

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into the effect)	DOCKET NO. 871206-PU
of the 1986 Federal Tax Reform for)	ORDER NO. 20800
1988)	ISSUED: 2-23-89

ORDER DENYING MOTIONS TO STRIKE
AND REJECTING PROPOSED PROCEDURAL PROCESS

In Order No. 20269, issued November 7, 1988, we proposed as agency action the establishment for GTE Florida Incorporated (GTEFL) of an earnings cap of 14.25% for 1988 and 1989. On November 22, 1988, the Office of Public Counsel (OPC) and the Florida Consumers for Responsible Utilities (FCRU) filed protests to this proposed agency action (the Protests), thereby preventing it from becoming final.

In its protest, OPC proposes that six issues be heard in this proceeding. At an issue identification meeting of the parties held on January 13, 1989, OPC proposed that one of these six issues be replaced by two issues and that two more issues be added. The nine issues currently proposed by OPC are:

1. What is the return on equity required by investors in GTEFL?
2. What return on equity should be set for GTEFL so that investors will have the opportunity to earn their required return on equity?
3. What should be the minimum of the range of the authorized rate of return on equity for GTEFL?
4. What should be the midpoint of the range of the authorized rate of return on equity for GTEFL?
5. What should be the maximum of the range of authorized rate of return on equity for GTEFL?
6. Should the new minimum, midpoint, and maximum of the range of the authorized rate of return on equity apply for all regulatory purposes?
7. Should the new minimum, midpoint, and maximum of the range of the authorized rate of return on equity be limited to the years 1988 and 1989, or should it be made permanent?
8. What equity ratio should be used to determine the regulated earned return on equity of GTEFL?
9. What are the present and projected earnings of GTEFL for 1988 and 1989, and what types and levels of O & M expenses are included in those earnings?

In its protest, FCRU proposes that the following two issues be heard in this proceeding:

1. The disputed issues of material fact are whether the Commission has properly decided the current cost of equity for GTE-Florida and whether the Commission erred by failing to set a range for authorized return on equity including a minimum, midpoint, and maximum.

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2. The current cost of equity for GTE-Florida is much lower than the earnings cap of 14.25% set forth in the Order No. 20269. The Commission should order a new midpoint, minimum, and maximum authorized return on equity reflecting a much lower cost of equity.

On December 27, 1988, GTEFL moved to strike the Protests (the Motion), alleging that OPC and FCRU are improperly attempting to place rate-of-return (ROE) and earnings matters at issue in this docket. In GTEFL's view, the issues listed above cannot unilaterally be placed at issue in this docket because it is a generic tax investigation. The company asserts that it has returned to its ratepayers the savings it realized from the Tax Reform Act of 1986.

The Motion points out that GTEFL made an offer in this docket on August 17, 1988, as a means of settling any outstanding issues. The offer claimed that by reducing access charges, changing zone rates and recording depreciation expense in accordance with Orders Nos. 17382, issued April 8, 1987, and 18584, issued December 21, 1987, the company has accounted for all of its tax savings. Nevertheless, GTEFL proposed an interim reduction in its authorized ROE for 1988 in order to resolve its participation in this proceeding. The offer excluded use of the proposed interim ROE for applying Rule 25-14.003, Florida Administrative Code (the Tax Rule).

Order No. 20269 proposed to accept a modification of GTEFL's offer by establishing a cap on earnings for 1988 and 1989. The Motion states that, since this order was protested, the earnings cap proposed therein is no longer of any legal force and effect. Accordingly, in GTEFL's view, the sole subject matter of this proceeding concerns "the tax liability of the company, if any, associated with the effects of the Tax Reform Act of 1986." The Motion maintains that it is improper for OPC and FCRU to attempt to make the company's settlement offer the subject matter of this proceeding. GTEFL further claims that the Commission lacks jurisdiction to consider the issues proposed by OPC and FCRU because Chapter 364, Florida Statutes, does not authorize limited proceedings and GTEFL's ROE cannot be changed in a vacuum.

GTEFL proposes that the only issues, if any, that should be considered in this proceeding are as follows:

1. Has the company disposed of the tax savings associated with the Tax Reform Act of 1986 in calendar year 1988?
2. Does Commission Rule 25-14.003 expose a telephone company to double liability if the company has voluntarily returned tax monies during the reporting period if the company is still earning above its midpoint return on equity?

The Motion requests that the Commission strike the ROE issues proposed by OPC and FCRU.

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On January 9, 1989, OPC filed its Response to GTEFL's Motion to Strike Petitions on Proposed Agency Actions (the Response), seeking the denial of the Motion. The Response argues that the Commission has authority to set GTEFL's ROE in this proceeding, citing Docket No. 880069-TL in which Southern Bell Telephone and Telegraph Company's ROE was changed in a proceeding other than a rate case. Similarly, such a proceeding was commenced when GTEFL petitioned for approval of a revenue-sharing plan. Also, the Commission exercised such jurisdiction in issuing Order No. 19726 on July 26, 1988, in which an interim ROE for 1988 and 1989 was established for United Telephone Company of Florida.

OPC maintains that the issues which it proposes are relevant to the subject matter of this proceeding because Order No. 20269 "did away with the existence of a midpoint return on equity." Absent a midpoint ROE, the operation of the Tax Rule is changed dramatically, in OPC's opinion. Had a 13.25% midpoint ROE been established, the Tax Rule is believed to be applicable because OPC projects 1988 earnings of between 13.25% and 14.25% for GTEFL. Accordingly, OPC believes that the application of the Tax Rule in such a circumstance would lead to a refund for GTEFL's ratepayers. Earnings projections are relevant, OPC claims, to the issue of whether a midpoint ROE should be set for the purpose of applying the Tax Rule. The setting of a midpoint ROE for United Telephone Company of Florida in Order No. 19726 makes relevant here the issue of why one was not proposed for GTEFL in Order No. 20269.

OPC asserts that GTEFL's argument that the company has returned its tax savings misses the point of the Tax Rule. The Tax Rule is dependent first, OPC states, upon a company's earning above its midpoint ROE and then calls for refunds, not depreciation expense adjustments, to the extent of tax savings.

On January 20, 1989, GTEFL filed a Proposed Procedural Process and Amended Motion to Strike Petitions on Proposed Agency Action (the Amended Motion) to address concerns expressed by the parties at an informal issue identification conference held on January 12, 1989. The company's position is that it has returned tax savings without regard to its ROE by reducing rates and charges and increasing depreciation expense, in lieu of making a one-time cash refund, in order to obtain long-term benefits. Also, GTEFL says that it has kept its achieved ROE in a range acceptable to the Commission irrespective of whether the company agreed with this determination. The results, according to the Amended Motion, are more than \$50 million in reduced rates and rate base since 1987 and a reduction in achieved ROE from 13.88% in calendar year 1985 to 13.07% in calendar year 1987, with an achieved ROE of 11.79% for the twelve months ended October 31, 1988.

One of GTEFL's reasons for taking these steps was to prepare for competition, particularly in the intraEAEA market where toll revenues are said to be subsidizing local rates. Another was to avoid extended litigation by implementing the Commission's perceived intent. A third reason was to correct historic depreciation reserve imbalances.

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The Amended Motion complains that by considering the issues proposed in this proceeding by OPC and FCRU, the Commission would subject GTEFL to "double jeopardy" in that further refunds may be ordered if the Tax Rule is applied after the company's ROE is reduced, in the manner suggested by OPC. Attempts to "double count" tax savings are unfair, according to GTEFL, because such tax savings "have already been returned to its ratepayers." Similarly, attempts to change its ROE in a vacuum are said by GTEFL to be unreasonable.

GTEFL proposes a two-phase procedural process to be adopted by the Commission for this proceeding in order to avoid this "double jeopardy" potential. Under the Amended Motion's plan, Phase One would consider GTEFL's two proposed issues listed above. Later, Phase Two would examine GTEFL's ROE with a view toward setting a new ROE for prospective application in Docket No. 870171-TL involving OPC's petition for such action. Should the Commission accept this two-phase plan, the Amended Motion states that GTEFL would consent to the Commission's change in the company's ROE without raising the question of the Commission's authority to take such action in a limited proceeding. The Amended Motion opposes OPC's assertion that an ROE can lawfully be set for GTEFL in 1989 and retroactively applied to January 1, 1988, in order to compel a refund under the Tax Rule. Whether such action constitutes "double liability or double jeopardy" should be determined before further action is taken here, in GTEFL's opinion. Phase One of this proceeding can be resolved through pleadings and oral argument, according to the Amended Motion, whereas Phase Two requires an evidentiary hearing to consider cost of capital.

GTEFL claims to have relied upon the Commission's past practices of accepting various adjustments in lieu of applying the Tax Rule in taking steps to resolve tax savings issues flowing from the Tax Reform Act of 1986. One particular action, Order No. 18661, issued January 7, 1988, illustrates to GTEFL that the Commission did not intend to proceed under the Tax Rule because it established a January 1, 1988 effective date for resolving 1988 tax savings. Such a step is unnecessary under the Tax Rule which requires that earnings exceeding an authorized midpoint ROE be refunded. The Amended Motion argues that this action was taken to increase the Commission's flexibility in dealing with tax savings without strictly relying upon the Tax Rule. GTEFL submits that it does not acquiesce to a retroactive application of the Tax Rule employing a newly-set ROE.

Finally, the Amended Motion opposes the consideration in this proceeding of the issues raised by OPC at the January 12, 1989 conference. However, GTEFL says that the proposed compounding adjustment issue may be appropriate in Phase Two of the proceeding if the Commission adopts its plan. The Amended Motion asserts that issues dealing with GTEFL's projected earnings for 1988 and 1989 and the types and levels of O and M expenses, which are proposed by OPC, are irrelevant here.

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OPC filed its Response to GTEFL's Amended Motion (the Second Response) on January 31, 1989, requesting that the Amended Motion be denied. The Second Response alleges that GTEFL is seeking to circumvent the Tax Rule. OPC claims that the Commission's action in Order No. 18661 accepting GTEFL's offer to acquiesce in a retroactive application of action in this docket to January 1, 1989, indicates that setting a reasonable ROE was intended in conjunction with applying the Tax Rule. By contrast, the Second Response points out that Order No. 18661 excluded Indiantown Telephone Company from this action because that company's authorized ROE was deemed acceptable. As a result, OPC concludes that GTEFL's authorized ROE was determined by the Commission to be excessive, leading to the commitment accepted in Order No. 18661.

Further, the Second Response quarrels with GTEFL's allegation that it has "given back" tax savings to its customers. OPC claims that an access charge reduction and a depreciation adjustment give back nothing to local ratepayers and that neither of these steps constitutes a refund of tax savings as contemplated by the Tax Rule.

OPC charges that GTEFL's "double jeopardy" argument is a red herring. The Commission is urged to go forward with one hearing in this proceeding and not to determine the "double jeopardy" issue separately from the other proposed issues. The Second Response opposes GTEFL's two-phase proposal in this docket, arguing that the Commission decided to deal with all matters concerning the company in one proposed agency action, Order No. 20269. Thus, any issue contained in that order is believed by OPC to be appropriate for consideration in this proceeding. Such issues include the proposed earnings cap and the failure to set a midpoint ROE. Finally, OPC suggests that an appropriate issue here is whether the Commission received any earning projections for 1988 and 1989 from GTEFL and relied upon them in constructing the proposed settlement of these matters contained in Order No. 20269.

Upon review, the Prehearing Officer denies the Motion and the Amended Motion. Stated simply, the scope of this proceeding is to determine whether GTEFL has carried out its obligations for 1988 under the Tax Rule, and if not, what steps need to be taken. The 11 listed issues proposed by OPC and FCRU all fall within this scope and therefore will not be stricken.

The company maintains that it has complied with the Tax Rule's spirit, at least, and it will be given an opportunity to demonstrate that in this proceeding. Both issues proposed by GTEFL appear to be appropriate considerations for the Commission in reaching its conclusion on this question. OPC and FCRU disagree with GTEFL's assertion, and they will have a similar opportunity to show in the forthcoming hearing that the company is not in compliance with the Tax Rule and should be made to comply. The 11 issues proposed by OPC and FCRU need to be resolved in determining this over-all question.

The parties have proposed certain issues that are outside the scope of this proceeding. The offer that GTEFL made is no longer before the Commission, and any further consideration of it, including the events leading up to the Commission's

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proposal to accept a modification of it, is an unnecessary waste of effort by the parties and the Commission. At bottom, the protests of Order No. 20269 rendered that proposed agency action a nullity. Consequently, the preliminary action that was proposed there, e.g., the earnings cap, is no longer viable and must be disregarded. In view of its current status, the Commission's proposed agency action should not continue to consume the time set aside for this proceeding.

What remains now that Order No. 20269 is removed from consideration are all of the issues that led the Commission to open this investigation and which have been developed to date through the course of this proceeding. These issues are still before the Commission for resolution, and their consideration is the proper focus of this investigation. As mentioned above, a hearing will be held to give the parties whose substantial interests will be affected by Commission action here an adequate opportunity to address the proper issues.

The Commission has explicit authority to enforce its rules, see, e.g., Sections 364.14 and 364.285, Florida Statutes. Rule 25-14.003(2)(a) provides:

(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).

Rule 25-14.003(5)(c) states, in pertinent part:

. . . each utility shall file a petition containing a calculation of and the method of refunding or collecting any tax savings or deficiency for the tax year of the report. The Commission will review the petition and either approve it, approve it with modification, or deny it; an opportunity for a hearing on the Commission's decision will then be provided, if requested. Thereafter, the utility shall either make the refund to or collect the deficiency from its existing customers in accordance with paragraphs (e) and (f) of this subsection.

Paragraphs (e) and (f) of the subsection quoted above govern the mechanics of refunding. The utility is compelled to refund tax savings with interest to current customers at the time the refund is implemented in a lump sum or as a credit on their bills to be exhausted within 12 months. Telephone companies must determine each customer's share based on existing general residence and business local rate relationships.

A review of the language quoted above illustrates the importance of ROE and earnings as elements in determine whether GTEFL's 1988 earnings exceeded its ROE. This step must be taken before tax savings can be measured and any refund can be ordered under the Tax Rule. For these reasons, ROE and earnings issues are fundamental to this proceeding. However, based on this decision, no conclusion should be drawn on the

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merits of OPC's argument that an ROE may be set in this proceeding and, pursuant to Order No. 18661, used in conjunction with the Tax Rule to make GTEFL liable to refund 1988 and 1989 revenues. A decision on that argument will be rendered after the parties are heard on these issues at hearing.

The only way in which GTEFL's "double jeopardy" argument would have validity is if the Commission required the company to refund more than the amount that would have been refunded under a proper application of the Tax Rule. Since the proper application of the Tax Rule is the central concern of the Commission in this proceeding, then any action taken here should not increase GTEFL's exposure to return revenues under the Tax Rule. The company is thus protected against an unlawful expansion of its obligations under our rules and regulations, which it apparently would term "double jeopardy."

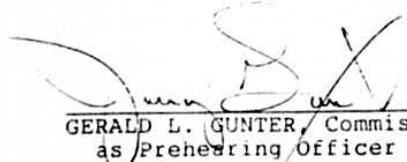
In view of the conclusion that GTEFL is protected against being forced to return more revenues to ratepayers than the Tax Rule requires, the Prehearing Officer denies the company's Proposed Procedural Process. The two-phase process recommended by GTEFL for this proceeding would unnecessarily complicate and delay the Commission's efforts to conclude this investigation with appropriate efficiency. Moreover, good cause has not been shown why the various steps called for under the Tax Rule cannot be accomplished in a single proceeding without violating the rights of any of the parties. Accordingly, it is the intention of the Prehearing Officer that this proceeding move forward with all due dispatch in accordance with the schedule currently in place.

Therefore, it is

ORDERED by Commissioner Gerald L. Gunter, as Prehearing Officer, that GTE Florida Incorporated's Motion to Strike Petitions on Proposed Agency Action filed December 27, 1988, is hereby denied. It is further

ORDERED that GTE Florida Incorporated's Proposed Procedural Process and Amended Motion to Strike Petitions on Proposed Agency Action filed January 20, 1989, is hereby denied.

By ORDER of Commissioner Gerald L. Gunter, as Prehearing Officer, this 23rd day of FEBRUARY, 1989.


 GERALD L. GUNTER, Commissioner
 as Prehearing Officer

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by this order, which is preliminary, procedural or intermediate in nature, may request: 1) reconsideration within 10 days pursuant to Rule 25-22.038(2), Florida Administrative Code, if issued by a Prehearing Officer; 2) reconsideration within 15 days pursuant to Rule 25-22.060, Florida Administrative Code, if issued by the Commission; or 3) judicial review by the Florida Supreme Court, in the case of an electric, gas or telephone utility, or the First District Court of Appeal, in the case of a water or sewer utility. A motion for reconsideration shall be filed with the Director, Division of Records and Reporting, in the form prescribed by Rule 25-22.060, Florida Administrative Code. Judicial review of a preliminary, procedural or intermediate ruling or order is available if review of the final action will not provide an adequate remedy. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.