

FLORIDA PUBLIC SERVICE COMMISSION
Capital Circle Office Center • 2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

MEMORANDUM

MAY 7, 1997

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

FROM: DIVISION OF WATER & WASTEWATER (MCCASKILL) *MC*
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (CAUSSEAU) *CA*
DIVISION OF LEGAL SERVICES (JAEGER) *JA*

RE: DOCKET NO. 961077-SU - DISPOSITION OF GROSS-UP FUNDS
COLLECTED BY EAGLE RIDGE UTILITIES, INC. *ER*

COUNTY: LEE

AGENDA: MAY 19, 1997 - REGULAR AGENDA - PROPOSED AGENCY ACTION -
INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: I:\PSC\WAW\WP\961077⁷.RCM

CASE BACKGROUND

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.

Order No. 16971 and Order No. 23541, issued December 18, 1986 and October 1, 1990, respectively, 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 also required that all gross-up collections 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. Eagle Ridge Utilities,

DOCUMENT NUMBER-DATE

04498 MAY-75

FPSC-RECORDS/REPORTING

DOCKET NO. 961077-SU
MAY 7, 1997

Inc. (Eagle Ridge or Utility), filed for authority to continue to gross-up on December 11, 1990. By Order No. 25436, issued December 4, 1991, Eagle Ridge was granted authority to continue to gross-up CIAC using the full gross-up formula.

On September 9, 1992, this Commission issued Proposed Agency Action (PAA) Order No. PSC-92-0961-FOF-WS, which clarified the provision of Orders Nos. 16971 and 23541 for the calculation of refunds of gross-up of CIAC. On September 14, 1992, PAA Order No. PSC-92-0961A-FOF-WS was issued. This order 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 PAA 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, on August 1, 1996, the Small Business Job Protection Act of 1996 (The Act) passed Congress and was signed into law by the President 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. Since there was no longer a need to review the Commission's policy on the gross-up of CIAC, on October 8, 1996, Order No. PSC-96-1253-FOF-WS was issued, closing Docket No. 960397-WS. However, as established in PAA Order No. PSC-96-0686-FOF-WS, all pending CIAC gross-up refund cases are being processed pursuant to Orders Nos. 16971 and 23541.

On October 17, 1996, staff filed its recommendation for the October 29, 1996, agenda conference regarding refunds of excess gross-up collections for 1993 and 1994. On November 20, 1996, PAA Order No. PSC-96-1394-FOF-SU was issued, requiring a refund of

DOCKET NO. 961077-SU
MAY 7, 1997

\$14,589 for 1993 and \$5,655 for 1994. On December 11, 1996, Eagle Ridge filed a timely protest of the referenced order, and the matter was set for a July 10 - 11, 1997, hearing. However, on April 23, 1997, Eagle Ridge along with three other utilities, submitted a settlement proposal to avoid the time and expense of further litigation in this docket. To give the Commission panel assigned to this docket time to consider this settlement offer, the July 10 - 11, 1997, hearing was cancelled. The purpose of this recommendation is to address this settlement offer and the disposition of gross-up funds collected by the utility for 1993 and 1994. Separate recommendations have been filed for each of the three other utilities.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission accept Eagle Ridge Utilities, Inc.'s settlement proposal of April 23, 1997 for the disposition of gross-up funds collected?

RECOMMENDATION: Yes, the Commission should accept Eagle Ridge's settlement proposal of April 23, 1997 for the disposition of gross-up funds collected. Based on acceptance of the settlement proposal, staff recommends that \$3,851 and \$2,517 of accounting and legal fees for 1993 and 1994, respectively, be offset against the calculated refunds for those years. As a result, staff recommends that the utility be ordered to refund \$10,738 for 1993 and \$3,138 for 1994, plus accrued interest through the date of the refund, for gross-up collected in excess of the above-the-line tax liability resulting from the collection of taxable CIAC. According to Orders Nos. 16971 and 23541, all amounts should be refunded on a pro rata basis to those persons who contributed the taxes. The refunds should be completed within 6 months of the effective date of the order. Within 30 days from the date of the refund, the utility should submit copies of cancelled checks, credits applied to the monthly bills or other evidence that verifies that the utility has made the refunds. Within 30 days from the date of the refund, the utility should also provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds. (MCCASKILL)

STAFF ANALYSIS: In compliance with Order No. 16971, Eagle Ridge filed its annual CIAC report regarding its collection of gross-up for 1993 and 1994. As previously stated, on October 17, 1996, staff filed its recommendation for the October 29, 1996, agenda conference. On November 20, 1996, PAA Order No. PSC-96-1394-FOF-SU was issued requiring refunds of \$14,589 for 1993 and \$5,655 for 1994. On December 11, 1996, Eagle Ridge filed a timely protest of the Order, and the matter was set for hearing.

The utility's protest concerned the following two issues: (1) The Commission did not allow the utility to reduce the amount of the contributor's refund by the amount of legal and accounting costs associated with the preparation and filing of the utility's gross-up reports (these costs totalled \$7,702 for 1993 and \$5,033 for 1994), and (2) in calculating the refund for 1993 and 1994, the Commission classified management fees totalling \$56,594 and \$50,000, respectively, as above-the-line expense. For 1993, the utility classified \$30,135 above-the-line and \$26,459 below-the-line. For 1994, the utility classified \$26,214 above-the-line, and \$23,786 below-the-line. However, the Commission found in PAA Order

DOCKET NO. 961077-SU
MAY 7, 1997

No. PSC-96-1394-FOF-SU, that the legal and accounting costs associated with the preparation and filing of the utility's gross-up reports should not be offset against the contributor's refund. Further, it found that management fees totalling \$56,594 for 1993 and \$50,000 for 1994 should appropriately be classified above-the-line.

On March 7, 1997, a meeting was held at the request of the utility to discuss the utility's settlement proposal to offset the legal and accounting fees incurred in preparing the CIAC gross-up reports with the contributors refund amount. On April 23, 1997, the utility submitted its proposed offer of settlement (See Attachment A), whereby it proposed that 50% of the legitimate legal and accounting fees incurred in any one year for the CIAC gross-up be offset against any refund calculated to be due in that same year. As a prerequisite to the offer, the utility agreed to waive several other mutual issues as to the PAA calculation of refunds in exchange for acceptance of its proposed recognition of the offset of 50% of net legal and accounting expenses with the calculated refund amount. The amount of the legal and accounting expense offset was limited to the amount of refund for the period.

In PAA Order No. PSC-96-1394-FOF-SU, the refund for 1993 was calculated to be \$14,589. The net amount of legitimate legal and accounting expenses directly associated with preparing the required reports and calculating the tax effect was determined to be \$7,702 for 1993. Fifty percent (50%) of this amount is \$3,851. When this amount is offset against the \$14,589, the refund is calculated to be \$10,738. In addition, the refund for 1994 was calculated to be \$5,655. The net amount of legal and accounting expense was determined to be \$5,033. Fifty percent (50%) of this amount is \$2,517. When this amount is offset against the \$5,655, the refund for 1994 is calculated to be \$3,138.

Staff notes that the Commission has considered on several occasions, the question of whether an offset should be allowed pursuant to the orders governing CIAC gross-up. In its last vote on that issue, the Commission voted 3 - 2 that no offset was contemplated. However, staff recognizes that acceptance of the settlement proposal would avoid the substantial cost associated with a hearing, which may in fact exceed the amount of the legal and accounting cost to be recovered. Staff further notes that the actual costs associated with making the refunds have not been included in these calculations, and will be absorbed by the utility. Finally, staff believes the utility's settlement proposal is a reasonable "middle ground" that effectively gives the utility an offset substantially less than that which it had originally proposed, both for this adjustment and other adjustments that the

DOCKET NO. 961077-SU
MAY 7, 1997

utility has agreed to drop for the purposes of attempting to negotiate a settlement. Staff, therefore, recommends that while not adopting the utility's position, the Commission should accept Eagle Ridge's settlement proposal.

If the Commission approves the settlement, the refunds should be completed within 6 months of the effective date of the order. Within 30 days from the date of the refund, the utility should submit copies of cancelled checks, credits applied to the monthly bills or other evidence that verifies that the utility has made the refunds. Within 30 days from the date of the refund, the utility should also provide a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds.

DOCKET NO. 961077-SU
MAY 7, 1997

ISSUE 2: Should the docket be closed?

RECOMMENDATION: No. Upon expiration of the protest period, this docket should remain open pending staff's verification of refunds. Staff should be given administrative authority to close the docket upon verification that the refunds have been completed. (JAEGER)

STAFF ANALYSIS: Upon expiration of the protest period, if a timely protest is not received from a substantially affected person, this docket should remain open pending completion and verification of the refunds. Staff recommends that administrative authority should be granted to staff to close the docket upon verification that the refunds have been made.

ROSE, SUNDBSTROM & BENTLEY, LLP

2548 BLAIRSTONE PINES DRIVE
TALLAHASSEE, FLORIDA 32301

(904) 877-6655

CHRIS H. BENTLEY, P.A.
F. MARSHALL DETERDING
BRIAN L. DOSTER
MARTIN S. FRIEDMAN, P.A.
JOHN R. JENKINS, P.A.
STEVEN T. MINDLIN, P.A.
ROBERT M. C. ROSE
DAREN L. SHIPPY
WILLIAM E. SUNDBSTROM, P.A.
DIANE D. TREMPER, P.A.
JOHN L. WHARTONMAILING ADDRESS
POST OFFICE BOX 1587
TALLAHASSEE, FLORIDA 32302-1587
TELECOPIER (904) 898-4029

April 23, 1997

VIA HAND DELIVERY**RECEIVED**
APR 25 1997Florida Public Service Commission
Division of Water and WastewaterRalph Jaeger, Esquire
Division of Legal Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399Re: Gross-up Refund Protest
Hydratech Utilities, Inc.; Dkt.#961076-WS; File No. 25021.07
Eagle Ridge Utilities, Inc.; Dkt.#961077-SU; File No. 20082.03
Forest Utilities, Inc.; Dkt.#961237-SU; File No. 25052.03
Hudson Utilities, Inc. dba Hudson Bay Company; Dkt.#961152-SU

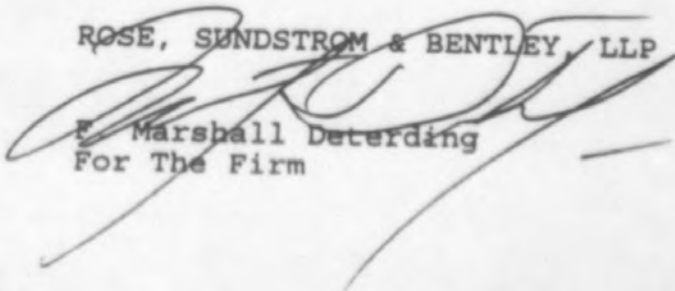
Dear Ralph:

As a follow-up to our discussion by phone today, I am writing this letter to propose settlement in accordance with the terms of the attached schedule. Acceptance of the "staff proposed" refunds in the attached schedule will fully settle the dispute concerning the PAA orders in each of the above referenced cases. I have the authorization from each of my clients and from Kenneth Hoffman, Esquire, counsel to Hudson Utilities, to make this offer in full settlement of those protests.

If you have any further questions in this regard or need anything further from me in order to move forward with the settlement proposal, please let me know.

Sincerely,

ROSE, SUNDBSTROM & BENTLEY, LLP


F. Marshall Deterding
For The FirmFMD/lts
Enclosurecc: Ms. Blanca Bayo
Connie McCaskill, CPA
Mr. Greg Shafer
Robert C. Nixon, CPA
Kenneth Hoffman, Esquire

STAFF PROPOSED REFUNDS

EAGLE RIDGE UTILITIES	1990	1991	1992	1993	1994	1995	TOTAL	DIFFERENCE
STAFF PROPOSED								
ORDER. OR RECAL. REFUND				14,589	5,655		20,244	
LEGAL & ACCTG. OFFSET				(3,851)	(2,517)		(6,368)	
PROPOSED REFUND				<u>10,738</u>	<u>3,138</u>		<u>13,876</u>	

UTILITY PROPOSED								
ORDER. OR RECAL. REFUND				14,589	5,655		20,244	
LEGAL & ACCTG. OFFSET				(3,851)	(2,517)		(6,368)	
PROPOSED REFUND				<u>10,738</u>	<u>3,138</u>		<u>13,876</u>	<u>0</u>

FOREST UTILITIES, INC.
STAFF PROPOSED

ORDERED REFUND	3,372	2,183	549	16,946	3,287	0	26,337	
LEGAL & ACCTG. OFFSET	(1,124)	(1,259)	(549)	(2,256)	(1,346)	0	(6,534)	
PROPOSED REFUND	<u>2,248</u>	<u>924</u>	<u>0</u>	<u>14,690</u>	<u>1,941</u>	<u>0</u>	<u>19,803</u>	

UTILITY PROPOSED								
ORDERED REFUND	3,372	2,183	549	16,946	3,287	0	26,337	
LEGAL & ACCTG. OFFSET	(1,124)	(1,259)	(1,035)	(2,256)	(1,346)	(1,284)	(8,304)	
PROPOSED REFUND	<u>2,248</u>	<u>924</u>	<u>(486)</u>	<u>14,690</u>	<u>1,941</u>	<u>(1,284)</u>	<u>18,033</u>	<u>1,770</u>

HUDSON UTILITIES, INC.
STAFF PROPOSED

ORDERED REFUND				1,817	47,052		48,869	
LEGAL & ACCTG. OFFSET				(1,817)	(2,132)		(3,949)	
PROPOSED REFUND				<u>0</u>	<u>44,920</u>		<u>44,920</u>	

UTILITY PROPOSED								
ORDERED REFUND				1,817	47,052		48,869	
LEGAL & ACCTG. OFFSET				(3,186)	(2,132)		(5,318)	
PROPOSED REFUND				<u>(1,369)</u>	<u>44,920</u>		<u>43,551</u>	

WINDY HILLS UTILITIES, INC.
STAFF PROPOSED

ORDERED REFUND				340	21,500		21,840	
LEGAL & ACCTG. OFFSET				(340)	(4,966)		(5,306)	
PROPOSED REFUND				<u>0</u>	<u>16,534</u>		<u>16,534</u>	

UTILITY PROPOSED								
ORDERED REFUND				340	21,500		21,840	
LEGAL & ACCTG. OFFSET				(3,603)	(4,966)		(8,569)	
PROPOSED REFUND				<u>(3,263)</u>	<u>16,534</u>		<u>13,271</u>	<u>3,263</u>