



# Public Service Commission

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RECORDS AND REPORTING  
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**DATE:** NOVEMBER 4, 1999

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

**FROM:** DIVISION OF WATER AND WASTEWATER (MCCASKILL),  
DIVISION OF LEGAL SERVICES (JAEGER)

**RE:** DOCKET NO. 991576-WS - DISPOSITION OF CONTRIBUTIONS-IN-AID-OF-CONSTRUCTION GROSS-UP FUNDS COLLECTED FOR 1996 BY PARKLAND UTILITIES, INC. IN BROWARD COUNTY  
COUNTY: BROWARD

**AGENDA:** 11/16/99 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

**CRITICAL DATES:** NONE

**SPECIAL INSTRUCTIONS:** NONE

**FILE NAME AND LOCATION:** S:\PSC\WAW\WP\991576.RCM

### CASE BACKGROUND

Parkland Utilities, Inc. (Parkland or utility) is a Class B water and wastewater utility providing service to the public in Broward County. A review of the utility's 1998 annual report reflected approximately 656 water and 652 wastewater customers as of December 31, 1998. Gross annual operating revenues were \$243,225 and \$432,684 for the water and wastewater systems, respectively. The utility reported net operating income of \$3,518 for water and \$37,505 of net operating income for the wastewater system.

By Order No. 16971, issued December 18, 1986, in Docket No. 860184-PU, the Commission granted approval for water and wastewater utilities to amend their service availability policies to meet the tax impact of contributions in aid of construction (CIAC) resulting from the amendment of Section 118(b) of the Internal Revenue Code. Order No. 23541, issued October 1, 1990, in Docket No. 860184-PU,

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ordered utilities currently grossing up CIAC to file a petition for continued authority to gross-up and also ordered that no utility may gross-up CIAC without first obtaining the approval of this Commission. Orders Nos. 16971 and 23541 also prescribed the accounting and regulatory treatments for the gross-up, and required 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.

By Order No. PSC-94-0653-FOF-WS, issued May 31, 1994, in Docket No. 931141-WS, Parkland was granted interim authority to collect CIAC 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 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, by Order No. PSC-96-1180-FOF-WS, issued September 20, 1996, in Docket No. 960965-WS, the Commission revoked the authority of utilities to collect gross-up of CIAC and cancelled the respective tariffs unless, within 30 days of the issuance of the order, affected utilities requested a variance. Parkland's interim gross-up authority was revoked and the tariff was cancelled as of October 20, 1996.

The disposition of gross-up funds for 1994 and 1995 was addressed in Docket No. 931141-WS, by Order No. PSC-98-0445-AS-WS, issued March 30, 1998. The purpose of this docket is to address the disposition of gross-up funds for 1996.

**DISCUSSION OF ISSUES**

**ISSUE 1:** Should Parkland Utilities, Inc. be required to refund excess gross-up collections for 1996?

**RECOMMENDATION:** Yes. The utility over collected CIAC gross-up monies for 1996. Based on past stipulations, staff recommends that the Commission accept Parkland's request that it be allowed to recover 50% of the legal and accounting costs that relate to the preparation of the gross-up refund report for 1996. If the Commission approves staff's recommendation, the utility should refund \$2,949 plus accrued interest through the date of refund, for gross-up collected in excess of the tax liability resulting from the collection of taxable CIAC.

In accordance with Orders Nos. 16971 and 23541, all amounts should be refunded on a pro rata basis to those persons who contributed the taxes. Since there is only one developer who contributed gross-up for 1996, the refund should be completed within two months of the effective date of the Order. The utility should submit a copy of the canceled check, or other evidence which verifies that the refund has been made, within 30 days from the date of refund. If the refund is not claimed, the utility should provide a letter documenting the amount of the unclaimed refund and an explanation of the efforts made to make the refund.

**STAFF ANALYSIS:** In compliance with Orders Nos. 16971 and 23541, Parkland filed its 1996 annual CIAC report regarding its collection of gross-up. By later dated July 26, 1999, staff submitted preliminary refund calculation numbers to the utility.

Staff 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.

**ANNUAL GROSS-UP REFUND AMOUNTS**

Based upon the foregoing, staff has calculated the amount of refund which is appropriate for 1996. Our calculation, taken from the information provided by the utility in its gross-up report, is reflected on Schedule No. 1.

**1996**

The utility's 1996 CIAC report indicates that the utility was in a taxable position on an above-the-line basis prior to the inclusion of taxable CIAC and gross-up. Therefore, all of the taxable CIAC received would be taxed. The report indicates a total of \$154,375 in taxable CIAC was received, with \$491 being deducted for the first year's depreciation, resulting in net taxable CIAC of \$153,884. Staff used the 37.63% combined marginal federal and state tax rate as provided in the 1996 CIAC Report to calculate the tax effect. The reported 37.63% combined marginal federal and state tax rate applied to the net \$153,884 results in the income tax effect of \$57,907. 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 \$92,845. The utility collected \$103,201 of gross-up monies; therefore, the utility overcollected CIAC gross-up by \$10,358.

A portion of the CIAC collected during 1996 was contributed property. It appears that the value of the contributed property actually received by the utility was less than the value initially estimated. The developer who contributed the property paid the gross-up based on the estimated value. Staff has determined that the developer paid \$2,949 of gross-up in excess of the amount that should have been paid based on the actual value of the contributed property. This amount is included in the \$10,358 calculated by staff as the overcollected gross-up amount.

Consistent with prior gross-up dockets, the utility requested that it be allowed to use 50 percent of its legal and accounting costs incurred in preparing the gross-up reports to offset the contributors' refunds. The utility provided documentation for \$22,602 of legal and accounting costs. However, staff recommends disallowing \$7,725 of legal and accounting fees as follows:

- (1) The estimate to complete the reporting for Cronin, Jackson, Nixon & Wilson, included \$450 for P. DeChario to prepare the refund schedule and transmit to staff. This represents 6 hours at \$75. Since the CIAC was received from one contributor, staff recommends that the time allowed to prepare the report be reduced to 2 hours at \$75, or \$150. Therefore, \$300 should be disallowed.
- (2) Staff recommends that \$4,425 of costs for Ron Nunes, the manager, be disallowed because it appears that they do not relate to the preparation of the 1996 CIAC gross-up report.

- (3) Staff recommends disallowing the estimated 20 hours, or \$3,000 of estimated cost to complete the case, which was included for Ron Nunes. Since there is only one contributor in this case, and anticipating that no additional hearings will be required, staff does not believe that this additional cost will be incurred by the utility. Staff believes that the estimated 25 hours to complete the case should be sufficient.

Staff therefore recommends that 50 percent of \$14,877 or \$7,438 be considered in determining the amount to be used to offset the contributors' refund. However, in calculating the amount of refund, legal and accounting fees should not be offset against the \$2,949 of excess collected gross-up related to contributed property previously discussed.

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. (See Order No. PSC-97-0647-FOF-SU, issued June 7, 1997, in Docket No. 961077-SU; Order No. PSC-97-0657-AS-WS, issued June 9, 1997, in Docket No. 961076-WS; and Order No. PSC-97-0816-FOF-WS, issued July 7, 1977, in Docket No. 970275-WS.) In these orders, the Commission accepted the utility's settlement proposals that 50 percent of the legal and accounting costs be offset against the refund amount.

However, it should be noted that Orders Nos. 16971 and 23541 do not provide for the netting of costs incurred with filing gross-up refund reports with the excess gross-up collection's refund. Those Orders specifically state that "all gross-up amounts in excess of a utility's actual tax liability resulting from its collection of CIAC should be refunded on a pro rata basis to those persons who contributed the taxes."

Therefore, staff believes that once the contributors have paid the gross-up taxes on the CIAC, the contributors have fulfilled their obligation under Orders Nos. 16971 and 23541. Further, since those orders also provide that gross-up in excess of the utility's actual tax liability be refunded on a pro rata basis to those persons who contributed the taxes, staff believes that once the tax liability is determined, it is the responsibility of the Commission to ensure that excess payments of CIAC taxes are refunded in compliance with those orders. Therefore, staff does not believe that a reduction in the amount of refund a contributor is entitled to receive as a result of his overpayment of gross-up taxes is appropriate. Staff acknowledges that the legal and accounting cost associated with preparing the gross-up report were incurred to

satisfy regulatory requirements; however, staff does not believe that the contributors should be held responsible for those expenses. Staff views those costs as a necessary cost of doing business, and as such, staff believes it is appropriate for the utility to seek recovery of those amounts in a rate proceeding. Finally, staff believes that this situation is similar to when a utility files for an increase in service availability charges. The costs of processing the utility's service availability case are borne by the general body of ratepayers, although the charges are set for future customers only.

However, as in the other cases referenced above, staff recognizes in this case that acceptance of the utility's request would avoid the substantial cost associated with a hearing, which may in fact exceed the amount of the legal and accounting costs 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. Moreover, staff believes that the utility's request is a reasonable "middle ground." Therefore, staff recommends that while not adopting the utility's position, the Commission accept Parkland's request that it be allowed to offset 50 percent of the legal and accounting fees against the refund.

As previously stated, the utility overcollected the gross-up by \$10,358. However, staff recommends that legal and accounting fees not be offset against \$2,949 of the overcollection related to the estimated value of contributed property. Since the developer would have been entitled to a refund of this overpayment regardless of the amount of refund calculated by staff, we have not offset this overpayment with the legal and accounting costs incurred in filing the gross-up report. Therefore, the amount of overcollection against which the legal and accounting fees may be offset is \$7,409. The allowable legal and accounting fees of \$7,438 exceed the \$7,409 of overcollected gross-up. Therefore, staff recommends that the utility refund only the \$2,949 plus interest from December 31, 1996 to the date of refund.

In accordance with Orders Nos. 16971 and 23541, all amounts should be refunded on a pro rata basis to those persons who contributed the taxes. Since there is only one developer who contributed gross-up for 1996, the refund should be completed within two months of the effective date of the Order. The utility should submit a copy of the canceled check, or other evidence which verifies that the refund has been made, within 30 days from the date of refund. If the refund is not claimed, the utility should

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provide a letter documenting the amount of the unclaimed refund and an explanation of the efforts made to make the refund.

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**ISSUE 2:** Should this docket be closed?

**RECOMMENDATION:** No. Upon expiration of the protest period, if no timely protest is received by a substantially affected person, the Order should become final and effective upon the issuance of a Consummating Order. However, this docket should remain open pending staff's verification of the refund. Staff should be given administrative authority to close the docket upon verification that the refund has been completed and there is no unclaimed refund. (JAEGER)

**STAFF ANALYSIS:** Upon expiration of the protest period, if no timely protest is received by a substantially affected person, the Order should become final and effective upon the issuance of a Consummating Order. However, this docket should remain open pending staff's verification of the refund. Staff should be given administrative authority to close the docket upon verification that the refund has been completed and there is no unclaimed refund.



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SCHEDULE NO. 1

PARKLAND UTILITIES, INC.  
STAFF RECOMMENDED GROSS-UP REFUND

	<u>1996</u>
A-T-L TAXABLE INCOME PER UTILITY BEFORE CIAC	\$ 89,809
Plus taxable CIAC	<u>154,375</u>
A-T-L TAXABLE INCOME PER UTILITY	<u>\$244,184</u>
STAFF ADJUSTMENTS:	
(a) First year's depreciation on contributed assets	(491)
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TOTAL STAFF ADJUSTMENTS	<u>(491)</u>
A-T-L TAXABLE INCOME PER STAFF	\$243,693
Less CIAC	(154,375)
Plus first year's depreciation on CIAC	491
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A-T-L TAXABLE INCOME PER STAFF BEFORE CIAC	<u>\$ 89,809</u>
Less NOL carryforward	<u>\$0</u>
NET TAXABLE A-T-L INCOME	<u>\$ 89,809</u>
TAXABLE CIAC RESULTING IN A TAX LIABILITY	\$154,375
Less first year's depreciation on CIAC	<u>(491)</u>
NET TAXABLE CIAC	\$153,884
Combined marginal state & federal tax rate	<u>37.63%</u>
Net Income tax on CIAC	\$ 57,907
Expansion factor to gross up taxes	<u>1.60333</u>
Gross-up required to pay tax effect	\$ 92,843
Gross-up collected to pay tax effect	<u>(103,201)</u>
(OVER) OR UNDERCOLLECTION OF GROSS-UP	\$ (10,358)
Less: Offset of Legal and Accounting Fees	<u>7,409</u>
NET 1996 YEARLY OVERCOLLECTION	<u>\$ (2,949)</u>
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RECOMMENDED REFUND (EXCLUDING INTEREST)	<u>\$ (2,949)</u>
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