IN THE SUPREME COURT OF FLORIDA

MCI TELECOMMUNICATIONS CORP.,	)	
	)	
Appellant,	)	
	)	
v.	)	CASE NO. 66,945
	)	
FLORIDA PUBLIC SERVICE COMMISSION,	)	
	)	
Appellee.	)	
	)	

ANSWER BRIEF OF APPELLEE FLORIDA PUBLIC SERVICE COMMISSION

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DESIGNATIONS AND ABBREVIATIONS

Appellee, Florida Public Service Commission, will be referred to in this brief as PSC or the Commission. Appellant, MCI Telecommunications Corporation, will be referred to as MCI. References to the transcripts of the September and October access charge hearings in Docket No. 820537-TP will be abbreviated Tr.---. References to the record on appeal are abbreviated R.---. Documents contained in the Appendix attached to this brief are indicated by A.---. All documents contained in the Appendix are numbered consecutively.

STATEMENT OF THE CASE AND FACTS

In 1984 the Florida Legislature amended Chapter 203, Florida Statutes, relating to the collection of gross receipts tax for utility services. As is relevant to this appeal, Chapter 84-342, Laws of Florida, changed the methods for payment and collection of gross receipts tax on telephone access charges. Prior to January 1, 1985, the effective date of Chapter 84-342, interexchange carriers (IXCs) such as the Appellant, MCI, were given a credit against the gross receipts tax they paid on revenues derived from the sale of long distance telephone service. The amount of that credit was equivalent to the gross receipts tax paid by local exchange telephone companies (LECs) on revenues derived from access charges collected from the IXCs. This arrangement was based on the fact that the LECs' access charges, which are set by the PSC, had an embedded component, or rate element, covering the gross receipts tax liability on those revenues. The theory was that the IXCs resold the access, for which they paid through access charges, to their long distance customers. Thus, if both the IXCs and the LECs paid gross receipts tax on revenues derived through the sale of access to the telephone network, there would be double taxation, unless the IXCs were not granted an off-setting credit.

Chapter 84-342 did away with the gross receipts tax liability of LECs relating to access charge revenues and made the IXCs responsible for the tax without an off-setting credit. The net effect of this change was simply to shift the liability for payment of gross receipts tax to the IXCs. It did not affect the amount of tax actually collected by the State.

Although the changes created by the 1984 amendments to Chapter 203 obviously address only the payment and collection of gross receipts tax, not the PSC's ratemaking authority, they do have an impact on the element of tax expense to be recognized in the ratemaking process. That impact was first considered by the Commission during the course of its hearings on intrastate access charges (Docket No. 820537-TP) held during September and October of 1984. At the beginning of the hearing on October 31,1984, Commissioner Cresse noted that the effect of the change in the gross receipts tax law had not been made an issue in Prehearing Order No. 13815 but that it should have been. (Tr. 2932) Commissioner Cresse suggested that the parties try and reach a stipulation on this issue and went on to explain his intent as follows:

> "All I am asking the parties to do is to, that's the law and there is nothing that this group can do about it between now and January, and you will all get a crack at it in April maybe, but between now and then that is the law and we ought to take

> cognizance of that when we set access charges and not leave I guess any of the interexchange companies short, or leave any surpluses with the local exchange companies because of the change in tax law that is within our capability to adjust." (Tr. 2934)

The parties present at the hearing, including representatives of Appellant MCI, made no objection to Commissioner Cresse's proposal that a stipulation be reached on the proper treatment of the change in the gross receipts tax law. (Tr. 2936; 2947)

During the afternoon session of the October 31, 1984, hearing Commissioner Cresse once again raised the issue of gross receipts tax and asked if the parties had been able to reach a stipulation on the effect of the change in the law and how it should be treated for the purposes of setting access charges. (Tr. 3504-3505) At that time William H. Neal, Jr., a witness appearing for AT&T Communications of the Southern States (AT&T) was recalled to the stand to explain what agreement had been reached by the parties on this issue. In response to Chairman Gunter's inquiry he replied:

> "Well, we reached an accord that the impact of the change in the gross receipts tax law should be reflected in the level of revenues that should be derived from access charges. All of the LECs were not represented in these discussions, but effectively, what we are saying is that you would determine the impact of the gross receipts tax change

> and subtract that amount from the level of revenues that you want to derive from access charges."
>
> One of the difficulties in determining numbers at this point is that certain decisions have to be made. Specifically, what is your starting point, as far as access revenues you want to derive; and secondly, what access charge revenue would come from the end user versus those coming from the carrier.
>
> If it comes from the carrier it would not be subject to gross receipts tax for the LECs. If it is derived from an end user, though, it would be subject to gross receipts tax.
>
> So those decisions would have to be reached by the Commission before actual numbers could be determined on the impact.
>
> So basically, I think there would be agreement that once those numbers were determined, what we would have to be -- what we would have to do is to be sure that the revenues to be derived from access were explicitly reduced to reflect the impact of the change in the gross receipts tax law." (Tr. 3513-3514)

Mr. Neal went on to discuss with Commissioner Cresse the mechanics of removing the 1.5 percent gross receipts tax from access charges. The discussion did not concern what specific element of access charges should be reduced but only how to calculate the reduction of the embedded gross receipts tax component of access revenues. In summary, Commissioner Cresse explained his method as follows:

> "And what I had thought the thing to do was to take 101.5 and divide it into 100 and then that would tell you how much the

> revenue reduction should be, but anyway, we will figure that out, it's 1.5 to 1-point, you know, less --" (Tr. 3520-3521)

The hearing closed without objection or questions regarding the proposed methodology to be used.

At its December 10, 1984 Agenda Conference, the Commission considered the issue of adjustments to 1984 and projected 1985 access charge revenues, including the effect of the change in the gross receipts tax law. The Commission quantified that effect at approximately $6.15 million and concluded that the billing and collection services element of access charges should be reduced by that amount. Billing and collection services are charges assessed by the LECs for recording billing information, rendering bills and collecting revenues for long distance calls made over the IXCs' facilities.

The net effect of the $6.15 million reduction was to remove from billing and collection services revenues that element of the LECs' charges which was embedded for the purposes of meeting gross receipts tax obligations. Since, effective January 1, 1985, LECs no longer had to pay gross receipts tax on the access charge revenues received from the IXCs, the net effect of the reduction on the LECs' earnings was zero. The Commission's decision in no way increased the obligation of IXCs to pay gross receipts tax on their revenues but instead provided an opportunity to pay a lesser

amount in access charges relating to billing and collection services. The Commission's decision was embodied in Order No. 1393 issued December 21, 1984. (A.1)

On January 7, 1985, MCI filed for reconsideration of the Commission's Order No. 13934. Among the issues raised by MCI was a claim that the Commission's $6.15 million reduction in the billing and collection services charge was inequitable because only AT&T, as the predominate user of these services, would receive a substantial benefit. (R.318)

The Commission rejected MCI's arguments, and on March 25, 1985 issued its Order No. 14232 denying reconsideration on this issue. (A.21) Thereafter, MCI filed its Notice of Appeal.

SUMMARY OF ARGUMENT

The change in Florida's gross receipts tax law created a potential windfall to LECs of $6.15 million. The Commission recognized an equitable obligation to make an adjustment in access charges to eliminate that windfall. The Commission's $6.15 million reduction in billing and collection charges achieved the goal of eliminating the LEC windfall. The adjustment did not cause MCI to pay double gross receipts tax or increase other elements of its access charge rates.

The decision to reduce billing and collection services was a proper exercise of the Commission's discretion in distributing the impact of rate adjustments. Billing and collection services is a particularly market-sensitive element of access charges. The Commission properly recognized that AT&T's plans to increase its own billing and collection should drive the cost of these services downward. The Commission further recognized that the total loss of billing and collection revenues would have a severe impact on the LECs. Its reduction of these charges was a legitimate attempt to deal with this problem. At the same time, the Commission also recognized that the income expectations of the LECs from billing and collection should be brought into line with market reality. The reduction

thus served the dual purpose of helping to maintain the use of LEC billing and collection by AT&T and the other IXCs but began reducing the LECs' dependency on excessive contribution from those services.

The parties to the access charge hearings stipulated on the methodology for removing the gross receipts tax element from access charges. The parties did not raise the issue of what specific elements of access charges should be reduced. There had been discussion in the hearing of reducing billing and collection services, and the parties could reasonably be presumed to be aware that the Commission might exercise its discretion in reducing billing and collection. The decision to reduce billing and collection services was based on competent evidence provided by AT&T and the LECs.

AT&T stated its intentions to do more billing and collection on its own. This was confirmed by the LECs. The LECs also provided the Commission with competent evidence on the pricing of billing and collection services and the impact of the loss of these revenues. The Commission's decision to reduce billing and collection services by $6.15 million was a proper exercise of its discretionary ratemaking authority.

ARGUMENT

POINT I

THE DECISION TO REDUCE ACCESS CHARGE REVENUES BY $6.15 MILLION THROUGH THE BILLING AND COLLECTION TARIFF TO OFF-SET THE LECS' REDUCED GROSS RECEIPTS TAX LIABILITY WAS A PROPER EXERCISE OF THE COMMISSION'S RATEMAKING AUTHORITY.

The Commission is not bound by statute or other law to adhere to a particular formula in setting rates and distributing their impact among customers. It has the discretion to set rates on "cost of service" as well as "value of service" criteria and may lawfully consider a wide range of other factors in establishing the level of rates for the various classes of customers. International Minerals and Chemical Corporation v. Mayo, 336 So.2d 548, 552 (Fla. 1976); Occidental Chemical Company v. Mayo, 351 So. 2d 336, 340 (Fla. 1977). There is no requirement that every class of customers provide a proportionate share of a utility's revenue requirement or that rate structures be entirely non-discriminatory. So long as there is a reasonable basis for the customer classification and it is not unduly discriminatory it must be upheld. City of Tallahassee v. Florida Public Service Commission, 441 So.2d 620, 623 (Fla. 1983); Polk County v. Florida Public Service Commission, 460 So.2d 370, 373 (Fla. 1984). Appellant, MCI stands before this Court as a disgruntled customer complaining only that the Commission has modified the access

charge structure in a way which does not allow it to benefit as much as AT&T from $6.15 million gross receipts tax reduction. Its complaint cannot support a charge of discriminatory rates or a classification not based on reasonable grounds.

A. The Commission properly eliminated the windfall to LECs which would have resulted had they continued to collect revenues to meet a non-existent gross receipts tax obligation.

The primary function of the hearings held by the Commission in September and October of 1984 was to determine the level of intrastate access charges for 1985. Among the major issues to be addressed were the effect of going to a "bill and keep" system that would eliminate pooling arrangements between the companies, peak-load pricing and the institution of directory assistance charges. (A.6-7; 15-18). The gross receipts tax issue arose incidentally to that process.

The Commission was under no legal obligation to consider the effect of the change in Florida's gross receipts tax law. While Chapter 84-342 did create an obligation in the IXCs to pay gross receipts on all revenues without a credit for access services purchased from the LECs, it did not purport to change in any way the manner in which the companies derive the revenues to pay those taxes. The Commission and the parties, of course, recognized that from an equitable point of view the LECs were no longer entitled

to collect revenues not needed to meet this specific tax expense. The Commission's ratemaking obligation was thus to eliminate the windfall that the LECs would experience by continuing to collect rates containing an element designed to cover gross receipts tax. There is no contention by Appellant MCI, or anyone else, that the Commission did not accomplish this goal by its $6.15 million reduction of access charges. The end result of this process involving gross receipts tax is that the State of Florida will continue to collect the same amount of gross receipts tax as it had before the change in the law, hence, there is no double taxation, and the LECs have had their revenue requirement adjusted consistently with their tax needs.

B. The Commission properly used the gross receipts tax reduction to adjust billing and collection charges.

The essence of the Commission's access charge methodology has been that the marketplace will determine the appropriate level of access charges more effectively than regulatory schemes based on the allocation of embedded costs. (A.4) Of the many elements contained in the access charge tariff, one of those most sensitive to market forces is billing and collection services. At hearing, Commissioner Cresse raised this issue in his cross-examination of Centel witness Wahlen:

> Commissioner Cresse: . . . since billing and collection is more market-based than it is cost-based, should we start backing some of that revenue out of billing and collection fees?
>
> Witness Wahlen: I think you could do that to the degree that the current rates exceed the revenue requirement. Once you get down below the cost of billing then I think you are looking at shifting costs to the local ratepayers.
>
> Commissioner Cresse: Below the cost, and that would be below the marginal cost of billing for the toll carrier, is that correct?
>
> Witness Wahlen: Right.

(Tr. 3169-3170)

After establishing that billing and collection services was a likely area for reduction by the $6.15 million excess in gross receipts tax, Commissioner Cresse asked for submission of a late filed exhibit, identified as 3-40-F, from all telephone companies. (A.30-42) The purpose of the exhibit was to "give us the cost that they would reduce if billing for the carrier of last resort (AT&T) was eliminated. That's the figure I'm looking for". (Tr. 3172)

During the course of their discussion witness Wahlen agreed with Commissioner Cresse that one of the reasons that billing and collection services might be a good place to reflect the $6.15 million adjustment was because the current $35.5 million revenue target for billing and collection might be so high as to encourage AT&T to do its own billing:

> Commissioner Cresse: . . . "Should we have any concern that that rate may be so high as to encourage AT&T to establish their own billing and collection system?
>
> Witness Wahlen: I think you absolutely should have, because I believe, if I'm not mistaken, AT&T has told us that they don't intend to continue to use their billing service more than another year or two." (Tr. 3168)

Based on the foregoing, it is clear that the Commission's consideration of billing and collection services as a place to reflect the $6.15 million adjustment to gross receipts tax was in no sense arbitrary or ill-considered. Billing and collection services is a market driven rate element. The main user of the service, AT&T, could reasonably be expected to respond to the pressures in the marketplace in deciding whether it should continue its arrangement with the LECs or establish its own system. The Commission could properly consider this factor in trying to reduce access charges to eliminate the windfall to LECs from former gross receipts tax revenues. At the same time, the Commission properly considered the effect that the elimination of some $35.5 million in revenues would have on the LECs, should AT&T establish its own billing and collection system. The Commission in this case exercised essentially the same discretion in its ratemaking approach that it did in International Minerals cited above. There the Commission was upheld when it applied factors other than cost of service in setting rates. Among other things, the

Commission gave consideration to the impact of market forces which might cause large users of electricity to set up their own facilities for generation, if the cost of electricity were set too high. 336 So.2d 553.

It is the role of the Commission to set utility rates, not the Court. Florida Retail Federation v. Mayo, 331 So.2d 308 (Fla. 1976). Appellant, MCI and the other IXCs cannot accuse the Commission of arbitrariness or unreasonable discrimination in this case. The fact is that MCI will pay only the gross receipts tax that the law requires. Moreover, MCI is not excluded from the class of ratepayers in which AT&T is the predominent customer, even if it participates to a lesser degree than AT&T because of the limited availability of equal access. The Commission has not increased any rate burden of MCI. It still pays other access service rates set in the same manner as before the gross receipts tax reduction and may realize some savings from its share of the reduced billing and collection services rates. In any case, the Commission was not addressing any potential losses which might be suffered by customer-utilities such as MCI. That matter is for another forum in which MCI presumably would advocate a revenue requirement of its own sufficient to cover its access services expenses.

POINT II

THE COMMISSION'S DECISION TO REDUCE ACCESS CHARGES THROUGH THE BILLING AND COLLECTION SERVICES TARIFF WAS SUPPORTED BY THE STIPULATION OF THE PARTIES.

The parties to a proceeding may resolve any issue or controversy by stipulation. The stipulation takes the place of an adversarial, fact finding proceeding but is no less valid and binding on the parties. Resolution of issues by stipulation is quite common before the PSC, and it is not unusual for minor rate cases and overearnings cases to be settled entirely by stipulated agreement. Such agreements are favored by the legal system. Utilities Commission of the City of New Smyrna Beach v. Florida Public Service Commission, No. 64,147 (Fla. Mar. 21, 1985).

The Commission gave the parties to the access charge hearing the opportunity to reach a stipulation on the gross receipts tax adjustment, and they did so. (Tr. 2934; 3513) The substance of the stipulation, that access charges should be effectively reduced by 1.5 percent, was presented by AT&T's expert accounting witness, William H. Neal, Jr. (Tr. 3513-3521) The Commission gave parties the opportunity to voice objections to the proposed procedure and to ask questions but there were none:

> Commissioner Cresse: Okay. Mr. Chairman, I think that's exactly what's going to happen, and I just think we have to keep that in mind when we set the access charges, and I don't think there's any objection -- is there any objections to that formula being used?

Chairman Gunter: Anybody have any questions?

Commissioner Cresse: Mr. Chairman, there being no further business, I move we do now rise. (Tr. 3521)

Following Mr. Neal's presentation, the Commission certainly had reasonable grounds to believe that the parties had agreed that the LEC's access charge revenues should be reduced by approximately 1.5 percent. Moreover, it is also reasonable to assume that, after the exchange earlier in the afternoon between Commissioner Cresse and Mr. Wahlen (Tr. 3168-3175) the parties also knew that the Commission was considering reducing billing and collection services. At the very least, the Commission could reasonably have concluded that the matter of reducing the LEC's access revenues had been left to its sound discretion. It would be naive to assume that the experts present were unaware of the complexity of reducing the tariffed access charges or that they did not understand the implications of their stipulation. If they did not, the forum to ask questions or voice protests was the Commission hearing room, not the courtroom. The parties present had actual notice of the issues raised and had an opportunity to respond.

POINT III

THE COMMISSION DECISION TO REDUCE ACCESS CHARGES BY $6.15 MILLION THROUGH THE BILLING AND COLLECTION SERVICES TARIFF IS SUPPORTED BY COMPETENT, SUBSTANTIAL EVIDENCE.

As a general proposition, the Commission's exercise of its ratemaking discretion must be upheld if its fact finding as a whole supports its decision. 336 So.2d 553. There is ample record evidence in this case to support the Commission's findings that access charges should be reduced $6.15 million through the billing and collection services tariff.

All parties accepted without contravention the testimony of AT&T's witness Neal that the change in Florida's gross receipts tax law should be reflected in a reduction of approximately 1.5 percent in access charges (Tr. 3513-3521) The testimony of Mr. Neal certainly contributes evidence which is "sufficiently relevant and material that a reasonable mind would accept it as adequate to support the conclusion reached. DeGroot v. Sheffield, 95 So.2d 912, 916 (Fla. 1957)

Just as there was competent evidence that access charges should be reduced to reflect the gross receipts tax adjustment, there was competent evidence to show that a reasonable element of access charges to reduce was the billing and collection services tariff. Before the

adjustment, the LECs were receiving approximately $35.5 million in revenue from charges assessed of IXCs under the billing and collection services tariff. (Tr. 3168) LEC witnesses Wahlen of Centel and Menard of Gentel confirmed to the Commission the obvious conclusion that this level of revenue was profitable to the LECs. (Tr. 3170; 2865) The Commission could reasonably conclude that the loss of those revenues, or their reductions below the cost of billing and collection would have a negative impact on the LECs (Tr. 3170)

In pursuit of information on the impact of the loss of billing and collection revenues, the Commission even went so far as to solicit a late filed exhibit, No. 3-40-F, from all LECs to determine what offsetting cost savings they might experience if they stopped billing for the IXCs, specifically AT&T. That exhibit was submitted to the Commission and became part of the record in this proceeding. (A.30-42)

Based on the testimony and exhibits filed, the Commission had competent evidence before it to conclude that the LECs would be hurt by AT&Ts discontinued use of the LECs billing and collection services. The Commission could thus reasonably believe, as confirmed by witness Wahlen (Tr. 3170), that it ought to be concerned about the possibility of the loss of these revenues and begin adjusting them downward toward a reasonable cost basis. This was

especially true in view of the possibility of AT&T setting up its own billing and collection system.

Although the evidence presented on the future plans of AT&T does not rise to level of irrefutable certainty, it does support the findings of the Commission, expressed in Order No. 13934, that a real possibility existed that AT&T would set up its own billing and collection system. (A.4-5). It would be unreasonable to assume that the remarks of AT&T Vice President Weber were idle conversation in his exchange with United's Mr. Berg on this subject:

> Q. Do you plan at some time in the future to do your own billing and collection?
>
> A. We're going to do some of it. We have definite plans to do more private line billing, and WATS and 800.
>
> Q. Could you give us the time frame on when you plan to start your own billing and collecting?
>
> A. We are going to -- we have historically, always have done some private line billing, if you will. We are picking up more of the private line billing during '85, and we are looking at WATS and 800 in the '85-'86 time frame.
>
> I think I can get you some specific information about that. I don't have it with me. I'll be happy to provide it. I think these plans, I'm sure, have been reviewed with United and all the companies as recently as last Friday in some cases. (TR. 1045-1046)

In view of Mr. Weber's remarks the statement of Centel's Wahlen that ". . . AT&T has told us that they don't intend

to continue to use our billing services more than another year or two" (Tr. 3168) is hardly unsubstantiated hearsay.

In consideration of this evidence, and in view of AT&T's basic philosophy that access services must be priced competitively, (Tr. 984-985) the Commission had ample grounds to conclude that it should be concerned about the continued viability of the LECs' billing and collection services charges. It had sound reasons to conclude that a real possibility existed that AT&T, like the large interruptible users of electricity in International Minerals, might find other ways to meet its needs, if the pricing of the services was set at too high a level. 336 So.2d 552. The evidence before the Commission on this point was by no means "so insubstantial that it does not support the result." Id. at 553.

CONCLUSION

The Public Service Commission's $6.15 million reduction of access charges to account for the effects of the change in Florida's gross receipts tax law was an altogether proper exercise of its ratemaking authority. The implementation of this reduction through an adjustment to the LEC's charges for billing and collection services was in keeping with the Commission's discretionary powers to allocate the effects of rate changes in the best interests of the ratepayers and the utilities. The Public Service Commission's decision to reduce access charges in a way which produces the largest immediate benefit for the largest user of billing and collection services, AT&T, was in no way arbitrary and did not discriminate unfairly against MCI or the other IXCs. The Commission was free to consider the realities of the access charge marketplace in deciding how to distribute the effects of the rate reduction and could not be expected to set rates as though it were a mere exercise in cost accounting. This Court should not substitute its judgment for the Commission's in ratemaking matters. The Commission's Orders Nos. 13934 and 14232 should be affirmed.

Respectfully submitted this 23rd day of July, 1985.

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I HEREBY CERTIFY that copies of the foregoing Answer Brief and Motion for Oral Argument of the Florida Public Service Commission have been served by U.S. Mail this 23rd day of July, 1985, on the following:

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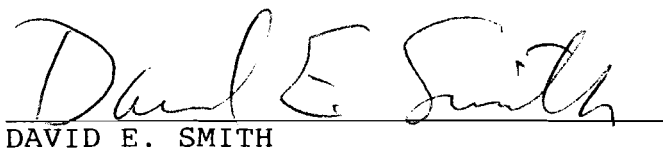

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