

FLORIDA PUBLIC SERVICE COMMISSION
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M E M O R A N D U M

DECEMBER 05, 1996

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF WATER & WASTEWATER (JOHNSON)
DIVISION OF LEGAL SERVICES (O'SULLIVAN) *mo JHS*

RE: DOCKET NO. 961211-WS - DISPOSITION OF CONTRIBUTION IN AID
OF CONSTRUCTION GROSS-UP FUNDS COLLECTED BY SUNRAY
UTILITIES, INC.
COUNTY: NASSAU
November 12, 1996

AGENDA: ~~DECEMBER 17, 1996~~ - REGULAR AGENDA - PROPOSED AGENCY
ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: S:\PSC\WAW\WP\961211.RCM

CASE BACKGROUND

Sunray Utilities - Nassau, Inc. (Sunray or utility) is a Class C water and wastewater utility which provides service to approximately 142 customers in Nassau County. According to their 1995 annual report, operating revenue of \$47,836 for the water system and \$54,814 for the wastewater system was reported. The utility reported a net operating loss of \$42,231 for the water system and \$77,873 for the wastewater system.

As a result the repeal of Section 118(b) of the Internal Revenue Code (I.R.C.), contributions-in-aid-of-const-uction (CIAC) became gross income and were depreciable for federal tax purposes. In Order No. 16971, issued December 18, 1986, the Commission authorized corporate utilities to collect the gross-up on CIAC in order to meet the tax impact resulting from the inclusion of CIAC as gross income.

Order Nos. 16971, issued December 18, 1986, and 23541, issued October 1, 1990, 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 require that all gross-up collections for a tax year, which are in excess of a utility's actual tax

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liability for the same year, should be refunded on a pro rata basis to those persons who contributed the taxes.

In Order No. 23541, the Commission required that any water and wastewater utility already collecting the gross-up on CIAC and wishing to continue, had to file a petition for approval with the Commission on or before October 29, 1990. Sunray filed for authority to continue to gross-up on February 1, 1991. By Order No. PSC-92-0130-FOF-WS, issued March 31, 1992, Sunray was granted authority to continue to gross-up using the full gross-up formula.

On September 9, 1992, this Commission issued Proposed Agency Action Order 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, Order No. PSC-92-0961A-FOF-WS, was issued which included Attachment A which reflects the generic calculation form. No protests were filed, and the Order became final.

On March 29, 1996, Docket No. 960397-WS was opened to review the Commission's 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, staff was directed to continue processing CIAC gross-up and refund cases pursuant to Order Nos. 16971 and 23541; however, staff was also directed to make a recommendation to the Commission concerning whether the Commission's policy regarding the collection and refund of CIAC should be changed upon staff's completion of its review of the proposals and comments offered by the workshop participants. In addition, staff was directed to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up.

However, The Small Business Job Protection Act of 1996 (The Act) was signed into law by President Clinton 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, Order No. PSC-96-1180-FOF-WS was issued to revoke the authority of utilities to collect gross-up of CIAC and to cancel the respective tariffs unless, within 30 days of the issuance of the order, affected utilities requested a variance. Because, there was no longer a need to review the Commission's policy to determine any changes, by Order No. PSC-96-1253-FOF-WS, issued October 8, 1996, the Commission closed Docket No. 960397-WS.

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However, as established in Order No. PSC-96-0686-FOF-WS, all pending CIAC gross-up refund cases are being processed pursuant to Order Nos. 16971 and 23541. The purpose of this recommendation is to address the disposition of CIAC refunds for the years 1993 and 1994.

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DISCUSSION OF ISSUES

ISSUE 1: Should Sunray be required to refund excess gross-up collections for 1993 and 1994?

RECOMMENDATION: No, the utility required more gross-up than was collected in each year; therefore, no refund is necessary.
(JOHNSON)

STAFF ANALYSIS: In compliance with Order No. 16971, Sunray filed its 1993 and 1994 annual CIAC reports regarding its collection of gross-up for each year. Staff has calculated the gross-up required to pay the tax liability resulting from the collection of taxable CIAC by grossing-up the net taxable CIAC amount, in accordance with the method adopted in Order No. PSC-92-0961-FOF-WS. On October 7, 1996, the utility contacted the staff and stated that it agreed with staff's preliminary calculations.

ANNUAL GROSS-UP REFUND AMOUNTS

Based upon the foregoing, staff has calculated the amount of refund per year which is appropriate. Our calculations, taken from the information provided by the utility in its gross-up reports and tax returns filed each year are reflected on Schedule No. 1. A summary of each year's refund calculation follows.

1993

The utility proposes that no refund is appropriate.

Staff agrees 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 in income. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$170,045 in taxable CIAC was received, with \$4,265 being deducted for the first year's depreciation. In addition, \$83,053 of gross-up collections were received. Staff has used the 37.63% combined marginal federal and state tax rates as provided in the 1993 CIAC Report to calculate the tax effect of \$100,021. Based upon the foregoing, staff calculates that the utility required more in gross-up to pay the tax impact than was collected; therefore, staff recommends that no refund is necessary.

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1994

The utility proposes that no refund is appropriate.

Staff agrees 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 in income. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$22,994 in taxable CIAC was received, with \$387 being deducted for the first year's depreciation. In addition, \$14,000 of gross-up collections were received. Staff has used the 38.57% combined marginal federal and state tax rates as provided in the 1994 CIAC Report to calculate the tax effect of \$14,195. Based upon the foregoing, the utility required more in gross-up to pay the tax impact than was collected; therefore, staff recommends that no refund is necessary.

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ISSUE 2: Should the docket be closed?

RECOMMENDATION: Yes, the docket should be closed upon expiration of the protest period. (JOHNSON, O'SULLIVAN)

STAFF ANALYSIS: Upon expiration of the protest period, if a timely protest is not filed by a substantially affected person, processing of this docket is complete and the docket should be closed.

STAFF CALCULATED GROSS-UP REFUND

SUNRAY UTILITIES - NASSAU, INC.

SOURCE: (Line references are from CIAC Reports)

	1993	1994
1 Form 1120, Line 30 (Line 15)	\$ 287,182	\$ 74,811
2 Less CIAC (Line 7)	(170,045)	(22,994)
3 Less Gross-up collected (Line 19)	(83,053)	(14,000)
4 Add First Year's Depr on CIAC (Line 8)	4,265	387
5 Add/Less Other Effects (Lines 20 & 21)	(23,918)	(18,069)
6		
7 Adjusted Income Before CIAC and Gross-up	\$ 14,431	\$ 20,135
8 Taxable CIAC (Line 7)	170,045	22,994
9 Less first years depr. (Line 8)	(4,265)	(387)
10		
11 Taxable CIAC Resulting in a Tax Liability	\$ 165,780	\$ 22,607
12 Less: NOL Carrforward	0	0
13		
14 Net Taxable CIAC	\$ 165,780	\$ 22,607
15 Effective state and federal tax rate	37.63%	38.57%
16		
17 Net Income tax on CIAC	\$ 62,383	\$ 8,720
18 Less ITC Realized	0	0
19		
20 Net Income Tax	\$ 62,383	\$ 8,720
21 Expansion Factor for gross-up taxes	1.603334937	1.627869119
22		
23 Gross-up Required to pay tax effect	\$ 100,021	\$ 14,195
24 Less CIAC Gross-up collected (Line 19)	(83,053)	(14,000)
25		
26 (OVER) OR UNDER COLLECTION	\$ 16,968	\$ 195
27		
28		
29 TOTAL YEARLY REFUND	\$ 0	\$ 0
30		
31		
32 PROPOSED REFUND (excluding interest)	\$ 0	
33		