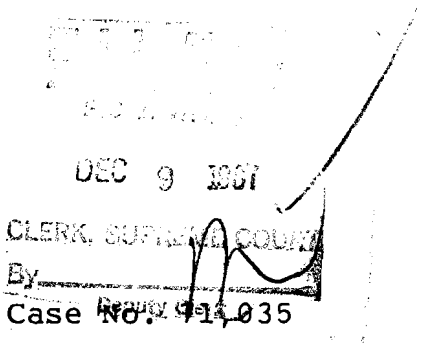
IN THE SUPREME COURT OF FLORIDA



SOUTH FLORIDA NATURAL GAS COMPANY

Petitioner,

vs.

PUBLIC SERVICE COMMISSION,

Respondent.

Case No. 77,035

Appeal from Final Agency Action of the Public Service Commission

Petitioner's Initial Brief

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Preliminary Statement

Throughout this brief South Florida Natural Gas Company will be referenced as "the Company" and the Public Service Commission will be referenced as "the Commission". Citations to the record on appeal will be shown as "R ____."

Statement of the Case

On July 14, 1986, the Company filed with the Commission a request for a permanent rate increase of $343,414 and an interim rate increase of $120,213 per year. (R 7). On September 22, the Commission suspended the Company's proposed permanent rates pending a hearing and final decision in the case. (R 13). On November 19, the Commission approved a revised interim rate request of $88,392. (R 33).[1]

On August 4, 1987, the Commission issued Order No. 17933, entitled Final Order, which approved a permanent rate increase of $49,542 and ordered a refund of $38,850 on an annual basis for interim rates which had been collected at an annual rate of $88,392. (R 336, 338, 347). A timely notice of appeal was filed in the Court with respect to Order No. 17933. (R 372).

Pursuant to a directive of the Court entered on October 5, the Company's initial brief was to be served on December 5, a Saturday. Counsel for the Company confirmed with the clerk of

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1 The Company had revised its interim rate request after the Commission waived the 60-day requirement of section 366.071(2)(a), Fla. Stat. (1985).

the Court that service on December 7 was appropriate. Upon application of the Company, the Commission approved a stay of its final order pending appeal.

Statement of the Facts

The procedural aspects of this case are as important to the issues on appeal as the substantive facts which underlie the Commission's determination of rate case issues. For the Court's convenience, the Company has separated the procedural facts from the substantive facts.

1. Procedural facts.

The Company's rate case began with a request for approval of a test year ended December 31, 1985 (R 1), which was approved. (R 31). The Company filed its petition for permanent and interim rate increases with the Commission on July 14, 1986. (R 7). This petition was submitted using the format for minimum filing requirements (known in utility parlance as MFRs) as required by the Commission. (R 7; Vol. V, p. 1). The Company was furnished a computer model program, in the form of a floppy disk, for its rate filing. This disk had been derived from a rate proceeding involving the state's largest gas utility company, Peoples Gas Company. (R 187). The Commission's disk provided a format for the Company to submit data for a so-called "test year", in order to provide an historical record on which to determine rate case issues, and for two consecutive twelve month

periods called "attrition years." Attrition years are used in rate proceedings to project the Company's financial position and revenue needs for the two successive years after the test year.

Shortly after the Company's petition was filed, the staff of the Commission challenged the Company's proposed interim rate increase as regards an intercompany debt carried on the Company's books, believing it required a so-called "acquisition adjustment" to the Company's proposal for interim rates. The staff's challenge to this entry delayed action on the interim rate increase for approximately 75 days (R 13-14), but after examining evidence and discussing the matter with Company officials and outside accountants the staff determined that the Company's original treatment of the items would stand. (R 33, 132-34, 149-53, 186).

On October 15, 1986, the Commission issued an order setting prehearing procedures and filing deadlines for all parties to the Company's rate proceeding. (R 27). The Company filed its prefiled exhibits and direct testimony in accordance with that order on November 24, 1986.

Toward the end of 1986 and continuing into early 1987, the staff of the Commission submitted more than 90 interrogatories to the Company, took the deposition of two consulting accountants and the financial vice-president of the Company, and requested that the Company produce approximately 26 exhibits relating to financial data. (R 50-51). At that time no

person or party had appeared in the proceeding to challenge the Company's rate requests.

In January 1987, Commission staff filed its direct testimony under the order on prehearing procedures, consisting only of testimony from one of its employees, Mark Cicchetti, on the issue of the reasonable cost of common equity capital. (R Vol. IV, pp. 196-218). No other testimony or pleading was pre-filed by the Commission staff, and no other person or party subsequently sought to appear or provide testimony in this rate proceeding at any stage. Pursuant to the order on prehearing procedures, the record of exhibits and direct testimony was at this point technically closed. (R 28).

On March 11, 1987, the staff of the Commission filed a prehearing statement which contained 56 "issues" which the staff had identified to be addressed in the rate proceeding, together with a number of exhibits prepared by staff of the Commission's various divisions. (R 66). The Company filed its prehearing statement, in accordance with the order on prehearing procedures, on March 12 (R 114), and amended it one day later. (R 116).

On March 13, counsel for the Company and staff members of the Commission held a pre-prehearing conference, to identify issues for the rate proceeding and to clarify the role of Commission staff in the proceeding. (R 225). On March 25, a prehearing conference was held before one Commissioner, at which time discussion took place regarding the role of Commission staff in the rate proceeding, and as to the alleged "issues" for the

rate hearing. (R Vol. III). At the same time and place that this conference was held, the Commission conducted a customer service hearing for the general public. (Id.)

On April 3, the Commission issued a prehearing order which purported to set the "issues" for the rate case hearing. (R 118). The issues raised in this directive consisted only of alleged issues which had been developed and put forward by the staff of the Commission, as there were no intervenors or other parties in the proceeding. (R. Vol. IV, pp. 12-14).

A public hearing was held on the Company's petition for a rate increase on April 8. (R Vol. IV). The only testimony presented was that of Company witnesses, who were cross-examined by a staff attorney of the Commission. At this hearing, the Company's MFRs and prefiled testimony were formally made a part of the record of the proceedings (R 38-39, 51, 52-76, 194), and the parties stipulated that the prefiled testimony of Mr. Cicchetti would be admitted and relied upon, for the limited purpose of determining the reasonable cost of common equity capital. (R 194). Certain documents used by staff of the Commission during cross-examination of Company witnesses were also admitted into evidence. (R 194-95). No substantially affected person testified, and no member of the staff of the Commission testified.

At the hearing, the Commission authorized the Company to submit a late-filed exhibit in order to document its revised figures for the Company's rate case expense. (R 192-93). This

late-filed exhibit, denominated exhibit 11, reflected aggregate rate case expenses of $142,093. (R Vol. V).

The Company filed a statement of issues and positions on May 26. The initial portion of this statement again questioned the role of the staff of the Commission in a proceeding where no substantially affected person intervened to challenge the Company's proposed rates, and no evidence other than that of the Company was placed on the record. (R 176). On June 18, the staff of the Commission filed a memorandum containing its recommendations, discussing again the matters the staff had previously raised as alleged issues and comparing the Company's position against the staff's. This memorandum is not before the Court as a part of the record on appeal. The Company requested its inclusion on the record but was advised it cannot be included by reason of the Court's decision in Occidental Chemical Co. v. Mayo, 351 So.2d 336, 341 n. 9 (Fla. 1977).

At a special agenda conference on July 13, which was continued on July 15, discussion was had and action was taken by Commissioners Wilson and Herndon on various issues in the rate proceeding. When the Company sought to have the transcripts of these conferences included in the record, the Commission advised that they could not be included as a result of the Occidental decision. The decisions of the two Commissioners became the Commission's Order No. 17933, which is the subject of this appeal.

2. Substantive facts.

The Company is a relatively small, regulated natural gas utility, having approximately 3,200 customers and only ten full time employees. (Vol. IV, pp. 87-88). The Company had requested and obtained rate increases in previous years, the last of which was obtained in 1984 at the end of its 1983 rate case. (R Vol. V, Exh. 1, p. 2; Vol. IV, p. 84).

Following the Commission's suggested format for MFRs, the Company placed before the Commission required data with respect to its request for proposed rate increases, in the form of detailed financial information and prefiled testimony of a Company vice-president and an outside, consulting accountant. (R Vol. V, Exh. 1; Vol. IV, pp. 16-19, 52-76). These same individuals later testified at the rate hearing, verifying the information presented and answering questions from the staff of the Commission. (R Vol. IV, pp. 14, 37).

Other than the prefiled statement of Commission employee Cicchetti, no staff person presented testimony or documentary evidence in support of positions and issues asserted on its behalf. No other person or party appeared or offered evidence in the proceeding. Consequently, the record in this case is composed solely of Company data and testimony, with the sole exception of Mr. Cicchetti's non-controversial testimony regarding the cost of common equity capital.

The Commission's final order denied the Company complete rate relief in several respects. Because of the space limitations for this appeal, the facts underlying all of the actions taken by the Commission can not be reviewed here. Rather, several representative acts of the agency are summarized in the following paragraphs.

(a) Attrition years. In its MFRs, the Company followed the format provided by the Commission for submitting data for a test year and two attrition years. (R 338). Substantial and competent evidence was provided, initially and subsequently, in support of the attrition calculations submitted. (R Vol. V, Exh. 1; Vol. IV, pp. 37-40, 85-89, 153-54). Throughout the evidentiary phases of the proceeding, the staff of the Commission raised concerns and caused the Company time and expense relative to a number of adjustments in the Company's calculations for attrition years. (E.g., R Vol. V, pp. 156-76). At no time, however, did the staff of the Commission (or any other person) suggest that the use of attrition years was inappropriate.

In its final order after the close of evidence, the two assigned Commissioners determined that no attrition years would be approved. (R 338). Rather, the Commissioners randomly selected and approved a few discreet adjustments to the test year

to reflect "known changes" in the test year data. (Id.).[2] No opportunity was available, or subsequently made available, for the Company either to challenge the elimination of attrition years or to demonstrate that other items of known change were omitted from consideration.

(b) Rate case expense. In the MFRs filed at the commencement of the rate case, the Company reported a projected expense of $63,000 for the rate case based on its prior rate case experience. (R Vol. V, Exh. 1; Vol. IV, pp. 40, 48). After having incurred the costs of defending the Company's interim rate request against the staff's challenge to an intercompany debt item as being an acquisition adjustment, and the costs of responding to the Commission staff's extensive, formal discovery efforts, the Company revised its estimate of rate case expense to $115,253, and later to $142,384, based on increased costs for lawyers, for accountants, and for the Company itself. (R IV, 48-51; Vol. V, Exh. 11).

A Company witness testified extensively as to the reasons for and basis of the increase over initial estimate. (E.g., R Vol. IV, pp. 40, 119-37, 189-90, 192). Neither the staff of the Commission nor any other person presented evidence

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2 In an appropriate case, utility rates may be set on the basis of a test year adjusted by known changes in facts occurring after the close of the test year. See United Telephone Company v. Mayo, 345 So.2d 648, 650 n. 1. (Fla. 1977). The Commission here, however, adjusted the test year only for known increases in property insurance (R 344) and rate case expense (R 345), and for a known decrease in the cost of long-term debt. (R 346).

on this issue. In its final order, the Commission arbitrarily determined that only $94,000 would be allowed as rate case expense. (R 344-45).

(c) Salary expense. In its MFRs, the Company included $2,800 as part of the compensation paid to one of its vice-presidents. (R Vol. V, Exh. 1). A witness for the Company verified that this amount had indeed been paid, and provided testimony supporting the appropriateness of this item of expense. (R Vol. IV, p. 79-80, 83-84, 115-18, 183-86). Neither the staff of the Commission nor any other person presented evidence on this issue. In its final order, the Commission denied this compensation expense on the ground that the expense was "nonrecurring". (R 341).

(d) Benchmark variances. In its MFRs, the Company reflected an expense in the test year for operating and maintenance expenses attributable to net variances of $32,332 from the Commission's so-called "benchmarks". (R Vol. V, Exh. 1). The computation of benchmark variances required by the Commission's format for MFRs is a methodology for examining line items to see how they increase above what might be considered a norm of operating and maintenance expenses, tested against like items in the Company's prior rate case. (R 341; Vol IV, p. 94). The Company's outside accountant, who had originally devised the benchmark variance concept for utility rate cases, submitted documentary evidence and testimony as to the basis for variance in the Company's MFRs. (R Vol. IV, pp. 90-95, 102-18). Neither

the staff of the Commission nor any other person presented evidence on this issue. In its final order, the Commission adjusted the Company's allowed expenses downward by $43,793, on the ground that the benchmark variances requested by the Company had not been "justified." (R 341-43).

(e) Billing determinants. In its MFR's, the Company identified billing determinants it had computed for the purpose of setting "per customer" rates to be charged. (R Vol. V, Exh. 1). Billing determinants result from a mathematical computation which divides projected or allowed rate recovery by the amount of therms of gas used by customers in the Company's various classes of service. The Company's outside accountant testified at length regarding an historical pattern of diminishing consumption for natural gas, and as to his methodology for reflecting that diminishment in projecting requested rate relief. (R Vol. IV, pp. 156-76). Neither the staff of the Commission nor any other person presented evidence on this issue. In its final order, the Commission rejected the Company's billing determinants and adopted in their place a set of determinants based on customer usage of gas as of December 31, 1985. (R 347).

(f) Other items related to rate base, net operating income and cost of capital were also adjusted by the Commission in its final order.[3] The Company will not discuss other

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3 These three elements compose the basis for determining rates which a public utility may charge. (R 338).

individual adjustments, except to note that they too result from the flawed, overall process of the Commission in dealing with this rate case.

Summary of Argument

The hearing conducted by the Commission for the Company's rate case did not comport with the requirements of the Administrative Procedure Act or provide due process of law. The Commission accepted evidence and testimony from its staff behind closed doors after the proceeding was closed, and relied on that data to deny rate relief for which competent and substantial evidence had been produced. The Commission's due process violations permeated the proceeding. They included the imposition of impossible burdens of proof, the creation of disputed issues although no party appeared to challenge the Company's evidence, the treatment of staff questions as substantive evidence, and the disregard of unchallenged and unrefuted evidence presented by the Company on numerous issues of fact.

Prominent examples of the Commission's arbitrary action are its rejection of the attrition year methodology for determining rate cases, its disallowance of rate case expenses incurred as a result of the staff's discovery activities, its disallowance of allegedly "nonrecurring" salary expense, its arbitrary adjustment of operating and maintenance expense benchmark variances, and its unwarranted adjustment of billing

determinants. Each of these arbitrary actions of the Commission can and should be reversed by the Court. As these items are merely exemplary of the flawed process by which the entire case was handled by the Commission, the Court should direct the entry of an order which awards all amounts proved by the Company in the non-adversarial proceeding below.

The Court should not remand for a new proceeding, however. The costs of a new rate proceeding, to cure the Commission's due process deprivations, should not be borne by the Company or its customers. Rather, the Court should direct the entry of an appropriate order granting the rate relief requested, as authorized by section 120.68(13)(a)1, Fla. Stat. (1985).

Argument

1. Introduction.

Unlike the usual utility rate case, in which arguments are presented as to whether competent and substantial evidence supports a Commission determination because parties in the proceeding had presented evidence to support Commission action adverse to the rate applicant, this case uniquely involves the denial of requested rate relief based on no record other than the Company's evidence.[4] Other than the agreed testimony of Mr.

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4 Documents were introduced during staff's cross-examination of Company witnesses. Technically, of course, this evidence was

Footnote continued on next page.

Cicchetti on rate on equity capital (which is not in dispute), there is no evidence of record beyond the written evidence and testimony of the Company itself. Yet the Commission has slashed a request for $343,414 for the test year down to $49,542, and has completely eliminated two attrition years of increased revenue for the Company. These actions were taken without a shred of evidence on the record to support them.

The staff consistently disavowed that it was speaking for the Commission in raising issues and developing non-record computations and assertions. (R 229-30). In allowing staff to play the dual roles of a non-party adversary and advisor to the Commission, the Commission disregarded the requirements of the Administrative Procedure Act ("the APA"), to which it is indisputedly subject, and the fundamentals of due process. In fact, the action of the Commission in this proceeding presents a due process issue of unprecedented magnitude, for not one but three distinct violations of due process occurred.

Footnote continued from previous page.

inadmissible, as it was offered during the Company's case in chief and could not be subjected to cross-examination or rebuttal evidence. (See discussions at Vol IV, pp. 95-102, 125-28, 156, 177-81, at which time this evidence was objected to.)

> Ordinarily it is improper to permit the introduction of exhibits during cross-examination.

Padgett v. State, 53 So.2d 106, 109 (Fla. 1951). See also Ehrhardt, Florida Evidence § 612.2 (2d Ed. 1984). The introduction of inadmissable evidence in this case goes to the due process of the proceeding, rather that the quality of the evidence itself.

(a) First, the Commission denied the Company due process by relying on calculations and testimony of the staff of the Commission which were not made a matter of record, were not subject to cross-examination, and were even characterized throughout the proceeding by the staff and Commission members as not being "evidence" on which the Commission could base an order.

(b) Second, the staff of the Commission acted in the dual roles of advocate against the Company (through discovery, presentation of issue papers, cross-examination of Company witnesses, and the submission of its own, self-generated financial data), and private, ex parte advisors to the Commission in its decision-making capacity. In this latter capacity, the staff of the Commission clearly "testified" and had its recommendations adopted by the Commission.

(c) Third, the traditional burden of presenting a rate case by competent and substantial evidence was jettisoned by the Commission, and in its place the Company was obliged to respond to non-testimonial, non-evidentiary assertions of the Commission's staff. The untenable posture into which the Company was placed produced an ever-increasing burden of going forward and disproving non-evidentiary calculations and testimony of the Commission staff, with as much prospect of success as boxing against one's own shadow.

The Company had been concerned about the direction of this proceeding from the first, and it raised this concern at the earliest, possible occasion. Due process issues were raised at a

pre-prehearing conference held on March 13, 1987 (R 229-45) and were renewed throughout the proceedings. (E.g. R Vol. IV, pp. 8, 10, 11, 14, 25, 26, 30, 31, 125-28, 177-78). The Company's concern was sloughed off by the staff and the Commission, however, on the grounds that the staff would not testify in the proceeding and that exhibits and financial data prepared by the staff would not be made a part of the record of the proceeding. (R Vol. IV, p. 14).

Despite staff and Commission assurances, the Company's worst fears came to pass. Staff having been allowed to raise "issues" as if it were a party, the Company's burden of proof became an evidentiary nightmare, and numerous, critical recommendations and computations of the staff were adopted by the Commission in its final order. Additionally, the very concept of attrition years which the Company had been expected to follow, and had to expend funds to defend, was discarded by the Commissioners themselves after the record of the proceeding had been closed and all Company input or comments were forbidden. These due process violations are discussed in more detail below.

2. Due process violations.

(a) The nature of agency staff's participation.

The Commission is directed by section 366.06(2), Fla. Stat. (1985), to hold a public hearing on rate increase requests, and thereafter to determine just and reasonable rates to be charged. The procedural requirements for such a hearing are

determined by the APA, however, for the Commission is an "agency" for purposes of the APA and as such is subject to all its provisions. See section 120.52(1)(b), Fla. Stat. (1985). Section 120.57 of the APA would govern this case, as it sets the only procedures by which an agency can enter an "order" within the meaning of the Act.[5]

Under section 120.57, there can only be either a formal proceeding under subsection (1) or an informal proceeding under subsection (2). The deciding factor between the two is whether there exists "a disputed issue of material fact." See the opening paragraph in section 120.57. A hearing under section 120.57(1) is required whenever material facts are in dispute.

The Commission proceeded in this case under section 120.57(1) as if there were disputed issues of material fact.[6] Yet the only disputed "issues" in this case were those raised by the staff of the Commission, and staff was not an authorized

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5 Since an "order" is defined to mean a final agency decision which does not have the effect of the rule (section 120.52(10)), the order on appeal in this case constitutes an order of an agency within the meaning of the APA.

6 The proceeding below could not have been conducted under section 120.57(2), as that subsection commands that an agency develop a position with respect to an application or petition and then give reasonable notice of its proposed action, whether proposed or already taken. See section 120.57(2)(a)1, Fla. Stat. (1985). At no point prior to its final order in this case did the Commission give notice of proposed agency action. In any event, the Commission's staff expressly stated that its prehearing list of issues was not proposed agency action. (R 234, 2237, 240, 244).

participant in the proceeding under the APA or the Commission's own rules.[7]

The Commission allowed its "staff" to act as an adversary party, as if it were some autonomous entity or body, but it did not require it (the "staff" entity) to appear as a party. The staff repeatedly disclaimed that it was representing the Commission itself. As a result of the Commission's deviation from the statute and its rules, the hearing in this case had an unauthorized participant which was accorded the rights of a party, without being bound by the due process responsibilities of a party.

A proceeding under section 120.57(1) requires the presence of "parties". The APA and the Commission's rules contemplate that "members" of an agency's staff may appear as a party if they are in fact authorized to intervene or participate as such. See sections 120.52(11)(c), Fla. Stat. (1985), and Rule 25-22.026(3), Fla. Admin. Code. Indeed, it has not been unusual for the members of the Commission's staff to testify in rate

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7 The rules of the Commission recognize that hearing procedures for the Commission are governed by the APA. See Rule 25-22.025, Fla. Admin. Code. Under those rules, parties are identified by title for 120.57 proceedings (Rule 25-22.026(1)) and the staff of the Commission is given discretionary authorization to participate "as a party". Rule 25-22.026(3). The rules further authorize a prehearing officer to require "each party" to file a prehearing statement (Rule 25-22.038(3)), and to require "the parties" to hold a prehearing conference. Rule 25-22.038(4). Finally, a prehearing order may be issued which sets forth the issues in the case and the positions "of the parties." Rule 25-22.038(5).

cases. (R Vol. IV, pp. 100, 135-37). That did not occur here, however. No member of the staff other than Mr. Cicchetti ever made himself or herself a party.

By allowing the participation of unauthorized personnel who were not parties, the Commission violated the directives of chapter 120 and its own rules implementing that statute. For this reason alone, the final order of the Commission cannot stand. See Citizens of Florida v. Mayo, 333 So.2d 1 (Fla. 1976), in which the Court explained that the due process requirements for hearings in a full rate proceeding connote testimony by interested parties, an opportunity for cross-examination, and direct contradictory evidence.

> [T]he public policy of this state [is] in favor of traditional due process rights in rate "hearings". . . Id. at p. 6.

The situation in this case is comparable to that in Deel Motors, Inc. v. Department of Commerce, 252 So.2d 389 (Fla. 1st DCA 1971). In that case the court held that the manner in which a public hearing before the Department of Commerce was conducted deprived the petitioners of administrative due process by failing to meet the minimum requirements of the prior APA. In Deel, the Department of Commerce ordered assessments against members of a self-insurance trust fund based solely on an informal, unsworn presentation of the trustee's attorney.

> No proof was offered as to the correctness or validity of the underlying records . . . . No witnesses were sworn, no testimony taken, no documents offered or received in evidence, and no proof adduced in support of any of the allegations of the petition. (Id. at 392-93).

The deficiencies in Deel were found to constitute a denial of petitioners' basic rights of due process as mandated by the APA; namely that an agency order must

> be based on competent and substantial evidence adduced by the parties consisting of sworn testimony of witnesses and properly authenticated documents bearing the required indicia of credibility. The parties must be accorded the right to confront and cross-examine the witnesses against them, and be reasonably heard on the contentions urged by them with respect to the action to be taken by the agency. (Id. at p. 394).

In this case, as in Deel, the order of the agency was based in substantial part on records and data not placed in evidence or subject to cross-examination. In fact, all factors present in Deel were present in this case.

The Commission also ignored notions of basic fairness by allowing the same staff which acted as its advisors during the decisional phase of the proceeding to act as attorneys having an adversarial interest against the Company. An early illustration of the staff's conflict of interest appears in the opening discussion which took place at a pre-prehearing conference on March 13 (R 229-31):

> [Company Counsel]: Mr. Smith, one of the things I would like to understand as a predicate to our meeting today is your feeling or your belief of what the commission staff is in this case; whether it is the adjunct of the Commission itself, or whether it's a party to this case, separate and independent from the Commission.
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> [Staff Attorney]: We are a party to the proceeding. We are putting on witnesses.

[Company Counsel]: Are your representations the representations of the Commission as far as this proceeding is concerned?

[Staff Attorney]: I am not sure I know what you mean by that. Representations of the Commission?

[Company Counsel]: Who is your client?

[Staff Attorney]: The staff is my client.

[Company Counsel]: The Commission is not your client?

[Staff Attorney]: I don't know how you can really totally separate the Commission from the staff. The staff is in an advisory function relative to the Commission. I take that back. It is representing a position, advocating a position as far as the proceeding is concerned.

[Company Counsel]: So that you are speaking on behalf of your client, the Public Service Commission, when you are speaking?

[Staff Attorney]: No, I am speaking on behalf of the staff.

[Company Counsel]: So, you are not speaking on behalf of the Public Service Commission as your client?

[Staff Attorney]: The Public Service Commission is acting as the trier of fact in this case, as you are well aware. The staff is advocating the position before it as the company is.

[Company Counsel]: So, you are not speaking on behalf of the Public Service Commission as your client?

[Staff Attorney]: That's correct, at least as I understand it.

Staff counsel later reconfirmed his belief that staff could be in an adversarial role without formally entering the proceeding as a party (R 239-40):

You know very well that the staff or [sic] the Public Service Commission is the PSC, and it is

> part of the agency. And we represent, we take an advisarial [sic] role in hearings and filings that come before the Commission. We are part of the Commission. We represent the Commission in its carrying out of its agency business, it's [sic] regulatory business.

As seen, counsel for the staff persisted in his belief that he was an adversary to the Company, although without a client for whom he would appear as a party. (General counsel to the Commission would later advise that, while materials developed by staff may not be admissible as evidence, they can be used by the staff when they act in their post-hearing advisory role to the Commission. (R Vol. IV, p. 13).)

The Company respectfully suggests that "staff" was improperly allowed to participate as a party without having the duties or burdens of a party, contrary to the APA and the dictates of due process.

(b) The Company's evanescent burden.

The Company has always acknowledged its burden, as the one seeking relief, to provide a preponderance of competent and substantial evidence to support its rate request. See Florida Power Corp. v. Cresse, 413 So.2d 1187, 1191 (Fla. 1982). It more than met that requirement in this proceeding. The issue before the Court in this appeal is whether an agency can simply reject all evidence of record--without challenging the credibility of the witnesses who testified--and instead rely on non-record data

from an "adversarial" attorney (to quote staff counsel).[8] The question of "burden" is at the heart of this inquiry.

There were several discussions throughout the course of this proceeding regarding the Company's burden of going forward with evidence to prove the necessity for a rate increase. Specific examples of the Company's difficulty in doing that, where burden and the absence of disputed issues of material fact intertwined, fill the record. See R. Vol. IV, pp. 19 ("Mr. Wilson, the difficulty here is who has the burden"), 20 ("As I apprehend the question by Counsel for the Staff, it is addressing an issue that Staff has raised. I think they have the burden of going forward with that issue. . . . We don't propose to have to defend against issues until they have been -- until evidence and testimony has been offered to which we can respond."), 21-36, 95-102, 155-56; Vol. III, transcript of prehearing conference of March 25, pp. 4-5). At one point, the Commission even acknowledged its inability to develop competent and substantial evidence on the record in a proceeding which has no adverse party and where the staff of the Commission is unwilling to testify. (R 248; and see R 232-38, 238).

The Commission's concept of burden in this case left

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8 In its Statement of Issues and Positions, the Company began with this pronouncement (R. 181):

> the basic issue in this case is simply stated: Will the Order of the Public Service Commission be derived from the record, and only the record?

the Company helpless. By rejecting all of the Company's factual showings without contradictory facts on the record, the Commission placed the Company in an impossible legal position. Every time the Company presented data, even though no contrary data appeared in the record and no notice of contrary testimony by the staff was made available, the Commission upped the burden by saying it simply didn't accept the Company's information. This escalating burden of going forward, and of proving matters which were not contested on the record, proved futile for the Company in the final analysis. The Commission merely wrote in its final order that the Company failed to justify items or meet its "burden". (E.g. R Vol. IV, pp. 95-96, 177). The Company respectfully suggests that the burden requirements applied by the Commission in this case were arbitrary, and do not comport with the requirements of law.

The Commission may, of course, choose to disbelieve the testimony of any witness. It did not do so here. Even the disbelief of a witness, however, cannot justify the rejection of the only evidence of record without production by the Commission of competent evidence of inaccuracy, impropriety or dishonesty regarding the testimony and evidence which the Company presented. See Florida Bridge Company v. Bevis, 363 So.2d 799, 802 (Fla. 1978), in which it was held that rejection of the only evidence on a particular rate case item was arbitrary, and a departure from the essential requirements of law.

(c) Misuse of cross-examination.

Throughout this proceeding, the staff of the Commission took the position that it was privileged to create disputed issues of fact through cross-examination. Despite repeated challenges to that position by Company counsel, the Commission not only authorized that methodology but then relied for its final determinations on non-record data used by its staff in cross-examination. At no point did the Commission understand that cross-examination may in appropriate cases provide a basis to undermine a witness' testimony, but that cross-examination can in no way consistent with due process be used to create evidence (unless of course the witness adopts and thereby sponsors contradictory facts).

For example, the Commission relied on a staff-generated, 4% O&M compound multiplier for its finding as to the appropriate benchmark variance for sales expense. (R 341-42). The only record reference to the staff's 4% multiplier came through a series of questions by staff counsel to the Company's outside accountant regarding an 8% rate he had used in preparing the MFR's. (R Vol. IV, pp. 109). In response to each question asked, however, the witness explained the inappropriateness of staff's 4% rate for this Company in this rate proceeding. No testimony was ever introduced or elicited as to the appropriateness of a 4% rate. In its final order, however, the Commission adopted the staff's 4% compound multiplier. (R 342). This finding is not supported by any

direct evidence, and it is not properly established by cross-examination. Cf. Steinhorst v. State, 412 So.2d 332, 337 (Fla. 1982):

> [Q]uestions on cross-examination must either relate to credibility or be germane to matters brought out on direct examination. . . . Stated more succinctly, this rule posits that the defendant may not use cross-examination as a vehicle for presenting defense evidence.

The misuse of cross-examination as a vehicle to create anti-Company inferences spawned confusion for the Company and prejudice to its rate case. Counsel for the Company repeatedly pointed out the problem, as when he complained:

> There's no affirmative showing that there is some standard up against which to measure the Company's choice to use one person, one place or not another. . . . We don't have an affirmative standard against which to measure it. And that's what I think that the Commission itself is trying to prove, an affirmative case through cross-examination and that's going to produce some problems. (R Vol. IV, pp. 95-96).

Worse, by treating the questions put to a witness in cross examination as substantive evidence in their own right, the Commission in effect allowed staff counsel to "testify", without any opportunity on the Company's part to subject the questioner to cross-examination or to produce rebuttal evidence.

In sum, the Company was denied the benefit of having met its burden of proof through its case in chief because an escalating burden was imposed on the Company to meet non-testimonial statements or figures from non-party staff. The

burden simply grew, receding out of the Company's reach by increasing increments. The Company's search for a finite limit on its burden of proof was a persistent and fruitless concern of its counsel.

3. Attrition years.

In its final order, the Commission acknowledged that the Company had calculated attrition and attrition allowance through December 31, 1987 as required by the Commission's own MFRs. (R 337-38). Although there was no evidence presented to counter the attrition calculations provided by the Company in its MFRs and later amplified at the Company's public hearing (R Vol. IV, pp. 85-89, 153-54, 185-86), two Commissioners concluded that no attrition allowance would be awarded. The Commission explained its rejection of the Company's record data and testimony in support of attrition in this fashion (R 338):

> [S]upplying the calculation required by the MFRs . . . simply provides a way to measure attrition once it has been established. The Utility has the burden to establish attrition as a relevant factor to be considered in setting rates. In this case, we find that South Florida has failed to meet that burden. We find no evidence, or even an allegation, that attrition has historically affected the Utility's earnings or that it will affect them in the future.

The Commission's final order goes on to state that:

> While we reject the concept of an attrition calculation as unsupported by the record, the Utility has presented evidence on some known changes in expenses which our regulatory responsibility demands we consider, notwithstanding the manner in which they were presented.

The Company submits that these statements in the Commission's final order are both inconsistent and inaccurate. It is difficult to understand how the Commission can state that the Company had indeed presented evidence of known changes in expenses, yet failed to meet its burden to establish attrition as a relevant factor to be considered in setting rates. Attrition reflects changes from a prior rate case.

No evidence of record contradicts or countermands the Company's MFRs and explanatory testimony regarding attrition. Yet while acknowledging hard evidence of known changes, the Commission has concluded that the Company failed to meet its burden on this issue. It is impossible to know what that burden could have been if the presentation of unrefuted evidence and testimony was insufficient. (See R Vol. IV, pp. 95-96). The Commission's acknowledgment that the Company proved known expense changes is simply irreconcilable with its declaration that there is neither evidence nor allegation that attrition (a phenomenon which "occurs when operating expenses increase at a faster rate than operating revenues" (R 338)) will affect the Company's earnings in the future.

In complying with the Commission's format for MFRs, the Company projected two attrition years based on known expense increases and a projection for increases in payroll, supplies, and all other expenditures which the Company will necessarily incur. (R Vol. V, Exh. 1). The staff of the Commission disagreed with the Company as to the percentage rate at which

attrition would occur, not because it disagreed with the fact that increases had taken place but because it preferred computations based on the consumer price index. (See R Vol. IV, pp. 86-87).[9]

The arbitrariness of the Commission is shown by the fact that, despite disagreement of its staff as to percentage rates and amounts in the attrition calculations, at least the staff acknowledged throughout the proceeding that the concept of attrition was appropriate. The Commission, however, simply discarded the concept after the close of evidence. This total rejection of the attrition year concept effectively deprived the Company of due process. The Company had no way to refute or rebut the Commission's rationale for the abandonment of the attrition year concept without any notice whatever that the Commission questioned its applicability. Applicability had never been placed in issue.[10] The issues as defined by the Company, by the staff and by the prehearing Commissioner were predicated upon the use of attrition years. The law requires that changes in

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9 The staff of the Commission presented no evidence, however, at any stage of the proceeding, regarding the consumer price index. Like other positions asserted only by the staff off the record, or hinted at through cross-examination of Company witnesses, the preference of staff for different data or concepts was not made a part of the record of the proceeding, and was not subjected to cross-examination or rebuttal.

10 The Commission's own rules recognize the inherent unfairness, and the denial of due process involved in the consideration of any issue or position to which "the parties" have had no opportunity to respond. See Rule 25-22.038(5)(b), Fla. Admin. Code.

rate-making concepts must be supported by evidence of record. City of Plant City v. Mayo, 337 So.2d 966, 974 (Fla. 1976).[11]

As the Company has noted, the Commission selected at random three items with known changes which it acknowledged that the record would support: property insurance, rate case expense and long-term debt rates. The second fallacy of the Commission's action in this regard is obvious. While giving the Company the right to earn revenue sufficient to pay its property insurance at increased cost levels, the Commission refused to give the Company revenue to pay other increased expenses such as salary, group insurance, supplies and the like. Thus, the effect of the Commission's action was dual arbitrariness. First, it arbitrarily decided to reject record data evidence of attrition throughout the Company's expense mix. Second, it arbitrarily

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11 The Commission does not justify its disregard of attrition on the gound of agency expertise. Nor could it. See City of Plant City v. Mayo, supra at 974. And see Florida Gas Company v. Hawkins, 372 So.2d 1118, 1121 (Fla. 1979), where the court has stated:

> "When factual matters affecting the fairness of utility rates are being considered by a regulatory commission the rudiments of fair play and due process require that the Company must be afforded a fair hearing and an opportunity to explain or rebut those matters."

rejected all but two items of increased expense, as if those two items of expense had more record support than all the others.[12]

While the Company does not contest that the record supports a negative capital attrition in the cost of long-term debt or a positive net operating attrition for rate case expense and property insurance, it vigorously contests that the record does not support the full net operating income attrition increases which were presented in its MFRs. The Commission's selection of only three items from the Company's attrition evidence was arbitrary, and its post-proceeding rejection of the attrition concept altogether was capricious.

4. Rate case expense.

The extremes to which the Commission went in this proceeding is perhaps illustrated best by the denial of a significant portion of rate case expenses of $142,093, incurred to prepare the Company's case and to respond to the staff of the Commission. The staff first forced the Company to justify its book entries on an intercompany debt which resulted from a recapitalization, then eventually conceded the item was properly

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12 A third "known change" in historic data which the Commission identified had a negative effect on proposed rates. In its MFRs, the Company reflected the cost rate for long-term debt at 14.52%. (R Vol. V, Exh. 1). Testimony of a Company witness acknowledged that this debt had been refinanced at 10.07%. (R Vol. IV, p. 40-41, 45, 147-49). In its final order, the Commission substituted 10.07% for 14.52% for the test year (R 346), resulting in a drop for allowed overall rate of return from 12.92% to 11.06%. (R 346-47).

reflected on the Company's books. The unrefuted evidence of record indicates that this exercise alone cost approximately $17,000-20,000 in outside accountant's fees. (R Vol. IV, pp. 49, 132-34, 186). Next, the Company was obliged to submit to over 90 interrogatories, three depositions, and the preparation of 26 exhibits during the preliminary phases of the rate proceeding.

A Company witness testified at length on the effect which staff discovery activities had on the Company's expense of presenting its rate case. (See R Vol. IV, pp. 48-51, 80-85, 119-37, 135-37, 189-90, 192-93). The witness testified, in effect, that an initial estimate of $63,000 was developed for rate case expense based on the Company's actual expenditure in the previous, 1983 rate case. The witness testified that the previous case had been a stipulated case, in which there were no controverted issues. The witness further testified, based on his extensive experience in rate case proceedings, that the standard practice of the Commission's staff had been to work with the Company informally, not against the Company formally through depositions and interrogatories, in refining data to be presented for ultimate Commission approval. (R Vol. IV, pp. 135-37).

The witness further testified that the financial burden on the Company in this proceeding, by reason of the way the staff chose to attack the Company's data, was not only unanticipated but extremely high for a company of this size. The witness explained that the Company had only ten employees on a full time basis, and the demands of staff for formal responses to

interrogatories and for the production of exhibits (some as thick as books, R Vol. IV, pp. 50-51), had the combined effects of disrupting operations, causing delays in the preparation of data, forcing the use of outside resources (lawyers and accountants), and diverting Company employees from their ongoing, normal activities.

Despite these explanations, the Commission subsequently determined that the Company's costs of responding to these staff initiatives was unjustified and therefore not recoverable as a rate case expense. The Commission's final order explained its rejection of the Company's record data in terms of what the staff "countered in its recommendation", and "pointed out." (R 344). What the Commission does not note in its final order is that these staff statements and recommendations are not a matter of record in this proceeding.

All of the data on which the Commission relied to reject the record basis of rate case expense was taken either from statements made by staff at the Commission's special agenda conferences, or elsewhere after the close of the evidence, at a time when the staff was acting in an advisory capacity to the Commission. No member of the staff testified to any of these positions, and the Company had no opportunity either to cross-examine these staff "witnesses" or rebut their "testimony". As in Deel Motors, Inc. v. Department of Commerce, supra, the reliance on this type of informal, off-the-record presentation of alleged facts constitutes a denial of due process.

There is a further explanation of record for the Company's difficulties and high cost in presenting its rate case, which the Commission wholly disregards. The Company's witness testified that the MFRs which the Company followed were submitted in the form of computer model disks developed from a previous rate case of the state's largest gas utility company. (R Vol. IV, p. 187). He testified that it was necessary for the Company to convert that disk data format for use in presenting Company data, and that this was extremely difficult because of the difference in the size of the companies, the differing data on which the two companies operate, and the absence of in-house staff to work on such a massive project. This testimony of the witness was unrefuted. Yet the Commission chose to castigate the Company in its final order, and to derogate its efforts to comply, based on the non-testimonial statements of staff after the rate proceeding had closed.

The action of the Commission in rejecting Company evidence lacks a record foundation, and the selection of an amount to be allowed reflects a gross abuse of administrative due process. The Commissioners set the rate case expense award at a level plucked from thin air, based on the hypothesis (uncorroborated on the record) that rate case expense in <u>another</u> company's proceeding was approximately in the amount awarded. Acknowledging that there have been few gas company rate cases which have gone through a full hearing process (just as the Company's witness had testified), the Commission arbitrarily

allowed the Company $94,000 for rate case expense because that was the amount allowed as rate case expense for West Florida Natural Gas Company in a prior proceeding. (R 345).

The arbitrary selection of another company's rate case expense cannot be justified on the grounds of Commission expertise or prerogative. The arbitrary selection of a fact from outside the record of the proceeding plainly violates the notions of agency due process which are embodied in the APA. A company must be allowed to know in advance, and to challenge, the data upon which the Commission chooses to rely. See General Development Utilities, Inc. v. Hawkins, 357 So.2d 408, 409 (Fla. 1978) ("The arbitrary selection of [an equity/debt ratio] as a "fact" comes from outside the record of the proceeding and plainly violates the notions of agency due process which are embodied in the administrative procedure act.") An agency cannot adopt schedules without a factual foundation for doing so. See Broward County Traffic Ass'n v. Mayo, 340 So.2d 1152 (Fla. 1977). There was no factual foundation for the Commission to adopt the rate case expense of the West Florida Natural Gas case in this case.

The evil in selecting a number from another administrative proceeding for use in this proceeding is obvious. There is no evidence of record in this proceeding that the rate case expense for West Florida Natural Gas in its last rate hearing case was indeed $94,000. If the Commission had intended to take judicial notice of that figure, it ignored section

120.61, Fla. Stat. (1985), which requires notice of intent to take judicial notice. See General Development Utilities, Inc. v. Hawkins, supra at p. 409, and see Rule 25-2.111, Fla. Admin. Code. (Even as a matter of judicial notice under its own rule, however, the Commission could only have noticed a prior decision and not the evidentiary underpinnings of a prior decision.) Judicial notice, then, was not appropriate because no notice of the West Florida case was given.

Even if the $94,000 figure from the other case was accurate, there is no evidence in the record to reflect the nature of West Florida Natural Gas Company's rate case, the extent of the staff's discovery efforts in that case, the burden on that Company's employees in regard to the requests for data which were submitted, or a host of other factors which would be relevant to comparing expenditures. The Commission acknowledged in its order that West Florida Natural Gas Company was "considerably larger" than the Company in this case. (R 345). Obviously, a larger company with more than ten employees to run its entire operation would have far less need for outside help, and less overall cost in developing rate case data. It may have had computer capability unavailable to this Company. There is no way to know these things, however, because the record of the proceeding was closed when the Commission arbitrarily selected the other company's rate case expense for application here, and the Company had no opportunity to explore the differences.

5. Salary expense.

This item involves a small dollar amount. In its MFRs, the Company included as part of its contingency reserve (really a salary item) the amount of $2,800 which was paid as incentive compensation to the Company's operations vice president. The Commission's decision to disallow this item was the result of staff's view that it constituted a "nonrecurring" item to be disallowed. The Commission was without legal justification for its disallowance of this item.

> Opinions of regulatory board staffs as to executive compensation and management fees unsupported by evidence cannot be sustained as the basis for disallowance of such expenses.

Florida Crown Utility Services, Inc. v. Utility Regulatory Board, 274 So.2d 597, 598 (Fla. 1st DCA 1973).

The Commission wholly lacked factual justification for disallowing this payment. A witness for the Company explained at length the basis and justification for this payment. (R Vol. IV, pp. 79-80, 183-86). He explained that the payment was necessary to make the overall compensation of the operations vice president competitive with industry-wide contemporaries. Further, the witness testified that the Company has no pension plan, so that salary payments to the Company's small staff were inherently out of line with the amounts necessary to attract and keep competent personnel.

Despite the record basis for Company payment of a $2,800 payment to its operations vice president, the Commission disallowed that amount on the sole basis that it was "nonrecurring". (R 341). This action of the Commission is factually not sustainable because there is no evidence in the record to suggest that the $2,800 payment to the operations vice president is in fact nonrecurring. So far as the record reveals, a payment to this employee may indeed be a recurring expenditure so long as his salary is maintained below competitive levels in the industry. Moreover, the fact that an expense is "nonrecurring" does not, by itself, justify its exclusion from the Company's net operating income computation. Nonrecurring expenditures reasonably incurred by the utility are frequently allowable to the same extent as recurring expenditures. Examples include rate case expenses and the costs of refinancing debt, among numerous others. The Commission's obligation is to determine whether amounts expended by the Company in the course of providing service to its customers were reasonable and reasonably related to the business activities of the operation. Where the only evidence of record supports that view, there is no legal basis to exclude it.

The Company recognizes that the Commission has discretion in rate making proceedings to remove items which are nonrecurring in nature from a test year computation. Florida Bridge Company v. Bevis, 363 So.2d 799 (Fla. 1978). As that case holds, however, the disallowance of a nonrecurring item of

expense will be sustained only when the Commission had a factual basis for its action--in that case, a comparison of test year legal fees against the five year average of fees in prior years.

6. Benchmark variances.

In prior rate cases, the Commission developed the concept of benchmark variances to identify a base line of operating and maintenance ("O&M") expenses that are normal for any particular company. The concept is to take the O&M expenses from the Company's last rate case, and consider how various expenses vary from that prior rate case for the current rate case.

In point of fact, the record reflects that this methodology for analyzing any company's O&M expenses was originally developed by Stanley Cohen, the Company's outside accountant and the principal witness in this proceeding. (R Vol. IV, p. 94). There is nothing in chapter 366, Florida Statutes, or in the rules of the Commission in regard to benchmark variances. The format for producing the data of variances did appear in the computer model provided for the Company's MFRs, however.

The Company complied with the MFRs and identified benchmark net variance of $32,332, which it explained in its MFR's and on the record at the hearing. (R Vol. V, Exh. 1; Vol. IV, pp. 90 et seq.) The Company's outside accountant testified at length regarding the basis for his calculation of these

variances. (R Vol. IV, pp. 90-95, 102-18). The gist of his testimony was that he prepared an aggregate set of plus and minus variances from the Company's last rate case, based in part on required adjustments made in the prior rate case and a redistribution of accounts. This resulted in a netting of the adjustments upward and the adjustments downward, to produce a net upward adjustment. He stated he had aggregated accounts which called for adjustment, using insurance, benefit plans and general administrative expenses as the dominate expense items to be evaluated.

Through its prehearing activities and at the hearing, the staff of the Commission insisted on knowing why the aggregate adjustments prepared by the Company exceeded the consumer price index. (E.g. R Vol. IV, p. 108-09). An explanation was provided, on the record, by the Company's witness. (Id.) This was the only evidence on the point.

Despite the Company's evidence and testimony, the Commission concluded that the evidence of benchmark variances had not been "justified", basing its decision on the language of an MFR schedule which states: "for each functional benchmark variance, justify the difference." (R 341). The Company asserts that the Commission's construction of the word "justify" created an impossible hurdle for the Company, and that instead of using its rule terminology to require an explanation of the source and reason for particular adjustments it placed an interpretation on that term which was tantamount to saying: "you not only have to

tell us why and how the variances were computed, but you have to convince us even if we do not choose to be convinced." (See R Vol. IV, p. 97).

The Commission's final order devotes two and one half pages to explaining why the Commission reduced the allowed benchmark variances by $43,793 to $11,168. (R 341-43). This discussion is illuminating. A first item rejected by the Commission was a variance in sales expense. The salary of one employee had been assigned payroll increases of approximately 8% during the year, and there was no dispute that that his salary was in fact raised by that amount. The Commission determined, however, that the approximate 8% increase was not "justified" because it was greater than "the O&M compound multiplier" (a staff generated notion (R Vol. IV, p. 109) which was nowhere placed in evidence in the proceeding). (R 342). In other words, the Commission simply said that it would not accept what the Company had in fact paid to the employee as a justification for demonstrating that the cost had increased. Rather, the Commission would disregard the evidence of record (R Vol. IV, p. 108-09) and decide that an arbitrary percentage increase, in a lower amount, was appropriate irrespective of what the Company in fact proved.

The same pattern was followed as to other items. For example, when a payroll account was redistributed because an assistant manager spent more time in a supervisory capacity in the test year than in the prior rate case test year, the Commission rejected the increase not because it was not paid but

rather because the accountant testifying on the issue could not specifically answer what supervisory duties the particular employee conducted during the test year. (R 342). The burden of proof imposed by the Commission under the guise of having the Company justify this item was, like the others, impossible to achieve.

The Company witness explained the basis for increasing the supervisory expense for this employee. (R Vol. IV, p. 92). There was no evidence that the assistant manager did not spend more time supervising in the test year than in prior years, or that this was an unjustified use of the limited number of employees that this Company maintained. There was no suggestion that his supervision was not used and useful with respect to the activities of the Company. The Commission simply demanded an explanation of a witness who could not possibly have been familiar with the daily, internal affairs of the Company (R Vol. IV, p. 93), and then it used that failure of explanation to penalize the Company financially. The Commission staff never inquired about supervisory duties when the Company's operations vice president was on the stand, and it did not introduce any independent evidence on the point whatsoever. This was simply another instance of arbitrary disallowance by the Commission, with its after-the-fact justification that the Company failed to meet the Commission's non-ending, impossible burden of proof. The Commission had taken similar action on a salary item in

Florida Bridge Co. v. Bevis, supra at pp. 800-01, which the Court reversed as arbitrary.

The same pattern in conduct occurred in each of the items adjusted downward. The Company justified a positive benchmark variance in general and administrative allocation by $11,168, and explained the adjustment as being attributable to the creation of a new position of vice president-finance, and a general increase in insurance costs. The Commission rejected the adjustment on the ground that the explanation "is a mere statement of how the increase cost came about", and it rejected the Company's testimony explaining the new and future duties of the financial vice president. Indeed, despite unrefuted testimony that this officer was responsible for the refinancing of the Company's long-term debt from a cost rate of 14.52% to a cost rate of 10.07% (R Vol IV, p. 185), the Commission blithely asserted it could "find no evidence that explains why it was necessary or justified to create the new position." (R 343). In other words, the Commission simply refused to accept the more than ample record evidence on this issue.

The Company attempted to explain to the Commission its difficulty with the Commission's legal application of a "justification" requirement.

> And the term "justify" is undefined. It's what I meant by how high is up. . . . And the fact that the Staff has stated some issues here does not, in my opinion, impose a burden on someone else's witness. It's their own affirmative burden to produce evidence which shows that the issues they have placed in

> this record are, in fact, supportable. (R Vol. IV, p. 97).
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> * * *
>
> [T]he basic proposition as I understand the Commission's accounting and MFRs rules is what did you do, what did it cost? At that point I think the burden needs to shift to someone, if someone wishes to come forward to say, "No, you're not -- this is not a prudent expenditure for these reasons." And that's what's lacking here, that's what's concerned us so deeply about this case since roughly the 19th of December. When that day came and went and there was no Staff testimony except for Mr. Cicchetti's. (R Vol. IV, p. 99).

The Company recognizes that it bears the burden of proof in seeking a rate change, and further, that simple production of cost records does not satisfy that burden where the costs are higher than the norm. The Company has the burden of showing that the excess costs incurred were reasonable. If the facts developed at hearing tend to indicate that the excess costs were caused by conditions, the responsibility for which could be attributed to management and for which management could be faulted, then the Company would fail to meet its burden of proof in justifying the excess costs.

In this case, however, the Company amply explained and justified cost items that exceeded the benchmark costs. After having done so, surely the burden of going forward with information to rebut the Company's justification shifted to some other party (such as the staff, if it had appeared as a party). However, there was no evidence presented by any party to contradict the Company's justification. Nor did the staff

produce testimony or evidence to indicate that the Company was at fault for creating conditions which necessitated the excess costs. Contrast Florida Power Corporation v. Cresse, 413 So.2d 1187, 1191 (Fla. 1982). The Company met both its burden of going forward on the reasonableness of these cost items and, by virtue of the staff's failure to produce any contrary or rebuttal evidence on reasonableness or fault, its burden of proof with regard to these benchmark variances.

7. Billing determinants.

In complying with the Commission's format for MFR's, the Company's outside accountant developed billing determinants based on the projected usage of natural gas by the Company's customers in the years for which the rates would be in effect. He had reviewed the history of gas consumption by the Company's customers, and he noted that per-customer usage in each class of service had been diminishing. Since rates are set for the future, he developed a linear regression analysis (a slope line, in effect) based on actual customer usage over an eleven year period running from 1976 into 1987. (R Vol. IV, Exh. 1). He took into account seasonal variations. (Id. at p. 163). He testified that a linear regression is the best method for developing this information, and he identified data in gas industry literature that confirmed his belief that more efficient appliances were having the industry-wide effect of causing less and less gas consumption by gas company customers. (Id. at p.

157). He testified to post-filing information from Company records -- data as current as March of 1987 -- which validated and confirmed his earlier projection of lower consumption by Company customers. (Id. at p. 167).

The staff of the Commission was preoccupied in their cross-examination of this witness with two things: the absence of an empirical study by the Company of its own customers to determine whether they had actually replaced old appliances with newer and more efficient units, and the staff's fixation belief that lower gas consumption in 1981 and 1982 had been the consequence of higher rates given the Company in its 1981 rate case. Using staff-generated numbers from a chart on schedules which were not introduced into evidence, staff counsel attempted to show that consumption had actually increased rather than decreased. Staff counsel was unsuccessful in eliciting from the witness any admission that consumption had increased. The Company's witness repeatedly confirmed that the factual data from the Company's actual monthly filings with the Commission showed a decline in gas consumption in recent years. Staff counsel finally recognized a possible error in his use of the non-record data from which he had been reading to the witness. Whoever prepared the data might have made his or her calculations over a different period of time, and used a different methodology. (Id. at 165-166). Of course, the preparer of that data never took the stand.

No evidence was ever introduced which contradicted the factual underpinning of the accountant's computation for billing determinants, or which challenged in any way the credibility of his linear regression analysis. The only record evidence before the Commission showed the pattern of diminished gas consumption as to which the linear regression analysis pointed, and a post-filing verification through testimony of the Company's accountant that actual customer usage into 1987 was at reduced levels in line with the usage projected by that linear regression analysis.

In its final order, the Commission disregarded all record evidence on billing determinants. Inasmuch as it had decided to scrap all attrition computations and employ a traditional test year methodology, the Commission simply set billing determinants at the level of usage at the end of the 1985 test year. The effect of so doing was to reject (without discussion) the actual usage level proved by the Company as a basis for billing determinants.

8. Summation.

The Commission's treatment of billing determinants, benchmark variances, salary expense, and rate case expense are not only arbitrary in their own right such as to require adjustment back to the Company's proved figures, but they demonstrate the capricious disregard of the process by which

rates are obliged to be set under the Administrative Procedure Act.

The five specific subjects discussed above--attrition, rate case expense, salary expense, benchmark variances, and billing determinants--were each improperly handled by the Commission, for the reasons expressed. At a minimum, they should be revised to the Company's figures, based on the only evidence of record. Because these items are also exemplary of the process by which the Commission dealt with the Company's rate case, however, the Company ordinarily would request that the entire case be remanded for a new proceeding. There is one problem with remanding the case, however, for were the Court to do so the Company's customers would be prejudiced by the cost of presenting a new rate case. With only about 3,200 customers, each $9,600 of new rate case expense would cost each of the Company's customers $1 per year for each of 3 years.[13] The Commission's default in providing due process in this proceeding should not produce a new financial burden on the Company or its customers.

The Company suggests, rather, that the Court enter an order directing the Commission to adjust each of the items discussed above to reflect the Company's proved position. The Court has adequate authority to determine on its own the Company's rights, and to set aside the Commission's action.

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13 The Commission requires amortization of rate case expense over 3 years. (R 345).

Section 120.68(13)(a), Fla. Stat (1985). Indeed, the Court is mandated to remand for proper action by the Commission when it finds, as here, that "the fairness of the proceedings . . . [was] impaired by a material error in procedure. . ." Section 120.68(8), Fla. Stat (1985).

The Company respectfully suggests that the Court direct the Commission:

1. to allow rate case expense of $142,093 (Exhibit 11), plus the costs of this appeal;
2. to increase allowed salary expense by $2,800;
3. to allow benchmark variances of $43,793; and
4. to set billing determinants at the level identified in the Company's MFR's.

The Court should also order the Commission to cancel its three pro forma adjustments to the test year, and in their place compute attrition years for the Company based on the rates of attrition set out in the Company's MFRs, as modified by the revisions described above and by testimony at the hearing. As these computations are simple and straightforward, the Commission can promptly re-determine the appropriate amount of the Company's permanent rate increase and enter its award order without further cost to the Company or its customers.

Conclusion

This is not a rate case appeal involving issues which were contested below, and which require the Court to determine if competent and substantial evidence in the record supports agency action. This rate proceeding lacked any semblance of administrative due process. It cannot be salvaged by an affirmance or disagreement with various actions of the Commission on items in the rate case mix.

The proceeding below was so arbitrary, so capricious, and so devoid of fundamental fairness that final agency action of the Commission must be vacated. The matter should be resolved by the Court, and returned to the Commission with directions to recompute new rates based on the amounts requested and proved by the Company.

Respectfully submitted,

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I certify that true and correct copies of this brief were mailed on December 7, 1987 to David E. Smith, Esq. and to Prentice P. Pruitt, Esq., Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0861.

Arthur J. England Jr.

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