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STATE OF FLORIDA

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JACK SHREVE
PUBLIC COUNSEL

July 10, 1998

Blanca S. Bayo, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: Docket No. 971663-WS

Dear Ms. Bayo:

Enclosed for filing in the above-referenced docket are the original and 15 copies of Citizens' Motion to Dismiss. A diskette in WordPerfect 6.1 is also submitted.

Please indicate the time and date of receipt on the enclosed duplicate of this letter and return it to our office.

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Sincerely,

Harold McLean
Associate Public Counsel

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: In re: Petition of Florida Cities Water Company for limited proceeding to recover environmental litigation costs for North and South Ft. Myers Divisions in Lee County and Barefoot Bay Division in Brevard County.	)	DOCKET NO. 971663-WS Filed: July 10, 1998

CITIZENS' MOTION TO DISMISS

The Citizens of the State of Florida, by and through JACK SHREVE, Public Counsel, (Citizens) move the Florida Public Service Commission (the Commission) to dismiss the above-referenced petition of Florida Cities Water Company (FCWC or the utility) and as grounds therefore say as follows:

Argument

The Petition of FCWC fails to state a claim upon which relief can be granted because: 1) it fails to allege that any expenses the FCWC has or is incurring places the utility's earnings outside the last authorized range of rate of return; and, 2) because the petition seeks retroactive ratemaking.

Discussion

Earnings

FCWC has filed a petition which seeks recovery of expenses it alleges it incurred in several years past in litigation with federal authorities. The utility does not allege that the payment of these various costs ever rendered the earnings of the utility to be other than fair and reasonable; the petition contains absolutely no allegation that the expenditures, if made, ever placed the utility

outside its authorized range. The Citizens submit that the commission can provide no relief to any utility which omits such an issue from its pleading and proof, with certain exceptions not applicable here.

The principle holds irrespective of whether it is the utility seeking an increase or whether it is the commission seeking to lower rates. The test prerequisite to commission action is whether the utility is earning outside its last authorized rate of return.[1]

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[1] In the pending Sanlando case (Docket No. 980670-WS - INVESTIGATION OF POSSIBLE OVEREARNINGS BY SANLANDO UTILITIES CORPORATION IN SEMINOLE COUNTY) the staff analysis, which was adopted by the Commission, addresses the prerequisite finding which justifies the Commission's taking action in an overearning case. It provides in part:

> According to staff s review of Sanlando's 1997 annual report, the utility achieved an 18.76% return on equity for water, and achieved a 48.25% return on equity for wastewater. In the utility's last rate proceeding by Order No. 23809, issued November 27, 1990, in docket No. 900338-WS, the Commission approved an overall rate of return of 11.51% with a range of 11.27% to 11.75%, and established a rate of return on equity of 13.51% with a range of 12.51% to 14.51%.
>
> Using the upper boundary of 14.51% for equity, and appropriate interest rates for other components in the capital structure, a 9.05% overall cost of capital is indicated. Additionally, our preliminary review suggests that the utility achieved an overall 38.54% return on equity in 1997.

Thus upon a recommendation that Sanlando was earning outside its authorized rate of return, the Commission acted. Had the staff investigation shown that the utility was within its last authorized rate of return, no further action would have been necessary.

Commission action in a rate case is judged by appellate courts on the basis of whether the commission has provided the utility rates which will produce a reasonable rate of return, because failure of the commission to do so is to take the utility's property in a constitutional sense.[2]

The principal that a utility must allege underearnings as a prerequisite to rate relief has been afforded full approval by this Commission. In the very early days of the Environmental Cost Recovery Clause, (ECRC) Gulf Power Company petitioned the commission for a recovery of certain costs to which it believed the ECRC applied. The Office of Public Counsel argued before the Commission, as it argues here, that there should be no recovery unless it be shown that the utility was outside the range of its last authorized rate of return. The commission accepted this argument in principle when, in order No. PSC-94-0044 FOF-EI; 94 F.P.S.C. 1:76, it said:

> Public Counsel argued that if a utility is earning within its allowed return on equity range, it is already being compensated for all environmental expenses, and it should not be allowed to recover any costs through the environmental cost recovery clause. Public counsel maintains that it does not matter whether the environmental activity was included in the test year of the utility's last rate case. The utility should only be allowed to recover costs through the clause if the utility is under-earning.

---

[2] In Southern States Utilities v. Duval Co., 82 P.U.R. 3d 452 (4th Cir. 1969), the court observed that where the effect of a rate order would be a rate of return of some 2.8%, and there was no evidence in the record that supported setting rates at that level, "[t]he conclusion is inescapable that such [order] constitutes an unlawful confiscation of the utility's property." If an agency rate order does not provide sufficient compensation to the utility, then that agency has taken utility property without paying "just compensation" in contravention of the United States Constitution. Duquesne Light Co. v. Barasch, 488 U.S. 299, 308 (1989). A utility is entitled to an opportunity to earn a reasonable rate of return on its invested capital. City of Miami v. Florida Pub. Serv. Comm'n, 208 So.2d 249 (Fla. 1968). "The rate of return which public utility companies may be allowed to earn is a question of vital importance to both rate payers and investors. An inadequate return may prevent satisfactory services to the public and concomitantly disappoint investors who will look for alternative sources of investment." United Tel. Co. v. Mayo, 345 So.2d 648, 653-54 (Fla. 1977).

> OPC argued that to allow any recovery through the clause if the utility is not under-earning would amount to double recovery.
>
> *Although regulatory philosophy indicates that OPC is theoretically correct,* we must consider the legislation establishing the environmental cost recovery cost. (Italics supplied)

Order at 4:78

Although the Commission then considered the special provisions of Section 366.8255(1)(d) (Florida Statutes 1991) which permitted a recovery of conservation expenses outside the normal ratemaking process, it accepted the ratemaking principle that rate relief must be predicated on the utility's earning outside its authorized range, in the absence of a special statutory route. (Section 366.8255(1)(d), F.S, of course, has no application here.) The principle is consistent with a fundamental tenant of American Jurisprudence: relief is inappropriate where no harm is shown.

The principal ratemaking statute by which the Commission is bound in water and wastewater cases is Section 367.081, F.S., which provides that the commission shall establish rates which provide for a fair return on the investment of the utility in its property used and useful in the provision of utility service to the public. There is absolutely no allegation before the Commission that the existing rates approved for FCWC do not provide for that fair return.

The Citizens submit that it is the Utility's burden to appear before the commission with allegation and proof that the existing rates of the utility are not compensatory, are thus confiscatory, and ought to be increased such that a fair return may be earned. In this the utility has failed.

The Citizens note that there are exceptions to this principle, as the commission found in Gulf Power concerning the Environmental Cost Recovery Clause. In that case, the Commission found that the Legislature intended for utilities, such as Gulf, to recover these special costs, their earnings posture notwithstanding..

> Accordingly we find that if the utility is currently earning a fair rate of return that it should be able to recover, upon petition, prudently incurred environmental compliance costs through the ECRC. If such costs were incurred after the effective date of the environmental compliance cost legislation, and if such costs are not being recovered through any other cost recovery mechanism.

Order at 94:79

Thus the Commission implicitly, if not explicitly, recognized that in the absence of the ECRC, that were the utility earning within its range, it would not recover these expenses.

Water and wastewater has its own partial exceptions, but the exceptions are carefully crafted by the legislature to include the test of earnings the Citizens urge here.

Section 367.081(4)(b) and (c) taken together provide for a yearly indexing and pass through by utilities which qualify under those sections. Yet subsection (c) provides that a utility must by affidavit certify that neither the index nor the pass through will cause the utility to earn outside its previously authorized rate of return. The penalty for violation of this section is a third degree felony and a refund of rates with interest.

Thus even in the sections establishing automatic pass through and indexing, strict attention is paid to the earnings posture of the utility. It is, of course, apparent that the index and pass through exceptions attempt to ensure that the utility is not earning *in excess* of its last authorized range, rather than a requirement that the utility show as a prerequisite that the utility is

underearning before the pass through and index is had. But it is incumbent on the utility to assure, and on the Commission to ensure, that the utility's earnings are considered even in automatic index and pass through cases.

Lastly, the limited proceeding under which FCWC has filed the instant case does not provide any statutory exception to the necessity that the utility show that it is earning outside the range of its last rate of return, and FCWC does not so allege. Far from providing an exception, the Citizens submit that the limited proceedings statute is a *coup de grace* to FCWC's petition. Section 367.0822, Florida Statutes (1997), provides in relevant part:

> The Commission shall determine the issues to be considered during such a proceeding and may grant or deny any request to expand the scope of the proceeding to include other related matters. However, unless the issue of rate of return is specifically addressed in the limited proceeding, the commission ***shall not adjust rates*** if the ***effect*** of the adjustment would be to change the last rate of return. (Italics added)

Thus the Commission is under a unequivocal statutory mandate not to approve rates the *effect* of which (not necessarily the *intent* of which) would be to change the last rate of return. Yet no party in this proceeding can provide any assurance whatsoever to the Commission that the rates sought by FCWC would not have the *effect* of increasing its last rate of return. FCWC's petition seeks higher rates, but provides the Commission with no assurance that approval of the surcharges sought will not directly violate the limited proceeding statute.

The instant petition of FCWC enjoys no statutory fast track to supposed relief. FCWC brings neither allegation nor evidence before the Commission that its existing rates are less than fully compensatory. The Commission and affected parties are left only to wonder whether the alleged expenses have already been recovered through its existing rates, whether the relief sought

by the instant petition would provide a double recovery thereof, and whether an award of a surcharge would effectively change the last authorized rate of return for this company.

Because FCWC alleges no harm, it is entitled to no relief.

Retroactive rate making

The Commission has long stood for the notion, as it must, that a utility may not recover in new rates expenses for past consumption. The doctrine is generally know as a prohibition against retroactive ratemaking, and has a long and unblemished history in Florida.

The Ortega Utility Company (Ortega) case, a case very similar in principle to the instant FCWC case, presented an excellent example of an attempt to gain approval by the Commission of retroactive rates. Ortega applied to the commission for a general rate increase, one element of which was an allegation that the utility had not recovered depreciation expenses for periods well before the test year. The Commission denied this aspect of the application with the following analysis:

> We believe the proposal to restore depreciation produces a "regulatory asset." It is a correction to the company's net plant balance that must be approved by a regulatory body.[3] The suggested adjustment does not qualify as a prior period adjustment: the plant's service life is not being extended, nor does it correct an obvious error.
>
> We believe that the request for authority to reverse depreciation expense that has already been recognized is a request to recover past losses. Granting the request would be a form of retroactive ratemaking because it seeks to recover past losses, however the utility wishes to define

[3] This 'regulatory asset' language is an apparent reference to FASB 71 directive regarding the recording of regulatory assets.

> which accounting terms might be affected. Whether that adjustment is titled a correction to accumulated depreciation or a correction to CIAC, the impact is the same, rate base is increased to eliminate a loss that has already been recorded.
>
> Ortega, based on the record in this case, by asking for a one-time adjustment to rate base to recover past losses, is asking us to authorize retroactive ratemaking. See City of Miami v. Florida Public Service Commission, 208 So.2d 249, 259 (Fla. 1968), Gulf Power Co. v. Cresse, 410 So.2d 492 (Fla. 1982), and Citizens of the State of Florida v. Florida Public Service Commission, 448 So.2d 1024 (Fla. 1984), for the principle that retroactive ratemaking occurs when new rates are applied to prior consumption. In this case, we believe that by making an adjustment to rate base for past losses, increased rates would apply to prior consumption, thus retroactively raising rates. Accordingly, we hereby deny the utility's request. (footnote added)

Order No. PSC-95-1376-FOF-WS; 95 F.P.S.C. 11:247, 258

The prohibition against retroactive ratemaking observed in Ortega should apply with even more force here: Ortega unsuccessfully tried to recover sums which the Commission recognized as *losses.* In the instant case, FCWC is attempting to recover past *expenses.* As is discussed in the first section of this motion, FCWC makes no attempt to elevate the litigation expenses sought to any loss or alleged loss suffered by the company.

In addition, Ortega at least attempted to camouflage past expenses as depreciation foregone. FCWC's approach is a bare attempt to recover expenses which reach back in time for years.

The prohibition against retroactive ratemaking survived a recent Florida Supreme Court case in which it was discussed. The rate application of a telecommunications company, GTE Florida, Inc., resulted in an order which was later found, on appeal, erroneous in some respects by the court. The court remanded the order to the Commission for further action[4]. The Commission, apparently cautious of the prohibition against retroactive ratemaking, attempted to make the Company only partially whole, as it declined to levy surcharges.[5] The Commission approved rates which would recover the contested expense only prospectively. Upon appeal, the court ordered surcharges *distinguishing* the GTE case from a case of retroactive ratemaking. In GTE Florida Inc. v. Clark, 668 So.2d 971 (Fla. 1996) the court said:

> We also reject the contention that GTE's requested surcharge constitutes retroactive ratemaking. This is not a case where a new rate is requested and then applied retroactively. The surcharge we sanction is implemented to allow GTE to recover costs already expended *that should have been lawfully recoverable in the PSC's first order.* (Italics added)

at 781

GTE is easily understood as the court's ensuring that the remedy it afforded GTE Florida, Inc. under its original order, was given full effect by the Commission. That is, GTE Florida, Inc. was to recover the contested expense just as if the Commission had correctly resolved the issue in the first place.

In GTE the court cited a similar situation where an erroneous order of the commission was corrected back to the time of the original order, this time by the Commission itself. In re:

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[4] GTE Florida, Inc. v. Deason, 642 So.2d 545 (Fla. 1994).

[5]Caution inspired, admittedly, upon some uring from the Citizens

Application of Holiday Lake Water System for authority to Increase its rates In Pasco County, Florida, 5 F.P.S.C. 620 (1979) the court reversed a Commission order. The Commission then gave full effect to the Court's mandate by ordering a refund to customers based upon consumption from the time of the Commission order.[6]

The instant case is dissimilar from GTE and Holiday. In both GTE and Holiday, a Commission order was found to be erroneous. The Commission upon remand, was then required to enter an order which gave full effect to the court's reversal of the commission order, effective from the date that the Commission error began to have consequences. In GTE, it was the company which deserved to be made whole, in Holiday, the customers.

The instant case presents no such factual or legal scenario. There is no Commission order, no challenge, no reversal, and no remand. There is only a reach back for expenses previously and allegedly incurred.

GTE did no violence whatsoever to the prohibition against retroactive ratemaking. In fact, the Citizens submit that the court gave the prohibition implicit approval by distinguishing it.

Far from "getting the pot right" after a successful appeal - as was the case in GTE and Holiday - this case presents FCWC's bare attempt to now recover in future rates expenses which it says it incurred years ago, a practice explicitly disapproved by this Commission in Ortega, and rejected by the courts in the cases cited In Ortega. The prohibition against retroactive ratemaking, enforced by this Commission, and approved by the courts, bars the sort of recovery sought by FCWC; accordingly, this case should be dismissed.

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[6] The reversal of the Commission's original Holiday order appears In Citizens v. Hawkins, 364 So.2d 723 (Fla. 1978). The Commission's second Holiday order, which is cited by the supreme court, was not challenged.

Rate case expense:

The Commission is normally compelled to award rate case expense to a petitioning utility because failure to do so would erode the earnings of the utility and presumably cause the utility to earn either outside its last authorized rate of return, or in the case where a new rate of return is to be established, below the mid point of the newly established range. With respect to rate case expense, as is the case with the litigation expenses in chief, there is no allegation or proof that the present rates of the utility are inadequate in any respect. Although it is the utility's burden to show a need for rate relief, FCWC brings no allegation or proof that denial of the rate case expense portion of its case would occasion any underearning by the utility. As with the case in chief, the Commission is provided with no assurance that the current rates fail to recover the rate case expense incurred in this proceeding. For this reason, FCWC's petition should be dismissed, including the portion(s) addressing rate case expense.

Summary

FCWC neither pleads nor proves that it is entitled to any relief from an underearnings situation. Moreover, it seeks to reach back in time and recover from present and future customers expenses which for reasons of its own - perhaps related to the earnings question - it forwent in the past. FCWC's petition does not state a claim upon which relief can be based. With respect to the lack of an allegation that current rates are inadequate, a cure might be had by a new, complete filing, which would necessitate a provision of time to affected parties to evaluate the new filing. However, with respect to FCWC's retroactive ratemaking request, no amendment

of the pleadings or proof will cure the utility's attempt to reach back and recover expenses from time. FCWC's petition should be dismissed with prejudice.

WHEREFORE, the Citizens of the State of Florida move the Florida Public Service Commission to dismiss the Petition filed by FCWC, with prejudice.

Respectfully Submitted,

Harold McLean
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Attorney for the Citizens of the
State of Florida

CERTIFICATE OF SERVICE

I certify that a true copy of the foregoing Citizens' Motion to Dismiss was served by United States Mail, or where the party is denoted by an asterisk (*) by hand delivery upon representatives of the following parties on this the 10th day of July, 1998.

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