

FLORIDA PUBLIC SERVICE COMMISSION  
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MEMORANDUM

DECEMBER 4, 1997

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FPSC - Records/Reporting

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

FROM: DIVISION OF WATER & WASTEWATER (JOHNSON)  
DIVISION OF LEGAL SERVICES (JAEGERS)

RE: DOCKET NO. 971524-WS - DISPOSITION OF CONTRIBUTION IN AID  
OF CONSTRUCTION GROSS-UP FUNDS COLLECTED BY SUNRAY  
UTILITIES, INC.  
COUNTY: NASSAU

AGENDA: DECEMBER 16, 1997 - REGULAR AGENDA - PROPOSED AGENCY  
ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: S:\PSC\WAW\WP\971524.RCM

CASE BACKGROUND

Sunray Utilities - Nassau, Inc. (Sunray or utility) is a Class C water and wastewater utility which provides service to approximately 163 water customers and 155 wastewater customers in Nassau County. According to their 1996 annual report, operating revenue of \$62,272 for the water system and \$75,997 for the wastewater system was reported. The utility reported a net operating loss of \$52,873 for the water system and \$69,087 for the wastewater system.

As a result of the repeal of Section 118(b) of the Internal Revenue Code (I.R.C.), contributions-in-aid-of-construction (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.

Orders 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

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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, the Commission 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. 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 Orders 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 Orders 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 gross-up 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 Orders Nos. 16971 and 23541. The purpose of this recommendation is to address the disposition of CIAC refunds for 1996.

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### DISCUSSION OF ISSUES

ISSUE 1: Should Sunray be required to refund excess gross-up collections for 1996?

RECOMMENDATION: No, the utility should credit the \$28 excess gross-up to CIAC. (JOHNSON)

STAFF ANALYSIS: In compliance with Order No. 16971, Sunray filed its 1996 annual CIAC report regarding its collection of gross-up for the 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-POF-WS. On May 20, 1997, 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 for 1996 which is appropriate. Our calculation, which is reflected on Schedule No. 1, is based on information provided by the utility in its gross-up report. A summary of the refund calculation follows.

#### 1996

The utility proposes that no refund is appropriate. Staff calculates an overcollection of \$28 for 1996.

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 in income. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$21,855 in taxable CIAC was received, with \$368 being deducted for the first year's depreciation, resulting in net taxable CIAC of \$21,487. Staff has used the 37.63% combined marginal federal and state tax rates to calculate the tax effect of \$8,086. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect of the CIAC is calculated to be \$12,965. The utility collected \$12,993 in gross-up taxes. Based upon the foregoing, staff calculates the utility collected \$28 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1996 which must also be refunded through the date of the refund.

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Staff believes the refund amount to be immaterial and the cost of processing the refund would be more costly. The gross-up funds were collected from 54 individuals or entities during 1996. Based on the total refund amount, each contributor would receive about \$0.52 each. The net CIAC level is 20.42% contributed. Staff believes that the administrative costs would more than likely exceed the individual refund amounts, and recommends the utility credit CIAC for the excess collections.

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ISSUE 2: Should the docket be closed?

RECOMMENDATION: Yes, the docket should be closed upon expiration of the protest period, if no protest is received. (JAEGER)

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.

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SCHEDULE NO. 1

STAFF CALCULATED GROSS-UP REFUND

SUNRAY UTILITIES - NASSAU, INC.

SOURCE: (Line references are from CIAC Reports)	1996
1 Form 1120, Line 30 (Line 15)	\$ 78,468
2 Less CIAC (Line 7)	(21,855)
3 Less Gross-up collected (Line 19)	(12,993)
4 Add First Year's Depr on CIAC (Line 8)	368
5 Add/Less Other Effects (Lines 20 & 21)	1,379
6	
7 Adjusted Income Before CIAC and Gross-up	\$ 45,367
8 Taxable CIAC (Line 7)	21,855
9 Less first years depr. (Line 8)	(368)
10	
11 Taxable CIAC Resulting in a Tax Liability	\$ 21,487
12 Less: NOL Carrforward	0
13	-
14 Net Taxable CIAC	\$ 21,487
15 Effective state and federal tax rate	37.63%
16	-
17 Net Income tax on CIAC	\$ 8,086
18 Less ITC Realized	0
19	-
20 Net Income Tax	\$ 8,086
21 Expansion Factor for gross-up taxes	1.60333493666827
22	-
23 Gross-up Required to pay tax effect	\$ 12,965
24 Less CIAC Gross-up collected (Line 19)	(12,993)
25	-
26 (OVER) OR UNDER COLLECTION	\$ (28)
27	-
28	-
29 TOTAL YEARLY REFUND	\$ 0
30	-
31	-
32 PROPOSED REFUND (excluding interest)	\$ 0
33	-