

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Disposition of
contribution of contribution-in-
aid-of-construction gross-up
funds collected by Lake Hills
Utilities, Inc. In Lake County.

DOCKET NO. 980077-WU
ORDER NO. PSC-98-0317-FOF-WU
ISSUED: February 23, 1998

The following Commissioners participated in the disposition of
this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.

NOTICE OF PROPOSED AGENCY ACTION ORDER REQUIRING REFUNDS FOR THE
YEARS 1989 THROUGH 1994

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service
Commission that the action discussed herein is preliminary in
nature and will become final unless a person whose interests are
substantially affected files a petition for a formal proceeding,
pursuant to Rule 25-22.029, Florida Administrative Code.

BACKGROUND

Lake Hills Utilities, Inc. (Lake Hills or utility), is a Class
C water utility providing service to the public in Lake County. As
of December 31, 1995, the utility served 480 water customers. The
utility had gross operating revenues of \$53,850 for the water
system. The utility reported a net operating loss of \$95,567.

As a result of the repeal of Section 118(b) of the Internal
Revenue Code, contributions-in-aid-of-construction (CIAC) became
gross income and were depreciable for federal tax purposes. In
Order No. 16971, issued December 18, 1986, we 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.

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FPSC-RECORDS/REPORTING

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Orders Nos. 16971 and 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 require 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, we 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. On September 12, 1991, pursuant to Order No. 23541, Lake Hills filed for authority to gross-up CIAC. The information as filed met the filing requirements of Order No. 23541. Order No. PSC-92-0253-FOF-WU, issued April 27, 1992, granted Lake Hills Utilities authority to gross-up.

On September 9, 1992, we 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, we issued PAA Order No. PSC-92-0961A-FOF-WS. This order included Attachment A which reflected 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 our 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, we directed our staff to review the proposals and comments offered by the workshop participants and make a recommendation concerning whether our policy regarding the collection and refund of CIAC should be changed. In addition, we directed our staff to consider ways to simplify the process and determine whether there were viable alternatives to the gross-up. Pending this review, we directed our staff to continue processing CIAC gross-up and refund cases pursuant to Orders Nos. 16971 and 23541.

However, on August 1, 1996, Congress passed the Small Business Job Protection Act of 1996 (the Act), and the President signed the law 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, we issued Order No. PSC-96-1180-FOF-WS revoking the authority of utilities to collect gross-up of CIAC and canceling 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 our policy on the gross-up of CIAC, we closed Docket No. 960397-WS by Order No. PSC-96-1253-FOF-WS, issued on October 8, 1996. 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 September 29, 1997, Lake Hills submitted its 1995 CIAC Gross-up Report. In that report, Lake Hills Utilities noted that no CIAC was collected in 1995 and therefore, no refund is due in 1995. The report indicated that all operating assets of the utility had been sold on May 4, 1995. In Docket No. 950421-WU, Lake Hills Utilities, Inc. was transferred to the City of Clermont, and the certificate was canceled.

This Order addresses the amount of CIAC gross-up funds that should be refunded for 1989 through 1995.

REFUND REQUIREMENT

In compliance with Orders Nos. 16971 and 23541, Lake Hills filed its 1989 through 1995 annual CIAC report regarding its collection of gross-up for the years. By letter dated December 14, 1995, the utility responded to our staff's preliminary refund calculation amounts. Our staff and the utility have submitted and revised the preliminary refund calculation several times.

We have 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. Our calculations,

taken from the information provided by the utility in its gross-up report and tax return are reflected on the schedule attached to this Order. A summary of the 1989 through 1995 refund calculation follows.

1989

The utility proposes a refund of \$5,818 for 1989 excess gross-up collections. We calculate a refund of \$5,814 for 1989.

Based upon our review of the utility's 1989 filing, the utility incurred an above-the-line loss of \$8,788 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that the above-the-line loss of \$8,788 be netted with the taxable CIAC collected. The CIAC report indicates that the utility collected \$85,250 of taxable CIAC, with \$1,321 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$75,141. Using the 37.63 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$28,276. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$45,336. The utility collected \$51,150 in gross-up taxes. Based upon the foregoing, the utility collected \$5,814 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1989, which must also be refunded through the date of the refund.

1990

The utility proposes a refund of \$23,035 for 1990 excess gross-up collections. We calculate a refund of \$23,032 for 1989.

Based upon our review of the utility's 1990 filing, the utility incurred an above-the-line loss of \$35,865 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that the above-the-line loss of \$35,865 be netted with the taxable CIAC collected. The CIAC report indicates that the utility collected \$231,744 of taxable CIAC, with \$3,592 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is

calculated to be \$192,287. Using the 37.63 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$72,358. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$116,014. The utility collected \$139,046 in gross-up taxes. Based upon the foregoing, the utility collected \$23,032 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1990, which must also be refunded through the date of the refund.

1991

The utility proposes a refund of \$3,481 for 1991 excess gross-up collections. We calculate a refund of \$3,479 for 1991.

Based upon our review of the utility's 1991 filing, the utility incurred an above-the-line loss of \$4,623 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that the above-the-line loss of \$4,623 be netted with the taxable CIAC collected. The CIAC report indicates that the utility collected \$114,501 of taxable CIAC, with \$1,775 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$108,103. Using the 37.63 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$40,679. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$65,222. The utility collected \$68,701 in gross-up taxes. Based upon the foregoing, the utility collected \$3,479 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1991, which must also be refunded through the date of the refund.

1992

The utility proposes a refund of \$18,484 for 1992 excess gross-up collections. We calculate a refund of \$18,483 for 1992.

Based upon our review of the utility's 1992 filing, the utility was in a taxable position with \$7,760 in above-the-line

income prior to the inclusion of taxable CIAC in income. The utility included \$37,677 net operating loss carry backs from 1995. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that losses be offset against CIAC income. Therefore, the \$37,677 net operating loss carry backs must be netted with the above-the-line income of \$7,760 and the taxable CIAC collected. The CIAC report indicates that the utility collected \$73,429 of taxable CIAC, with \$1,138 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$42,374. Using the 37.63 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$15,945. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$25,565. The utility collected \$44,048 in gross-up taxes. Based upon the foregoing, the utility collected \$18,483 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1992, which must also be refunded through the date of the refund.

1993

The utility proposes a refund of \$15,689 for 1993 excess gross-up collections. We agree with the utility's proposed refund amount.

Based upon our review of the utility's 1993 filing, the utility incurred an above-the-line loss of \$24,118 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that the above-the-line loss of \$24,118 be netted with the taxable CIAC collected. The CIAC report indicates that the utility collected \$170,644 of taxable CIAC, with \$2,830 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$143,696. Using the 37.63 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$54,073. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$86,697. The utility collected \$102,386 in gross-up taxes. Based upon the foregoing, the utility collected \$15,689 more in gross-up than was required to pay the taxes. This amount

does not include the accrued interest as of December 31, 1993, which must also be refunded through the date of the refund.

1994

The utility proposes a refund of \$53,385 for 1994 excess gross-up collections. We calculate a refund of \$53,384 for 1994.

Based upon our review of the utility's 1994 filing, the utility incurred an above-the-line loss of \$51,515 prior to the inclusion of taxable CIAC in income. As a result, all of the CIAC collected would not be taxed. Order No. 23541 requires that the above-the-line loss of \$51,515 be netted with the taxable CIAC collected. The CIAC report indicates that the utility collected \$115,200 of taxable CIAC, with \$2,131 being deducted for the first year's depreciation. As a result, the amount of taxable CIAC is calculated to be \$61,554. Using the 20.36 percent combined federal and state tax rate as provided in the CIAC report, we calculate the tax effect to be \$12,532. When this amount is multiplied by the expansion factor for gross-up taxes, the amount of gross-up required to pay the tax effect on the CIAC is calculated to be \$15,736. The utility collected \$69,120 in gross-up taxes. Based upon the foregoing, the utility collected \$53,384 more in gross-up than was required to pay the taxes. This amount does not include the accrued interest as of December 31, 1994, which must also be refunded through the date of the refund.

1995

The utility proposes no refund is appropriate for 1995, because the utility did not collect CIAC in 1995. The utility was later sold in 1995. We agree that no refund is appropriate.

In accordance with Orders Nos. 16971 and 23541, all refunds shall be made on a pro rata basis to those persons who contributed the taxes. The refunds shall be completed within six months. The utility shall submit copies of canceled checks, credits applied to monthly bills or other evidence which verifies that the refunds have been made, within 30 days from the date of refund. Within 30 days from the date of refund, the utility also shall file a list of unclaimed refunds detailing contributor and amount, and an explanation of the efforts made to make the refunds.

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CLOSING OF DOCKET

Upon expiration of the protest period, if a timely protest is not filed by a substantially affected person, this docket shall remain open pending completion and verification of the refunds. The docket may be administratively closed upon our staff's verification that the refunds have been made.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the settlement offer of Lake Hills Utilities, Inc., shall be accepted. It is further

ORDERED that no refunds are required for 1995. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective unless an appropriate petition, in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" attached hereto. It is further

ORDERED that the schedule attached to this Order is incorporated into and made a part of this Order. It is further

ORDERED that pursuant to the settlement offer, Lake Hills Utilities, Inc., shall refund excess gross-up of contributions-in-aid-of-construction in the amount of \$5,814 for 1989, \$23,032 for 1990, \$3,479 for 1991, \$18,483 for 1992, \$15,689 for 1993, and \$53,384 for 1994. It is further

ORDERED that the refunds shall be carried out as set forth in the body of this Order. It is further

ORDERED that Lake Hills Utilities, Inc., shall refund accrued interest through the date of refund, for gross-up of contributions-in-aid-of-construction collected in excess of the tax liability. It is further

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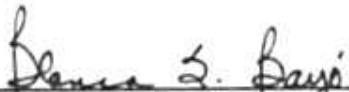
ORDERED that, pursuant to Orders Nos. 16971 and 23541, all refund amounts shall be refunded on a pro rata basis to those persons who contributed the funds. It is further

ORDERED that the refunds required herein shall be completed within six months of the effective date of this Order, and that Lake Hills Utilities, Inc., shall submit copies of canceled checks, credits applied to monthly bills or other evidence verifying that the refunds have been made within 30 days of completion of the refund. It is further

ORDERED that within 30 days of completion of the refund, Lake Hills Utilities, Inc., shall provide a list of unclaimed refunds detailing the contributor and the amount, and an explanation of the efforts made to make the refunds. It is further

ORDERED that the docket shall be administratively closed upon expiration of the protest period, if no timely protest is filed, and upon our staff's verification that the refunds have been made.

By ORDER of the Florida Public Service Commission this 23rd day of February, 1998.



BLANCA S. BAYO, Director
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), 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.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on March 16, 1998.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing

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fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

COMMISSION CALCULATED GROSS-UP REFUND

	1989	1990	1991	1992	1993	1994
1 Form 1120, Line 30 (Line 15)	\$ 126,291 \$	331,333 \$	176,804 \$	124,099 \$	246,872 \$	132,736
2 Less CIAC (Line 7)	(85,250)	(231,744)	(114,501)	(73,429)	(170,644)	(115,200)
3 Less Gross-up collected (Line 19)	(51,150)	(139,046)	(68,701)	(44,048)	(102,366)	(69,120)
4 Add First Year's Depr on CIAC (Line 8)	1,321	3,592	1,775	1,138	2,830	2,131
5 Less: NOL Carryback				(37,677)		
6 Add/Less Other Effects (Lines 20 & 21)	0	0	0	0	(590)	(2,062)
7						
8 Adjusted Income Before CIAC and Gross-up	\$ (8,786) \$	(35,865) \$	(4,623) \$	(29,917) \$	(24,118) \$	(51,515)
9						
10 Taxable CIAC (Line 7)	\$ 85,250 \$	231,744 \$	114,501 \$	73,429 \$	170,644 \$	115,200
11 Less first years depr. (Line 6)	(1,321)	(3,592)	(1,775)	(1,138)	(2,830)	(2,131)
12						
13 Adjusted Income After CIAC	\$ 75,141 \$	192,287 \$	108,103 \$	42,374 \$	143,898 \$	61,554
14	\$ 0 \$	0 \$	0 \$	0 \$	0 \$	0
15						
16 Net Taxable CIAC	\$ 75,141 \$	192,287 \$	108,103 \$	42,374 \$	143,898 \$	61,554
17 Combined Marginal state & federal tax rates	37.63%	37.63%	37.63%	37.63%	37.63%	20.36%
18						
19 Net Income tax on CIAC	\$ 28,278 \$	72,358 \$	40,679 \$	15,945 \$	54,073 \$	12,532
20 Less ITC Realized	0	0	0	0	0	0
21						
22 Net Income Tax	\$ 28,278 \$	72,358 \$	40,679 \$	15,945 \$	54,073 \$	12,532
23 Expansion Factor for gross-up taxes	1.603334937	1.603334937	1.603334937	1.603334937	1.603334937	1.25565
24						
25 Gross-up Required to pay tax effect	\$ 45,336 \$	116,014 \$	65,222 \$	25,665 \$	86,697 \$	15,736
26 Less CIAC Gross-up collected (Line 19)	(51,150)	(139,046)	(68,701)	(44,048)	(102,366)	(69,120)
27						
28 (OVER) OR UNDER COLLECTION	\$ (5,814) \$	(23,032) \$	(3,479) \$	(18,483) \$	(15,669) \$	(53,384)
29						
30						
31 TOTAL YEARLY REFUND	\$ (5,814) \$	(23,032) \$	(3,479) \$	(18,483) \$	(15,669) \$	(53,384)
32						
33						
34 PROPOSED REFUND (excluding interest)	(119,861)					
35 REFUND W/K						