IN THE SUPREME COURT OF FLORIDA

GULF POWER COMPANY, Appellant, v. JOHN R. MARKS, et al., in the official capacity as and constituting the Florida Public Service Commission, Appellee.	CASE NO. 66,632

ANSWER BRIEF OF APPELLEE FLORIDA PUBLIC SERVICE COMMISSION

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STATEMENT OF FACTS

Maxine Mine is an underground mine in Jefferson and Walker Counties, Alabama (Tr. 124). There are several coal seams in the area of that mine, two of which were actively mined out of Maxine Mine by Alabama By-Products Corporation (ABC) (Tr. 124, Ex. 1, Vol. 1, p. 3). The America seam, which is above the Mary Lee seam and below the Pratt seam, was the first seam to be mined. It was opened under the terms of a 1952 agreement between ABC, as seller, and Alabama Power Company (Alabama), Georgia Power Company (Georgia) and Gulf Power Company (Gulf) as collective purchasers (Ex. 1, Vol. 1, p.3; Ex. 3, Sch. 1).[1]

The original coal purchase minimum was 588,000 tons/year (Ex. 3; Sch. 1). This amount was changed over time. Reserves were dedicated to the original contract and more reserves added (Tr. 132). The coal was estimated to meet an average annual analysis of 13,000 Btu/lb and 3.5% sulfur when adjusted to a 5% moisture basis (Ex. 3, Sch. 1). For price adjustment purposes, however, Btu was set at 12,750 Btu/lb minimum and 12,900 Btu/lb max (Tr. 127). If the average annual Btu content failed to meet the minimum, the price was to be adjusted pro rata during the next year (Tr. 127).

The original term of the contract was 15 years from the date

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[1]Gulf Power Company is a wholly owned subsidiary of the Southern Company, a holding company which owns three other electric utilities (Tr. 682, 683). These three utilities are Alabama Power Company, Georgia Power Company and Mississippi Power Company.

of commercial operation (June 1954), and would have terminated June 1969 (Tr. 126). There was a rewrite of the contract in 1954 that extended its term until June 1974. The purchasers were also given an option to extend the contract another ten years or earlier if the recoverable coal was earlier mined out (Ex. 3, Sch. 5). The option was to be exercised at least 6 months before June 1974. The contract required that, at termination, the buyers were to pay ABC for any unamortized development cost and the book value of equipment and structures (Ex. 3, Sch. 5).

Georgia relinquished its deliveries to Alabama until January 1955. All three companies executed an agreement in August 1956 providing that after 1960, each party was to take one-third of the output of the mine (Tr. 132, Ex. 1, Vol. 1, p. 14). During 1956, capital expenditures were approved that increased the mine's capacity to 1,056,000 tons/year (Tr. 132).

In 1963, the purchasers entered into an agreement reducing Gulf's deliveries to 16% of output in 1964, and 0% thereafter. Georgia's deliveries were eliminated from 1964 on (Tr. 132, Ex. 1, Vol. 1, p. 15). This agreement obligated Gulf and Georgia to pay Alabama the cost of Maxine coal in excess of alternative sources of coal to Alabama (Tr. 134).

Gulf entered into the 1963 Agreement in order to purchase other coal at lower prices (Tr. 137, Ex. 1, Vol. 1, p. 26). The 1963 agreement was not an amendment to the contract with ABC, but a separate agreement among the purchasers (Tr. 133, Ex. 1, Vol. 1, p. 19). Technically, Gulf Power remained obligated to purchase coal from ABC (Ex. 1, Vol. 1, p. 24).

Excess cost payments under the 1963 agreement were made by Gulf to Alabama from 1964 through 1969 (Tr. 135, 136)). During the period 1964-1967, Gulf purchased alternative coal that produced a net saving over Maxine Coal, including the excess cost payments (Ex. 3, Sch. 26). Gulf took some Maxine Mine production during 1968 and 1969, replacing the balance of its needs with natural gas (Tr. 138).

In 1969, Dekoven Mine, a Gulf supplier, suffered a severe mine fire which shut down production (Tr. 139). Gulf began to operate at dangerously low inventory levels (Tr. 139). Gulf directed Southern Services to conduct an economic analysis of alternative sources (Tr. 139).[2] The results were shown in a 1970 study (Ex. 1, Vol. 1, p. 32). The study recommended that Gulf take Maxine Mine coal as the most economic alternative, citing Maxine's lower cost and reliability. The report projected that Gulf would make excess cost payments to Alabama from 1970 through 1974. The report shows that the only factor that makes Maxine less expensive than alternative coal is the excess cost payments that would have to be paid under the 1963 agreement if coal other than Maxine was purchased (Tr. 141). Gulf reactivated its Maxine Mine deliveries and, in 1972, all three companies executed another agreement releasing Georgia completely and formally reinstating Gulf's

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[2]Southern Company Services, Inc., is a wholly owned subsidiary of the Southern Company and provides technical services to the four operating companies and the Southern Company (Tr. 682). Among other services, Southern Services provides fuel procurement services, including the advice in the selection and administration of contracts.

one-third share of Maxine output (Tr. 141, 142, Ex. 1, Vol. 1, p. 39).

In May 1972 Southern Services recommended that the Maxine contract be extended and that Alabama exercise its Pratt option (Ex. 1, Vol. 1, p. 44). The Pratt option was extended to Alabama by ABC and involved the mining of the Pratt seam, which overlaid the America seam. Southern Services also transmitted ABC's estimates of production volume and cost of a combined America/Pratt operation (Ex. 1, Vol. 1, p. 44d).

On May 17, 1972, George Layman of Gulf recommended that Gulf participate in the extension (Ex. 1, Vol. 1, p. 45). Gulf advised Southern Services that it was interested in the extension, but that the details had to be worked out (Ex. 1, Vol. 1, p. 45a). Gulf was concerned about the impact of the proposed Pratt seam operation on its America seam receipts. (Tr. 649). America seam production had originally been projected to last until 1977 at a rate of 1.4 million tons/year (Ex. 1, Vol. 1, p. 44e). The Pratt operation was expected to begin in 1975 and slow America seam output significantly, creating a production gap from 1980 through 1986 (Ex. 1, Vol. 1, p. 44e). Gulf wanted to obtain its normal volume of America seam coal as if Pratt never existed (Tr. 403, 649, 650).

In July 1972, Gulf and Alabama agreed that Gulf would participate in the extension of the contract, receive its proportionate share of America seam coal, receiving Pratt seam coal for three years (through 1977) and then terminate its participation in the mine (Ex. 1, Vol. 1, p. 45a, 54).

In November 1972, Gulf and Alabama agreed to an increase in ABC's rate of return under the 1952 contract. The return on debt was increased from 4% to actual cost for new investment (Ex. 3, Sch. 13).[3]

In December 1973, Southern Services advised Alabama and Gulf of the need to provide formal notice to ABC of their option to extend the contract. It also requested Alabama to expressly concur in Gulf's limited participation in the extension (Ex. 1, Vol. 1, p. 47f). Alabama expressly concurred in Gulf's limited participation and approved notice to ABC (Ex. 1, Vol. 1, p. 47l). Gulf authorized Southern Services to give notice of extension limiting Gulf's participation until 1977. Gulf stated that it approved this procedure in early 1977 and formalized its intent in November 1977 (Ex. 1, Vol. 1, p. 54).

Southern Services gave notice of extension to ABC on December 31, 1973 (Ex. 1, Vol. 1, p. 47m). The notice indicated that Gulf and Alabama were extending the contract until June 1974 or whenever the coal was worked out, whichever occurred first (Ex. 1, Vol. 1, p. 47m). The notice contained no statement that Gulf would participate only through 1977.

On July 18, 1974, Southern Services transmitted a draft amendment of the Maxine contract to Gulf which formalized the extension (Ex. 3, Sch. 43). On July 22, 1974, Gulf returned the

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[3]The 1952 contract was a "cost plus" agreement. Included in the "costs" were ABC's cost of debt ad equity invested in the mine, fixed by terms of the contract. The "plus" was a fee per ton produced by ABC.

draft amendment, objecting to the fact that it did not limit Gulf's participation in the extension as agreed (Ex. 1, Vol. 1, p. 60). In 1974, production and prices at Maxine Mine appeared stable (Tr. 699). However, mine production began to decline in 1974 and mine labor productivity continued its prior downward trend (Tr. 699). In February 1975, Southern Services returned the amendment to Gulf and urged Gulf to sign it (Ex. 1, Vol. 1, p. 60a). Southern advised Gulf that production rates had slowed, reserves had been added and American seam production was projected through 1984 (Ex. 1, Vol. 1, p. 60a). Southern Service's letter contained projected production rates through 1979 and projected reserves through 1980, but provided no projected costs or other pertinent data (Tr. 1046, 1083, 1084). Mr. Addison signed the amendment for Gulf in March 1974 (Ex. 3h, Tr. 882).

In April 1975, Southern Services provided Gulf with revised production and reserve estimates through 1984 and advised Gulf to sign a revised amendment (Ex. 3, Sch. 45). This amendment was similar to the earlier amendment, except that it raised ABC's return on equity and debt invested in the mine. The revised amendment provided Gulf with nothing more than the earlier amendment. It was, in fact, an addendum to the Pratt contract between Alabama and ABC; an addendum Alabama pledged its best efforts to get Gulf to sign (Tr. 884-886). In May 1974, Southern Services advised ABC that it was imperative that the rate of production from America seam and Pratt seam be substantially improved (Ex. 3, Sch. 46). Gulf signed the revised amendment in February 1976 (Ex. 3, Sch. 18).

Southern Services became concerned about mine productivity in 1976 and those concerns became greater in 1977 (Tr. 699). In 1977, Maxine Mine Coal became Gulf's highest cost coal under a long term contract. Mining plans and projections by ABC received in May 1977 were rejected by Southern Services (Tr. 700). Revised projections and budget were received in October 1977 (Tr. 700). Southern Services advised Gulf and Alabama not to approve the budget for the mine (Tr. 700). On December 16, 1977 ABC submitted revised cost projections for the mine through termination of America seam operation (Tr. 701). Southern Services then recommended that an independent mining consulting firm be retained to conduct a study (Tr. 701). Gates Engineering Company of Beckly West Virginia was selected (Tr. 701).

By January 1978, Maxine Coal was Gulf's highest cost fuel and Gulf expected the cost to continue to climb (Tr. 674, Ex. 5, Sch. TFJ-6). In a January 16, 1978 Gulf memorandum from George Layman to B.M. Guthrie, it was recommended that the mining of pillars be abandoned, capital expenditures for loaders and substations not be made and that Gulf should accept coal for 1978 and then terminate the agreement (Ex. 5, Sch. TFJ-6). Gates' initial report was received in September 1978, with the final supplement and revision received in May 1979 (Ex. 3, Sch. 19). Gates' conclusions closely paralleled those of Southern Services and were contrary to the ABC position (Tr. 702). In May 1979, Southern Services advised Alabama and Gulf that there was no economically viable alternative but to close Maxine Mine (Tr. 702). In a May 1979, memorandum to Earl Parsons and Herman Witt, George Layman stated that he

concurred in the recommendations made by Southern Services concerning Maxine Mine (Ex. 5, Sch. TFJ-10).

In April 1979, ABC had submitted revised cost and production estimates for Maxine Mine based on a Revised Mode of Operations (Ex. I, Vol. 2, Sch. TF-HA4). Southern Services conducted an economic analysis to determine if it should immediately close the mine or continue operations until June 1984. This report, called the Woodfin Study, was issued December 21, 1979 and stated that operation until June 1984 was the least cost alterative if ABC's costs estimates were not exceeded by more than 5%. The report noted that ABC had consistently underestimated the costs at Maxine Mine and that confidence in the study results were a major concern.

Southern Services placed little confidence in the results of the Woodfin Study. On January 14, 1980, it advised that ABC be told that Alabama and Gulf would participate in the mine through June 1984 if they could cancel when costs exceeded ABC's projections (Ex. 5, Sch. TJF-13).[4] On January 17, 1980, Gulf and Alabama made such a proposal to ABC (Ex. 5, Sch. TJF-13). ABC responded in March 1980, effectively rejecting the proposal (Ex. 5, Sch. TJF-13). On July 17, 1980, ABC stated that it was agreeable to working under the Revised Mode of Operations to close the mine in June 1984 (Ex. 5, Sch. TJF-13).

By 1980, the price paid by Gulf for Maxine coal was the highest of comparable coals purchased by utilities throughout the

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[4]TJF-13 is a packet of letters.

United States (Tr. 171, 172). ABC and Southern Services continued negotiations into 1981. In March 1981, Southern Services formally agreed to ABC's Revised Mode of Operations and termination of the mining operation in June 1984 (Tr. 738).

In April 1981, Gulf requested a meeting with the Commission staff to discuss an unusual expense that would be filed in the fuel adjustment hearings (Tr. 118). At the meeting, Gulf informed staff that it had decided to phase down mining operations of ABC's Maxine Mine due to high production costs, decreasing output and other considerations (Tr. 118).

Gulf proposed to set up an accounting mechanism to accrue the estimated cost of closing and reclaiming the mine and began charging the accrual against the Maxine price in March 1981 (Tr. 120). The accrual would then be included in Gulf's fuel adjustment filing (Tr 120). At the time that Gulf informed the staff of the accrual, the effective price of Maxine coal was $51.57 per ton, again the highest price of comparable coals purchased throughout the United States (Tr. 171). The addition of the accrual increased the effective price to $66.36 (Tr. 121). The staff informed the Director of the Electric and Gas Department of the problem and he authorized a study of the Maxine accrual and price (Tr. 121). During its study, the staff became much more involved in the Maxine contract (Tr. 122). There were several issues raised by staff which could not be satisfactorily answered by Gulf and SCS (Tr. 122). The staff concluded that these unresolved issues should be brought to the Commission (Tr. 122).

Hearings were held before the Commission. Expert testimony

was presented by six witnesses; two for the staff, four for Gulf. Messrs. Foxx and Hill testified in favor of the staff's position that Gulf had acted imprudently under the contract with ABC and that a refund of excess costs should be ordered. Messrs. Gilchrist, Meier, Ludwig and Gibbons testified in favor of Gulf's position that it had acted prudently and that no refund was proper. The Commission was exposed to a full range of viewpoints on nearly every factual and policy question to be considered.

Mr. Foxx, the Supervisor of the Power Plant Efficiency and Fuel Procurement Section of the Commission's Electric and Gas Department, testified as to his opinion of the prudence of Gulf's actions and the level of Maxine Mine's price to other coals. (Tr. 111-554, 1030-1140). Mr. Foxx reviewed the actions of Gulf Power, Alabama Power, Georgia Power and ABC from the inception of the contract in 1952, through its extension in 1974 and, ultimately, to the decision in 1981 to close the mine in 1984 (Tr. 124-223). His principle conclusions were that Gulf Power Company's contract with ABC was unreasonable as to price, improperly administered, imprudently incurred and contained a price component which should not be recovered through the Fuel Adjustment Clause (Tr. 118).

Specifically, he determined that Gulf had acted imprudently in 1975 when it agreed to extend the Maxine contract for the full term without adequate information(Tr. 1047, 1048, 1083, 1084). He determined that it acted imprudently in 1975 when it agreed to participate for the full 10 year extension without reserving any protection for itself (Tr. 159, 168, 268-269, 385-386, 407, 461, 511, 1051). He determined that it acted imprudently in failing to

terminate the contract when prices rose to excessive levels (Tr. 209, 310, 342-344, 350, 383-384, 461, 469, 517, 1059-1060). Finally, he found that the amount of $2,263,928, plus interest, should be refunded by Gulf to its rate payers (Tr. 196, 197).

Gulf's witnesses testified that Gulf acted prudently in administering the contract with ABC (Tr. 559-1024, 1233-1340). They testified that the contract had provided high quality coal, economically priced, with supply and transportation flexibility (Tr. 560, 709). They testified that Gulf acted prudently in extending the contract (Tr. 566, 567). They cited to fuel supply and inventory problems experienced by Gulf in the early 1970's and the Arab Oil Embargo that occurred in the fall of 1973 (Tr. 695).

They testified that Gulf acted prudently in responding to decreasing productivity and high price after the extension (Tr. 731). They testified that ABC would not agree to early termination of the contract (Tr. 735), but that a confrontation was not necessary because Southern Services concluded that the most economic course was to continue through 1984 (Tr. 735).

Gulf's witnesses criticized Mr. Foxx's market price analysis and presented their own analyses designed to show that Maxine Mine coal was competitively priced (Tr. 730, 1256, 1258-1259).

In rebuttal, Mr. Foxx took issue with the conclusions of Gulf's witnesses regarding the prudence of Gulf's actions (Tr. 1035, 1045-1046, 1051, 1053, 1059, 1060, 1068, 1069) and the validity of their price comparisons of Maxine coal (Tr. 1035, 1048-1049, 1062-1066, 1069-1072).

Mr. Hill, an independent consultant employed by the

Commission, testified regarding the methods used by the staff to analyze coal markets and the prudence of Gulf's decision to remain in the Maxine contract through June 1984 (Tr. 1141-1206). It was his opinion that Gulf definitely should have terminated its participation in the mine (Tr. 1180). He testified that it was possible to develop a price that is a reasonable estimate of market for a given type of coal (Tr. 1158). He criticized Mr. Gibbons' analysis (Tr. 1164, 1170). He defended the validity of his analysis (Tr. 1165, 1168). He testified as to his preferred method of developing market price (Tr. 1175).

SUMMARY OF ARGUMENT

The Commission's decision is supported by substantial and competent evidence. The Appellant has merely reiterated the factual arguments presented to the Commission in the hope that this Court will substitute its judgment for that of the trier of facts. When confronted with competing expert testimony the Commission may select the opinion from the competing testimony which is most credible. The Commission found that the Company had acted imprudently in 1975 in extending for the full term of the agreement, and again in 1979 by not terminating its contractual agreement with Alabama By-Products Co., thus incurring additional unnecessary expenses that were passed on to unsuspecting ratepayers.

In determining the amount of overcharges to the customers, the Commission relied upon a study of the market value of the fuels purchased conducted by an expert on the staff of the Commission. The accuracy of the staff study was verified by an outside expert hired by the Commission to give an unbiased opinion as to the validity of the study.

The Commission routinely makes after-the-fact adjustments to fuel expenses. Fuels, are fungible and once in storage, a particular fuel is not readily identifiable as to purchase and is accounted for on an average cost of inventory basis. As such, the fuel adjustment proceeding is a continuous proceeding. Retroactive rate making, res judicata and estoppel by judgment are inapplicable to continuous proceedings. Even if the doctrine of res judicata is applicable to the fuel adjustment proceeding, the

issue of prudence was never raised and litigated, therefore never making the issue of res judicata an operative question. If the Court were to find that the issue of res judicata was raised, the Commission is the appropriate forum to determine the applicability of the doctrine and that finding may only be overturned upon a showing of a flagrant abuse of discretion. The facts in this case show that the Commission must review the fuel purchases of the utilities in order to ensure that fuel is purchased in the public interest. Finally if the doctrine could have been applied, there is a necessary exception to the application of the doctrine. Res judicata will not be imposed as a bar to litigating an issue where the application of the principal will work a manifest injustice on the parties.

The decision of the Commission is supported by substantial and competent evidence and is in compliance with the essential requirements of law and should be affirmed.

POINT I

THE COMMISSION'S DECISION IS SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE.

A. Gulf is improperly asking this Court to reweigh the evidence.

Gulf has simply restated the facts that it presented to the Commission. Its brief is mostly a verbatim transcription of the brief and petition for reconsideration it filed with the Commission. See Appendix A-1, for example. In places, Gulf simply substitutes the word "he," a reference to a witness with the words "the Commission."

What Gulf is asking this Court to do is to give it a proceeding de novo and determine that the record favors its position. This is an obvious case of asking this tribunal to reweigh the evidence rather than demonstrating error below. The role of this Court is to determine whether there is substantial and competent evidence in the record to support the Commission. United Telephone Co. v. Mayo, 345 So.2d 648, 654 (Fla. 1977). This Court has repeatedly stated that it will not overturn a Commission order because it would arrive at a different result had it made the initial decision and it will not reweigh the evidence. Gulf Power Company v. Florida Public Service Commission, 453 So.2d 799, 803 (Fla. 1984).

Our jurisprudential system is based upon the premise that finders of fact are competent to find fact and that reviewing courts should not substitute their judgment for the findings made by a competent agency. This is true even if the reviewing court would have reached a different conclusion had it independently

tried the facts. Florida Retail Federation, Inc. v. Mayo, 331 So.2d 308, 311 (Fla. 1976). It is the Commission's prerogative to evaluate the testimony of competing experts and accord whatever weight to the conflicting opinions it deems necessary. Gulf Power Co. v. Florida Public Service Commission, supra, at 805. The burden on the Appellant seeking to overturn a fact finder's determination is to demonstrate that either the record is devoid of evidence supporting the fact finder's decision or that the evidence relied upon by the fact finder was not substantial or competent. Citizens v. Public Service Commission, 425 So.2d 534, 539 (Fla. 1982). Gulf has failed to meet its burden.

B. The Commission's findings are based upon competent and substantial evidence.

The Commission was presented with conflicting evidence on every issue in the case. The Commission heard the evidence, observed the demeanor of the witnesses, considered the credibility of their testimony and weighed the evidence presented. In its final order, the Commission arrived at three ultimate conclusions that are relevant to this case:

> 1. Gulf Power Company acted imprudently in agreeing to participate for the full term of the extension of the Maxine Mine contract without seeking adequate protection for itself and its ratepayers.
>
> 2. Gulf Power Company acted imprudently when it failed to act to protect its interests when the cost of Maxine Mine coal rose to extreme levels.

> 3. Gulf Power Company's imprudent actions caused it to incur excessive costs for coal purchased from Maxine Mine in the amount of $2,575,540.

Order No. 13452, p. 20 (R. Vol. I, p. 146, Appendix A-2).

These conclusions are based upon detailed findings of fact, findings that are supported by competent, substantial evidence.

Mr. Foxx arrived at several conclusions at the conclusion of his detailed inquiry into Gulf's actions under its contract with ABC. These conclusions, contained within his testimony, are germane to the Commission's findings:

> 1. In 1972, Gulf decided to participate in the Maxine extension based on an agreement with Alabama Power that Gulf's future involvement would be limited to three years. (Tr. 150, 259, 260, 405, 407-408, 410, 466, 507).
>
> 2. Gulf's decision in 1975 to participate for the full ten-year extension was based on inadequate information and was imprudent. (Tr. 1047, 1048, 1083, 1084).
>
> 3. Gulf acted imprudently in 1975 when it failed to properly protect its interests and those of its ratepayers when it signed the ten-year extension. (Tr. 159, 268, 269, 385, 386, 396, 407, 461, 511, 1051).
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> 4. Gulf acted imprudently when it later failed to terminate its participation in Maxine Mine when costs got out of control (Tr. 209, 310, 342, 343, 344, 350, 383, 384, 461, 469, 517, 1059-1060).
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> 5. Gulf's imprudence caused it to incur excessive costs for Maxine Mine coal and it should refund the excess cost payment to its ratepayers (Tr. 118, 299, 300, 311, 501-502, 513).

Mr. Foxx's conclusions were based upon the principle that the prudence of a decision should be determined in light of the facts

that were known or should have been known at the time of the decision (Tr. 456).[5] According to Mr. Foxx, a person acts prudently when he acts as any reasonable man, given the same circumstances, same information and same situation (Tr. 456).

Mr. Foxx presented his testimony as an expert in the field of utility fuel procurement and that is how it was received (Tr. 224). Gulf challenged Mr. Foxx's expertise at hearing (Tr. 104-105) and the Commission overruled Gulf's objection (Tr. 110). On appeal, Gulf has made no challenge to Mr. Foxx's expertise.

The Commission treated the events from 1952 through 1974 as pertinent to Gulf's actions under the Maxine Contract, but made no findings on the prudence of Gulf's actions made during that time (Order No. 13452). Instead, it focused principally on Gulf's actions from 1974 through 1981.

There was conflicting evidence placed before the Commission regarding the value of the Maxine Mine contract between 1952 and 1974. Mr. Foxx criticized many aspects of Gulf's actions during that time and questioned the overall value of Gulf's participation in the Maxine Contract during that time (Tr. 132-146).[6] The Commission considered the conflicting testimony offered and found

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[5]The Commission expressly adopted this view of prudence in Order No. 13452. On page 10, the Commission states that it has "looked at the prudence of Gulf's actions in terms of the facts that were known or that should have been known at the time of the decision."

[6]There was no testimony from anyone with direct knowledge of events surrounding this contract prior to 1972. All witnesses viewed such events on the basis of company files and knowledge of company practices.

that the testimony of Gulf's witnesses concerning of Maxine during the 1952-1974 period was "broad and overstated." (Order No. 13452, p. 3).[7]

The Commission's finding that Gulf decided to extend the contract in mid-1972 is clearly demonstrated by the record. Documents taken directly from Gulf's files show that Gulf decided to participate in the extension in July 1972.[8]

A memorandum dated May 17, 1972 from George Layman to Mr. E. L. Addison, Senior Vice-President of Gulf, recommends participation in the extension (Ex. 1, Vol. 1, p. 45; Appendix A-27). A letter dated May 31, 1972 from Mr. Addison to Southern Services expresses Gulf's interest in the extension (Ex. 1, Vol. 1, p. 45a; Appendix A-28). The bottom of that letter shows a handwritten note by Mr. Layman, dated July 17, 1972, which states: "Agreed with A.P.Co. to continue contract...." (emphasis supplied).

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[7]The principle reason the Commission focused on the price of Maxine coal over this period was the repeated references by Gulf's witnesses to the low price of Maxine coal during this period. The discussion from the middle of page three to the top of page four of Order No. 13452 was intended to dispel those references. Of additional note is the fact that Maxine's transportation "flexibility" is common to all Gulf fuel contracts (Tr. 927).

[8]Documentary evidence was fragmented in some places, but not here. However, even when it was fragmented, Gulf failed to call witnesses with direct knowledge of the facts. At least two of the principle actors in Gulf's management were directly involved in the events from 1972 through 1984 and were available to Gulf, yet neither testified. Instead, Gulf presented testimony principally from the perspective of Southern Services using witnesses (with one exception) who had no direct knowledge of the events in question.

The fact that Gulf's decision to extend was made in mid-1972 is confirmed by another exhibit. In response to Southern Services' request for formal approval of a notice of extension to ABC, Gulf states:

> Please proceed with the preparation of notice and the appropriate agreement to the Maxine Mine Contract for Gulf Power Company's participation in the extension until 1977 of its one-third (1/3) share of the output. We expressed our approval of this procedure in early 1972 and formalized our intent by approving the ABC-GWO-M-19 in November of 1972. (emphasis supplied) (Ex. 1, vol. 1, p. 54; Appendix A-29).

Thus, the record clearly supported a finding that Gulf decided to extend the contract in mid-1972.[9]

The Commission determined that a majority of the justifications for the decision to extend given by Gulf's witnesses related to events occurring after it decided to extend. In some cases, the evidence is conflicting, in others it is clear. Regardless, the Commission's decision is supported by competent, substantial evidence.

Mr. Gilchrist testified to problems involving coal supply and inventory occurring in 1973 (Tr. 565, 566 and 567). Mr. Ludwig referred to documents dated January 23, 1973, December 31, 1973 and November 23, 1973 (Ex. 3, Sch. 33, 34 and 35) and documents dated October 1973 and March, September, October and November 1974

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[9]The record is replete with other Gulf documents referring to the earlier "agreement."

(Ex. 3, Sch. 41). Mr. Ludwig's recommendation to file a fuel emergency report was made on February 4, 1974 (Ex. 3, Sch. 42).

Gulf's witnesses repeatedly emphasized the impact of the Arab Oil Embargo on Gulf's decision and relied upon the resulting price escalations to show the prudence of Gulf's decision to extend. Gulf's actual decision to extend preceded the oil embargo by over a year. The embargo occurred in the fall of 1973. Even if Gulf had actually deferred the decision, it still would have had to make a decision by the middle of 1973, before the embargo (Tr. 638, 639).

The Arab Oil Embargo occurred well after Gulf decided to extend the Maxine contract. The sudden rise in alternative fuel costs during the years 1974-1975 was completely unrelated to Gulf's original decision to extend the contract. Gulf's reliance on the oil embargo and other post-1972 events to prove the prudence of its decision to extend is, in its own words, "the epitome of 20/20 hindsight" justification.

The record is clear that until 1975, Gulf fully intended to participate in the Maxine contract for a short time during which it would receive all of its entitlement under the 1952 contract using Pratt coal in lieu of America seam coal (Ex. 1, Vol. 1, p. 54; Appendix A-29). Gulf wanted to receive its coal at the full output of the mine as if Pratt never existed (Tr. 649, 650). This would provide Gulf with one-third of 1.4 million tons/year (Ex. 1, Vol. 1, p. 44e). At that rate, Gulf would have received its proportionate share under the 1952 contract by the end of 1977 (Tr. 411).

When Southern Services provided Gulf with the contract amendment in July 1974, Gulf immediately objected because it did not indicate that Gulf would be relieved of its obligations as soon as it received its proportionate share of the America seam reserve (Ex. 1, Vol. 1, p. 60). In response, Southern Services recommended that Gulf participate until 1984, "rather than termination at an earlier specified date" (Ex. 1, Vol. 1, p. 60a). Southern Services provided a revised estimate of production through 1979 and reserves through 1980. Gulf signed the amendment in March 1975 (Tr. 882). This was almost a month before Southern Services provided it with revised production and reserve estimates through 1984.

Mr. Foxx was of the opinion that Gulf acted imprudently in 1975 when it agreed to the full extension. First, he concluded that Gulf lacked the basic information necessary to extend for the full term (Tr. 1045-1048, 1083, 1084). Second, he concluded that Gulf failed to protect its interests and those of its ratepayers when it signed the extension without any provision protecting itself from future uncertainties (Tr. 268, 269, 386, 396, 407, 461, 466, 511).

According to Mr. Foxx, in order to make a sound business judgment, Gulf needed to know:

1. the volume of coal available through 1984;
2. the annual production volumes;
3. Gulf's proposed share;
4. the quality of the coal;
5. the forecasted mine price; and

6. the cost of comparable coals. (Tr. 1045-1046)

According to Mr. Foxx, at the time it agreed to the full extension Gulf only had production rates through 1979 and reserves through 1980 (Tr. 1046, 1083, 1084).

Mr. Foxx pointed out that Southern Services' February 1975 letter stated that production had slowed and that it is a known fact of mining economics that changes in production rates affect total per unit cost (Tr. 1047). Maxine Mine's production costs for 1974 had been 76% over ABC's original estimate and for 1975 were 127% over estimate (Ex. 1, Vol. 1, p. 44e; Ex. 4, Sch. 3). At the same time, production volumes for 1974 had been 26% below ABC's original projection and for 1975 were 30% under projection (Ex. 1, Vol. 1, p. 443; Ex. 2A) According to Mr. Foxx, Gulf did not have the minimum information with which a prudent evaluation could have been made and extended for the full term without adequate information (Tr. 1047, 1048).

It was Mr. Foxx's opinion that Gulf had an agreement with Alabama to limit its participation in the extension and was imprudent to sign the amendment as written (Tr. 269, 296, 396, 461). He was of the opinion that Gulf could have obtained an amendment protecting its interests, citing to ABC's ability to obtain one-sided amendments in its favor (Tr. 407, 511).[10] He stated that Maxine was an old mine and that Gulf had good

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[10]In 1972, ABC was able to negotiate an increase to its cost of debt, which was fixed by the 1952 contract (Ex. 3, Sch. 13). Again in 1976, ABC successfully negotiated an (footnote continued)

reason to expect costs to rise and production to decline (Tr. 385).[11] He was of the opinion that Gulf acted imprudently in failing to negotiate terms protecting its interests (Tr. 385, 386).

Shortly after Gulf signed the revised amendment providing ABC with an increased rate of return, Southern Services became concerned about productivity and cost problems at Maxine mine (Tr. 699). These concerns became greater in 1977 (Tr. 699). Southern Services began to reject ABC's mining plans and projections (Tr. 699).[12] In November 1978, George Layman noted that Maxine coal was the highest cost of all of Gulf's fuels and recommended that Gulf take Maxine coal for the rest of 1978 and terminate the agreement (Ex. 5, Sch. TJF-6).

In 1978, Gates Engineering was employed to review ABC's mining

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[10] (Cont'd) increase to its cost of debt and equity (Ex. 3, Sch. 18). The 1976 amendment increasing ABC's rates of return was provided in draft form to Gulf in February 1972 (Ex. 1, Vol. 1, p. 60a). In neither of these instances did Gulf or Alabama receive a contractual right in return.

[11] Mr. Foxx's opinion is borne out by correspondence from ABC to Southern Services dated March 26, 1980 (Ex. 5, Sch. TJF-14). There, Mr. Jones reminds Mr. Ludwig that, in adding 5,000,000 tons of America seam to the reserves of Maxine Mine in 1956, ABC advised Southern Services that it did not expect a high production rate to be realistic in later years and that the added reserves were thinner and a greater distance from the mine opening. In fact, Gulf's witnesses confirmed that it was the age of the mine, the thinning of the seams and the distance from the mine mouth that caused production rates to fall and costs to rise (Tr. 610, 611, 689, 1253).

[12] Had Gulf participated in Maxine only through 1977 as it originally agreed, it would have avoided all of the problems that follow.

plans (Tr. 700). In its final report, issued in May 1979, Gates said that the mine had reached the end of its economic life (Tr. 343). It recommended that the mining operation be terminated (Tr. 702). In March 1979, Mr. Layman again recommended a clean break with Maxine (Ex. 5, Sch. TJF-8). In April 1979, Southern Services recommended that the contract with ABC be terminated. Again, Mr. Layman advised that he concurred in that recommendation (Ex. 5, Sch. TJF-10). In May 1979, Mr. Witt advised Mr. Layman that the Southern Services recommendation contained a transportation error that, when corrected, made alternative coals look even better then reported (Ex. 5, Sch. TJF-11).

Mr. Foxx was of the opinion that Gulf should have been out of Maxine between December 1979 and year-end, 1980 (Tr. 207, 383). It was his opinion that the analysis prepared by Gates and Southern Services, as well as Gulf's own recognition of the excessive cost of Maxine, clearly showed that the contracts should have been terminated (Tr. 341, 350, 461, 469, 517). He was of the opinion that the Woodfin study confirmed that the contract should be terminated (Tr. 209). It was his opinion that the contract provided adequate remedies for Gulf (Tr. 310) and that both Gulf and Southern Services personnel believed that the agreement could be terminated (Tr. 342, 343, 469). He was of the opinion that Gulf acted imprudently in failing to act to terminate the contract (Tr. 461, 469, 517-518, 1059-1060).

Mr. Ludwig defended Gulf's decision to continue the contract until 1984. He testified that the Woodfin study demonstrated that the best alternative action for Gulf was to continue through June

1984 (Tr. 735). This, of course, was not what Southern Services recommended. It recommended operation through 1984 if ABC's price estimates held true (Ex. 1, Vol. 2, Sch. TF-HA3).[13] He also testified that ABC refused to acknowledge any right to terminate (Tr. 707).[14] Mr. Foxx questioned Mr. Ludwig's assertions, pointing to Gulf and Southern Services documents advising that notice of termination be given (Tr. 341). He was of the opinion that any termination problems experienced by Gulf flowed directly from Gulf's imprudence in 1975 (Tr. 385, 386).

The Commission determined that Gulf should have acted to terminate its interest in Maxine in mid-1979 and, assuming a one-year termination requirement, should have ended its purchases of Maxine coal by mid-1980. It further determined that any termination problems encountered by Gulf were caused by its imprudent actions in 1975 and 1976.

Having determined that Gulf acted imprudently and should have been out of Maxine Mine by Mid-1980, the Commission had to determine the impact of Gulf's imprudence on the fuel costs it passed onto its ratepayers. According to Mr. Foxx, a comparison of Maxine prices to other coals yields a "premium" which should be

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[13]The Commission rejected Mr. Ludwig's claim that the Woodfin study justified operation through June 1984. On appeal, Gulf does not question this finding, apparently conceding that it is correct.

[14]He even went so far as to sponsor the hearsay opinions of counsel employed by Southern Services, who responded with written opinions drafted over a year after negotiations between ABC and the power companies ended and after the proceeding below was commenced.

refunded (Tr. 299, 300). According to Mr. Foxx, the purpose of the premium is not to penalize Gulf but to require Gulf to refund imprudent expenditures (Tr. 501-502). The Commission adopted this "market price" approach proposed by Mr. Foxx.

There is no legitimate dispute as to whether the cost of Maxine Mine coal was excessive. At the initial meeting between the staff, Mr. Hill and Southern Services, Mr. Ludwig said that a study wasn't needed to show that Maxine was over market. He said that anyone familiar with the coal market will agree that Maxine's prices are over market (Tr. 1178). This was reiterated in Mr. Ludwig's direct testimony where he stated that a special study was not required to show that the cost of Maxine coal has been higher than alternative sources in the past three years (Tr. 753). Mr. Gilchrist said, "we realize Maxine was above the market..." (Tr. 600). Even Mr. Gibbons, who caustically criticized the staff's approach, stated that the price has been way outside market for the last three years (Tr. 1333).

The Commission was presented with conflicting opinions as to how to calculate the market price for a coal and the reliability of certain data. It ultimately chose to rely upon an analysis of delivered prices prepared by Mr. Foxx.

Mr. Foxx had originally proposed to establish market price using an F.O.B. mine price analysis (Tr. 196, 197). His F.O.B. mine analysis took delivered price data and backed out transportation costs to derive an F.O.B. mine price (Tr. 174). This F.O.B. mine price was the combined with F.O.B. mine prices obtained from Coal Week, an industry publication (Tr. 179,

186).[15] Mr. Foxx then applied a 20% margin of error in favor of Gulf to account for the variability inherent in the market data he used in his F.O.B. mine analysis (Tr. 297).

The Commission ultimately decided to rely on delivered price as a measure of market price. It was thus able to avoid the question of reliability attached to Coal Week, as well as the effect of transportation differentials. Mr. Foxx developed his delivered price analysis by a computer analysis of representative coals purchased under long-term contracts through the United States, as reported to the Federal Energy Regulatory Commission (FERC.) on its Form 423 (Tr. 167). In making the analysis, Mr. Foxx specified coals with Btu content, ash content and sulfur content comparable to Maxine Mine coal (Tr. 166, 167). It was Mr. Foxx's opinion that a nationwide sample of coal transactions yielded a valid market price (Tr. 362-365, 1036-1037, 1080). If was his opinion that the narrower samples and spot prices used by Gulf's witnesses were not valid (Tr. 167, 360, 361-362, 364, 365, 1065).

The Commission's decision to rely upon a weighted average price under the FERC Form 423 delivered price analysis was based directly upon the testimony of Mr. Foxx. It was Mr. Foxx's opinion that a market price using FERC Form 423 data should be

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[15]Mr. Foxx's F.O.B. mine analysis was subject to strong criticism, particularly due to its use of Coal Week data (Tr. 967, 1262). The Coal Week data was attacked as not accurate (Tr. 967, 987, 1262, 1265-1266). In addition, use of an F.O.B. mine analysis was criticized as ignoring transportation differentials (Tr. 1256, 1257).

calculated on the basis of the weighted average price of the coals selected (Tr. 170, 279). Payments by Gulf above that price would be excessive (Tr. 170). Mr. Foxx was of the opinion that the average would be most representative of the population used (Tr. 482). Rather than use extremes, a weighted average is used, effectively balancing out the good and the bad (Tr. 483).

Gulf criticizes the Commission's use of weighted average as statistically unacceptable (Brief at 37).[16] However, no witness who was competent to testify on statistical theory ever made such a claim.[17] In fact, Gulf's entire argument on the requirement to use standard deviations about the mean was not supported by any qualified expert. Mr. Hill simply stated that use of standard deviations might be better (Tr. 1176). Gulf asserts that there is a zero percent chance that a single numerical estimate is exactly correct. Mr. Hill, on the other hand, stated that a sample of 100% of the population (a nationwide sample) has a confidence level of 100% (Tr. 1214-1216).

If there is any error in the FERC Form 423 delivered price analysis, Gulf has done nothing to show that it works to Gulf's detriment. Gulf simply proposes that all questions of error work in its favor and against the ratepayer by applying a range of

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[16]Gulf misleads the Court in its reference to Mr. Hill's Ex. 6, Sch. 3, as Mr. Hill emphasized that the data were not all adjusted for quality (Tr. 1187-1188, 1190).

[17]Only Mr. Gibbons questioned the statistical validity of the staff's analysis. He was wholly without expertise in the field of statistics (Tr. 1253, 1298, 1316-1317).

error about the mean. This is simply unconscionable. Under the FERC Form 423 delivered price methodology, it is just as likely that the derived market price is too high (in Gulf's favor) as it is too low (Tr. 483). In fact, if anything, the record suggests that it may be too high. Mr. Foxx selected coals of a quality similar to Maxine's (Tr. 280, 289). According to Mr. Hill, staff's approach was over-generous to Gulf. Gulf could use coals of lower quality in its Crist Plant (Tr. 1172). If there is to be any allowance for error it must begin with an adjustment downward to eliminate this bias in favor of Gulf.

The record contains competent and substantial evidence to support the Commission's findings of imprudence and the method it used to measure the dollar impact of that imprudence.

II.

THE PROHIBITION AGAINST RETROACTIVE RATE MAKING AND THE DOCTRINE OF RES JUDICATA ARE INAPPLICABLE TO A CONTINUOUS PROCEEDING LIKE THE FUEL ADJUSTMENT PROCEEDING.

The Fuel Adjustment Proceeding

The fuel adjustment proceeding has been a continuous proceeding since 1974 with one break in 1980. Prior to 1980, the Commission held monthly hearings to adjust charges for fuels consumed by the utility. In 1980, the Commission changed from a historical fuel adjustment with a two month lag to a projection and true-up proceeding. The projection/true-up is not a pure true-up. Several factors influence the calculations, making it a continuous true-up rather than a discrete one-time correction proceeding for all past errors and misestimations. Projected fuel adjustment factors are derived from estimates of future sales, fuel use and fuel cost. The variance between estimated and actual expenses produces a true-up that is included in subsequent fuel adjustment factors. Three factors that make it a continuous process are:

- The recovery of fuel expenses is based upon projections of future sales. For example, assume that an under recovery of fuel expense has occurred in the amount of $100, and the company projects sales of 1000 kwh. Therefore, the adjustment is set to include a true-up factor of $.10/kwh on future sales. If the company only sells 900 kwh, there is an under recovery of the past under recovery of $100 - 900 x ($.10) = $10. If the company sells 1100 kwh, an over recovery of the

past under recovery occurs in the amount $100 - (1100) x ($.10) or -$10.00. This new over or under recovery is continuing projection and true-up process.

- Companies calculate the projected fuel consumption needed to meet projected sales. Many factors can affect the fuel consumption: The weather, more purchased power, different combination of generation (oil, gas, coal nuclear), greater or lesser efficiency and other factors. These may cause the introduction of additional under or over recovery. In the above example assume the company projects sales of 1000 kwh and it sells 1000 kwh. Rates are set at $.23 for projected fuel costs plus $.10 for the true-up, or a total of $.33 per kwh. If the generation mix changed and more high cost oil had to be burned, fuel actually ended up costing $.25 per kwh, only $.08 was left to true-up the previous under recovery. Therefore, on sales of 1000 kwh, the company recovered 1000 x $.08 or $80. Since $100 was needed for true-up, $20 had to be rolled forward into the next true-up.
- If fuel purchases during the projection period are different than projections, the average cost of fuel burned may vary, causing either an over or under recovery of the correction factor of $.10 per kwh used in the above example. This would look similar to the calculation used in the second example.

With all fuels, there are two questions associated with the recovery of fuel expenses: How the expenses were incurred and how much is to be passed on through the clause. The fuel adjustment proceeding typically addresses the issue of how much. The issue

of "how," the prudence decision, is generally spun-out of the routine hearings. The fuel adjustment hearings are accounting oriented with determinations that consider "how much" fuel was purchased; "how much" the average cost of the pile (inventory) changed; and, "how much" was burned. The issues connected with the decisions to purchase are usually considered in a spun-off proceeding dealing with whether to execute a contract, changes in sampling procedures, market price, the spot market or a number of other considerations of prudence.

Retroactivity

Fuel adjustment is an expense for electric utilities where the utility is compensated on a dollar-for-dollar basis for its expenditure through the fuel adjustment clause. This after-the-fact adjustment has been approved by this Court. The fuel adjustment proceeding is a continuous proceeding where retroactive rate making has no applicability.

In Florida Power Corporation v. Cresse, 413 So.2d 1187 (Fla. 1982), the power company lost the use of a nuclear reactor, thereby incurring higher fuel costs through the purchase of more expensive replacement fuels. The length of the outage was increased due to the failure to have a replacement pump on-hand. The utility petitioned the Commission for the recovery of $46.3 million in revenues which the company had earlier failed to recover through the fuel adjustment clause.

After a hearing, the Commission allowed the company to pass on to the consumer all of its additional fuel expenses except $3.5 million dollars associated with the extension of the outage (for

167 days) due to the failure of the utility to have on-hand a replacement pump. The Commission found that the company had acted imprudently and should not be allowed to recover those past expenses. The Court affirmed the Commission's decision.

On April 1, 1980, the Commission went from a two-month after-the-fact recovery of fuel expenses to a six month projection with a true-up. Citizens v. Public Service Commission, 403 So.2d 1332 (Fla. 1981). In the new procedure, fuel costs are estimated for a period, and after incurring three months of actual expenses, the Commission conducts a true-up of the actual and estimated expenses against the projected charges. (See Appendix A-30). This after-the-fact adjustment allows the company an opportunity to recover past expenses incurred, but not collected from the ratepayer. The proceeding also provides an opportunity for the adjustment downward of rates to the ratepayer for over-collection of fuel expenses by the utility. Richter v. Florida Power Corp., 366 So.2d 798, 800-801 (Fla. 1979).

This adjustment for past errors, misestimations and imprudence is a two edge sword protecting the ratepayer from over-collection of fuel expenses and protecting the company from the under-collection of expense dollars as a result of misestimation.

> Adjustment clauses were developed to protect the customer in the case of sharp decreases in fuel or commodity costs, and the utility in cases of sharp increases.

Pinellas County v. Mayo, 218 So.2d 749, 750 (Fla. 1969).

Adjustments to expenses are intended to compensate the utility after-the-fact and seeks to make the utility whole for past

incurred costs. There is no profit associated with the recovery of expenses. When the Commission finds that a cost has been incurred imprudently, it does not pass that cost on to the ratepayer. Payment for imprudent expenses is the responsibility of management and comes from the company's earnings, resulting in an incidental diminution in earnings.

The Appellant has misapplied the law dealing with retroactivity by applying it to the recovery of an expense in a continuous proceeding. Power companies are often placed in the situation of having to adjust for the over or under recovery of past expenses and purchases. For electric companies, the Commission adjusts for fuel related matters on an after-the-fact basis.

There are analogous adjustments for the telephone companies. In Citizens v. Florida Public Service Commission, 415 So.2d 1268 (Fla. 1982), the Commission opened a docket in September 1980 to consider the represcription of depreciation rates (an expense) for calendar year 1980. On January 1981, the Commission entered an order approving the represcription of depreciation rates making those expenses recoverable effective on January 1, 1980. This effective date was nine months prior to opening the docket. Public Counsel (like the utility here) argued that depreciation represcription "is not a bookkeeping entry but, rather, constitutes a retroactive change in the rate base," citing to, as the Appellant has, City of Miami v. Florida Public Service Commission, 208 So.2d 249 (Fla. 1968). This Court held that the reliance was misplaced in that the case did not concern rate

making. It is simply the recovery of an expense.

Shortly after the Citizens case was decided, the Commission was again faced with represcribing depreciation rates for telephone companies. This time the represcription of depreciation expenses lowered the rates to be charged the consumer, and Southern Bell appealed. In Southern Bell Telephone & Telegraph Co. v. Florida Public Service Commission, 443 So.2d 92 (Fla. 1983), Bell contended that the Commission had not comported with the essential requirements of law in making an adjustment to past depreciation expense. It was precisely the reverse situation from the Citizens case. However, the Company did not make the challenge to the adjustment as retroactive rate making. It had become established law that the Commission could adjust past incurred expenses. The Court found that the Commission decision was supported by competent evidence and was in compliance with the essential requirements of law. The represcription of depreciation expenses like fuel adjustment is an after-the-fact adjustment to an expense. In the case for fuels it is done periodically and like represcription, results in both increases and decreases to the charges.

In Citizens, the ratepayers were complaining that the Commission had increased an historical expense (causing rates to go up) and the utility supported that after-the-fact treatment of the expense. In Southern Bell, the utility was complaining about an after-the-fact reduction of an expense and the Citizens were supporting that position. This second situation is the case here. Fuel adjustment is a two-edged sword that fairly cuts both ways.

The Appellant cites to Southern Bell Telephone and Telegraph Co. v. Florida Public Service Commission, 453 So.2d 780 (Fla. 1984), for the proposition that the Commission may not adjust rates on a retroactive basis. The case is supportive of the Commission's position. In Bell, Southern Bell and General Telephone Company had been dividing intrastate long distance toll revenues pursuant to two settlement agreements. These revenues were derived from tariffs filed with the Commission. The tariffs had been established and approved during rate case proceedings and constituted part of the companys' base rates. The revenues derived from those agreements contained substantial profits and contributed to the companies' earnings. The two companies got into a dispute concerning the method of calculating the division of those revenues. The parties could not reach agreement on the division for almost a year prior to bringing the issue to the Commission for resolution. The Commission resolved the controversy and applied the adjustment to revenues earned a year prior to assuming jurisdiction over the controversy. This the Court found was retroactive rate making.

Here, the Commission has not changed the filed tariffs of the utility nor has it affected the earnings of the utility except to the extent that the stockholders are bearing the risk of management imprudence and not the ratepayer. No company is guaranteed a rate of return. If it acts imprudently in the handling of an expense, the stockholders and not the ratepayer bear the risk through the diminution of earnings.

Long-Term Contract Review

Another reason for the Commission having the ability to review the expenses associated with fuel contracts occurs when a utility plans for the construction of a new facility. When the boilers are initially designed, they are designed to burn a particular fuel. Coals significantly vary in characteristics requiring the specification of coal at the time of design. Often utilities will purchase reserves of coal before the construction of the boiler commences to ensure the availability of the particular fuel when the facility goes into service six or seven years later. The Commission cannot review the prudence of the purchase or the contract provisions for that fuel until: 1) the utility seeks to pass the costs on to the consumer in a fuel adjustment proceeding; and 2) the company raises the issue of prudence. That could be years after the contract was executed.

The Commission's review of a contract has no effect upon the enforceability of that contract between the utility and the provider of fuel. City of Plant City v. Mayo, 337 So.2d 966 (Fla. 1976). The Commission has no jurisdiction to regulate the contracts executed between the utility and its suppliers. The Commission's authority lies with regulating the effect that that contract has on utility rates and charges. After the utility has incurred the expenses pursuant to the agreement and attempts to recover those expenses, the Commission may determine the prudence of that contract if the issue is raised. In determining prudence, the Commission applies a "public interest" test. The logical justification for this procedure lies in the Commission's

statutory authority. The Commission only has need determination authority for the certification of new power plants pursuant to section 403.519, Florida Statutes. There is no prior determination of the specific fuel requirements nor is there a review of the prudence of any decision regarding fuel contracts prior to the request for the recovery of those costs and a request to determine prudence.

Other Authority Cited

The Appellant cites to the City of Miami v. Florida Public Service Commission, supra, for the proposition that the Commission cannot engage in retroactive rate making. The Commission agrees with the proposition and contends that the case is supportive of the Commission's position in this case. In City of Miami, Southern Bell and Florida Power and Light were found to have rates in effect that were unreasonably high. The Commission ordered the rates reduced and made certain accounting adjustments which the City contended were departures from the essential requirements of law. Point D raised by the City asserted that the Commission erred in allowing the Companies to keep excessive base rate earnings realized through lawfully imposed tariffs collected prior to the test year. The Court correctly recognized that for rate making purposes, base rates are set prospectively; giving the company an opportunity to earn a reasonable rate of return on investment used and useful in the public service. (At 259-260). Had the Commission attempted to adjust future earnings to reduce past over-earnings by the company from the ratepayer, it would have engaged in retroactive rate making.

In this proceeding, the Commission is neither considering base rates to be "thereafter charges for services" nor is it looking at over-earnings or earnings at all. It is concerned with past expenses and an overcharge for fuels. The Commission is not dealing with a case of the prospective operation of base rates. The prohibition against retroactive rate making does not apply to this continuous proceeding.

Res Judicata

Generally:

The fuel adjustment proceeding is an on-going, continuous proceeding wherein each projection is a projection of the aggregate of all past misestimations and errors. The doctrine of res judicata and estoppel by judgment are inapplicable to continuous proceedings. Beverly Beach Properties, Inc. v. Nelson, 68 So.2d 604 (Fla. 1953). By its very design, the fuel adjustment proceeding is intended to continuously adjust for past cumulative misestimations and errors prospectively. This is necessary because of the large fluctuations in fuel costs and usage and the fact that the charge is based upon estimates.

Using a weighted average cost of fuels simplifies the accounting and reflects the fact that coal and oil are fungible and not identifiable on the pile or in the tank as being related to any one purchase. However, using a weighted average fuel cost means that an increment of the cost of fuel purchased in 1980 is still being recovered in this and every month's fuel adjustment clause.

Recovery of cost and a determination of prudence are the two

distinct elements of setting fuel charges. The first, recovery of cost, is an imprecise accounting method of projecting use and costs and setting rates to recover those costs. An incremental factor is added to adjust for past misestimations and errors. The second element, the determination of prudence, usually occurs in an evidentiary hearing and deals with how the companies entered into their agreements and made their decisions.

To apply the principles of res judicata to Commission proceedings works a manifest injustice on the utilities and the customers of the utility. After a utility has sought and received a rate increase it would be foreclosed from raising any rate making issues in any subsequent hearing. The reason for this is that the doctrine of res judicata would bar a subsequent suit between the same parties on an identical cause of action and would be conclusive as to all issues that were or could have been raised. A utility's rate base, once established could never be changed. Expenses once determined could not be adjusted because of inflation. Estoppel by judgment would bar relitigating issues common to both actions that were actually adjudicated in the first action. Gordon v. Gordon, 59 So.2d 40, 44 (Fla. 1952). Thus, any rate setting issue decided by the Commission in an earlier proceeding would be barred from subsequent relitigation if the doctrines were to be applied. It is arguably for this reason that this Court held that the doctrine would create injustice and unfairness and was not applicable to the Commission's decision.

In Matthews v. State, 648 So.2d 149 (Fla. 1933), this Court stated:

> An order of the railroad commission made pursuant to chapter 14764, Acts of 1931, while quasi judicial in character, is not res adjudicata of another application of exactly the same nature subsequently filed. Every promulgated order of an administrative tribunal, such as is the railroad commission, may be superseded by another order. Likewise the commission has the power to modify, and indeed, it is its duty to modify, its pre-existing orders, when new evidence is presented which warrants a change.

In this proceeding, no evidence had ever previously been presented concerning the prudence of the purchases from the Maxine Mine. This proceeding brought forward evidence for the first time, warranting the refund of recoveries of imprudent expenses. The decision as to whether res judicata applies to an issue in a particular administrative proceeding is a decision made by the administrative agency. If the Court assumes that res judicata is applicable to Commission proceedings, it is the Commission that decides whether to apply the doctrine. That determination is reversible only where the body acted with "manifest" and "flagrant" abuse of its discretion. Coral Reef Nurseries, Inc. v. Babcock Co., 410 So.2d 648, 655 (Fla. App. 3d 1982).

The question here would be whether the commission flagrantly abused its discretion in rejecting the claim that the proceeding was barred by the principles of res judicata or estoppel by judgment. Appellant does not assert that the decision was a manifest and flagrant abuse of discretion.

Appellant relies upon the fact that the Company, in a verified petition for projected rates, made the apparent allegation that it acted prudently in purchasing fuel. The verification was by the

representative of the firm who, although competent to testify as to how much fuel was purchased, how much fuel was burned and what it cost, was incompetent to testify as to whether the company was prudent in its purchasing practices (Ex. 9, Vol. IV, Tr. 379-384, February, 1983, projection hearing). Prudence is not reviewed when a company simply projects future costs and consumption. It should be offered for proof during true-up. As stated in Order No. 13452, Gulf never alleged nor sought to prove the prudence of its actions in the after-the-fact true-up hearings. There was no testimony presented in the records of the fuel adjustment proceedings demonstrating that the company acted prudently. The Company only met its burden as to how much money was spent and not whether it had in fact acted prudently in spending that money.

Manifest injustice

If the Court assumes that the company pled prudence, it cannot reach the conclusion that it proved prudence. The record does not support such a finding. But even if the company did offer proof of prudence (which it did not), additional facts indicating that the company was imprudent in its purchases of coal from Maxine Mine were not uncovered until the hearing in this case.

If the Court were to find that res judicata was applicable to this proceeding, there is an appropriate recognized exception to the rule that should be applied. In Flesche v. Interstate Warehouse, 411 So.2d 919, 924 (Fla. App. 1st 1982) the Court found:

> The doctrine of res judicata, which is equally applicable to the decisions of administrative tribunals and courts, is said to be an obvious rule of expediency, justice, and public

> tranquility, and further: "Public policy and the interests of litigants alike require that there be an end to litigation, which, without the doctrine, would be endless." It is equally clear, however, that there are recognized exceptions in the application of the doctrine, one of which is that it will not be invoked where it will work an injustice. (footnote omitted)

In this case, there would be just such a manifest injustice if res judicata was applied. The company purchased fuel without regard to the advice of experts. It passed those excessive costs on as an average cost of fuel to the unsuspecting ratepayers through the fuel adjustment clause. It never raised the issue that the cost of that coal had risen to more than twice the cost of any other comparable coal. It was recovering dollar for dollar every expense dollar it incurred. The rule is well settled that the sole purpose of the doctrine of res judicata is to end litigation "in the interest of the state" but the interest of justice dictates whether the doctrine should be applied.

> As we stated in Gordon v. Gordon, supra, it is not proper, technically speaking, to consider the doctrine of res judicata as a branch of the law of estoppel. The basic principle upon which the doctrine of res judicata rests is that there should be an end to litigation and that "in the interest of the State every justiciable [sic] controversy should be settled in one action in order that the courts and the parties will not be pothered [sic] for the same cause by interminable litigation." 59 So.2d at page 44; italics supplied. Nevertheless, when a choice must be made we apprehend that the State, as well as the courts, is more interested in the fair and proper administration of justice than in rigidly applying a fiction of the law designed to terminate litigation.

Universal Construction Co. v. City of Ft. Lauderdale, 68 So.2d 366, 369 (Fla. 1953).

Here the interests of justice demand that the imprudence of the company be reviewed and the attempt to hide behind an unsubstantiated pleading to pass on improper costs to the ratepayer not be used to shield the company's acts.

Lack of Issue

The doctrine of res judicata will not bar an adjudication of an issue that did not exist at the time of the first judgment. Res judicata is a rule of convenience, the purpose of which is to prevent relitigation over matters that have been decided and have remained unchanged factually and legally.

> The doctrine of res judicata as to the finality of the judgment and the doctrine of law of the case as to the binding effect of interlocutory orders in litigation are rules of convenience 'designed to prevent repetitious law suits over matters which have once been decided and which have remained substantially static, factually and legally (and must give way where there has been a change in the fundamental controlling legal principles). It is not meant to create vested rights in decisions that have become obsolete or erroneous with time.' Clearly, a judgment is not res judicata as to rights which were not in existence and which could not have been litigated at the time the prior judgment was entered.

Wagner v. Baron, 64 So.2d 267, 268 (Fla. 1953).

In this proceeding, the issue of the prudence of the contract executed between the company and the mine was never litigated. What the company points to for support of its contention that the issue has been litigated is the allegation in the petition for projected rates that the company acted prudently in all fuel purchases. This self serving statement does not rise to the level

of proof nor does it satisfy the threshold for raising an issue. During the hearings, the attorney for the utility tried to contend that the pleading constituted proof. Counsel for the company alleged that it was a prima facie showing and that it did not have to be supported by an expert. (Ex. 9, Vol. IV, Tr. 428, February 1983 projection hearing). Commissioner Cresse stated: "It sounds to me like we're fixing to get snookered if we don't get that out of there." The Commission did allow the pleading to stand but found that the witness supporting the allegation was not the proper person to testify as to the purchasing practices of the company.

"Commissioner Cresse: Well, it seems to me like Mr. Haskins said he didn't know much about the purchasing, either." (Ex. 9, Vol. IV, Tr. 429, February 1983 projection hearing). The information concerning the prudence of the purchases from the Maxine Mine were never before the Commission for consideration. The only thing in the record was the verified petition making a general allegation of prudence. The issue never having been raised was, therefore, never litigated. The doctrine of res judicata is not applicable.

It is an extremely complex procedure to determine whether the purchase of a fuel was done prudently. Often experts are hired, hearings are held and a good deal of discovery is necessary. It cannot be accomplished within the frame work of a regular fuel adjustment hearing. The cycle is too short and the issues too complex to determine every six months. The issues are often "spun-out" of the fuel adjustment proceeding and handled on a

case-by-case basis. This is not the first time that the Commission has spun-out an issue for the determination of the prudence of the company's purchases.

The fuel adjustment proceeding is not intended to make quick determinations of whether fuels were purchased in a prudent manner. The proceeding is designed to ensure that the utilities may pass through the clause the money expensed for fuels on a timely basis. In exchange for quick recovery there is the uncertainty that the Commission will subsequently review the prudence of the decision. The Commission's procedure is not retroactive rate making nor barred by the principle of res judicata. The exiting procedure ensures that the interests of the ratepayers and the companies are protected. The reasons are simple:

- The ratepayers bear the risk of imprudence until a determination is made that particular transactions were done prudently. They pay higher rates to the companies who have those funds until a determination of prudence is made.
- The company bears the risk that the Commission will review transactions at a later date and order refunds in the event that, after all due process rights are afforded, the company is found to have acted imprudently.
- The company can, at any time, commence a proceeding to determine the issue of prudence and foreclose or estop the Commission's subsequent review of the issue of prudence.
- The company, and not the Commission, has the burden of establishing prudence and reducing its risk of the uncertainty of future Commission inquiry.

The fuel adjustment proceeding is an on-going continuous proceeding in which all preceding misestimations, errors and projections are readjusted prospectively. Each fuel adjustment is the aggregate of all past fuel adjustment proceedings.

The fuel adjustment procedure works fairly. The company is disgruntled because it acted without due regard to the interest of its ratepayers and must now be held accountable.

Interest on the Refund

The Appellant has transformed its "penalty" into "damages" to suit the argument of the moment. Its cases on unliquidated damages are inapposite. The refund is simply part of the fuel adjustment, which has incorporated two-way interest payments since March 1980. A utility pays interest when it spends less for fuel than projected or when its expenditures are later disallowed as imprudent. Likewise, its customers pay interest when the utility spends more than projected. The notion that underlies this process is equity and fairness. Its purpose is to keep each side whole. It is an administrative process borne of a pass-through mechanism that has nothing to do with torts or contracts. The Appellant is in favor of the process, except when it contests the result.

CONCLUSION

The Commission found that Gulf acted imprudently, viewing the facts on the basis of what Gulf knew or should have known at the time it acted. It measured the dollar impact of Gulf's imprudent acts and properly required Gulf to refund imprudent expenditures. The evidence was conflicting, but the record contains competent and substantial evidence to support the Commission's decision.

Appellant contends that the legal doctrine of res adjudicata applies to fuel adjustment proceedings. It does not. If res judicata applied to rate making of the Commission, then a company once having sought rate relief could never relitigate that issue in subsequent rate hearings. The issues of rate base, expenses, earnings, cost of capital, depreciation and all the other issues in a rate case would be settled, never to again be litigated.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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