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IN THE SUPREME COURT OF FLORIDA

C.F. INDUSTRIES, INC., Appellant, v. KATIE NICHOLS, ET. AL, Appellees,	CASE NO. 70,196

INITIAL BRIEF OF APPELLANTS
FLORIDA CRUSHED STONE COMPANY, ET. AL

Attorneys for Appellants:

Florida Crushed Stone Company
Occidental Chemical Corporation
U.S. Sugar Corporation

Paul Sexton has no objection to Justice Ehrlich sitting on this case. No objection to O.A. 10-4-88

TABLE OF CONTENTS

TABLE OF CITATIONS

PREFACE

The Florida Public Service Commission will be referred to herein as "the Commission." The Appellants will be referred to collectively as "Industrial Cogenerators"

References to the record will be by volume number and page (R, Vol. I, p.1) and references to the transcript of hearing will include "TR" in lieu of "p." (R, Vol. III, TR 1)

STATEMENT OF THE CASE AND OF THE FACTS

The proceeding below was initiated by the Florida Public Service Commission (Commission) to implement regulations of the Federal Energy Regulatory Commission (FERC) in Florida.[1] FERC regulations require that electric utilities interconnect with cogenerators and small power producers (QFs), purchase energy from QFs, sell energy to QFs and, when requested, provided "standby service" to QFs.[2] Power produced by QFs may be consumed by a variety of uses, including manufacturing facilities, hospitals and schools. When a QF cannot meet the full load of the consumer because of an outage, utilities are required to provide "maintenance" or "back-up" service. If the consumer's load exceeds the normal output of the QF, the utility must provide "supplemental" service.[3]

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[1]In 1978, Congress enacted the Public Utilities Regulatory Policy Act (PURPA), 16 United States Code Section 824a, et Seq., requiring FERC to promulgate regulations governing the relationship between cogenerators, small power producers and electric utilities. Each state was required to implement those regulations.

[2]Power sold to QFs is required to be provided at just, reasonable and nondiscriminatory rates, terms and conditions.

The terms Qualifying Facility or QF refer to certain electrical generating facilities defined under Federal Law. They are cogeneration facilities and small power producers which meet specific efficiency standards or fuel use criteria. A cogeneration facility is one which produces (a) electric energy and (b) steam or forms of useful energy (such as heat) which are used for industrial, commercial, heating or cooling purposes. 16 U.S.C. Sec. 796(18)(A). Small power producers are defined as facilities which produce electric energy solely by the use, as a primary energy source, of biomass, waste, renewable resources or any combination thereof. 16 U.S.C. Sec. 796(17)(A).

[3]In its final order, the Commission refers to these services collectively as "standby service." This brief will also use that term.

During rulemaking proceedings in 1981 and 1983, the Commission had adopted rules governing the obligation of public utilities to interconnect with QFs to purchase energy from QFs and to sell energy to QFs. Among those rules was Rule 25-17.082(3)(f), which required public utilities to sell energy to QFs at the same rates as non-generating customers:

> Should a qualifying facility elect to make simultaneous purchases and sales, purchases of electric service by the qualifying facility from the utility shall be billed at the retail rate schedule under which the qualifying facility would receive service as a non-generating customer of the utility; sales of electricity by the qualifying facility to the utility shall be purchased at the utility's avoided energy and capacity rates, where applicable, in accordance with Rules 25-17.0825 and 25-17.083.
>
> Should a qualifying facility elect to make net sales, the hourly net energy and capacity sales to the utility shall be purchased at the utility's avoided energy and capacity rates, where applicable, in accordance with Rule 25-17.0825 and 25-17.083. For those hours during which a qualifying facility is a net purchaser, purchases from the utility shall be billed at the utility's retail rate schedule under which the qualifying facility would receive service as a non-generating customer of the utility. (Emphasis supplied)

In its Order below, the Commission described the effect of Rule 25-17.082(3)(f) as follows:

> Thus, under our current rules, any purchases a QF makes from the purchasing utility are billed at the utility's retail rate schedule under which the QF would receive service as a non-generating customer, regardless of the use for which that power was being provided.

Id at 2 and 3. (Appendix A-1)

However, the Commission's rules did not fully implement FERC regulations and the proceeding below was initiated for the specific purpose of implementing "standby" rates in accordance with FERC rule Section 18 CFR 292.305(b).[4] That Section provides in part:

> (1) Upon request of a qualifying facility, each electric utility shall provide:
>
> (I) Supplementary power;
> (II) Back-up power;
> (III) Maintenance power; and
> (IV) Interruptible power.[5]

Initially, the Commission intended to adopt rules governing the rates for standby service but subsequently chose to act on an ad-hoc basis in order to expedite the process and because its policy was not yet refined. See Order No. 16011. (R.Vol. I, p. 9). Accordingly, no notice of rulemaking was published and the Commission proceeded, instead, pursuant to Section 120.57(1), Florida Statutes.

A public hearing was held in August 1986. Witnesses were sponsored by the Industrial Cogenerators and Metropolitan Dade County, as well as the four electric public utilities, Florida Power & Light Company, Florida Power Corporation, Tampa Electric Company and Gulf Power Company.

At hearing, witnesses for the Industrial Cogenerators and Metropolitan Dade County proposed that the standby tariffs be optional for QFs, that is, that a QF be entitled to choose to

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[4] See Order No. 17159, at 3. (R.Vol. III, p. 144).

[5] 18 CFR 292.305(b)

remain on the rate for non-generating customers or opt for standby service instead (R. Vol. V, TR 71-72). They further testified as to the proper rate structure for such optional standby service tariffs (R. Vol. V, TR 15-334, 713-766).

All parties filed post-hearing briefs. In their brief Industrial Cogenerators argued, among other things:

1) The standby rates adopted as a result of the proceeding should be optional and QFs not requesting service under the standby rates should be served in accordance with FERC Section 292.305(a) and Commission Rule 25-17.082(3)(f) under the rate applicable for non-generating customers;[6] and

2) Rates for standby service must not discriminate against QFs in terms of pricing or rate structure.[7]

In its final order, the Commission prescribed the rate structure for standby service and directed the utilities to file standby service tariffs. In particular, the Commission required that the standby tariffs be mandatory for QFs, preventing them from obtaining service under tariffs applicable to non-generating customers.

> Accordingly, we shall require that the tariffs resulting from this proceeding <u>shall be mandatory</u> for all self-generating customers unless there is evidence to demonstrate that

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[6]Section 292.305(a) provides in part that rates for sales to QFs are not discriminatory if they apply to the class the QF would belong to if it were a non-generating customer. <u>See</u> 45 FR 12228.

[7]R.Vol. II, p. 275

> their load characteristics resemble those of normal full requirements customers.
>
> In view of our decision on this issue, our reference to self-generating customers (SGC) shall include all cogenerators and small power producers whether or not they have obtained qualifying facility (QF) status.

Id at 6 and 7.

However, the Commission did not amend Rule 25-17.082. Thus, subsection (3)(f) of that rule, which requires QFs to be billed under the same rate schedule as non-generating customers, remains in effect.

In its final order, the Commission prescribed the rate structure for the mandatory standby tariffs. In so doing, it incorporated elements not normally applied to non-generating customers. In particular, it reintroduced a "ratchet," or minimum charge, which it had previously eliminated for all non-generating customers. Id, at 15-17.

A notice of appeal was filed with this Court on March 9, 1987. This Court stayed the appeal on the Appellant's motion until the Commission disposed of a Motion for Reconsideration. The Commission ruled on that motion and, after the Appellants notified the Court, it lifted the stay. A second motion to stay was filed with the Court by the Appellants so that certain federal issues could be raised before the FERC and, if FERC declined jurisdiction, those issues could then be raised before this Court. That Motion was denied on January 26, 1988.

This brief addresses only issues arising under state law and is specifically not intended to raise any issues arising under the

constitution, laws or treaties of the United States. Further, it is specifically not intended to bring into issue the Commission's compliance or noncompliance with the regulations of FERC or the provisions of PURPA. Those issues have been raised exclusively in a separate proceeding initiated before FERC, entitled: Industrial Cogenerators v. Florida Public Service Commission, FERC Case No. EL88-10-000. References to PURPA and FERC regulations in this brief are made only to provide the Court with an understanding of the context of the proceeding before the Commission.

SUMMARY OF ARGUMENT

In its order, the Commission required QFs to purchase electrical service only under utilities' special standby service tariffs. This requirement is inconsistent with Rule 25-17.082(3)(f), which provides that sales to QFs by public utilities will be at the rates for non-generating customers. This inconsistency violates Section 120.68(12)(b), Florida Statutes, and accordingly that requirement must be set aside.

In its order, the Commission approved a mandatory rate structure for standby service that discriminates against QFs. This discriminatory rate structure violates Section 366.81, Florida Statutes, which prohibits the Commission from approving any rate or rate structure that discriminates against the use of renewable energy sources or highly efficient systems. QFs, by definition, use renewable energy resources and/or highly efficient systems, thereby falling within the protection of Section 366.81, Florida Statutes. The discriminatory rate structure approved by the Commission includes a "ratchet" or minimum charge, which is not applied to non-generating customers.

The Commission's requirement that QFs purchase electrical service exclusively under utilities' standby service tariffs and the discriminatory ratchet approved for the mandatory standby rates should be set aside.

THE COMMISSION'S ORDER IS INCONSISTENT WITH RULE 25-17.082, FLORIDA ADMINISTRATIVE CODE, IN VIOLATION OF SECTION 120.68, FLORIDA STATUTES

In its Order, the Commission required QFs to purchase electric service from utilities only under their standby tariffs. This requirement means that QFs may not purchase service under the normal rate for service to non-generating customers. This requirement is contrary to Commission Rule 25-17.082(3)(f), which provides that purchases by a QF from a utility, shall be at the utility's retail rate schedule under which the QF would receive service if it was a non-generating customer. This conflict violates Section 120.68(12)(b), Florida Statutes (1987), which prohibits any agency action that is inconsistent with a rule.

Rule 25-17.082(3)(f) remains in full force and effect. This proceeding was initially intended to adopt rules governing standby service provided to QFs but the Commission elected, instead, to proceed on an ad hoc basis. The final result of the proceeding was an order, not a rule. Rule 25-17.082(3)(f) was not amended by the Commission and the Commission must abide by its terms.[8]

Prior to 1984, an agency could enter an order inconsistent with one of its rules simply by explaining its deviation. Section 120.68(12), Florida Statutes (1983), provided in part:

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[8]At no time did the Commission take any action to formally initiate rulemaking under Section 120.54, Florida Statutes, and its actions did not satisfy the procedural requirements of that Section. No notice of rulemaking was issued pursuant to Section 120.54(1)(a), Florida Statutes, nor was any rule or rule amendment filed with the Secretary of State for adoption.

> The court shall remand the case to the agency if it finds the agency's exercise of discretion to be:
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> * * *
>
> (b) Inconsistent with an agency rule, an officially stated agency policy, or a prior agency practice, if deviation therefrom is not explained by the agency;
> (Emphasis supplied)

This provision has been relied upon to hold that an agency may deviate from its rules.[9] However, in 1984 the legislature amended Section 120.68(12) to prohibit any inconsistency with an agency rule:

> (12) The court shall remand the case to the agency if it finds the agency's exercise of discretion to be:
>
> * * *
>
> (b) Inconsistent with an agency rule;
>
> (c) Inconsistent with an officially stated agency policy or a prior agency practice, if deviation therefrom is not explained by the agency;[10] (emphasis supplied)

The 1984 amendment to Section 120.68(12) clearly shows a legislative intent that agency orders must now be consistent with agency rules. Once agency policy is codified by rule, the agency may only change that policy via rulemaking pursuant to Section 120.54.

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[9] see General Telephone Company of Florida v. Florida Public Service Commission, 446 So.2d 1063, 1070 (Fla. 1984); Florida Waterworks Association v. Florida Public Service Commission, 473 So.2d 237, 245 (Fla. 1st DCA 1985). Notably, the Commission did not even comply with Section 120.68(12)(b), Florida Statutes (1983). Its final order does not explain why it was deviating from rule 25-17.082(3)(f).

[10] Section 4, chapter 84-173, Laws of Florida.

The requirement of Rule 25-17.082(3)(f) is clear and no exception is stated in the rule.[11] The Commission must act consistently with its rule and cannot require that QFs purchase electric service solely under a public utility's standby rate tariffs. The Commission's requirement that QFs purchase electrical service exclusively through utilities' standby service tariffs must be set aside.

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[11]It should be recognized, of course, that the rule is an implementation of FERC regulations, one of which requires a utility to provide standby service on the request of a QF. See 18 CFR 292.305(b)(2); Oglethorpe Power Corporation, et. al., Docket No. RE 81-56-001, 35 FERC 61,069, April 21, 1986. The rule should be construed in that light.

THE COMMISSION'S ORDER APPROVES RATE STRUCTURES THAT DISCRIMINATE AGAINST THE USE OF RENEWABLE ENERGY RESOURCES AND HIGHLY EFFICIENT SYSTEMS, IN VIOLATION OF SECTION 366.81, FLORIDA STATUTES

In its order, the Commission approved a mandatory rate structure for standby service that results in discrimination against QFs. This discriminatory rate structure violates Section 366.81, Florida Statutes, and must be set aside.

Section 366.81, Florida Statutes, encourages the use of renewable energy sources and highly efficient systems and prohibits the Commission from approving any rate or rate structure which discriminates against any class of customers on account of the use of such systems:

> The Legislature finds and declares that it is critical to utilize the most efficient and cost-effective energy conservation systems in order to protect the health, prosperity, and general welfare of the state and its citizens. . . . Since solutions to our energy problems are complex, the Legislature intends that the use of solar energy, renewable energy resources, highly efficient systems, and load-control systems be encouraged. Accordingly, in exercising its jurisdiction, the Commission shall not approve any rate or rate structure which discriminates against any class of customers on account of the use of such systems or devices. . . . The Legislature further finds and declares that ss. 366.80-366.85 are to be liberally construed in order to meet the complex problems of reducing the growth rates of electric consumption and weather-sensitive peak demand; increasing the overall efficiency and cost-effectiveness of electricity . . . production and use; and conserving expensive resources, particularly petroleum fuels. (Emphasis supplied)

QFs, by definition, use "renewable energy sources" and/or are "highly efficient systems."[12] The stated purpose of PURPA is to encourage conservation of energy and the efficient use of energy resources by public utilities. FERC noted in its 1980 rulemaking that its standard for cogeneration efficiency is more efficient than any combination of separately generated electricity and steam using efficient, state-of-the-art technology. 45 FR 17967. In its report on Senate Bill 2114, the Senate stated that two-thirds of the energy used in electricity generation and distribution is wasted.[13] FERC also stated that a typical backpressure steam turbine cogeneration facility has an effective heat rate as low as 4500 BTU/KWh - twice the efficiency of central station utility generation. 45 FR 17969. In a publication issued after its rulemaking FERC stated that energy production by QFS could save

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[12]Under 16 United States Code Section 796(17)(A), a small power production facility must produce energy solely by the use of biomass, waste, renewable resources or geothermal resources. Under 16 United States Code Section 796(18)(B) a cogeneration facility must meet FERC requirements respecting fuel use and fuel efficiency.

Under 18 CFR Sec. 292.204(b), a small power production facility must rely on biomass, waste or renewable energy sources for more than 50% of its energy input and may not use oil, natural gas or coal for more than 25% of its input. Under 18 CFR 292.202(a), "biomass" means any organic material not derived from fossil fuels. Under 18 CFR 292.202(b), "waste" means by-product materials other than biomass.

Under 18 CFR Sec. 292.205(a), a cogeneration facility must meet minimum efficiency standards for useful power output and useful thermal output.

[13]S. Rep. No. 95-142, 95th Cong., 1st Sess., 21 (1977).

the nation 1.75 million barrels of oil per day by 1995.[14] QFs fall squarely within the scope of Section 366.81, Florida Statutes, and the Commission may not approve any rate or rate structure which discriminates against them. However, this is precisely what the Commission has done.

The prohibition against discrimination in Section 366.81 is strict and literal. It prohibits discrimination per se. In contrast, Sections 366.03-366.07 prohibit "unjust" discrimination, "undue" or "unreasonable" preference or advantage. Thus, the Commission may normally approve a rate or rate structure that "reasonably" discriminates among customers. However, under Section 366.81, there is no allowance for "reasonable" discrimination against the use of renewable resources or highly efficient systems. Such discrimination is strictly forbidden because it interferes with the stated goal that these uses be "encouraged."[15]

The purpose of the proceeding below was to establish standby service rates for QFs which, by definition, must utilize renewable

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[14] Rulemakings on Cogeneration and Small Power Production, Federal Energy Regulatory Commission, Introduction 1981. In its 1983 rulemaking, the Florida Commission itself recognized that QFs reduce Florida's dependence on the use of foreign oil. See Amendment of Rules 25-17.80 through 25-17.89 relation (sic) to cogeneration, Florida Public Service Commission Docket No. 820406-EU, Order No. 12634, October 27, 1983.

[15] Additionally, had the legislature intended to allow the Commission to approve "reasonable" discrimination against the use of renewable resources or highly efficient systems it would simply have relied on existing provisions of Chapter 366. Quite clearly, the Legislature intended a different rule to apply under Section 366.81.

resources or highly efficient systems. In its final order the Commission made these rates mandatory for QFs. Thus, the rates and rate structure for standby service are subject to Section 366.81, Florida Statutes. Any discriminatory rate structure included in the standby rates for QFs necessarily contravenes Section 366.81, Florida Statutes.

The Commission approved just such a discriminatory rate structure for standby service. In designing the mandatory rate structure for standby service, the Commission utilized many of the same ratemaking elements used to establish the rate structure for services to non-generating customers.[16] However, the Commission also utilized one ratemaking element that it does not use to establish rates for other services: a ratchet. Normally, demand charges for service are based on a monthly meter reading. That means that a customer's demand charge normally rises and falls from month to month. However, when a ratchet is employed, the highest demand becomes the minimum demand for future periods. Thus, the customer's demand charges easily rise but do not easily fall.

Prior to 1980, all public utilities in Florida had ratchets on the demand charges in their tariffs. Normally, these ratchets had a fixed period of operation, for example 12 months. Under a

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[16]These elements included customer charges, demand charges and energy charges. A customer charge is a fixed monthly charge designed to recover certain fixed costs of serving a customer, such as meter reading and billing. A demand charge is a charge designed to recover the cost of providing the capacity to deliver service to a customer. An energy charge is designed to recover the cost of generating and delivering electricity to a customer.

12-month ratchet, a customer's highest demand became his minimum demand for 12 months and he was billed for at least that demand each month, even if his actual demand was well below that amount. If the customer kept his demand down for 12 months, the ratchet would fall to the next lowest demand within the prior 12 months. However, any increase in demand would raise his minimum demand charge for the next 12 months.[17]

Beginning in 1981, the Commission began to eliminate ratchets from the tariffs of public utilities. By February 1983, all ratchets had been eliminated and no customer's demand charge was subject to a ratchet.[18] In Order No. 10557, the Commission stated:

> We find that ratchets, while recognizing the benefits of peak load pricing, ignore the diversity of customers' peak loads. One customer may constantly be at his peak demand throughout the peak season. Another customer may attain his maximum load only briefly

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[17]As an example, over a one-year period a customer may have a 5,000 Kw demand for the first month, a 2,000 Kw demand for each of the next ten months and a 5,000 Kw for the twelfth month. Without a ratchet, the customer would pay demand charges for his actual monthly demand, which would fluctuate up and down each month. With a 12-month ratchet, however, the customer would pay demand charges for 5,000 Kw for all twelve months and no less than 5,000 Kw per month for the next twelve months.

[18]In re: Petition of Florida Power & Light Company for authority to increase its rates and charges, Florida Public Service Commission Docket No. 810002-EU, Order No. 10306, September 23, 1981; In re: Petition of Gulf Power Company for an increase in its rates and charges, Florida Public Service Commission Docket No. 810136-EU, Order No. 10557, February 1, 1982; In re: Petition of Tampa Electric Company for an increase in rates and charges, Florida Public Service Commission Docket No. 820007-EU, Order No. 11307, November 10, 1982; In re: Petition of Florida Power Corporation to increase its rates and charges, Florida Public Service Commission Docket No. 820100-EU, Order No. 11628, February 17, 1983. See Appendix A.

> and/or infrequently during the peak season. Yet, with a ratchet, both customers would pay demand charges based on their maximum demand. This seems inequitable. (Emphasis supplied).
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> Id, at 46.

In its order below, the Commission reintroduced ratchets only for standby service for self-generating customers, which is mandatorily applicable to QFs. Application of a ratchet to only mandatory standby service discriminates against QFs. This discrimination is prohibited by Section 366.81, Florida Statutes.

In its order, the Commission recognizes that QFs are being treated differently from other customers and states that it plans to "investigate and consider imposing ratcheted charges . . . for all customers in future rate cases." Id, at 17. In fact, however, the Commission is doing nothing to alleviate the disparity between the rate structure for mandatory standby rates and the rates for non-generating customers. Even if there were a plan of action, it would not alleviate the ongoing violation of Section 366.81. However, the Commission has chosen to take no action to address this disparity, even though it has just recently concluded a rate case, by settlement, for Florida Power Corporation. The Commission neither investigated nor considered the imposition of ratchets in that case.

The Commission's application of a ratchet to mandatory standby rates for QFs constitutes a discriminatory rate structure in violation of Section 366.81 and should be set aside.

CONCLUSION

The Commission's order mandates that QFs receive electric service from utilities only through their standby service tariffs. This requirement deviates from the Commission's own rules and must be set aside. The Commission established a discriminatory rate structure for these mandatory standby rates, in violation of Section 366.81, Florida Statutes. This discriminatory "ratchet" must be set aside.

Dated: February 26, 1988

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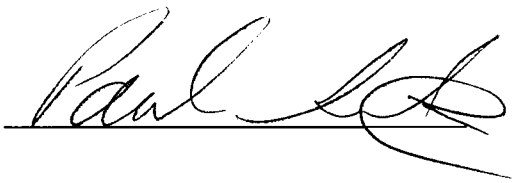

INDEX TO APPENDIX