So 2d 663 (Fla. 1st DCA 1991).

In determining what the Commission intended by its use of the word "prospective" in Order No. PSC-92-0961-FOF-WS, we must review the entire purpose of that Order. The Commission issued Order No. PSC-92-0961-FOF-WS for the purpose of clarifying the provisions in Orders Nos. 16971 and 23541 with respect to the calculation of CIAC gross-up refunds, and not depreciation. (TR 74) That Order at p. 3 specifically states that:

This clarification in the appropriate calculation of gross-up refunds to include the tax liability associated with the amount of gross-up retained shall be applied on a prospective basis. Attachment A hereto reflects the calculation we will employ in our determination of the amount of taxable CIAC. (Composite Exhibit No. 6, APC-1, P. 3 of 7).

The facts contributing to the issuance of Order No. PSC-92-0961-FOF-WS are as follows. A utility raised the issue of whether the taxes paid on the amount of gross-up collected should be included in the calculation of the refund. In analyzing that issue, the Commission discovered that it had used two different interpretations or methodologies in its treatment of the taxes paid on the amount of gross-up. It is that clarification that the Commission made in Order No. PSC-92-0961-FOF-WS. It is that clarification that the Commission stated would be applied on a prospective basis. Nowhere in Order No. PSC-92-0961-FOF-WS did the Commission state that the refund formula would only be applied for the years 1992 forward. Further, it is important to note here that Attachment A (found in Order No. PSC-92-0961A-FOF-WS), which is the Commission's calculation of the refund, specifically addresses the years 1987 through 1990.

Since Order No. PSC-92-0961-FOF-WS only involved a clarification in the refund formula with respect to the Commission's treatment of the taxes paid on the amount of gross-up, and did not address depreciation in any manner, Staff fails to see the validity in the utility's argument that retroactive ratemaking has occurred. As discussed in Issue 2, the Commission has always determined the amount of gross-up required by analyzing the utility's actual tax liability. Order No. PSC-92-0961-FOF-WS did not modify, change nor supersede any prior order with respect to the treatment of depreciation. The Order did, however, clarify, that on a prospective basis (as opposed to prospective years), the Commission would treat the taxes paid on the amount of gross-up in accordance with the formula found in that Order. No other element of the refund formula was addressed in that Order.

Finally, staff agrees with the utility that retroactive ratemaking is never appropriate. For that very reason, the Commission did not require the utilities previously ordered to make refunds to go back and recalculate the refund amount based on the formula found in Order No. PSC-92-0961-FOF-WS. In Sunshine, the Court in affirming the Commission's order, stated that the PSC has the authority to determine whether there are mistakes in its prior orders and has a duty to correct such errors. Id. at 665. Staff firmly believes that the clarification made in Order No. PSC-92-0961-FOF-WS was consistent with the case law on this issue and does not constitute retroactive ratemaking. The Commission's ability to review a formula found in a previous order or used by the Commission in calculating refunds is a power inherent in the Commission's statutory ratemaking authority to set rates which are just, fair and reasonable.

Based on the foregoing, staff recommends that the calculation provided in Order No. PSC-92-0961-FOF-WS and Order No. PSC-92-0961A-FOF-WS should be used in calculating the refund of excess gross-up collections for each year 1987 through 1990. The recommended refund amounts are discussed in Issue 1.

**ISSUE 4:** Should the docket be closed?

**RECOMMENDATION:** No. Staff should be given administrative authority to close the docket upon verification that the refunds have been completed. (MEADOR, JABER)

**STAFF ANALYSIS:** The docket should remain open pending completion and verification of the refunds. Staff recommends that administrative authority be granted to staff to close the docket upon verification that the refunds have been made.

SCHEDULE NO. 1

FLORIDA CITIES WATER COMPANY STAFF CALCULATED GROSS‑UP REFUND

SOURCE: (Line references are from CIAC Reports)

1987 1988 1989 1990 1991

‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

1 Form 1120, Line 30 (Line 15) $ 3,793,099 $ 8,666,070 $ 6,901,695 $ 5,459,735 $ 0

2 Less CIAC (Line 7) (1,266,708) (4,265,300) (3,863,484) (3,140,623) 0

3 Less Gross‑up collected (Line 19) (961,547) (2,572,243) (2,329,660) (1,893,911) 0

4 Add First Year's Depr on CIAC (Line 8) 47,502 159,949 144,881 117,773 0

5 Add/Less Other Effects (Lines 20 & 21) 0 176,261 669,110 676,856 0

6 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

7 Adjusted Income Before CIAC and Gross‑up $ 1,612,346 $ 2,164,737 $ 1,522,542 $ 1,219,830 $ 0

8

9 Taxable CIAC (Line 7) $ 1,266,708 $ 4,265,300 $ 3,863,484 $ 3,140,623 $ 0

10

11 Taxable CIAC Resulting in a Tax Liability $ 1,266,708 $ 4,265,300 $ 3,863,484 $ 3,140,623 $ 0

12 Less first years depr. (Line 8) (47,502) (159,949) (144,881) (117,773) 0

13 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

14 Net Taxable CIAC $ 1,219,206 $ 4,105,351 $ 3,718,603 $ 3,022,850 $ 0

15 Effective state and federal tax rate 43.30% 37.63% 37.63% 37.63% 37.63%

16 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

17 Net Income tax on CIAC $ 527,916 $ 1,544,844 $ 1,399,310 $ 1,137,498 $ 0

18 Less ITC Realized 0 0 0 0 0

19 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

20 Net Income Tax $ 527,916 $ 1,544,844 $ 1,399,310 $ 1,137,498 $ 0

21 Expansion Factor for gross‑up taxes 1.76366843 1.603334937 1.603334937 1.603334937 1.603334937

22 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

23 Gross‑up Required to pay tax effect $ 931,069 $ 2,476,902 $ 2,243,563 $ 1,823,790 $ 0

24 Less CIAC Gross‑up collected (Line 19) (961,547) (2,572,243) (2,329,660) (1,893,911) 0

25 ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑ ‑‑‑‑‑‑‑‑‑‑‑‑

26 PROPOSED REFUND (excluding interest) $ (30,478) $ (95,341) $ (86,097) $ (70,121) $ 0

27 ============ ============ ============ ============ ============

28 No Gross‑up

29 TOTAL REFUND $ (282,037) Collected

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