O/A 11-7-84

IN THE SUPREME COURT OF FLORIDA

CITIZENS OF THE STATE OF FLORIDA,

Petitioner,

v.

PUBLIC SERVICE COMMISSION,
et. al.,

Respondents.

Case No. 64,680

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APPEAL FROM THE DISTRICT
COURT OF APPEAL, FIRST DISTRICT,
STATE OF FLORIDA

PETITIONER'S REPLY BRIEF

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I. THE MOST REVEALING ASPECT OF APPELLEE PSC'S BRIEF IS THAT IT CHOSE NOT TO DIRECTLY DEFEND THE COMMISSION'S RETROACTIVE CHANGE OF PAST ORDERS WHICH HAD ALLOWED CIAC DEPRECIATION EXPENSE.

More noteworthly than the points raised by Appellee PSC is the major point which the Appellee declined to address. The most glaring omission in the answer brief is the failure to directly defend the Commission's regulatory sleight-of-hand, as explained in detail in the Citizens' Brief on the Merits (p. 26-28). When the Commission realized that this Court had imposed a specific treatment for previously authorized CIAC depreciation expense, rather than follow this Court's mandate, the PSC "solved" the problem by retroactively changing the name of this expense. The Commission's response:

> [T]he dollars collected from the customers in the past labeled as "depreciation on CIAC" represented an attrition allowance.
>
> Order No. 9443, 80 FPSCR 7: at 19.

The Commission's reaction brings to mind the proverbial municipal council which determined to find a solution to the chronic traffic accidents on Main Street. The council changed the name of Main Street to "Avenue A," thus insuring there would never be another accident on "Main Street." Similarly, the Commission simply chose a method to ignore this Court's clear mandate, by renaming what the PSC itself had authorized as CIAC depreciation expense in a multitude of past orders.

It is clear from its in-depth analysis of the matter in Holiday Lake that this Court knew full well the substance, not merely the name, of the authorized CIAC depreciation expense. And, knowing that substance, this Court required that a specific treatment be the result of that CIAC

depreciation expense. The Commission cannot avoid that required treatment merely by retroactively changing the name of previously authorized expense.

It must be kept in mind that the Commission's name-changing is at the very heart of this entire controversy. The change of name was the sole reason given by the Commission to justify the add-back. It was the cornerstone of the offensive policy that motivated this entire appellate process.

Nevertheless, Appellee PSC has chosen not to directly defend the Commission's authority to go back and change every order previously issued that had allowed CIAC depreciation expense. The conspicuous absence of such a defense in the answer brief is indeed revealing.

II. IN ARGUING THAT THE CITIZENS' POSITION CONSTITUTES RETROACTIVE RATEMAKING, THE COMMISSION DEMONSTRATES ITS OWN FUNDAMENTAL MISINTERPRETATION OF THE VERY CLEAR MEANING OF HOLIDAY LAKE.

Appellee PSC argues that the Citizens' assertion that the CIAC should not be added-back constitutes unlawful retroactive ratemaking (See, p. 6-8 of Respondent PSC's Brief on the Merits). It is interesting that this charge comes from the agency which retroactively changed a multitude of orders issued years before to read "attrition allowance" where they had previously read "CIAC depreciation expense." More to the point, however, is that the same treatment which the PSC argues is illegal retroactive ratemaking is precisely the treatment required by this Court in Holiday Lake. All arguments of retroactive ratesetting were presented to, and rejected by, this Court in Holiday Lake.

The Commission's retroactivity argument rests solely on its conclusion that in Holiday Lake, the only reason this Court prohibited the add-back was that it expected future collections of CIAC depreciation expense would be allowed. On page 6 of its brief, the Commission states its interpretation:

> To offset the continuation of [CIAC depreciation] expense in the new rates, the Court reduced the rate base by the amount of accumulated depreciation on CIAC.
>
> [Emphasis added].

Strikingly, the Commission is careful not to point out any specific reference in Holiday Lake to support its interpretation. The very good reason for the Commission's omission is that no such reference exists. Nowhere does the Court state or imply that the prohibition of the add-back

is premised upon future collection of CIAC depreciation expense. To the contrary, this Court explicitly stated the issue as being dependent on the Commission's previous depreciation policy.

> What is contested by petitioners is the Commission's further practice of allowing the utility to add back into the computation of rate base a figure which represents that portion of previously deducted depreciation attributable to CIAC property.
>
> [Emphasis added]
>
> 364 So.2d at 724

Under its mistaken impression that this Court's concern was with future depreciation expense, the Commission argues that the previous depreciation expense was merely a mistake (in Order No. 9443, the Commission offered that the expense was a "fiction"). The Commission submits that to adjust for this mistake constitutes retroactive ratemaking.

In addition to misreading Holiday Lake, the Commission's confusion is compounded by its failure to understand the inextricable relationship between depreciation expense and accumulated depreciation. At the heart of Holiday Lake is the fundamental accounting principle that the treatment of depreciation expense must be consistent with the treatment of accumulated depreciation. This follows naturally because accumulated depreciation on an asset is nothing more than the accumulated total of the depreciation expense which has been taken since the initial purchase of that asset. Hence, the current accumulated depreciation balance is exactly equal to the total of the previous depreciation expense taken.

The treatment of the current accumulated depreciation balance, therefore, must be consistent with the treatment authorized for the depreciation expense. If last year's depreciation expense was allowed in

rates, then the corresponding accumulated depreciation, which shows on the books this year, must be removed from rate base.

In Holiday Lake, the Court was not attempting to correct a past mistake, it was merely applying to the accumulated depreciation the only treatment which would be consistent with the treatment which had been applied to the depreciation expense that gave rise to that accumulated depreciation.

By the same token, in the instant case the Citizens are not trying to correct a previous error at all. They are merely seeking to apply the only treatment for accumulated depreciation which is consistent with the treatment applied to the corresponding depreciation expense. As in Holiday Lake, the CIAC accumulated depreciation should not be added back in the instant case.

III. THE STATUTORY LANGUAGE CITED BY THE APPELLEES SUPPORTS THE CITIZENS CONTENTION THAT THE ADD-BACK IS IMPROPER.

Both Appellees quote directly from a statute which has been passed subsequent to the beginning of this case (See p. 8, 9 of PSC Brief and p. 37 of Utility Brief). Since both Appellees hasten to add that this Court should not apply the statute which they had just quoted, the Citizens are somewhat at a loss in addressing this point.

The Citizens would happily address the implication of this statute. Contrary to the Appellees' assertions, the statute clearly supports the position of the Citizens in the instant case and the holding of Holiday Lake. The plain language and the legislative history leave little doubt about the requirement that CIAC accumulated depreciation must be treated consistently with the treatment of CIAC depreciation expense, just as the Citizens suggest and just as Holiday Lake requires. If the Commission makes this same error in a future case for which the quoted statute applies, the Citizens will dutifully demonstrate the proper application of the new statute.

In the meantime, however, it seems futile to argue the interpretation of a statute which all parties agree has no application. If the appellees had an argument on statutory grounds, it would seem more logical to quote the statute which does apply.

IV. THE UTILITY'S ASSERTION THAT THE CITIZENS HAVE CHANGED THEIR ISSUE FAILS TO RECOGNIZE THAT THE ISSUE HAS ALWAYS BEEN THAT HOLIDAY LAKE PROHIBITS THE ADD-BACK OF ALL CIAC ACCUMULATED DEPRECIATION THAT ACCUMULATED BEFORE THE IMPLEMENTATION OF THE COMMISSION'S NEW CIAC DEPRECIATION POLICY.

In its Introduction and in its Point I. (see p. 4-12 of Answer Brief of Appellee), the Utility charges that the Public Counsel has changed the nature of the issue presented to this Court. The Utility has apparently misunderstood the argument. Before the Commission, before the DCA, and before this Court, the issue raised is that none of the CIAC accumulated depreciation that accumulated before the Commission changed its depreciation policy should be added back into rate base. The issue has not changed; the argument is not even being cut in a "thinner slice."

On appeal to the First District Court of Appeal, the Citizens argued that none of the Utility's CIAC accumulated depreciation should be added back to the rate base. Both the Utility and the Commission attempted to distinguish the instant case from Holiday Lake by pointing out that in this case the Commission did not allow depreciation expense on CIAC. Neither party pointed out, however, that until the instant case, the Commission had always allowed depreciation expense on CIAC. As the Citizens have by now amply illustrated, the Commission's treatment of any future CIAC depreciation expense can only affect the CIAC accumulated depreciation that accumulates after that new depreciation policy becomes effective.

The First District Court of Appeal, however, missed that subtle point. The DCA fixated on the Commission's new depreciation policy.

> "[I]n this case ... the PSC did not allow depreciation expense on CIAC as an operating expense.
>
> 399 So.2d, at 10.

The lower court missed the most relevant fact of all, namely, that the PSC previously had allowed CIAC depreciation as an operating expense. By overlooking that central fact, the court failed to understand that the previous CIAC depreciation policy should dictate the treatment of CIAC accumulated depreciation that accumulated while that policy was in force; the prospective policy, implemented for the first time in this case, can dictate only the CIAC accumulated depreciation which accumulates after that new policy is implemented.

The lower court simply overlooked this all-important point. The Citizens perceived that the DCA's misunderstanding stemmed directly from its preoccupation with the fact that "the PSC did not allow depreciation expense on CIAC ...." Id.

The Citizens were, of course, stunned by the District Court's misunderstanding and determined to avoid the same confusion in the presentation to this Court. Knowing, therefore, that the Utility and the Commission would again urge distinction, the Citizens sought to explain this point before the confusion could be generated. In their initial brief, the Citizens carefully explained the two very different treatments of CIAC accumulated depreciation which must be followed when: on the one hand, that depreciation accumulated before the Commission changed its policy; and, on the other hand, that depreciation will accumulate subsequent to the implementation of the new policy.

The Citizens' Brief on the Merits should have made it clear that date of the implementation of the new policy is the pivotal point in time. From that point into the future, there is no issue because the Citizens agree that the add back is proper; from that same point back into the past, however, there is an issue. The issue exists from the implementation date into the past because during that period, the Commission allowed CIAC depreciation expense , so there is no factual distinction from Holiday Lake.

Because the date of implementation is pivotal and because the Citizens sought to avoid a repeat of the confusion that swept the District Court of Appeal, the Citizens tried to make it perfectly clear:

> One further nuance must be examined to illustrate a particular area in which a controversy does not exist, but which might create some confusion if not explored. The area upon which no disagreement exists is the accumulated depreciation that has accumulated since the inception of the Commission's new policy.
>
> Citizens' Brief on the Merits, p. 20.

The above proposition is precisely the same as the one raised initially, that is, that none of the Utility's CIAC accumulated depreciation should be added back in the instant case. The "pivotal date" is the factor that makes one single issue out of what the Utility perceives as two separate issues.

Because the new policy was not implemented until the instant case, all of the Utility's CIAC accumulated depreciation filed for this case accumulated prior to the Commission's policy switch. Since none of the CIAC accumulated depreciation as filed for the instant case accumulated subsequent to the new policy, none of it should be added back to rate base.

The Citizens will agree that the first case filed by the Utility subsequent to the instant case will involve a "spilt" CIAC accumulated depreciation account, wherein a portion should be added back and a portion should not. For the instant case, however, all of the accumulated depreciation fits under the old policy and must be treated consistent with the requirements of Holiday Lake.

The Utility is seeking to bind the Citizens in a Catch-22. By presenting the DCA a simplified version of the argument, namely, that no CIAC depreciation should be added back, the Citizens saw that court confused by the Appellees who pointed to an illusory distinction. By attempting at the outset to explain that confusion to this Court, the Citizens have now encountered the charge that the argument has changed.

The issue has not changed. As applied to the instant case, the proposition that no add-back should be allowed is identical to the proposition that no add-back should be allowed which accumulated under the old depreciation policy. That add-back is prohibited, as a matter of law, by Holiday Lake.

V. THE UTILITY'S CONTENTION THAT HOLIDAY LAKE REQUIRED A DEMONSTRATION THAT THE CIAC DEPRECIATION EXPENSE HAD ACTUALLY BEEN COLLECTED OMITS DIRECT STATEMENTS BY THIS COURT THAT DEMONSTRATE THE CORRECTNESS OF THE CITIZENS' POSITION.

In its Points III and V, the Utility contends that Holiday Lake prohibited the add-back only if the previous depreciation expense actually had been actually collected by the utility. The Utility agrees that depreciation expense was allowed, but argues that the expense was not collected because the Utility failed to achieve its allowed rate of return. This fallacious argument is founded upon the Utility's mischaracterization of the Court's holding in Holiday Lake.

The Utility contends that this Court implied that if a company failed to achieve its allowed rate of return, then the add-back is proper. This contention is directly at odds with the language employed by the Court in Holiday Lake. This Court did not examine the past financial statements of Holiday Lake, Inc., to see if that utility ever earned its allowed return. Rather, this Court made the proper assumption that if CIAC depreciation expense had been allowed, then the utility had the opportunity to collect that expense and the CIAC accumulated depreciation could not be added back. This proposition is inescapable from a reading of that opinion in its entirety.

By leaving out selected portions of the opinion, however, the Appellee attempts to demonstrate that this Court required a showing that the utility actually collected each and every dollar of the allowed expense. A look at certain portions omitted from Appellee's brief reveals the fallacy. In

establishing the hypothetical used to demonstrate its principle, the Court gave this central assumption:

> Now assume the utility is allowed to charge depreciation expense on the entire plant, including that portion funded by CIAC .... This is the procedure followed by the Public Service Commission.
>
> [Emphasis added]
>
> 364 So.2d at 725

The foundation for the Court's hypothetical is that the utility was allowed to collect CIAC depreciation expense. The Court's concern was with the procedure used by the PSC in setting rates. Further:

> 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.
>
> [Emphasis added]
>
> Id., at 725, 726.

The Court again makes it plain that the focus is on the expenses which the rates were designed to recover.

As it continues to explain the hypothetical, the Court simply assumes that the expenses allowed by the Commission are collected by the utility. After defining the legal principle through the hypotical which asumed the allowance of CIAC depreciation expense, this Court then applied that legal principle to the facts of the actual case that it had before it. In explaining the actual factual situation before it, this Court again concentrated on whether the expense was allowed.

> The Commission also allowed respondent to claim as an operating expense depreciation on facilities purchased from investment capital and CIAC funds.

[Emphasis added].

Id., at 724.

Unequivocally, the Court was concerned only with what the Commission allowed as an expense, and was unwilling to enter the factual morass surrounding the question of whether actual cash was collected to cover a specific expense.

The Court was prudent, of course, to ignore that question because it simply cannot be answered. The rates are set to give the opportunity to earn a fair return, not to guarantee that return. After rates are set to give a utility the opportunity to earn a fair return, the utility will invariably earn something other than the exact targeted return. The actual earnings are influenced by a myriad of factors, some of which are beyond the utility's control, but many of which directly result from decisions made by the utility itself.

In spite of the unpredictability of the actual earnings, the regulatory framework nevertheless must be applied through internally consistent policies that will result in rates that are fair to utilities and their customers. In making the determination whether a policy is internally consistent, one can only look at the accounting treatment employed by the PSC in designing the allowed rates. As has been shown, the examination of the previously allowed rates was the basis for this Court's holding in Holiday Lake. It is precisely that same examination that the Citizens are seeking to form the basis for a decision in the instant case.

CONCLUSION

The most striking aspect of the PSC's answer brief is that it did not directly defend the validity of the Commission's decision to retroactively change all of the CIAC depreciation expense that had been granted for many years by the Commission. The PSC's retroactive change formed the cornerstone of its rationale for allowing the add-back, yet as Appellee, the PSC provided no justification for the change.

As explained, all of the points which the Appellees have raised are invalid because they are grounded on a mischaracterization of this Court's holding in Holiday Lake, on an insufficient understanding of the concept of depreciation, or on a misunderstanding of the argument raised by the Citizens throughout this appellate process.

The decision of the First District Court of Appeal should be reversed, and this case should be remanded to the Commission for removal of the add-back and a refund with interest of excess rates collected pursuant to Order No. 9533.

Respectfully submitted,

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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 or by hand-delivery to the following parties of record this 24th day of August, 1984.

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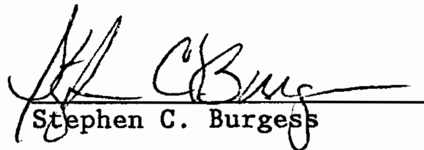

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