IN THE SUPREME COURT OF FLORIDA

CITIZENS OF THE STATE OF FLORIDA, Appellants, v. FLORIDA PUBLIC SERVICE COMMISSION, Appellee.	)	CASE NO. 75,029

ANSWER BRIEF OF APPELLEE
FLORIDA PUBLIC SERVICE COMMISSION

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SYMBOLS AND DESIGNATIONS OF THE PARTIES

Appellee, the Florida Public Service Commission is referred to as the "Commission".

Appellants, the Citizens of the State of Florida, are referred to as "Citizens of the State of Florida".

References to the appendix to Appellant's brief are designated "A-____"

References to the record are designated "R-____"

STATEMENT OF THE CASE AND FACTS

This appeal concerns the Florida Public Service Commission's interpretation of Rule 25-14.003, Florida Administrative Code, as that rule applies to the tax savings accumulated by United in the years following Congress's enactment of the Tax Reform Act of 1986.

In 1982, the Commission adopted Rule 25-14.003, Florida Administrative Code, entitled "Corporate Income Tax Expense Adjustments". The rule provided a formula for treatment of the tax savings or tax expense deficiencies of regulated utilities resulting from a change in corporate income tax rates. (A-1)

In 1986, when the Tax Reform Act lowered basic income tax rates for corporations from 46 percent to 34 percent (R-12), the industries under the Commission's purview continued to collect revenues from their ratepayers which reflected the higher tax rate. (R-12) The Commission initiated a variety of proceedings to investigate and respond to the effect of the tax rate changes. Several of the proceedings involved. Public Counsel participated in all of these proceedings.

In 1987, the Commission investigated the earnings of United in light of the tax reforms. It also considered a petition by Public Counsel "to Reduce Rates and Charges for United Telephone Company of Florida to Reflect a Reduction in Tax Expenses Due to a Change

in the Corporate Tax Rate".[1] Both the Commission and Public Counsel were concerned that United's rate of return as authorized in its last rate case was too high to produce a reasonable dispensation of the company's tax savings under the provisions of the tax rule.

At the same time, the Commission was in the process of investigating recovery of non-traffic sensitive costs, and intrastate access charges for toll use of local exchange services.[2] The Commission saw the opportunity to reduce access charge rates of local exchange companies and treat the effect of lower tax rates at the same time. Thus, in Order No. 17053, January 1, 1987, the Commission established permanent reductions in the access charge rates of the regulated local exchange carriers, including United, and ordered long distance carriers to lower rates to long distance customers in the amount of the access charge reductions. The Commission determined that the reduction in revenues from decreased access charges would be offset in whole

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[1] Docket No. 861363-TL: In Re: Investigation into Earnings of United Telephone Company of Florida; Docket No. 861615-TL; In Re: Petition by the Citizens of the State of Florida for a Limited Proceeding to Reduce Rates and Charges of United Telephone Company of Florida to Reflect a Reduction in Tax Expense Due to a Change in the Corporate Tax Rate

[2] Docket Nos. 860984-TP and 820537-TP; In Re: Investigation into NTS Cost Recovery and In Re: Intrastate Telephone Access Charges for Toll Use of Local Exchange Services

or in part by the amount of the companies' tax savings. The Commission said:

> We believe that, in addition to local rates, each LEC has various additional sources of revenues available to it which may be used to partially or totally offset any lost access charge revenues. As only one example, we note that the Tax Reform Act of 1986, will result in a tax expense savings for each LEC. This savings may offset the access revenue reduction and, if the tax savings is sufficient, a LEC could reduce its access charges as we have directed herein and still suffer no net revenue loss. (Order No. 17053, p.3., A-6)

The Commission made clear its intention to tie the reduction in local exchange company access charges to a reduction in long distance charges by AT&T Communications of the Southern States, Inc. (ATT-C). In this manner, the Commission assured that the access charge reduction would benefit customers.

> In addition to reducing access charges as set forth above, we also find it appropriate to require ATT-C to reduce its MTS, OUTWATS and 800 Service rates. The reductions should be spread proportionately between each of the services according to the revenue currently generated by each service. This is the same methodology which was previously utilized in the settlement agreement reached by Public Counsel and ATT-C as approved by Order No. 16070. The total amount of the reduction in MTS, OUTWATS and 800 Service rates will be based on the total amount of the reduction in access charges which are actually implemented by the LEC's pursuant to this order. (Order NO. 17503, p.4., A-7)

Initially, United filed a request for hearing on the Commission's Order No. 17503. However, after negotiations with

Commission staff and Public Counsel, United agreed to withdraw its request for hearing. It accepted the terms of the order.

Then, in final Order No. 17429, The Commission staff and United agreed that United's estimated 1987 tax savings would be offset by reducing United's access charges to long distance carriers, and by increasing United's depreciation expense. (Order No. 17429, p.2., A-13) The Commission found that the effect of the permanent rate reduction and the temporary depreciation expense adjustment would be to reduce United's revenues for 1987 by an amount which corresponded to the amount of its tax savings for 1987. The Commission stated:

> We find that the public interest would be served through our ordering United to reduce access charges and increase depreciation expense by the amount of its anticipated tax expense.
>
> Our action here is intended to deal with a number of outstanding issues. In recognition of the tax law change, we will order the disposition of $7,150,000 associated with United's tax expense reduction for 1987. This will be in lieu of the application of Commission Rule 25-14.003. Our action also represents a step toward deloading non-traffic sensitive (NTS) costs from access charges, which was the principal goal of the proposed agency action in Docket No 860984-TP...(Order NO. 17429 p.3., A-13)

In this manner, the Commission reached a just resolution of United's tax savings: a permanent rate reduction in the amount of the tax savings. The Commission closed all tax savings dockets relating to United for 1987, and it excused United from further participation in the remaining dockets, because United's

acceptance of the terms of the Order had resolved the outstanding issues concerning United. (Order No. 17429 p.3., A-14) Public Counsel filed no objection to the Commission's actions for 1987.

In 1988, the Commission also confronted the question of an appropriate return on equity to be used in measuring tax savings. The question was particularly important to reaching a just resolution of United's and other utilities' post-1986 tax savings. The 1982 tax rule defined the term "midpoint" as the midpoint of the range of return approved by the Commission in the utility's last rate case. Unless the rates of return were adjusted to a lower rate than that authorized in the utilities' last rate cases, the formula for determining tax savings would yield no tax savings refund in most cases. Public Counsel filed a petition "For a Limited Proceeding to Reduce Rates and Charges of United Telephone Company of Florida to Reflect a Reduction in Authorized Return on Equity." United also filed a petition for approval of "A Return on Equity to be used in 1988 for Purposes of Rule 25-14.003, F.A.C.". (Docket Nos. 861616-TL and 880444-TL) Public Counsel proposed a reduction of United's authorized return from 15.75 percent to 12.25 percent while United proposed a return of 14.5 percent for 1988 and 14.375 percent for 1989.

In Proposed Agency Action order No. 19726 (A-15), the Commission decided to authorize a return on equity for United of 13.5 percent as the midpoint, with a range of 12.5 percent to 14.5 percent. The Commission said the new return on equity would apply

to tax rule calculations, including the definition of "midpoint" in Rule 25-14.003(1)(f).[3]

> This ROE shall be used for all purposes, which shall include, but not be limited to, the following: (1) earnings; (2) surveillance reporting: (3) Rule 25-14.003 regarding income tax expense; (4) Section 364.055, Florida Statutes, concerning interim rates and refund amounts....(Order No 19726, p.2., A-)

Neither Public Counsel nor United protested the Commission's action in that Order.

The proceeding that gave rise to this appeal began in 1989. Public Counsel filed a petition to compel United's compliance with Rule 25-14.003. (Docket No. 890486-TL, R-1) Public Counsel argued in its petition that since the Commission had set a midpoint of 13.5 percent return on equity for 1988 in Order No.

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[3]Rule 25-14.003, Florida Administrative Code, provides in relevant part:

(1) Definitions . . .

(f) "Midpoint." The midpoint of the range of return approved by the Commission in the utility's last rate case, adjusted for the cost of any debt issued subsequent to that rate case and prior to the commencement of a tax deficiency collection...

(2) Tax Savings Refunds...

(a) When, during the reporting period described in paragraph (5)(a) below, a utility is earning a rate of return which is at or above the midpoint of its authorized range computed without consideration of a tax rate reduction, the utility shall refund all associated revenues as described in paragraph 5(c)...

19726, and since United had earnings in excess of that midpoint, United should refund its tax savings according to the provisions of Rule 25-14.003. (R-1)

United answered that the access charge reduction the Commission had ordered in 1987 continued into 1988 and had eliminated any tax savings for that year, because the access charge reduction had decreased United's revenues by the amount of the tax savings. (R-8) United also stated that if the rule required a refund of tax savings only, the determination of the amount of tax savings should also be made using the midpoint defined in the rule, rather than the midpoint ordered by the Commission in Order No. 19726. (R-4) United asserted that the appropriate midpoint of its return on equity according to the terms of the tax rule would be 15.75 percent, the midpoint authorized in its last rate case. If that midpoint were used ". . . no application of the tax rule would be available". (R-10) In other words, there would be no tax savings refund for United in 1988.

After considering Public Counsel's petition and United's response, the Commission rejected Public Counsel's argument. In Order No. 22060, the Commission said,

> The effects of both the access charge reduction and the Act continue into 1988 and beyond. When we approved the reduction in United's access charges, we viewed this action as an acceptable disposition of tax savings. At the time of this action, we expected the access charge reduction to have ongoing impact on United's tax savings. Accordingly, our action in reducing United's access charges in 1987

> must be considered in determining whether the company's 1988 tax savings have been properly disposed of. The first step in applying the Tax Rule is to determine the amount of a company's tax savings and then to determine if any of that amount has been disposed of through Commission action. If any tax savings remain after such action has been considered, then the Tax Rule requires that an earnings test be applied to find if any additional refund is necessary. . . .
>
> We believe that a reduction in rates which goes into effect in time to prevent overpayment by ratepayers is preferable to a cash refund because the customer never overpays the company. We disagree with OPC's interpretation of how the Tax Rule should be applied. In our opinion, it becomes applicable only if rate reductions have not already disposed of tax savings. (Order No. 22060, R-63)

The Commission dismissed Public Counsel's petition, and Public Counsel filed notice of this appeal.

SUMMARY OF ARGUMENT

In Order No. 22060, the Florida Public Service Commission determined that United Telephone Company did not have any 1988 tax savings subject to refund under the provisions of Rule 25-14.003, Florida Administrative Code. The Commission found that United Telephone Company's 1988 tax savings had been eliminated by an access charge rate reduction which the Commission had ordered in 1987 and, therefore, the tax rule would not apply.

The Commission's determination was reasonable and consistent both with its tax rule and with the regulatory statutes which empower it to set reasonable rates and charges of public utilities.

The Commission interpreted the provisions of its tax rule according to basic rules of statutory construction in a manner designed to fulfill the intent of the rule. The Commission clearly had the authority to do *so,* and the interpretation it made is entitled to great deference. Appellant has not shown that Order No. 22060 was clearly erroneous or contrary to essential requirements of law and, therefore, the Commission's order should be upheld.

Public Counsel may not raise the issue of whether the Commission should consider rate increases in its treatment of tax savings of regulated utilities, because it did not raise that issue before the Commission in this case.

I.

THE COMMISSION CORRECTLY DECIDED THAT UNITED HAD NO TAX SAVINGS FOR DISPOSITION IN 1988.

A. The Commission Has the Authority to Interpret the Provisions of Rule 25-14.003, Florida Administrative Code; and to Determine When They Would Apply.

The specific question before this Court is not whether the Commission acted inconsistently with its tax rule. The question is whether the Commission had the authority to determine if its tax rule would apply when a company's tax savings for one year had been disposed of by Commission action in an earlier year. The answer is that the Commission did have the authority and the responsibility to interpret the provisions of its rule, and to determine when they would apply.

Rule 25-14.003 was adopted by the Commission in 1982 to provide a method for returning tax savings to a utility's ratepayers. The rule, however, does not address the question which faced the Commission in 1988: do the rule's provisions apply at all when the tax savings treatment of one year carries over and effectively eliminates tax savings for subsequent years?

The Commission found that the provisions of the tax rule did not apply under those circumstances. It held that the access rate reductions of 1987 "continue into 1988 and beyond."

> [O]ur action in reducing United's access charges in 1987 must be considered in determining whether the company's 1988 tax savings have been properly disposed of. The first step in applying the Tax Rule is to

> determine the amount of a company's tax savings and then to determine if any of that amount has been disposed of through Commission action. If any tax savings remain after such action has been considered, then the Tax Rule requires that an earnings test be applied to find if any additional refund is necessary...
>
> We disagree with OPC's interpretation of how the Tax Rule should be applied. In our opinion, it becomes applicable only if rate reductions have not already disposed of tax savings. (Order No. 22060, R-63) Supra, 7-8.

The law is clear that the Commission is authorized to interpret its own rules, and its interpretation is entitled to great deference. Reedy Creek Improvement District v. Department of Environmental Regulation, 486 So.2d. 642 (Fla. 1st DCA 1986), Franklin Ambulance Service v. Department of Health and Rehabilitative Services, 450 So.2d 580 (Fla. 1st DCA 1984). Courts will not depart from the interpretation unless it is clearly erroneous. Cohen on behalf of Cohen v. School Board, 450 So.2d. 1238 (Fla. 3d DCA 1984). In Pan Am World Airways v. Florida Public Service Commission, 447 So.2d 716 (Fla. 1983), the Supreme Court reviewed the law regarding an agency's interpretation of its own rules. The Court said that the same deference accorded an agency's construction of its regulatory statutes will be accorded an agency's interpretation of its rules. The Court went on to say that federal courts also have recognized agency expertise in regulatory interpretation. An agency's interpretation of its regulation is also entitled to

deference when the meaning of the regulation is unclear or when its interpretation is merely one of several reasonable alternatives.

The Court held that Pan Am had not shown that the Commission's reading of its tariff rules was clearly erroneous or departed in any way from the essential requirements of law, and, therefore, the Commission's interpretation would stand. Id. at 719-720.

The authority to interpret rules implies the authority to determine when they apply. Here, the Commission determined that no 1988 tax savings remained for disposition under the provisions of the tax rule, because the rate reduction of the previous year had offset tax savings for 1988. where a permanent rate reduction is instituted to cover tax savings, the tax rule does not come into effect.

Public Counsel has not shown that the Commission's interpretation of when to apply the tax rule is clearly erroneous or contrary to essential requirements of law. The Commission's authoritative interpretation of its rule should be upheld.

B. The Commission's Interpretation of the Provisions of Rule 25-14.003 was Consistent with the Intent of the Rule, and Section 364.14, Florida Statutes.

Rule 25-14.003, Florida Administrative Code, clearly intends to pass savings from decreased tax expense back to those who paid the expense. However, when the Commission prepared to apply the particular methods of the 1982 tax rule to 1987 and 1988 tax

savings it discovered that a literal application of the midpoint definition and the refund provisions of the rule would yield results exactly contrary to the intent of the rule. As United pointed out in the proceedings below, since its 1988 earned rate of return was 14.28 percent, and the midpoint of the rate of return authorized in its last rate case was 15.75 percent, a literal application of the rule would produce no return of tax savings at all. (R-10)

To avoid this unacceptable result, the Commission found other methods to fulfill the intent of the rule. It ordered a permanent reduction in the access charge rates of the regulated local exchange carriers, including United. It ordered AT&T-C to reduce long distance charges in the amount of the access charge reductions. In so doing the Commission exercised its authority in a manner consistent with the intent of Rule 25-14.003, which was to return tax savings to ratepayers.

when the Commission interprets its rules, it uses the same general rules of construction that apply to the interpretation and construction of statutes. 1 Fla.Jur.2d Administrative Law, § 57. Those general rules of construction say that statutes or rules must be interpreted to avoid unreasonable, absurd, or ridiculous consequences. Foley v. State, 50 So.2d 179 (Fla. 1951), Gracie v. Deming, 213 So.2d 294 (Fla. 2d DCA 1968), (statute should be construed to effectuate intent of the Legislature): State v. Webb, 398 So.2d 820 (Fla. 1981), (construction of statute which would

lead to absurd or unreasonable result or would render statute purposeless should be avoided).

None of the cases cited by Public Counsel say that section 120.68(12)(b), Florida Statutes, requires an agency to follow provisions of a rule that would lead to results which are exactly contrary to the clear intent of the rule.

The Commission was required to avoid any construction of its Rule 25-14.003 which would impair, nullify, or defeat the result intended by the rule. This is exactly what the Commission did in Order No. 17429, Order No. 19726, and Order No. 22060.

Furthermore, the Commission has the statutory responsibility and authority under the provisions of section 364.14, Florida Statutes, to fix reasonable rates and charges for telephone companies in the State of Florida. In order to fulfill this responsibility the Commission must respond to changes in the industry and tailor its responses to current circumstances. The Commission must always interpret its rules in light of its statutory responsibilities to set fair and reasonable rates.

In C.F. Industries v. Nichols, 536 So.2d. 238, (Fla 1988), appellants argued that the Commission had acted inconsistently with the provisions of Rule 25-17.082(3)(f) by providing separate rates for standby service for cogenerators. The Commission argued that appellants had urged the Commission to establish the separate rates, and that it had not acted in a manner inconsistent with its rule by following the mandate of federal and state law. The Court upheld the Commission's action, saying:

> ...[A]ssuming there is conflict with the rule, the rule must give way to state and federal law which requires that fair and reasonable rates be established based on traditional cost-of-service concepts." Id. at p. 238

The reasoning of C.F. Industries is applicable to this case. Even if conflict between the Commission's actions in Order No. 22060 and Rule 25-14.003 is assumed, that rule must yield to the requirements of state law that the Commission set fair and reasonable rates for telephone companies.

Public Counsel has advocated departure from the provisions of the rule which he now argues must be followed (See, In Re: Amendment of Rule 25-14.003, F.A.C., Corporate Income Tax Expense Adjustments, Docket No. 861190-PU, Petition for the Initiation of Emergency Rulemaking Procedures. (AA-1) That is why he did not object to the Commission's resolution of United's tax dockets and the dispensation of United's tax savings in 1987. That is why Public Counsel initiated his petition to lower United's return on equity for 1988-89. Like the Commission, Public Counsel did not want to apply a literal construction to the rule when such a construction would yield little or no tax savings and thus defeat the intent of the rule.

In 1989, however, after the Commission lowered the midpoint return on equity, Public Counsel changed his tune. This time Public Counsel argued that one section of Rule 25-14.003, the refund section should be literally applied, and decreased access charge rates should be excluded as a method to dispose of tax

savings. At the same time Public Counsel argued that another section of the rule, the definition of "midpoint", should not be literally applied. Public Counsel simply cannot urge this Court to remand Order No. 20060 to the Commission for purposes of following the provisions of one section of the rule and not another.

The inconsistency of Public Counsel's position with regard to the Tax Savings Rule and the proper disposition of tax savings demonstrates the wisdom of the legal principle that an agency's interpretation of its own rules is entitled to great deference. The Commission, not Public Counsel, has a continuing obligation to consider its rules and policies in relation to all current circumstances which affect their operation. McDonald V. Department of Banking and Finance, 346 So.2d 569, 584 (Fla. 1st DCA 1977). Where the Commission determines that a strict application of certain provisions of its rule would lead to a result inconsistent with its statutory responsibilities and contrary to the intent of the rule, the Commission is required to interpret the rule in a manner which will be consistent with the intent. The Commission will not violate section 120.68(12)(b), Florida Statutes, by doing so.

C. The Commission Exercised its Authority in a Manner Consistent with the Requirements of Chapter 120 and Basic Tenets of Administrative Law.

Since the time this appeal was filed the Commission has continued to investigate the effects of tax reform on the operation of regulated industries. The Commission has exercised its ratemaking authority over the effects of corporate tax savings for individual companies, as it has in United's case, tailoring its treatment of tax savings to the particular circumstances of each company. For example, in the General Telephone of Florida case (GTE-FL), the Commission conducted extensive hearings on the effect of the the tax rule on GTE-FL's tax savings (Order No. 22352 in Docket Nos. 870171-TL and 890216-TL, A-53). There the Commission found, that even with reduced access charge rates, GTE had collected tax savings that should be refunded to its customers. (Order No. 22352, p. 14, A-66)

The Commission has recognized that Rule 25-14.003 should be revised to deal more effectively with large increases or decreases in corporate tax rates. To that end, the Commission proposed changes to the tax rule in regular rulemaking proceedings. (Docket Nos. 861190-PU; 891296-PU, In Re: Amendment of Rule 25-14.003, F.A.C., Corporate Income Tax Expense Adjustments) It also adopted an emergency rule to preserve 1990 tax savings for the utilities' ratepayers while the regular rulemaking proceedings take their course. (Docket No. 891278-PU, A-49)

The Commission has exercised its authority over the rates and charges of regulated public utilities in a manner entirely consistent with the dictates of administrative law and its own regulatory statutes. The Commission applied the provisions of Rule 25-14.003, Florida Administrative Code, in a manner consistent with the intent of the rule and section 366.14, Florida Statutes. It adjudicated solutions to the tax issues designed to return tax savings to the ratepayers. It also initiated regular rulemaking procedures and emergency rulemaking procedures to deal with the effect of major income tax changes.

As the Court stated in Anheuser-Busch, Inc. v. Dept. of Business Regulation, 393 So.2d 1177, 1181 (Fla. 1st DCA 1981),

> The model of responsible agency action under the APA is action faithful to statutory purposes and limitations, foretold to the public as fully as practicable by substantive rules, and refined and adapted to particular situations through orders in individual cases.

The Commission has treated the tax savings of United and other utilities in a manner entirely consistent with this model.

II.

PUBLIC COUNSEL MAY NOT RAISE THE ISSUE OF THE COMMISSION'S TREATMENT OF THE EFFECT OF RATE INCREASES ON TAX SAVINGS WHEN THAT ISSUE WAS NOT RAISED IN THE PROCEEDINGS BELOW.

In his third argument before this Court, Public Counsel states that the Commission applied Rule 25-14.003 inconsistently, because it rejected an argument made by Public Counsel in the GTE-FL case. The issue raised by Public Counsel in the GTE-FL case was whether the Commission should take rate increases into account in its treatment of tax savings. This issue was never raised in the case at bar. It is axiomatic that a reviewing Court will not consider points raised for the first time on appeal. In order to preserve a question for appeal a party must object and obtain a ruling on the issue. This is a basic principle of fairness which encourages judicial economy and prevents abuse of the appellate process, Castor V. State, *365* So.2d 701 (Fla. 1978).

CONCLUSION

Public Counsel has not shown that Commission Order No. 22060 is clearly erroneous or contrary to the essential requirements of law. Therefore, this Honorable Court should defer to the Commission's interpretation and application of Rule 25-14.003, Florida Administrative Code, and uphold the Commission's order.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Answer Brief of Appellee, Florida Public Service Commission, has been furnished by U.S. Mail this 19th day of February, 1990 to the following:

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