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IN THE SUPREME COURT OF FLORIDA

SARASOTA COUNTY, a political subdivision of the State of Florida,

Petitioner,

vs.

TAMARON UTILITIES, INC.,

Respondent.

Case No. 63,646

REPLY BRIEF OF SARASOTA COUNTY

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INTRODUCTION

This brief consolidates SARASOTA COUNTY's reply to the answer brief of TAMARON UTILITIES, INC. and to the amicus curiae brief filed by Florida Cities Water Company. "TAMARON" will continue to refer to TAMARON UTILITIES, INC.; the amicus will be referred to as "FLORIDA CITIES".

STATEMENT OF THE CASE AND FACTS

With regard to TAMARON's version of the case and facts, SARASOTA COUNTY, agrees that rate regulation law in the county has been in a state of flux since the Circuit Court's ruling in Southeastern Development and Utilities v. Board of County Commissioners of Sarasota County, Case No. 79-3555-CA-01, decided May 12, 1980. TAMARON's implication that these changes somehow create constitutional rights that have never before been found to exist is without foundation, as will be discussed further in the following portions of this brief.

It was SARASOTA COUNTY's position in its brief to the lower courts that TAMARON had not properly presented a rate case to the Board of County Commissioners that would support an allowance for what TAMARON called a "reserve contingency account", and that it presented no case at all for allowance of depreciation of contributed property as an operating expense. The thrust of the argument was not (as TAMARON suggests) that the Board would have allowed CIAC depreciation as an operating expense, but rather that the issue was not properly preserved for appeal.

The question of how to treat CIAC in the rate base was never an independent issue raised by any party in the lower courts. The real issue was whether a utility has a constitutionally protected right to collect revenues based on depreciation of contributed property. The peripheral rate base issue arose when the District Court of Appeal failed to come to grips with the primary constitutional issue independently. TAMARON has not

complained about the rate base calculation used by SARASOTA COUNTY in this case because it is a correct calculation. In fact, it is exactly the same as the formula used by the Public Service Commission and litigated in Citizens of the State of Florida v. Florida Public Service Commission, 399 So.2d 9 (Fla. 1st DCA 1981), and approved by the court in its opinion. The rate study report of Darby, Sheahen & Weissman, the Board's rate consultants, is attached as Appendix 4. Reference to page 3 of that report clearly shows this to be true.

Equally perplexing is FLORIDA CITIES' expressed concern about the rate base calculation used by SARASOTA COUNTY. Although it is outside the record in this instant case, FLORIDA CITIES' entry as an amicus curiae on the basis of its own rate case makes it necessary to dispell any notion that an improper formula was followed in that case. Page 24 of the Darby, Sheahen & Weissman rate study report in the FLORIDA CITIES' rate case is attached as Appendix 5. Examination of the calculations made there shows that the same formula was followed in that case. No claim was made for depreciation or contributed property as an operating expense, so that separate issue did not present itself.

It appears that FLORIDA CITIES' disagreement with SARASOTA COUNTY's rate base calculation methodology arises from semantic and bookkeeping procedure differences between the rate consultants of the respective parties. The formula urged by FLORIDA CITIES, as used by the First District Court of Appeal, is complex and apparently reflects the order of bookkeeping calculations used to arrive at the result. However, as the court pointed out in its opinion, the formula can be mathematically

reduced to much simpler terms:

$$RB = (X + Y) - [(A + B) + X] + A$$

$$RB = X + Y - A - B - X + A$$

$$RB = Y - B$$

RB is rate base; X is CIAC; Y is invested capital; A is accumulated CIAC depreciation; B is depreciation on invested capital.

If invested capital and depreciation on invested capital are ascertainable without going through the steps of calculating total assets, total depreciation, total CIAC property, and total CIAC depreciation, it is mathematically unnecessary to use the more complex formula. It is the simplified formula that was used by SARASOTA COUNTY in the examples in its brief which were criticized by FLORIDA CITIES. Further examples are attached as Appendix 6, demonstrating the equivalence of the two formulae under three different rate study scenarios: no CIAC, all CIAC, one-half CIAC.

With the above clarifications made, SARASOTA COUNTY, herewith replies to the argument presented by TAMARON.

ARGUMENT

A DULY ENACTED COUNTY ORDINANCE DOES NOT DEPRIVE A FRANCHISED PUBLIC UTILITY OF ITS PROPERTY WITHOUT DUE PROCESS OF LAW MERELY BECAUSE CONTRIBUTED PROPERTY IS EXCLUDED FROM THE UTILITY'S RATE BASE AND DEPRECIATION ON CONTRIBUTED PROPERTY IS NOT ALLOWED AS A RECOVERABLE OPERATING EXPENSE.

The responsive argument advanced by TAMARON in its answer brief does not come to grips with the true facts and issue in this case. TAMARON seeks to distinguish the cases cited by SARASOTA COUNTY on their facts and, by such attempt, to have the Court ignore the legal principles for which those cases stand. There is no question that the cases are factually different from the one before the Court -- no cases have been found which are in direct harmony with the facts of this case -- but the legal principles concerning the definition and function of depreciation in the ratemaking context can certainly be aptly applied and can hardly be regarded as irrelevant, as TAMARON suggests.

TAMARON offers up another red herring at page eight of its brief by suggesting that adoption of SARASOTA COUNTY's position "would necessarily lead to the absurd conclusion that a utility would be entitled to no compensation in the event that its (contributed) property is taken by eminent domain proceedings". Absurd it is, indeed. At no time has SARASOTA COUNTY taken the position that there is no protected property interest in contributed property per se; it is the depreciation on contributed property in this case and on these facts that SARASOTA COUNTY asserts is not a constitutionally protected property right. The treatment of property for ratemaking purposes is not the same as in

eminent domain proceedings.

TAMARON and FLORIDA CITIES emphasize that purchased and contributed property both wear out and have to be replaced. SARASOTA COUNTY does not take exception to this truism, but that fact does not go to the real issue: who pays for the replacement, and how many times? As was pointed out in SARASOTA COUNTY's initial brief, the homeowners paid for the contributed property in the purchase price of their building lots, the developer had available a tax election that allows the cost of the property contributed to the utility to be written off with a corresponding financial benefit from that source, and upon replacement of the depreciated contributed property the homeowners will pay the utility a return on its investment.

If the homeowners buy $100 worth of plant which is given to the utility for its use in serving the homeowners, the developer has received a tax benefit that offsets its actual cost, the utility receives the use of the plant without committing any of its own cash and without borrowing any cash (worth at least eight to ten percent in interest savings to the utility). Total cost to the utility to use the plant through its useful life: zero (and, in fact, a theoretical or actual profit based on the interest savings or the internal rate of return on money the utility did not have to spend).

If, on the other hand, depreciation on the contributed property is also charged to the homeowners, at the end of the property's useful life the utility has accumulated another $100, plus the income thereon, to use to replace the plant. Upon replacement the homeowners begin paying a return to the utility on

the homeowners' investment. Total cost to the utility: zero. Plus, the utility has avoided commitment of its own cash and has had available for its own use the amount paid by the homeowners in depreciation. If the depreciation reserve is no more than a bookkeeping entry (instead of an escrowed fund), there is no guarantee that the money would even be there to make replacements.

TAMARON's answer brief recognizes that certain jurisdictions adhere to the theory that the purpose of a depreciation allowance should be limited to permitting a utility to recoup its actual investment in the property being depreciated. See page 12 of answer brief. However, TAMARON asserts that Florida has followed a different theory. The Florida cases cited have not presented the issue inherent in this case. None dealt with a situation where a utility was claiming constitutional entitlement to depreciation on contributed property as an operating expense where the "added-back" provisions regarding inclusion of an allowance for CIAC depreciation in rate base was not effective to provide positive cash flow for the utility.

In addition to the factual distinctions between those cases and this one, there is an important legal distinction. SARASOTA COUNTY is a chartered, home rule county under authority of the Florida Constitution, and as such, is empowered to enact and enforce local ordinances not in conflict with general law. Florida Constitution, Article VIII, Section 1(g). Sarasota County Ordinance 80-62 is not inconsistent with general law, and although similar, the statutes governing the Public Service Commission do not apply inasmuch as SARASOTA COUNTY has lawfully elected to retain jurisdiction over water and sewer utility regulation within

its boundaries. Having separate jurisdictional authority, SARASOTA COUNTY is only bound to meet constitutional requirements and not run afoul of general law in its ordinances. Ordinance 80-62 satisfies these requirements.

An examination of the sentence in Section 8(e) of Ordinance 80-62 that is the object of this controversy reveals no constitutional defect, if the language is construed in favor of a constitutionally valid interpretation, as the law requires. Dunedin v. Bense, 90 So.2d 300 (Fla. 1956). The contested language is as follows:

> The Board shall fix and determine a rate which allows for reimbursement of operating costs including depreciation on all properties, excluding contributed properties, and a fair and reasonable net return on the original cost of a system incurred by the person first dedicating it to public service, which shall not include contributions in aid of construction or customer contributions.
> (Emphasis supplied for reference.)

The first phrase of the sentence (underlined) clearly disallows CIAC depreciaiton as an operating expense. There is no dispute as to the effect of that language. The second phrase (not underlined) provides only that no CIAC or customer contributions be included in a utility's rate base. It does not specify the precise manner in which rate base is to be calculated. It does not speak to the "add-back" concept or how the amount of CIAC to be excluded is calculated.

As is evident from the opinion of the First District Court of Appeal in Citizens of the State of Florida v. Florida Public Service Commission, 399 So. 2d 9 (Fla. 1st DCA 1981), neither CIAC nor depreciation on it have to appear in the rate base formula if

the value of invested capital and the depreciation on it are calculated properly. The court reduced the complex equation used by the Public Service Commission to its essential terms and concluded that RB = Y - B effectively eliminated CIAC from the rate base, where RB represents rate base, Y represents invested capital, and B represents depreciation on invested capital. Direct reference to the rate study summaries attached hereto as Appendices 4 and 5 shows that SARASOTA COUNTY applied the proper formula in both instances in rate base calculations.

TAMARON's dilemma is that the rate base calculation does not put cash in its pocket because of its zero rate base and that SARASOTA COUNTY has met the requirement that depreciation contributed property must be considered somewhere in the ratemaking process. Southeastern Development and Utilities v. Board of County Commissioners, 398 So.2d 882 (Fla. 2d DCA 1981). SARASOTA COUNTY has met this requirement by using a ratemaking procedure that is equivalent to the "add-back" concept (although it has never been called such in this jurisdiction).

TAMARON is in its present position of no profit to its investors as a direct result of its own business decision to finance its operation through developer contributions rather than by direct capital outlay. The utility has consciously made this choice for what is undoubtedly considered good financial reasons. It cannot be heard to complain that Ordinance 80-62 has unconstitutionally created unreasonable classifications of utilities on the basis of what financial model is used in calculation of rates. It is perfectly reasonable to classify utilities in such a way that those which have invested capital get

a return on investment and those with no investment get none. The much reiterated assertion that all property wears out -- purchased or contributed -- is simply not material to the real function of a depreciation allowance for ratemaking purposes. It is not a question of cost, but rather who should bear the cost, as argued above.

TAMARON further asserts that the "end-result" doctrine should not be applied in this case. See page 18 of the answer brief. As is demonstrated by the rate study summary of Darby, Sheahen & Weissman, attached as Appendix 4, this is the very type of case in which the doctrine should be applied. If the District Court had examined the actual financial result of the rate order in this case, it would have seen that SARASOTA COUNTY used a procedure which was functionally equivalent to the "approved" Public Service Commission formula and which was within the scope of the language of Section 8(e) of Ordinance 80-62.

CONCLUSION

SARASOTA COUNTY has not violated any constitutional right of equal protection or substantive due process by its enactment of Ordinance 80-62 or by its enforcement of it in the rate order embodied in Resolution 81-344. TAMARON has failed to prove beyond a reasonable doubt that Ordinance 80-62 is unconstitutional in any respect.

The brief of FLORIDA CITIES, as amicus curiae, does not raise any real issue that is not resolved by examination of the actual computational procedure used by SARASOTA COUNTY and the proper construction of the language of Section 8(e) of Ordinance 80-62.

On the basis of the argument presented herein and upon the record before the Court, the opinion of the Second District Court of Appeal should be quashed insofar as it declares Section 8(e) of Ordinance 80-62 unconstitutional. (The District Court's finding of no procedural due process violations should be allowed to stand since no party has sought review of that portion of the decision.)

Respectfully submitted,

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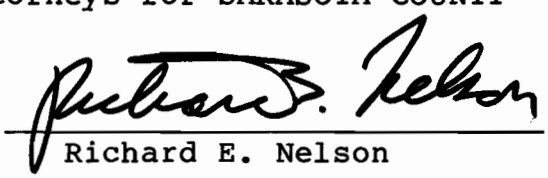
By: 
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true copy of the foregoing has been furnished by U.S. Mail to M. Joseph Lieb, Esq., 1900 Ringling Boulevard, Sarasota, Florida 33577, Daniel Joy, Esq., 2055 Wood Street, Suite 200, Sarasota, Florida 33577, and B. Kenneth Gatlin, Esq., P. O. Box 669, Tallahassee, Florida 32302, this 22nd day of December, 1983.

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