OJa 11-7-84

IN THE SUPREME COURT OF FLORIDA

THE CITIZENS OF THE STATE OF FLORIDA, Petitioners/Appellants, vs. FLORIDA PUBLIC SERVICE COMMISSION, Respondent/Appellee, and JACKSONVILLE SUBURBAN UTILITIES CORPORATION and SOUTHERN UTILITIES COMPANY, Respondents/Appellees.	CASE NO. 64,680 APPEAL FROM DECISION RENDERED BY THE DISTRICT COURT OF APPEAL FOR THE FIRST DISTRICT OF FLORIDA IN CASE NO. AE-103

ANSWER BRIEF OF RESPONDENTS/APPELLEES, JACKSONVILLE SUBURBAN UTILITIES CORPORATION and SOUTHERN UTILITIES COMPANY

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STATEMENT OF THE CASE AND OF THE FACTS

Jacksonville Suburban Utilities Corporation and Southern Utilities Company (collectively, the "Utility") hereby adopt the contents of the Statement of the Case and Facts contained in Petitioner's Brief on the Merits ("Petitioner's Brief"), at pages 1-2, with the following factual additions:

The first rate order in which the Commission may have allowed depreciation expense on contributions-in-aid-of-construction ("CIAC") to be charged by the Utility was Commission Order No. 7037 dated December 4, 1975, entered in Docket Nos. R-74517-WS and R-74518-WS [infra, p. A-31].

The first rate order in which the Commission specifically disallowed depreciation expense on CIAC from being charged by the Utility was Commission Order No. 9533 dated September 12, 1980, entered in Docket Nos. 790316-WS and 790317-WS [infra, p. A-19].

The Commission discontinued its practice of allowing depreciation expense on CIAC to be charged by water and sewer utilities in 1979, in the General Waterworks proceeding in Docket No. 780022-WS, as documented in Commission Order No. 9443 entered on July 9, 1980 [infra, p. A-22].

The net effect of disallowing depreciation expense on CIAC and continuing to permit the "add-back" of accumulated depreciation on CIAC is that ratepayers are charged lower rates than prior to the disallowance of depreciation expense, since each dollar of genuine depreciation expense is paid for by ratepayers on a dollar-for-dollar basis. Citizens of the State of Florida

v. Florida Public Service Commission (General Waterworks), 399 So.2d 9 (Fla. 1st DCA 1981), at p. 10.

Prior to 1979, the Commission routinely granted as an expense what it called "depreciation on CIAC," as a form of attrition allowance. Commission Order No. 9443, at Sheet Seven [infra, p. A-28].

The Utility has failed to earn its allowed rate of return during the entire period of time relevant to this proceeding [Exhibit J/S-7, at p. 16; infra, p. A-33].

ARGUMENT

THE COMMISSION'S "ADD-BACK" OF ACCUMULATED DEPRECIATION ON CIAC IS IN ACCORDANCE WITH THE TREATMENT REQUIRED BY THIS COURT IN HOLIDAY LAKE AND THEREFORE IS CONSISTENT WITH THE ESSENTIAL REQUIREMENTS OF LAW. THE LOWER COURT CORRECTLY UPHELD THE COMMISSION'S DECISION IN ORDER NO. 9533.

INTRODUCTION

In Petitioner's Brief filed herein, Public Counsel has requested that this Court reverse the decision of the First District Court of Appeal (the "First District") in The Citizens of the State of Florida v. Florida Public Service Commission, (Jacksonville Suburban), 440 So.2d 371 (Fla. 1st DCA 1983), and remand the case to the Commission with regard to that portion of the Commission's Order No. 9533 permitting the so-called "add-back" of accumulated depreciation on CIAC into the rate base of the Utility. As a basis for this Court's scrutiny, Public Counsel has alleged a conflict of decisions between the First District's decision in Jacksonville Suburban and this Court's opinion in The Citizens of the State of Florida v. Hawkins (Holiday Lake), 364 So.2d 723 (Fla. 1978). There is no such decisional conflict here, however, and the factual setting is such that this Court should affirm the decision in the case below.

The central issue in this appeal concerns the proper rate-making treatment of a component of utility rate base. At its most basic level, the question on appeal is whether the Utility's rate base properly should include all or any portion of the

amount carried on the books of the Utility as "accumulated depreciation on CIAC." In order to resolve this issue, this Court must apply the principles of law announced in its Holiday Lake and Westwood Lake, Inc., v. Dade County [246 So.2d 7 (Fla. 1972)], decisions to the particular facts in the instant case.

Before both the Commission and the First District below, Public Counsel contended that the Commission's ratemaking practice of permitting the so-called "add-back" of accumulated depreciation on CIAC to rate base was legally contrary to this Court's holding in Holiday Lake. Both the Commission and the First District rejected Public Counsel's legal argument. Both found that, while the Commission continued to allow the "add-back" of depreciation on CIAC, it no longer allowed depreciation on CIAC as an operating expense, contrary to its ratemaking practice rejected by this Court in Holiday Lake.

In his Motion for Clarification and Rehearing filed with the First District below, and in his appeal to this Court, the Public Counsel has changed the nature of the issue from legal to factual. He no longer contends that the Commission's ratemaking practice of allowing the "add-back" of accumulated depreciation on CIAC is contrary to Holiday Lake as a general legal principle. Admitting, in effect, his erroneous argument before the Commission and the First District, Public Counsel now argues a factually based point, contending that the practice of allowing the "add-back" violates Holiday Lake only with respect to depreciation that accumulated during those few years in which the

Commission also allowed what it labeled "depreciation on CIAC" as an operating expense.

Public Counsel's rather disingenuous change of the issue during the appeal process is more than cutting his argument in a thinner slice. It constitutes the raising of a new issue on appeal and a new theory that was not properly raised below before the Commission or the First District.

Public Counsel's new issue and theory must fail as well, for a number of reasons:

(1) It is now too late in the proceedings for Public Counsel to adopt a new issue and theory on appeal. See, point I below.

(2) The Public Counsel's new issue is essentially a factual argument. Unfortunately, there is no evidence in the record to support it. In fact, because Public Counsel did not formulate this new issue until shortly before his appeal to this Court, he did not even attempt to introduce below any evidence in support of it. See, points VI and VII below.

(3) Public Counsel's new theory is erroneous as a matter of law. The Commission's ratemaking policy used in the present proceeding, even for those years included within Public Counsel's new argument, is consistent with this Court's ruling in Holiday Lake. See points III, IV and V below.

In Holiday Lake, this Court stated its duty, on certiorari, as follows:

> "On certiorari the duty of this Court is to examine the record to determine whether

> the Commission's order is in accord with the essential requirements of law and whether the agency had before it competent substantial evidence to support its findings and conclusions." [Id. at 727; citations omitted.]

Even if this Court were to reconsider the evidence before the Commission and the First District, it would find that both had before them competent, substantial evidence to support their findings and conclusions that the present case is distinguishable from the Holiday Lake case. Therefore, this Court should conclude that the Commission's Order No. 9533 and the lower court's decision are in accord with the essential requirements of law.

I.

PUBLIC COUNSEL CANNOT RAISE A NEW ISSUE AND THEORY ON APPEAL AT THIS STAGE OF THE APPEAL PROCESS.

After the decision of the First District below, Public Counsel formulated a new issue on appeal and a new theory of his case. Before the Commission, Public Counsel contended that the Commission's entire ratemaking policy of allowing in rate base an "add-back" of accumulated depreciation on CIAC was contrary to law in that it was violative of this Court's ruling in Holiday Lake. For example, in Public Counsel's Exceptions to the Examiner's Recommendation, he argued that:

> The utilities calculated rate base by a method that is mathematicaly equivalent to adding back accumulated depreciation on CIAC. The staff did not disagree with this presentation but adjusted the schedules to show the add back separately. This allowance is in direct conflict with the Florida Supreme Court's opinion in Citizens of the Stte [sic] of Florida v. Hawkins (Holiday

> Lakes), 364 So.2d 723, 725 (1978), wherein the Court found that the Commission violates its own policy and contravenes Section 367.081(2), Florida Statutes, by adding back the accumulated depreciation of CIAC into the rate base calculation. [R:692]

Similarly, before the First District below, Public Counsel's initial issue and legal theory on appeal were that the entire "add-back" ratemaking policy of the Commission was contrary to Holiday Lake. For example, he argued that:

> The Public Service Commission never complied with the Supreme Court's Holiday Lake decision, except, on remand, in that particular case. The Citizens therefore challenged the add-back practice again before this Court in General Waterworks, relying upon the Holiday Lake decision. This Court held that the Commission's disallowance of depreciation as an operating expense served to distinguish Holiday Lake, making the add-back proper. It stated that this treatment resulted in lower rates and that the add-back does not reintroduce CIAC into rate base but completely eliminates its influence. The rate base formula used by this Court is mathematically identical to that rejected in Holiday Lake.
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> * * *
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> The General Waterworks decision out of this Court simply cannot be read consistently with the Supreme Court's in Holiday Lake. [Public Counsel's Initial Brief Before the First District Court of Appeal, pp. 7-8.]

In his Motion for Clarification and Rehearing before the First District, however, and now before this Court, Public Counsel has conceded that he is no longer contending that the entire "add-back" ratemaking policy is contrary to Holiday Lake. He now summarizes the issue and theory of his appeal, as follows:

> The only disagreement in the issue at bar is the proper treatment of the accumulated depreciation balance which accumulated during the period in which the Commission allowed utilities to charge CIAC depreciation expense in their rates. [Petitioner's Brief, p. 21.]

Thus, Public Counsel is not now challenging the entire ratemaking practice of the Commission to permit the so-called "add-back" of accumulated depreciation on CIAC. He is saying that this practice is contrary to Holiday Lake only when it is applied to specific facts relating to periods of time during which the Commission allegedly allowed the Utility to recover depreciation expense on CIAC in its rates.

If Public Counsel wished to raise this issue in this proceeding, he should have done so before the Commission and early in the proceeding before the First District. By waiting until his appeal before this Court to emphasize his new issue and theory of the case, Public Counsel has precluded the Utility and the Commission from responding adequately to his theory and from introducing evidence with respect to it. For example, if, in the proceeding below before the Commission, Public Counsel had challenged only the application of the Commission's "add-back" policy to specific facts involving a limited and specific number of years of the Utility's operation, the Utility could have introduced evidence directed to this argument that would have established that the application of such policy (a factual issue)

was supported by competent, substantial evidence.* Because Public Counsel elected to challenge the validity of the entire policy, as a matter of law, the Utility responded primarily with legal arguments and was not required to present any evidence. If Public Counsel is able now to change his theory of the case, the Utility will have effectively been "sandbagged."

In appeals from an administrative agency,

> [a] court may decline to pass upon questions which could have been raised but were not raised before an administrative agency. [1 Fla.Jur.2d, "Administrative Law" § 161, p. 781; footnote omitted.]

This rule has been adopted universally by appellate courts "[i]n order to avoid the delay and expense incident to appeals, reversals, and new trials upon grounds which might have been corrected in the trial court if the question had been properly raised there. . . ." 5 Am.Jur.2d "Appeal and Error" § 545, p. 29; Mariani v. Schleman, 94 So.2d 829 (Fla. 1957). As a corollary to the rule that issues not raised below will ordinarily not be considered on appeal, reviewing courts have also determined that they will "consider the case only upon the theory upon which it was tried in the court below." 5 Am.Jur.2d, supra, at § 546, p. 31.

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*The Utility did introduce some evidence that works to defeat Public Counsel's argument. See for example, Points VI and VII below. This evidence was introduced for purposes other than to rebut this argument of Public Counsel, however.

This Court consistently has refused to review matters that had not been properly presented to the lower court. In Jones v. Neibergall, 47 So.2d 605 (Fla. 1950), this Court stated, with respect to an attempt by the plaintiff to change his theory from a purely legal to an equitable argument:

> The pleadings in the case did not present any such alleged equities and they were not urged at the bar of this court until the reconsideration. It is quite true that reasonable inferences from the evidence may be said to point to said equities, but not having been presented or ruled on by the trial court, it would be utter folly to urge their adjudication by this court at this time. We will not divine issues from the ether nor attempt to adjudicate those not presented by the pleadings or ruled on by the trial court. [Id. at 606.]

Here, Public Counsel has committed a similar error in attempting to change his argument from a purely legal one to a factual one. Additionally, in Chomont v. Ward, 103 So.2d 635 (Fla. 1958), this Court affirmed the judgment of the trial court, in part, because matters submitted on appeal were not properly presented through the lower court. This Court stated:

> As to the damage to the automobile, if the matter had been properly presented to the trial judge and therefore properly tendered to us as a matter for disposition, we would be inclined to hold that negligence had been proved and that damages at least to the extent of $34 had been indisputably proved as the result of the negligence. This particular isolated item, however, was not submitted to the trial judge and is therefore not properly here. [Id. at 638.]

In Linder v. Combustion Engineering, Inc., 342 So.2d 474 (Fla. 1977), this Court considered an appeal based, in part, on

the doctrine of strict liability in tort, when this Court had only first adopted the doctrine of strict liability of tort (in West v. Caterpillar Tractor Company, Inc., 336 So.2d 80 [Fla. 1976]) after the judgment by the trial court and opinion of the district court in Linder. This Court in Linder refused to review the ruling of the lower court on the doctrine of strict liability of tort because the pleadings below failed to raise the theory of strict liability. The Linder Court held:

> In the case sub judice, plaintiffs' complaint consisted of one count based upon negligence and one count based upon breach of implied warranty. The complaint did not seek recovery under the doctrine of strict liability nor did the plaintiffs make a motion at any time to have the pleadings amended so as to conform to the evidence. . . .
>
> Plaintiff's first attempt to rely on the theory of strict liability was by a requested instruction. Strict liability was not within the issues raised by the pleading and the court properly rejected such a charge. Under the circumstances the strict liability rule was not appropriately and properly raised during the litigation. [Id. at 476; citation omitted.]

The rationale of the Court's holdings in Linder and Chomont has been applied by this Court to appeals from the Commission. In Pensacola Transit, Inc. v. Douglass, 34 So.2d 555 (Fla. 1948), this Court declined to rule on an issue not raised before or ruled upon by the Commission, stating:

> The contention is made that the Railroad Commission failed and omitted to proceed according to the essential requirements of the law in the entry of the order dated May 28, 1947, as being in derogation of and in conflict with Senate Bill No. 989 Sp.Acts 1947, c. 24806, which became effective as a

> law several days after the date of entry of the challenged order. On this assignment we decline to rule or express an opinion, as the contention was not ruled upon by the Commission below. [Id. at 560-61.]

Unlike the Plaintiff in Linder, Public Counsel is not here contending that a new legal theory has been adopted by this Court since the order of the Commission and ruling of the First District below. Rather, Public Counsel is simply adopting a new theory of the case. If this Court will not consider an appeal based on a new issue or theory when there has been a substantive change in the law, as in Linder, surely it should not consider an appeal based upon a new issue and theory of appeal as in the present case.

II.

PUBLIC COUNSEL'S NEW ISSUE AND THEORY ON APPEAL ARE QUITE LIMITED IN SCOPE.

In any event, it must be recognized that it is not the entire amount of accumulated depreciation on CIAC that Public Counsel now would have this Court require the Commission to remove from the Utility's rate base, but rather only a smaller portion attributable to rate years in which, Public Counsel asserts, the Commission permitted the Utility to treat depreciation on CIAC as an operating expense as part of its rates.

Public Counsel now concedes, at page 20 of his brief, that "[t]he area upon which no disagreement exists is the accumulated depreciation that has accumulated since the inception of the Commission's new policy [of not allowing depreciation expense in

determining rates]." Public Counsel then acknowledges the generally accepted utility practice:

> It must be understood that a utility books both depreciation expense and accumulated depreciation on CIAC, regardless of what the Commission allows for rates. Even after the Commission stopped allowing the utilities to charge depreciation expense on CIAC, the accumulated depreciation account balance continues to grow at the same rate as previously.
>
> Therefore, many utilities have a CIAC accumulated depreciation balance, some of which accumulated during the period when depreciation expense was collected on the CIAC property, and some of which has accumulated during the subsequent period when CIAC depreciation expense was not allowed in the rates. [Petitioner's Brief, pp. 20-21; original emphasis.]

Public Counsel now also recognizes, by implication, that, for older utilities like Jacksonville Suburban and Southern Utilities, a large portion of the accumulated depreciation balance accumulated during the period prior to regulation by the Commission, when CIAC depreciation expense was not allowed in the rates or collected from ratepayers. Therefore, that portion of the balance constitutes a part of the rate base with which this appeal is not concerned.

Public Counsel admits, in fact, that "[t]he only disagreement in the issue at bar is the proper treatment of the accumulated depreciation balance which accumulated during the period in which the Commission allowed utilities to charge CIAC depreciation expense in their rates." Petitioner's Brief, p. 1. He further concedes that the accumulated depreciation balance that

accumulated during the period of time when the Commission did not allow depreciation expense in determining rates should not be removed from the original investment of the Utility in determining rate base:

> It cannot be overemphasized that the Public Counsel totally agrees that the portion of the accumulated depreciation balance which has accumulated after the Commission began disallowing CIAC depreciation expense should not be removed from the original investment (in other words, it should be added back). It is the portion of the accumulated depreciation account which accumulated when depreciation expense on CIAC was charged to ratepayers that should be removed from the original investment to properly determine rate base. The distinction lies in whether the rates for a given year included a charge for depreciation expense on CIAC: for those years in which CIAC depreciation expense was charged, the corresponding CIAC accumulated depreciation must be removed from the original investment; for the years in which CIAC depreciation expense was not allowed in rates, the corresponding CIAC accumulated depreciation should not be removed from the original investment. [Idem.; emphasis added.]

Therefore, the only amount of accumulated depreciation on CIAC that Public Counsel even arguably questions in this appeal is the amount of accumulated depreciation that accumulated between the date on which the Commission authorized the Utility to collect depreciation expense on CIAC and the date on which the Commission ceased to allow the Utility to collect depreciation expense on CIAC. The first full rates of the Utility that were authorized by the Commission became effective pursuant to Order No. 7037 dated December 4, 1975, in Docket Nos. R-74517-WS and R-74518-WS [infra, p. A-31]. The rates that became effective

pursuant to Order No. 9533 dated September 12, 1980, in Docket Nos. 790316-WS and 790317-WS [infra, p. A-19], were authorized after the Commission ceased to allow utilities to charge CIAC depreciation expense in their rates [Commission Order No. 9443, at Sheet Five, infra, p. A-26]. As a result, the only amount of accumulated depreciation on CIAC that is even remotely in question in this appeal is that which accumulated from December 4, 1975, to September 12, 1980--not the entire balance of the "accumulated depreciation on CIAC" account formerly claimed by Public Counsel.

As is discussed below, however, even those portions of accumulated depreciation on CIAC that did accumulate during the years 1975 through 1980, when the Commission permitted the Utility to treat "depreciation on CIAC" as an operating expense, should not be deducted from rate base, because the record in this case indicates that the corresponding amounts labeled as "depreciation on CIAC" were actually granted by the Commission as an attrition allowance [infra, pp. A-21, A-28]. The record also contains competent, substantial evidence showing that the so-called "depreciation on CIAC" allowed by the Commission was not actually collected by the Utility [infra, p. A-33]. Therefore, no portion of accumulated depreciation on CIAC should be removed from the Utility's rate base, and the decision of the lower court should be affirmed.

III.

THIS COURT'S HOLIDAY LAKE DECISION DEALT ONLY WITH MONEY ACTUALLY PAID BY CUSTOMERS AND RECEIVED BY THE UTILITY COMPANY.

In its Holiday Lake decision, this Court prohibited the practice of requiring customers to pay for CIAC property initially and then to pay for such property again through the collection of depreciation expense on CIAC, without also requiring the utility company to reduce its rate base by the amount of both the initial collection and the subsequent collection from the customers.

No question was raised in either the Holiday Lake case or the present case concerning the proper treatment of the customers' initial payment for CIAC property. Therefore, the sole issue in both cases concerned the proper treatment of the second payment supposedly made by the customers for CIAC property.

There can be no question that this Court was concerned in Holiday Lake with the actual payment of money by the customers and the actual collection of money by the utility company. In Holiday Lake, this Court stated:

> It is important to note that because the utility's rates were designed to recover depreciation expense, the utility will have received $500,000 in revenues over the expected life of the plant. If this cash is reinvested in the utility to improve or replace equipment, the value of the gross utility plant will rise. . . . [Id. at 725-726; emphasis added.]
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> * * *
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> . . . the depreciation expense was reinvested in the utility [in the Court's example] . . . [Id. at 726; emphasis added.]

This Court then continued its example by stating:

> Consider now the proper ratemaking treatment if the utility instead uses the cash to pay off its loans and to return the equity capital originally contributed by the owners. [Idem.; emphasis added.]

In pointing out the error in the Commission's calculation and continuing to explain its example, this Court stated:

> Using the above example, if the cash received for depreciation is reinvested in the utility. . . . [Idem.; emphasis added.]

After again illustrating the error in the Commission's computation by the use of its example, this Court emphasized:

> It is noteworthy that the increase in the amount of Gross Utility Plant was not funded by an increase in the amount of invested capital; rather it was due to the reinvestment of the cash provided by the ratepayers through rates set to recover depreciation expense.
>
> Similarly, under the Commission's approach, if the utility pays off its loans and returns all of the owner's capital. . . . [Idem.; emphasis added.]

At the conclusion of its example, this Court further emphasized that it was concerned with actual funds received by the utility company and not mere accounting entries:

> The crucial fact that [the Commission] ignores is that the utility also would have recovered $250,000 from the assets purchased by CIAC. Assuming, as the Commission does, that none of the depreciation expense is reinvested in the utility. . . . [Idem.; emphasis added.]

It is apparent from the language used in the Holiday Lake case that this Court was concerned primarily with the effects of money collected by the utility company from its ratepayers and

the uses to which that money was put--not with the accounting technicalities employed by the utility company. Generally accepted utility accounting practice requires that utility companies record both depreciation expense and accumulated depreciation on CIAC regardless of whether the regulatory commission considers such accounting entries in determining rates. Petitioner's Brief, p. 20.

Neither the recording of the accounting entries nor the consideration of such entries by the regulatory commission in determining rates, however, provides the utility company with cash that will be available to reinvest in its utility plant, pay off its loans or return to its owners as a return of capital, as this Court discussed in the Holiday Lake case. Therefore, the crucial fact that was required to be considered by the Commission and in the First District in the instant case in order to comply with the requirements of the Holiday Lake case is whether the Utility, in fact, received cash from the allowance of the depreciation expense on CIAC. The record shows that it did not [infra, p. A-33].

The very real distinction between authorization to recover depreciation expense and the actual collection of that expense from the ratepayers is analogous to the practical difference between possession of a money judgment, and the ability to collect on that judgment. No one would argue that the entry of a judgment by a court is equivalent to collection of money from the defendant. Most attorneys have had too many experiences to the

contrary not to know the difference, yet Public Counsel equates the Commission's allowance of depreciation expense with actual receipt of payment of such expense by the Utility.

IV.

THIS COURT'S HOLIDAY LAKE AND WESTWOOD LAKE DECISIONS ALLOW DEPRECIATION ON CIAC TO BE CONSIDERED IN DETERMINING RATE BASE.

The Commission's treatment of accumulated depreciation on CIAC in rate base in the instant case (i.e., use of the "add-back") accords with this Court's holdings in the cases of Holiday Lake and Westwood Lake, and it complies with the essential requirement of law. Moreover, the record in the instant case is sufficiently different from those in Holiday Lake and Westwood Lake to distinguish this case from the earlier cases and to place it squarely within the exceptions affirmed in Holiday Lake.

In Holiday Lake the Commission was engaging simultaneously in two accounting procedures: allowance of depreciation on CIAC as an operating expense, and the so-called "add-back" of accumulated depreciation on CIAC to the rate base. It was this combination of accounting procedures that this Court found to be impermissible in Holiday Lake.

A review of this Court's opinions in both Holiday Lake and Westwood Lake reveals that there can be no doubt that depreciation on CIAC may properly be considered in determining rate base. In its earlier opinion in Westwood Lake, for example, this Court clearly recognized that "[t]he rate base may . . . take such matters [as depreciation on CIAC] into account in fixing the rates." Id. at 11. The Court went on to observe:

> . . . to disregard arbitrarily that part of a utility's equipment because it was "contributed" and to allow no recognition of its replacement ignores reality; it would only mean a raise in rates later on when it became necessary to replace it. A depreciation loss factor may be proper if necessary to prevent a resulting unfair rate, because its purpose is to save against loss and this must be anticipated. [Idem.]

This Court concluded that:

> a loss factor by way of depreciation may be taken into account in a fair and reasonable manner which would give consideration to the "contributions" here IF it takes that (or a portion of it) to assure a rate of fair return. [Id. at 12; original emphasis.]

In Holiday Lake, this Court subsequently affirmed the propriety of considering depreciation on CIAC in the rate-base calculation:

> The Commission also properly allows the utility to include the accumulated depreciation of the facilities purchased from investment and CIAC funds in the rate base calculation. In this way the utility is provided with the cash necessary to replace the property as it wears out. Therefore, the total dollar amount of investment and CIAC property stays constant over time, as does the rate base. This is as it should be, since the ratepayers are paying for the cost of using up the equipment which provides services. [Id. at 725.]

In fact, the Commission's consideration of depreciation on CIAC was approved by this Court in Holiday Lake, but in the form of the then-permitted practice of treating depreciation on CIAC as an operating expense:

> In calculating respondent's rate of return, the Commission determined the original cost of the utility's plant and subtracted the amount representing CIAC funds. The Commis-

> sion also allowed respondent to claim as an operating expense depreciation upon facilities purchased from investment capital and CIAC funds. Neither of these practices is at issue in this case. [Id. at 724.]

In the instant case, however, this method of taking CIAC into account was foreclosed, as the Commission no longer permitted the Utility (or any water or sewer utility) to treat depreciation on CIAC as an operating expense. Therefore, only the "add-back" procedure remained as a viable alternative to the depreciation expense approach formerly used by the Commission, provided that concurrent use of the "add-back" and the expense approach did not occur, as was forbidden in Holiday Lake.

In Holiday Lake, this Court specifically reaffirmed that "depreciation of contributed property may be considered in rate base if necessary to prevent an unfair rate" [id. at 726], quoting Westwood Lake approvingly, and stating:

> In the instant case the proper accounting method includes a depreciation loss factor on contributed assets in the rate base. The problem giving rise to this dispute, unlike the situation in Westwood Lake, is the reintroduction of CIAC property into the rate base over and above its depreciation value. [Id. at 726-727.]

From the foregoing language it is obvious that this Court was confirming that it was the combination of the two CIAC-related procedures that constituted the Commission's error.

This Court's opinion in Holiday Lake recognized that even the proscribed combination of depreciation on CIAC-related procedures ("add-back" and depreciation expense) is permissible in some situations, provided that there also exist "offsetting factors":

> Respondents have failed to produce evidence of offsetting factors which would neutralize this practice and the harmful effects that ensue from allowing utilities to earn a return on contributed capital. In the absence of such factors the rates remain unjust and unreasonable. . . . [Id. at 727.]

One would be hard pressed to imagine a more significant "offsetting factor" than the disallowance of depreciation on CIAC as an operating expense, and the Commission and the First District properly treated it as such. In fact, the Commission stated in Order No. 9443, which is incorporated by reference in Order No. 9533 in the instant case, that ". . . we are concerned with the impact on the utility of the double effect [of] disallowing depreciation on CIAC as an expense and reducing rate base at the same time." Order No. 9443, at Sheet Eight [infra, p. A-29].

In the case below, Judge Booth succinctly stated the position of Public Counsel as follows:

> On appeal, Citizens contend that PSC erred in permitting Utilities to include in their rate base an "add-back" of accumulated depreciation on contributions-in-aid-of-construction (CIAC), citing Citizens of the State of Florida v. Hawkins (Holiday Lakes) [sic], 364 So.2d 723 (Fla. 1978). [Jacksonville Suburban, at p. 372.]

Judge Booth then stated that the contention of Public Counsel was without merit and that it had been rejected in a previous decision of that court, wherein the court distinguished the Holiday Lake case as follows:

> This contention has no merit. A similar argument was rejected in Citizens of the State of Florida v. Florida Public Service Commission, 399 So.2d 9, 11 (Fla. 1st DCA 1981) (General Waterworks), wherein this

court distinguished the Holiday Lakes [sic] case and held:

> [D]epreciation is not merely a measure of the recovery of investment; rather, it also reflects deterioration of equipment, which, inevitably, will have to be replaced. Here, by utilizing the PSC's formula for rate base the utility can make provisions today for the replacement of property as it is retired from service. The formula allows the utility to receive a fair return on its investment and in no way penalizes the rate payers who are paying for the cost of using up the equipment which provides them service.

Accord, Westwood Lake, Inc. v. Dade County, 264 So.2d 7 (Fla. 1972). [Jacksonville Suburban, at p. 372.]

In the General Waterworks case, Judge Liles stated the position of Public Counsel as follows:

> . . . [T]he Public Counsel is before this Court urging that we disallow a rate base which includes "add back" of accumulated depreciation attributable to contributions-in-aid-of-construction (CIAC). [Id., at p. 10.]
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> . . . Public Counsel maintains that this is that type of "double-dipping" prohibited by the Supreme Court in Citizens of the State of Florida v. Hawkins (Holiday Lakes) [sic], 364 So.2d 723 (Fla. 1978). [Idem.]

The First District then explained the reasons why the General Waterworks case is factually distinguishable from the Holiday Lake case, as follows:

> First, and most importantly, Holiday Lakes [sic] is factually distinguishable because there the PSC, in addition to allowing the

> add-back into the rate base, also allowed the utility to treat that depreciation on CIAC as an operating expense. In this case, however, the PSC did not allow depreciation on CIAC as an operating expense. This difference in treatment is important. The practice of allowing CIAC depreciation as an operating expense instead of allowing the add-back in the rate base would lead to a greater revenue requirement for the utility and, consequently, higher rates for the utility's customers because a utility receives a dollar-for-dollar return on operating expenses, but only a percentage on its rate base. [Idem.]

The First District also distinguished the General Waterworks case from the Holiday Lake case because, contrary to this Court's finding in the Holiday Lake case, there was in the General Waterworks case evidence of "offsetting factors" that would neutralize the practice of adding back accumulated depreciation on CIAC into the rate base and the effects therefrom:

> Further, while the practice of allowing depreciation on CIAC as an operating expense was not at issue in Holiday Lakes [sic], the end result of that case disallowed the add-back in the rate base so as to prevent the utility from double-dipping. Accordingly, we think that the PSC's present practice of disallowing depreciation on CIAC as an operating expense constitutes an offsetting factor "which would neutralize this practice (adding back accumulated depreciation on CIAC in the rate base) and the harmful effects that ensue from allowing utilities to earn a return on contributed capital." Id., at 727. [Idem.]

V.

PUBLIC COUNSEL HAS MISPERCEIVED THE LEGAL EFFECT OF HOLIDAY LAKE IN THE INSTANT CASE.

Throughout his brief, Public Counsel has failed to recognize the most significant factor involved in the Holiday Lake case. From both his analysis of the case and his application of it in numerous hypotheticals, illustrations and examples, it is apparent that Public Counsel has failed to perceive that the very foundation of this Court's decision in the Holiday Lake case included the twin assumptions of actual collection by the utility company of the amounts allowed as depreciation expense on CIAC, and actual payment of such amounts by the utility's customers.

The complete failure to recognize the critical factor of actual receipt of money, so thoroughly discussed by this Court in Holiday Lake, makes the numerous hypotheticals, examples and illustrations contained on pages 4 through 20 of Petitioner's Brief of little value in resolving the issues presented in the present case. For instance, Public Counsel refers to:

> 1. "[E]ach deposit and withdrawal" in a savings account. [Petitioner's Brief, p. 4; emphasis added.]
>
> 2. "'Withdrawals' by the utility." [Idem.; emphasis added.]
>
> 3. "The investment [in a savings account] would be determined by subtracting the accumulated total of the $100 principal withdrawals from the initial $1000 deposit." [Id. at p. 5; emphasis added.]
>
> 4. In Hypothetical I, the following references are made: "the company collects $300 from its customers"; "the company will

> then have $220 cash at the end of the year"; "Assuming there is no re-investment (and no taxes), the company will distribute the entire $220 to the shareholders . . . ."; "The following year they will be entitled to earn 12% on only $900 because $100 of their initial $1000 investment has already been returned to them . . . ."; "At the end of the 10-year life of the plant, the company will have no more investment to earn on, having had their full $1000 investment returned in ten $100 installments." [Id. at p. 6; emphasis added.]
>
> 5. In Hypothetical II, Public Counsel refers to "$148 to be distributed to the investor"; "$100 distributed to the investor"; and "customers had paid $100 in depreciation expense." [Id. at p. 9; emphasis added.]

As Public Counsel continues in the course of his brief to attempt to demonstrate the application of the Holiday Lake principles to his hypothetical examples, he completely ignores the fact that both his examples and the Holiday Lake case emphasize cash receipts and payments, by discussing "total authorized depreciation expense" [Petitioner's Brief, p. 10]; the amount of "depreciation expense [that] was authorized" [id., p. 11]; "the full amount of the accumulated depreciation account" [idem.]; and many other references too numerous to quote.

Public Counsel then emphasizes the confusion in his hypothetical examples and his failure to distinguish between cash received and depreciation expense authorized:

> The result is precisely as fairness dictates because the accumulated depreciation account is the total of the depreciation expense authorized to be taken by the investor . . . . It should be fully removed from the initial investment to accurately reflect the remaining investment.

> The former Commission policy had the astounding result of requiring the customers to pay twice for the same property. . . . The utility would be extracting the full price of the pipes from the customers a second time. [Petitioner's Brief, pp. 11-12; emphasis added.]

Nowhere does Public Counsel attempt to demonstrate or even to argue that the depreciation expense authorized resulted in cash received by the Utility, as was so clearly the situation in the Holiday Lake case.

An examination of the other hypotheticals, examples and illustrations, and the attempted application of the Holiday Lake principles to them contained on pages 11-20 of Public Counsel's Brief, reveals the same confusion. Continued use of references to cash receipts and cash payments interchangeably with references to depreciation expense authorized and accumulated depreciation makes the examples and comparisons contained on pages 4 through 20 of Petitioner's Brief particularly inapposite for the purposes of this case. Certainly the making of accounting entries by the Utility and the authorization of rates by the Commission cannot be equated to the collection of money from the customers of the Utility. Although Public Counsel attempts to equate the accounting debit and credit entries for depreciation expense and accumulated depreciation to his "admittedly simplistic" savings account example [Petitioner's Brief, p. 5], it is too clear for debate that accounting entries do not equal cash received or cash paid. The record below clearly demonstrates that such money was not received by the Utility [infra, p. A-33].

Obviously, the making of accounting entries on the records of the Utility does not produce any payment by the customers, nor does the mere allowance of depreciation expense on CIAC by the Commission produce any payment by the customers. It is only the collection of money from the customers that results in any payment by the customers. Public Counsel acknowledges this distinction when he volunteers that the accumulated depreciation balance that has accumulated after the Commission began disallowing CIAC depreciation expense should not be removed from the original investment. Petitioner's Brief, at p. 21.

At page 17 of Petitioner's Brief, Public Counsel states:

> From the time that the Commission began disallowing depreciation expense, the accumulated depreciation should be added back; for the time during which the utilities were entitled to collect CIAC depreciation expense, the accumulated depreciation should not be added back. [Emphasis added.]

This new formulation illustrates again the basic error in Public Counsel's analysis in that it equates mere entitlement to collect CIAC depreciation expense with the actual collection of such expense. Such an approach ignores the very reality that Public Counsel claims to be recognizing, that is, accounting for the actual return of investment to the Utility's investors.

This Court did not hold in Holiday Lake, as Public Counsel now contends, that to the extent that depreciation expense was "authorized" it must be removed from rate base. In order for application of this Court's decision in Holiday Lake to reflect fairness both to the ratepayers and to the Utility, any amount of

the accumulated depreciation on CIAC account used to reduce rate base necessarily must be only the amount that the customers actually paid and that the Utility actually received for the depreciation expense. Fairness certainly would not dictate that depreciation expense recorded on the books of the Utility, but not collected from its customers, be used to reduce the amount of money that the Utility invested in its utility plant in determining its rate base.

VI.

THE INSTANT CASE INVOLVES "OFFSETTING FACTORS" OF THE KIND IDENTIFIED BY THIS COURT IN HOLIDAY LAKE.

Both the Commission and the First District have determined that the record in the present case provides sufficient evidence of "offsetting factors" to make the present case distinguishable from that in Holiday Lake. The First District specifically addressed several of the objectionable factors that this Court found in the Holiday Lake case. Instead of rejecting this Court's reasoning, as Public Counsel continues to suggest through his comparison of supposedly parallel language [Petitioner's Brief, pp. 31-32], the First District found that there was evidentiary support in the record for making distinctions between Holiday Lake and the present case:

A. This Court stated in the Holiday Lake case:

> "This procedure reintroduces CIAC into the rate base structure . . . ." [Id. at p. 725.]

The First District, in the present case, directed attention to its decision in General Waterworks, where it found:

"PSC's allowance of the add-back does not reintroduce CIAC into the rate base. Rather, it completely eliminates its influence!" [Id. at p. 11.]

The First District reached this conclusion BECAUSE

(1) the evidence presented to the Commission led to the final determination of the Commission that, in reality, no depreciation expense on CIAC was ever allowed by the Commission, but rather, a mislabeling occurred in an attempt to allow utility companies an attrition allowance and an additional amount of cash flow [infra, p. A-28];

(2) the uncontradicted evidence in the present case shows that the Utility never earned its allowed rate of return and, therefore, never collected the depreciation on CIAC from its customers [infra, p. A-33]; and

(3) The mislabeled attrition allowance did not reduce the investment in assets made by the Utility [infra, p. A-28].

B. This Court stated in the Holiday Lake case:

"This procedure . . . results in a windfall to the utility . . . ." [Id. at p. 725.]

The First District, in the present case, directed attention to its decision in General Waterworks, where it found:

"The formula allows the utility to receive a fair return on its investment. . . ." [Id. at p. 11].

The First District reached this conclusion BECAUSE

(1) the Commission in the present case did not allow depreciation on CIAC as an operating expense [infra, p. A-26];

(2) the Commission recognized the fiction of providing depreciation for cost-free

assets and determined that to reduce the value of real dollar investments by the total amount of the fictional depreciation allowed on CIAC in the past would be to perpetuate the mistakes of the past [idem.];

(3) allowing depreciation on CIAC as an operating expense in the past was, in fact, an attrition allowance to provide additional cash flow to the utility [idem.];

(4) the uncontroverted evidence demonstrates that during no year that the utility was regulated by the Commission did it actually earn the rate of return allowed to it by the Commission [infra, p. A-33];

(5) the Commission's method of handling depreciation on CIAC does not allow the utility to recover through depreciation the cost of property contributed by the ratepayers [infra, p. A-26];

(6) to the extent that CIAC has been used up, the utility is not penalized by subtracting a "double deduction" from its rate base [idem.];

(7) the uncontroverted evidence in the record demonstrates that the utility has not even collected the full cost of the service provided to the ratepayers because it has not earned the full amount of the rate of return allowed to it by the Commission [infra, p. A-33]; and

(8) even if the utility was authorized depreciation expense on CIAC, it would not recover the money because of the income tax treatment of the expense [infra, p. A-29].

C. This Court stated in the Holiday Lake case:

> "This procedure . . . results in . . . unfairness to the ratepayers . . . ." [Id. at p. 725.]

The First District, in the present case, directed attention to its decision in General Waterworks, where it found:

"The formula . . . in no way penalizes the rate payers . . . ." [Id. at p. 11.]

The First District reached this conclusion BECAUSE

(1) the Commission's method of handling depreciation on CIAC does not allow the ratepayer to pay twice for his CIAC [infra, p. A-29];

(2) the Commission's method of handling depreciation on CIAC only allows depreciation expense on assets invested by the utility [idem.];

(3) the ratepayers, in fact, have not been charged for depreciation expense on property for which they originally paid [infra, p. A-28];

(4) the ratepayers have not paid any depreciation expense on property for which they originally paid [infra, p. A-33];

(5) the ratepayers have not even paid the full cost of the service provided to them [idem.];

(6) the Commission's method of handling depreciation on CIAC allows the ratepayer the benefit of his contribution over the life of the asset he contributed [infra, p. A-26]; and

(7) because the ratepayers are not charged for depreciation on CIAC, not deducting accumulated depreciation on CIAC from rate base is fair to them [idem.].

D. This Court stated in the Holiday Lake case:

"[T]he ratepayers . . . must pay higher rates in spite of their contributed capital." [Id. at p. 725.]

The First District, in the present case, directed attention to its decision in General Waterworks, where it found:

> "[T]he rate payers . . . are paying for the cost of using up the equipment which provides them service." [Id. at p. 11.]
>
> The First District reached this conclusion BECAUSE
>
> (1) the ratepayers originally paid for the contributed capital but since then have not been charged an additional amount for the use of the CIAC [infra, p. A-28];
>
> (2) the ratepayers originally paid for the CIAC, and the CIAC is being used to provide them service without any additional cost of the CIAC being collected from the ratepayers [infra, p. A-26]; and
>
> (3) the Commission's method of handling depreciation on CIAC resulted in lower rates than if the Commission allowed depreciation expense on CIAC [General Waterworks. at p. 10].

In summary, the First District's opinion and the Commission's order in the case below are replete with "offsetting factors which would neutralize this practice [of not reducing rate base by accumulated depreciation on CIAC] and the harmful effects that ensue from allowing utilities to earn a return on contributed capital." Holiday Lake, at p. 727. Therefore, the First District's decision is in complete accord with this Court's decision in the Westwood Lake case and the Holiday Lake case, and with the First District's decision in the General Waterworks case.

VII.

THE FACT THAT WHAT THE COMMISSION LABELED AS "DEPRECIATION EXPENSE" WAS REALLY AN ATTRITION ALLOWANCE PRECLUDES DENIAL OF THE "ADD-BACK."

In his brief, Public Counsel argues that the Commission permitted the Utility to collect from ratepayers depreciation on CIAC as an operating expense. Public Counsel then suggests that this Court should order the Commission to remove from the Utility's rate base the amounts contained in its account labeled "accumulated depreciation on CIAC," but only for the years during which the Commission authorized depreciation on CIAC as an operating expense.

In his discussion of Order No. 9443 entered by the Commission in the General Waterworks case, Public Counsel ridicules that order and the finding by the Commission that:

> The facts in this case demonstrate that allowing depreciation on CIAC as an operating expense in the past was not to recover capital invested by the company, because in fact CIAC was charged to the customer. Since no capital was invested by the company in these facilities, in essence, the dollars collected from the customers in the past labeled as "depreciation on CIAC" represented an attrition allowance. [Order No. 9443, at Sheet Seven; infra, p. A-28; emphasis added.]

Public Counsel continues to ignore, however, the fact that the amounts attributable even to the years now under scrutiny never constituted true depreciation expense on CIAC at all, but an attrition allowance.

An examination of the record reveals that collection of true depreciation expense on CIAC from the Utility's customers never

occurred. As mentioned above, the Commission granted depreciation on CIAC as an operating expense only to serve as a form of attrition allowance, rather than to serve as true depreciation on CIAC [infra, p. A-28]. Secondly, the federal income tax effect on the Utility, in and of itself, reduced any amount of so-called "depreciation on CIAC" actually received by the Utility to 54% or less of the amount supposedly collected [infra, p. A-29]. Finally, the record shows that the Utility consistently failed to achieve its allowed rate of return during the subject years of 1974 through 1978, which failure reduced the achieved rate of collection of the amounts denominated as "depreciation on CIAC" even further [infra, p. A-33].

Although Public Counsel now characterizes the Commission's admission that it has treated CIAC depreciation expense as an attrition allowance as "nothing short of the most contrived, twisted logic imaginable" [Petitioner's Brief, p. 26], the Commission's Order No. 9443 in General Waterworks, incorporated by the Commission into its Order No. 9533 and cited by Public Counsel and attached as part of the appendix to his brief, confirms that this is an accurate description of the procedure actually followed by the Commission. Public Counsel suggests that this finding of fact is deficient because adversarial parties were not permitted an opportunity to contest the use of the practice in earlier cases, but it is noteworthy that the finding was made in the General Waterworks case, in which all interested persons were permitted to address the depreciation

expense issue, a case to which Public Counsel was a party, and which Public Counsel chose not to request this Court to review. Following Public Counsel's failure to appeal the First District's decision in General Waterworks, the other parties rightly assumed that the issue of the true nature of the allowance for "depreciation expense on CIAC" granted by the Commission lay in repose. Therefore, it now sounds a bit hollow for Public Counsel to complain, three years later, that the Commission is "making an absolute mockery of the most fundamental rights available to the parties in the adversarial system." Petitioner's Brief, p. 27.

One wonders why, if Public Counsel was so offended by this finding of fact in the Commission's Order No. 9443 in General Waterworks, after fully participating in the public hearings, after arguing his position before the Commission, after appealing the Commission's Order to the First District, and after having his position in that case rejected, Public Counsel did not choose to ask this Court to review that decision several years ago, when it was still timely to do so.

It certainly is reasonable to assume at this point that the Commission's order and the First District's decision in General Waterworks were well supported by the record in that case. Public Counsel did not introduce or elicit, and has not identified, any evidence in this record to support his contention that the reserve account labeled "accumulated depreciation on CIAC" contains a single dollar that was collected from the customers or that should be removed from the rate base of the

Utility. Public Counsel has not even demonstrated that any portion of the amount in such account actually constitutes anything other than an attrition allowance, or that it is equivalent to the "accumulated depreciation on CIAC" referred to by this Court in Holiday Lake and Westwood Lake. In light of the foregoing, Public Counsel should not now be permitted to challenge in this proceeding the Commission's finding of fact in the General Waterworks case concerning the nature of the allowance for "depreciation on CIAC" previously granted by it.

VIII.

THE FLORIDA LEGISLATURE HAS APPROVED THE COMMISSION'S TREATMENT OF THE "ADD-BACK" BY ENACTING IT INTO LAW.

Shortly before the entry of Commission Order No. 9533, appealed in the case below, the Florida Legislature evidenced its approval of the Commission's treatment of depreciation on CIAC by modifying the ratemaking scheme for water and sewer utility companies, as it relates to the treatment of CIAC and depreciation on CIAC. The amendment to Section 367.081(2), Florida Statutes (1980 Supp.), effective on July 1, 1980, provides, in pertinent part, as follows:

> . . . However, the commission shall not allow the inclusion of contributions-in-aid-of-construction in the rate base of any utility during a rate proceeding; and accumulated depreciation on such contributions-in-aid-of-constuction shall not be used to reduce the rate base, nor shall depreciation on such contributed assets be considered a cost of providing utility service. . . . [Ch. 80-99, Section 10, Laws of Fla.]

Conceding that the foregoing amendment is not directly applicable to the present case, it nevertheless is instructive that the Florida Legislature has determined the proper treatment of CIAC by enacting a statute that prescribes precisely the Commission's method below for treatment of depreciation on CIAC in computing rate base and in setting rates. There is no dispute that the present treatment of depreciation expense on CIAC and accumulated depreciation on CIAC is in accord with said statute. If, however, interpretation of the new statutory section is needed, resolution of such issues can best be served by waiting until they are presented to this Court in a case involving the revised statute.

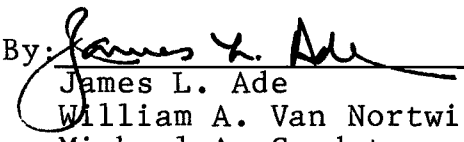
CONCLUSION

Not only did the Commission and the First District below correctly follow this Court's holding in Holiday Lake in applying the legal principles enunciated therein to the determination of the Utility's rate base, but they also correctly perceived the distinguishing factual setting of the instant case: there was no concurrent allowance of the "add-back" with the allowance of depreciation expense on CIAC; the past allowance of "depreciation expense on CIAC" actually constituted an attrition allowance; and there is no evidence that any portion of the mislabeled allowance for "depreciation on CIAC" was ever collected from the customers during the years now in issue. Therefore, Public Counsel's new theory should be rejected, and the decision of the First District in the case below, upholding the treatment of accumulated

depreciation on CIAC in Commission Order No. 9533, should be affirmed and approved by this Court in all respects.

Respectfully submitted,

MARTIN, ADE, BIRCHFIELD & JOHNSON, P.A.

By: 

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished, by U. S. Mail, to each of the following parties of record, this 30th day of July, 1984:

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