

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Petition for) DOCKET NO. 910110-WS
Continuation of Gross-Up of) ORDER NO. PSC-93-0635-PHO-WS
Contributions-in-Aid-of-) ISSUED: April 22, 1993
Construction (CIAC) in Lee)
County by GULF UTILITY COMPANY.)
_____)

Pursuant to Notice, a Prehearing Conference was held on April 2, 1993, in Tallahassee, Florida, before Commissioner Thomas M. Beard, as Prehearing Officer.

APPEARANCES:

B. Kenneth Gatlin, Esquire, Gatlin, Woods, Carlson & Cowdery, 1709-D Mahan Drive, Tallahassee, Florida, 32308. On behalf of Gulf Utility Company.

Patrick Wiggins, Esquire, Wiggins & Villacorta, 501 East Tennessee Street, Tallahassee, Florida, 32302. On behalf of Southwest Florida Capital Corporation.

Robert M. C. Rose, Esquire, Rose, Sundstrom & Bentley, 2548 Blairstone Pines Drive, Tallahassee, Florida 32301 On behalf of The Florida Waterworks Association

Matthew J. Feil, Esquire, Florida Public Service Commission, 101 E. Gaines Street, Tallahassee, Florida 32399-0863. On behalf of the Commission Staff.

PREHEARING ORDER

I. CASE BACKGROUND

On February 1, 1991, pursuant to Order No. 23541, issued October 1, 1990, Gulf Utility Company (Gulf or utility) filed its request for authority to continue Contributions-in-aid-of-Construction (CIAC) gross-up. On June 14, 1991, Southwest Florida Capital Corporation (SFCC) filed a petition for leave to intervene, and by Order No. 24808, issued July 12, 1991, SFCC's petition to intervene was granted. On July 30, 1992, by Order No. PSC-92-0742-FOF-WS, the Commission proposed to allow Gulf to continue gross-up of CIAC. On August 20, 1992, SFCC protested Order No. PSC-92-0742-FOF-WS. On March 30, 1993, the Florida Waterworks Association (FWWA) filed a petition to intervene, which is granted hereinbelow. Pursuant to SFCC's protest, this matter is scheduled for an administrative hearing on May 5 and 6, 1993.

DOCUMENT NUMBER-DATE

04377 APR 22 93

FPSC-RECORDS/REPORTING

II. PROCEDURE FOR HANDLING CONFIDENTIAL INFORMATION

A. Any information provided pursuant to a discovery request for which proprietary confidential business information status is requested shall be treated by the Commission and the parties as confidential. The information shall be exempt from Section 119.07(1), Florida Statutes, pending a formal ruling on such request by the Commission, or upon the return of the information to the person providing the information. If no determination of confidentiality has been made and the information has not been used in the proceeding, it shall be returned expeditiously to the person providing the information. If a determination of confidentiality has been made and the information was not entered into the record of the proceeding, it shall be returned to the person providing the information within the time periods set forth in Section 367.156(2), Florida Statutes.

B. It is the policy of the Florida Public Service Commission that all Commission hearings be open to the public at all times. The Commission also recognizes its obligation pursuant to Section 367.156, Florida Statutes, to protect proprietary confidential business information from disclosure outside the proceeding.

In the event it becomes necessary to use confidential information during the hearing, the following procedures will be observed:

- 1) Any party wishing to use any proprietary confidential business information, as that term is defined in Section 367.156, Florida Statutes, shall notify the Prehearing Officer and all parties of record by the time of the Prehearing Conference, or if not known at that time, no later than seven (7) days prior to the beginning of the hearing. The notice shall include a procedure to assure that the confidential nature of the information is preserved as required by statute.
- 2) Failure of any party to comply with 1) above shall be grounds to deny the party the opportunity to present evidence which is proprietary confidential business information.

- 3) When confidential information is used in the hearing, parties must have copies for the Commissioners, necessary staff, and the Court Reporter, in envelopes clearly marked with the nature of the contents. Any party wishing to examine the confidential material that is not subject to an order granting confidentiality shall be provided a copy in the same fashion as provided to the Commissioners, subject to execution of any appropriate protective agreement with the owner of the material.
- 4) Counsel and witnesses are cautioned to avoid verbalizing confidential information in such a way that would compromise the confidential information. Therefore, confidential information should be presented by written exhibit when reasonably possible to do so.
- 5) At the conclusion of that portion of the hearing that involves confidential information, all copies of confidential exhibits shall be returned to the proffering party. If a confidential exhibit has been admitted into evidence, the copy provided to the Court Reporter shall be retained in the Commission Clerk's confidential files.

III. POST-HEARING PROCEDURE

Rule 25-22.056(3), Florida Administrative Code, requires each party to file a post-hearing statement of issues and positions. You must include in that statement, a summary of each position of no more than 50 words, set off with asterisks. If a party's position has not changed since the issuance of the prehearing order, the post-hearing statement may simply restate the prehearing position; however, if the prehearing position is longer than 50 words, it must be reduced to no more than 50 words. The rule also provides that if a party fails to file a post-hearing statement in conformance with the rule, that party shall have waived all issues and may be dismissed from the proceeding.

A party's proposed findings of fact and conclusions of law, if any, statement of issues and positions, and brief, shall together

total no more than 60 pages, and shall be filed at the same time. The prehearing officer may modify the page limit for good cause shown. Please see Rule 25-22.056, Florida Administrative Code, for other requirements pertaining to post-hearing filings.

IV. PREFILED TESTIMONY AND EXHIBITS

Testimony of all witnesses to be sponsored by the parties has been prefiled. All testimony which has been prefiled in this case will be inserted into the record as though read after the witness has taken the stand and affirmed the correctness of the testimony and associated exhibits. All testimony remains subject to appropriate objections. Each witness will have the opportunity to orally summarize his or her testimony at the time he or she takes the stand. Upon insertion of a witness' testimony, exhibits appended thereto may be marked for identification. After all parties and staff have had the opportunity to object and cross-examine, the exhibit may be moved into the record. All other exhibits may be similarly identified and entered into the record at the appropriate time during the hearing.

Witnesses are reminded that, on cross-examination, responses to questions calling for a simple yes or no answer shall be so answered first, after which the witness may explain his or her answer.

V. ORDER OF WITNESSES

<u>Witness</u>	<u>Appearing For</u>	<u>Issues #</u>
<u>Direct</u>		
William Randall Mann	Utility	1, 2, 3, 4, 5
Robert Scheffel Wright	SFCC	1, 2, 3, 4, 5
Paul H. Freeman	SFCC	1, 2, 3, 4, 5, 6
David Howard Goldberg	SFCC	1, 2, 3
Robert J. Chapnick	SFCC	1
James Moore	SFCC	1, 2, 3

ORDER OF WITNESSES cont.

<u>Witness</u>	<u>Appearing For</u>	<u>Issues #</u>
<u>Rebuttal</u>		
Robert C. Nixon	Utility	1, 2, 3, 4, 5
William Randall Mann	Utility	1, 2, 3, 4, 5
Gresham R. Stoneburner	Utility	3
James W. Moore	Utility	1, 2, 3, 4, 5
Barry Asmus	SFCC	1, 2, 3, 4, 5, 6

Surrebuttal

Robert C. Nixon	Utility	1, 2, 3, 4, 5, 6
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Neither staff nor FWWA intend to call any witnesses.

VI. BASIC POSITIONS

UTILITY: The basic position of Gulf is that it has complied with the Commission's policy regarding gross-up and is entitled to continue the use of full gross-up.

SFCC: Gulf Utility Company's request to subject CIAC to full gross-up should be denied. Full gross-up subjects the contributor of the CIAC to a "tax on a tax," guaranteeing that the maximum tax possible is paid to the federal government at the expense of the contributor. As a matter of policy, the Commission should not approve any gross-up unless (1) it is absolutely necessary to the financial integrity of the utility, and (2) it is necessary to keep the utility whole with respect to the position it would have experienced without receiving the contribution. The burden must be on the utility to prove the necessity of any gross-up. In this particular case, Gulf cannot demonstrate the necessity of the full gross-up because several viable alternative exist that would

allow SFCC to avoid "tax on tax" effects while not threatening the financial integrity of the utility.

Since the utility has collected CIAC tax impact monies in excess of those paid, and has a continuing depreciation benefit, alternatives that might otherwise have some impact on the utility's general body of ratepayers can be implemented without any adverse effect to either the utility or its general body of ratepayers.

FWWA: The basic position of the FWWA is that the Commission has decided in Order No. 23541, and other Orders issued in Docket No. 860184-PU, that private water and sewer utilities may petition the Commission for authority to gross-up CIAC for the related tax impact and may choose the method for applying such gross-up authority. That Order and the Commission's existing policy which had been developed over the past seven years do not favor one method of gross-up over another, but leave that choice to the utility. The utility is required in its request for initial gross-up authority to state the reason for the method selected. The issue of the gross-up methods to be allowed and the question of the utility's ability to select such methods was fully litigated in Docket No. 860184-PU to which both the FWWA and SFCC were parties. The SFCC should not be allowed to re-litigate the generic issue before this Commission and in one utility's specific proceeding.

STAFF: Staff's positions are preliminary and based on materials filed by the parties and on discovery. The preliminary positions are offered to assist the parties in preparing for the hearing. Staff's final positions will be based upon all the evidence in the record and may differ from the preliminary positions. The information gathered through discovery and prefiled testimony indicates, at this point, that the utility may be entitled to continue full gross-up of CIAC.

VII. ISSUES AND POSITIONS

ISSUE 1: Should Gulf Utility Company be granted authority to continue gross-up of CIAC?

POSITIONS

UTILITY: Yes. Gulf Utility Company has met the criteria of Order No. 23541. (Mann, Nixon, Moore)

SFCC: No. Following the Commission's reasoning and holdings in Order No. 23541, the Commission's policy on CIAC tax gross-up should be:

(1) to "encourage the water and wastewater industry to continue to search for viable methods" of avoiding or minimizing taxes on CIAC;

(2) to permit utilities to collect a CIAC tax gross-up pursuant to Commission approval and pursuant to the utility's affirmative demonstration that it has an actual tax liability and that sources of funds to satisfy the tax liability are not otherwise available at reasonable cost; and

(3) to keep the utility whole with respect to costs actually caused by capital contributions while avoiding cross-subsidization of the utility's shareholders or ratepayers by contributors of CIAC. (Wright, Freeman, Goldberg, Chapnick, Moore, Asmus)

FWWA: Yes, to the extent the utility has complied with the requirements of Order No. 23541, it should be granted continued gross-up authority.

STAFF: No position pending development of the record.

ISSUE 2: If Gulf Utility Company is granted authority to gross-up CIAC, what method of gross-up should be used?

POSITIONS

UTILITY: The full gross-up method. Gulf has met the criteria of Order No. 23541 for the full gross-up. (Mann, Nixon, Moore)

SFCC: Gulf should not be allowed to generally apply the full gross-up method as it has requested. If any gross-up is granted, it should be the net present value method. (Wright, Freeman, Goldberg, Moore, Asmus)

FWWA: The gross-up method proposed by Gulf Utility Company in accordance with Order No. 23541.

STAFF: No position pending development of the record.

ISSUE 3: Should Gulf be allowed to apply the full gross-up specifically to SFCC as it has proposed?

POSITIONS

UTILITY: Yes. SFCC should not be allowed special or discriminatory treatment. Gulf has met the criteria of Order No. 23541 for the full gross-up. (Mann, Nixon, Stoneburner, Moore)

SFCC: No. SFCC has proposed several workable alternatives to full gross-up, each of which Gulf has rejected because it demands full gross-up. These include, for example:

- a. the net present value method;
- b. a method under which SFCC would loan the utility sufficient funds to pay any CIAC tax impact occasioned by SFCC's contributions;
- c. the guaranteed revenue charge method
- d. a method under which Gulf would return to SFCC the depreciation benefits created as the contributed property is depreciated for tax purposes; and
- e. a bulk services agreement method under which SFCC would form or become a homeowner association utility or a community development district utility.

Because at least one of these alternatives is workable, Gulf's petition should be denied, and the Commission should order Gulf to implement one of the above methods. (Wright, Freeman, Goldberg, Moore, Asmus)

FWWA: The gross-up method selected by Gulf and approved by the Commission should be applied across the board consistently to all customers or potential customers of Gulf.

STAFF: No position at this time.

ISSUE 4: Does Gulf's Industrial Development Revenue Bond (IDRB) require the Commission to approve the full gross-up method?

POSITIONS

UTILITY: No. The utility is required to pay all governmental charges lawfully assessed, however, the utility is also required to apply for those rates to which it is lawfully entitled so that certain financial ratios can be maintained. The full gross-up method is needed by Gulf to maintain its financial integrity and to meet existing and future debt obligations incurred to provide for system maintenance and growth. (Moore, Mann, Nixon)

SFCC: No, nor could it do so. Gulf has cited the IDRB, and certain promises and covenants it made to obtain it, as the reason it cannot voluntarily use certain alternatives to the full gross-up method, e.g., the NPV method and the contributor loan method. However, by the terms of the IDRB agreements, Gulf must comply with any lawful order of the Commission without breaching the IDRB agreements. More importantly, Gulf may not tie the hands of the Commission when it secures financing of its expansion plans. Thus, for the purposes of this proceeding, the IDRB is irrelevant.

Nothing in the IDRB limits or otherwise affects the Commission's purpose in this docket, which is to ensure that Gulf Utility Company implements a method or methods that will: (1) result in either no tax liability or minimum tax liability, and (2) keep the utility whole

while avoiding cross-subsidization of the utility shareholders or ratepayers by contributors of CIAC. (Wright, Freeman, Asmus)

FWWA: No position.

STAFF: In principle, no. The IDRB is but one consideration among many. The Commission should consider whether the financial integrity of the utility will be jeopardized by forcing the utility to use one of SFCC's offered methods.

ISSUE 5: What should be the treatment of depreciation from contributed property in determining whether to allow Gulf to gross-up?

POSITIONS

UTILITY: Agree with Order No. 23541 as stated on page 21:

Since the practical considerations militate against passing the tax depreciation benefits back to developers and, since we believe that developers generally recover their costs, we find that the tax depreciation benefits should be passed back to the utility ratepayer. However, we note that, to the extent that utilities use the NPV method of grossing-up, they are passing the tax depreciation benefits of the gross-up back to developers, since the effect of that method is to offset the current taxes by the net present value of the future depreciation. (Moore, Mann, Nixon)

SFCC: The person or persons who contributed the property and who paid the tax on it should receive the benefit of the depreciation. To allow the depreciation benefits created by the contribution to inure the benefit of Gulf's shareholders would create a windfall to those shareholders that is not earned by any productive effort or entrepreneurship on their part; to allow these benefits to accrue to the general body of ratepayers is to cross-subsidize these entities at the expense of the contributors. Either outcome is unjust, unreasonable,

and unfair. In SFCC's case, both the contributions and gross-up amounts collected subject to refund have been very great, so no legitimate argument can be made that the administrative effort required to administer such a depreciation flow-back system is unreasonable relative to the amounts involved. Moreover, if the amounts involved were small enough that the effort required to administer a depreciation flow-back system was unreasonable, then serious questions regarding the necessity of collecting such amounts would be raised as well. (Wright, Freeman, Asmus)

FWWA: As fully developed in the record of Docket No. 860184-PU, and as specifically found by the Commission in Order No. 23541 at page 21, the depreciation benefits on contributed property should accrue to the general body of ratepayers. Such benefit will accrue to those ratepayers in all rate proceedings or will eliminate the need for such proceedings. Order No. 23541 specifically dealt with the issue of depreciation on CIAC, but in no way suggested that the existence of such tax depreciation rights could impact the appropriateness of gross-up itself. The factors to be considered in granting gross-up authority have been litigated and decided in Docket No. 860184-PU. This issue should not be re-litigated in this proceeding, and SFCC should be collaterally estopped from doing so.

STAFF: No position at this time.

ISSUE 6: Has Gulf complied with its tariff provisions relating to the collection, escrow, and refunding of CIAC tax impact monies?

POSITIONS

UTILITY: Yes. (Nixon)

SFCC: No. (Freeman, Asmus)

FWWA: No position.

STAFF: No position pending development of the record.

VIII. EXHIBIT LIST

<u>Witness</u>	<u>Proffered By</u>	<u>I.D. No.</u>	<u>Description</u>
<u>Direct</u>			
William Randall Mann	Utility	WRM-1	Projected Revenues.
	Utility	WRM-2	Gulf Utility Company, CIAC Summary, 1987-1991.
	Utility	WRM-3	Letter addressed to Mr. James W. Moore, dated April 28, 1992 from W. Rob Hough, Jr.
Paul H. Freeman	SFCC	PHF-1	Letter from Mr. Stephen Scott of the Estero United Methodist Church to Mr. Paul H. Freeman.
	SFCC	PHF-2	PSC Document No. 09458, a letter from Mr. Paul H. Freeman filed with the Commission on August 20, 1992, including supporting attachments.

<u>Witness</u>	<u>Proffered By</u>	<u>I.D. No.</u>	<u>Description</u>
<u>Rebuttal</u>			
William Randall Mann	Utility	WRM-1	Gulf Utility Company Actual vs. IDR B Pro Forma.
	Utility	WRM-2	U t i l i t y Financing Method.
	Utility	WRM-3	Interest Free Loan Method.
William Randall Mann	Utility	WRM-4	Net Present Value Gross-up Method.
	Utility	WRM-5	Summary of Methods.
James W. Moore	Utility	JWM-1	Order No. PSC-92-0742-FOF-WS.
	Utility	JWM-2	Utility Service Availability Charge Comparison.
	Utility	JWM-3	Lee County - Residential Building Activity.
	Utility	JWM-4	Letter dated March 23, 1993 to Mr. James W. Moore from Mr. W. Rob Hough, Jr.

<u>Witness</u>	<u>Proffered By</u>	<u>I.D. No.</u>	<u>Description</u>
<u>Rebuttal cont.</u>			
Robert C. Nixon	Utility	RCN-1	Gulf Utility Company financial analysis based on audited financial statements for the years ended December 31, 1991 and 1990.
Robert C. Nixon	Utility	RCN-2	Deferred Tax Liability - Depreciation Under FASB 109 as of December 31, 1991.

Staff will not sponsor any exhibits, but intends to ask that the Commission take official notice of several Commission Orders, including Orders Nos. 23541, issued October 1, 1990, and 16971 issued December 12, 1986. FWWA does not intend to sponsor any exhibits. The parties and staff reserve the right to use exhibits for the purpose of cross-examination. SFCC intends to use the following exhibits on cross-examination:

- (1) Depreciation Schedule for Post-1987 CIAC Contributions and Tax Effects on Gulf Utility Company.
- (2) Pro Forma Re: Interest Free Loan.
- (3) Schedule of CIAC Tax Collected vs. Tax Paid, Gulf Utility Company.

IX. RULINGS


(1) SFCC's March 29 motion to correct the testimony of Barry K. Asmus is granted. As requested at the Prehearing Conference, Gulf shall have until April 26, 1993, to file surrebuttal to Mr. Asmus' rebuttal.

(2) The FWWA's March 30 petition to intervene is granted without opposition.

It is therefore,

ORDERED by Commissioner Thomas M. Beard, as Prehearing Officer, that this Prehearing Order shall govern the conduct of these proceedings as set forth above unless modified by the Commission.

By ORDER of Commissioner Thomas M. Beard, as Prehearing Officer, this 22nd day of April, 1993.


THOMAS M. BEARD, Commissioner and
Prehearing Officer

(S E A L)

LAJ/MJF

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.

Any party adversely affected by this order, which is preliminary, procedural or intermediate in nature, may request: 1) reconsideration within 10 days pursuant to Rule 25-22.038(2), Florida Administrative Code, if issued by a Prehearing Officer; 2) reconsideration within 15 days pursuant to Rule 25-22.060, Florida Administrative Code, if issued by the Commission; or 3) judicial review by the Florida Supreme Court, in the case of an electric, gas or telephone utility, or the First District Court of Appeal, in the case of a water or wastewater utility. A motion for reconsideration shall be filed with the Director, Division of

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Records and Reporting, in the form prescribed by Rule 25-22.060, Florida Administrative Code. Judicial review of a preliminary, procedural or intermediate ruling or order is available if review of the final action will not provide an adequate remedy. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.