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GULF STATES UTILITIES V. PUC

RATLIFF: Mr. Chief Justice, and may it please the court. As incredible as it may sound Gulf States Utilities is here 8 years after the entry of the order from which it appeals from this proceeding, and 10 years after the River Bend project began successfully generating power. It still seeks what this court spoke of in Coalition of Cities as a straight-forward adjudication of its right to place the capital invested in River Bend in its rate base and earn a return on that invested capital.

Instead of that result what we are faced with and what we seek relief from this court with regard to is the CA's opinion, which we believe has converted Coalition of Cities into what purports according to the CA to be a PUC decision to effectively permanently disallow $1.45 billion from the rate base of Gulf States.

We submit to you that under the established jurisprudence of this court, that the appropriate interpretation of the PUC's order from which we appealed is based upon a review of that entire order. And from that entire order it is clear that the PUC sought to defer the question of prudence and the quantification of prudence with regard to the $1.45 billion until a later proceeding. It is true that there are findings in the order with regard to a determination of the burden of proof and GSU's discharge. However, when taken in full context of the order it is clear that the PUC was saying that neither GSU had carried its burden to prove prudence, nor had the opponents carried their burden to demonstrate imprudence. Therefore, they specifically refuse to disallow.

ENOCH: I guess this procedure is not something I am used to as a trial judge. Are there overlapping burdens here? If the Coalition of Cities had not come forward to show imprudence would Gulf States be entitled to include all of those expenditures in its rate base?

RATLIFF: We believe that the way the burden operates is that GSU can discharge its burden of going forward establishing prima facie case because of its rate filing package, which demonstrates the cost that it has invested in this plant, and along with its pre-filed testimony demonstrates at least for a prima facie basis the prudence. And we believe that this is consistent with the way the commission has treated these matters both before and after Coalition of Cities. It is also clear from the order that we are looking at here that what the commission said is GSU has the burden to prove those elements of cost which are reasonably challenged.

ENOCH: Now is the posture of this case where the PUC refused to make a ruling; is that the posture of this case?

RATLIFF: I think what the PUC did I suppose you can call it a refusal. I think what in fact

it was is it was a recognition that with the financial condition of GSU at that time, that a deferral was in the best interest of the public, the ratepayers, and the utility. And that what they were going to do was to analyze in more detail the $1.453 billion. If you remember from this record what happened was that there was a definitive cost estimate which had primarily been used by GSU or was primarily used in this hearing to determine whether GSU had been prudent in its restart decision to go ahead and construct this unit.

In the course of this proceeding, that DCE was modified, and there was a determination at that time that those costs and the definitive cost estimate should be included in the rate base at this time. There was a further decision that they wanted more evidence.

ENOCH: I am familiar with where these two numbers came from. But I am just more interested in the procedure. Now does the PUC conclude the rate hearing?

RATLIFF: They conclude this rate hearing and they direct GSU to file a subsequent rate hearing which was the subject matter of the Coalition of Cities opinion.

ENOCH: But the Coalition of Cities basically says they can't do that?

RATLIFF: Yes, sir, and said they could not sever.

ENOCH: So is the posture now that we go back and order the PUC to now rule? I guess my question is this. If this had been the trial of the case, the evidence had been submitted, the evidence had been closed, and the judge comes up and says well I think you can make your burden on X issue, but you haven't made it on the Y issue, so I am just not going to rule on the Y issue. And now I am going to render judgment. You go up on appeal and you sit there and say well Judge you've got to rule on that issue. So you send it back. Is this a new hearing, or do we simply now command the PUC: PUC tell us do they get included or do they not get include? And then we come up and decide whether or not that decision has been based on substantial evidence. Is that the posture of this case or not?

RATLIFF: I would differ with you in this regard. I think the appropriate order from this court would be that the error that occurred in this case requires a reversal and remand to the commission for the reason that I think one of the vices in what we see here is that we have a court order coming along after the fact and creating a permanent disallowance. It seems to me these are matters that are constitutionally and statutorily committed to PUC.

ENOCH: My question is are you seeking a new hearing at which you would intend to introduce evidence of the prudency, or is the posture of the case not unlike us mandamusing a trial judge to rule who's otherwise refused to rule?

RATLIFF: I think that is a good analogy except that I believe it does not recognize that it seems to me the more appropriate order is to say to the PUC: You are the experts in this area; you will

determine whether there should be additional evidence adduced, whether you are going to decide it on the basis of the record that is before you with the correct understanding now of what you could and couldn't do. But I would I think implore the court that I believe it would not be an appropriate method of proceeding to simply say to the PUC: Tell us whether you are going to include it or not, and then we will decide whether it is supported. It seems to me what's more consistent with the framework is is that it would be remanded to the PUC and that agency would apply its expertise in determining what it thought was necessary.

ENOCH: It would seem to me that that would be a viable solution if the hearing was somehow truncated or concluded prematurely. Is there any indication in the record that the PUC said, We just don't have time to hear all of this, so let's go ahead and make a preliminary ruling and then we will take that up later.

RATLIFF: I don't think there is anything that says we don't have time. I think there is plenty of stuff in the order where they say like in their finding 164a, that it should be excluded from plan in service at this time. They go onto say that a phase-in for rates that was going to be done over a period of time in order to avoid rate shock, that that was unnecessary because they had determined that they were going to defer that issue. And it was unnecessary to address that at this time. So it is very clear when you say truncated, it's hard to say that a 130 day hearing I suppose was truncated, but it is clear that the decision process did not carry all the way through. And that it is clear to me that the reason for that is because the commission believe it could do what this court said in Coalition it could not do.

ENOCH: Let me be clear about it. This is not a situation where the trial judge says: I don't want to hear that because I am not going to address it. Is this a situation where they heard it and said, Well we just can't make up our mind so we are not going to decide it. Now which situation is it?

RATLIFF: I think it's the second situation.

ENOCH: In that situation should our decision be to send it back and say: Open it back up to more evidence; or should our decision say: PUC you can't not decide that question just because you are not sure about it. You have to decide that question in recognizing who has the respected burden to prove it.

RATLIFF: I think the appropriate order is: PUC you should decide this question and you now understand you cannot decide it in bits and pieces, that you've got to make a decision with regard to prudence on all of the expenditures and that you are not allowed simply to divide it. So I believe the correct order would be to remand it to the commission for its further consideration.

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RESPONDENT

BARON: May it please the court. I am Steve Baron representing the PUC of Texas. I would like to note that Chairman Patwood and Commissioner Judy Walsh of the commission are in attendance in the courtroom this afternoon.

Your honors River Bend, the evidence showed, was the fourth or fifth most expensive nuclear plant ever built in this country on a per kilowatt basis. The total cost for the plant was $4.5 billion. The definitive cost estimate that GSU submitted for the commission's consideration was $1.73 billion.

The hearing examiner in the course of his 400 page examiner's report stated the burden of proof issue in plain terms: GSU has the responsibility to explain why River Bend cost so much. And that accords exactly with the burden of proof provision in §40 of the PUC Regulatory Act.

The hard truth is that after 132 days of hearings at which this court found in the Coalition case every issue had been exhaustively looked at, the commission made a hard decision. It decided on the one hand that GSU had presented credible evidence, and was persuasive to a certain point, but beyond that point was not persuasive at all. GSU's definitive cost estimate as the chart indicates the commission found was professionally and thoroughly prepared, that GSU prudently relied upon it. And then beyond that the commission looked at evidence in other parts of the record and concluded that an additional - more than $500 million should be added and considered to have been prudently incurred. And they found that the outside cost for River Bend would have been $2.273. But the definitive cost estimate was not the centerpiece of GSU's prudence case. The centerpiece, and that is the word of the hearings examiner not mine, was this auditor's report, a PLG report. And here the commission reviewed it and found the report extremely superficial, very cursory, relying on document which categories were so broad as to be almost meaningless. Offering no clue as to the reasonableness of changes.

So I think on the burden of proof question there is no doubt that once GSU came in and the evidence was looked at, that if there had been any presumption, which this court said there is not in Coalition simply by opening your books, and it shifted and GSU had the responsibility to explain why it cost so much. Now the commission's good faith reading of this court's opinion today, and ever since 6 years ago when the opinion was issued, is that the commission made a decision, it made a call, and that although it believed incorrectly that it could reexamine the issue, that was simply an error of law. The commission found having evaluated the evidence that the $2.273 billion was prudent and should be in, but that GSU had not had its burden of proving that the amount above that was reasonably and prudently incurred. And the commission concluded that that remainder $1.453 billion of River Bend cost should not be included in GSU's rate base.

That is what we read the Coalition of Cities decision to say is that in this proceeding the underlying administrative appeal, the burden is on GSU to show that the PUC's order is not supported by substantial evidence. The question of whether the PUC issued a final order, which is what is being reargued today, we believe was decided in the Coalition case. The underlying sentence identifying the

remaining issue before the court today and before the CA is omitted from the opening page 7 of GSU's application for writ of error. That is the key issue. And to put the issue more precisely the issue is is the commission's determination that GSU failed to meet its burden of proof reasonably explained by evidence and substantial evidence in the record and by adequate findings. And the CA correctly found there was.

HECHT: That was a finding, but that was not a conclusion. The finding as to whether the burden had been met or not was not the conclusion that the commission reached.

BARON: The commission reached that very conclusion that they had not met its burden.

HECHT: It made that finding, but it was unwilling to draw the conclusion that that finding entails. It expressly refused to draw that conclusion.

BARON: What our interpretation your honor is of this court's decision is that the very issue of whether the commission reached its final decision or not was squarely joined and is an issue in the Coalition case. And the majority found that the PUC had made a final decision by stating that GSU failed to meet its burden of proof on that prudence of that $1.45 billion, PUC effectively disallowed that amount from the rate base. The PUC order must be considered final unless it has the authority to defer, which the court found it did not. The dissent disagreed. There is no doubt that this was an issue. The dissent urged that res judicata makes final a matter which has finally been adjudged. And that clearly matter that was expressly reserved has not been decided.

HECHT: But if a trial judge says I am going to render a take nothing judgment against the plaintiff, and I think the plaintiff actually might be able to prove the case and he can turn around and refile it tomorrow, and I encourage him to do so and may be able to prove it, I am not sure he has done it in this case, but I don't want to include that in this case, but I am going to render a take nothing judgment, but I do that with the understanding that that doesn't cut him off.

BARON: If you apply that analogy your honor, you undue the ruling that the commission made a final decision, which is the underpinning for the res judicata holding that the court made.

OWEN: The commission clearly did not make the final decision. They expressly referred resolution and the prudency issue to another proceeding; do you agree with that or not?

BARON: I agree that the commission believed mistakenly that it had the authority once it found GSU failed to meet its burden of proof, that it had the authority to reexamine the issue and let GSU have a second chance. And that's what was enjoined.

OWEN: There has never been a final determination one way or the other of the prudency of these expenditures has it?

BARON: Your honor there has been a final determination as to what amount of cost GSU proved was prudent. It is true that there are not specific affirmative imprudence findings that detailed every dollar that was not allowed in rate base.

OWEN: The commission's order had a fundamental legal premise was wrong. Do you agree with that, that the fundamental legal premise...

BARON: I agree that it was incorrect error of law. But it did not have an effect on the rates that were set. What the commission did I think it is clear from the evidence and the findings in setting the rates evaluated the credibility of the evidence, and applied the legal standard of the prudence standard: What a reasonable manager would have done under similar situation. And that's what set the level of rates. And that's what led the commission to make its findings: Finding of Fact 237, that GSU was to have invested capital and would have an opportunity to earn a reasonable return on its invested capital use and useful; and its conclusion of law 37 in which the rate set were just and reasonable.

The DC on the causation issue, the DC I think offered a good analogy to baseball in which it likened the commission to the baseball umpire in which the umpire watches a pitched ball, watches the strike, watches it, calls a strike mistakenly thinking that there had only been one strike, and so didn't realize that there had been two strikes and there was unintended consequence for that. And when the matter is called to his attention though the call stands. Because the issue of what set the rates is whether the call was in the strike zone, the fact there may have been a misconception about an unintended consequence didn't affect the commission's call of what the rates should be, what the level of rates should be.

HECHT: That's not quite the analogy. The analogy is the umpire says I am not sure it was a strike or not, so I am going to let you take another pitch, and then I will decide whether it was a strike or not.

BARON: I think it's hard to read it otherwise from what this court wrote in Coalition is that once the commission said: you make the burden of proof this much, and you failed to meet your burden of proof this much that a party who fails to meet its burden of proof loses and the commission effectively disallows. The commission's understanding these many years is that the commission called the strike and the remaining issue as I indicated in footnote 7 is whether there is substantial evidence that the call was in the strike zone.

OWEN: But the remainder of that footnote clearly says that we are not as the dissent suggest saying that this is an immediate penalty of $1 some odd billion. It's clear from footnote 7 that the court did not think, my read of it, you left that sentence off, that it was not an immediate disallowance.

BARON: There is no doubt about that. There was not a permanent disallowance, and GSU has not taken a permanent write-off on this. Because what remained was the important but necessarily

limited question of whether the commission's negative finding that GSU failed to meet its burden of proof was reasonably supported by substantial evidence under the deferential charter medical standard. And that's the issue that the CA grapples with and decides correctly. And we believe that that is what the court meant when it said that there isn't an immediate permanent disallowance because the substantial evidence issue is left.

SPECTOR: Does the PUC have the statutory power to hold aside a determination of this nature?

BARON: This court held that after the case has been brought to it and it's issued a decision, it cannot then decide to put off another issue. But I believe if I recall in a footnote that the court makes clear that it is not prohibiting the commission, and at least the commission has authority, at an earlier stage to sever as may be appropriate earlier in the hearing before we get through 132 days of hearing, a 400 page examiner's report, and a commission call on what the evidence proves.

ENOCH: Do you agree with Mr. Ratliff this is not a case where the commission said: I don't want to hear that, we will deal with it later. This is a case where everything was heard and at the end the commission said it couldn't make up its mind and so it will just defer it until a later date.

BARON: Well I agree up until that last point. I think certainly that there...

ENOCH: Well I mean clearly the conclusion...I mean a lot of this conclusion is some of the commissioners saying: Well you haven't proved prudence but they haven't proved imprudence and so we will just defer it. I mean there is some language in there.

BARON: There is language. It's mostly from final order in the transcripts which are not appropriately part of the record.

ENOCH: Assuming that's the case, this is a situation where you just had the decision-maker refusing to rule. This isn't a case where they kept evidence from coming in that needs to be put before the...

BARON: I guess the $1.4 billion question is when you say the commissioner refused to rule is: What is required for a ruling? We believe that this court held in Coalition that what is required for a ruling to make a final order is a ruling on whether GSU met its burden of proof and that it did this much, and didn't.

OWEN: Let's explore that a minute. You say it's a final order. If we left the order in place, untouched as it is today, the $1.4 billion remains on the utility's books. It is not taken off the books and it would just remain there. The commission never made that call did it saying that it's disallowed, you have to take it off the books, write it off?

BARON: No, but that's the utilities choice under the accounting rules. It is not the commission's call...

OWEN: But the order was not final from that aspect, that's still up to the utility. But if we now by your argument we are changing the effect of the commission's order because we are saying in fact that it is a disallowance, the court instead of the PUC is making the call that is a disallowance.

BARON: I think that the question though is whether changing it as you say to make it a permanent disallowance would have an effect on what the commission has the power to do. And GSU has argued that a permanent disallowance would have an impact on financial integrity, which it doesn't elaborate on, but alleges that as distinguished from just keeping it on the books.

We think that that is a fundamental misconception of the financial integrity concept. Financial integrity is not a trump card that allows a utility to avoid proving the prudence of a case. The constitutional cases that are cited, none of them say that the constitution guarantees financial integrity.

OWEN: My specific question is not about all of the constitutional issues. If there had been a deferral, if there had been a disallowance, GSU would have been required to write this off? It could not carry it in its books; is that correct?

BARON: That's correct.

OWEN: And that's not the current effect of the PUC's order?

BARON: It's the utility's choice, that's right.

OWEN: Doesn't that tell us that it's not a final order?

BARON: That's right. But the question that follows from that your honor is whether it makes a difference to the rates that the commission set because it would be a permanent disallowance. And you can only conclude that it would make a difference in the rates that are set if the commission has the power in the name of financial integrity to say: Even though the utility failed to meet its burden of proof we are going to allow higher rates to avoid the financial effects of the write-off. And if you consider the deferred accounting cases that you decided just 2 years ago, you held that in the name of financial integrity the commission had the authority to allow a utility to engage in a deferred accounting practice when necessary to financial integrity, to preserve the opportunity to recover costs. But the court understood and all parties understood that before those costs actually could come from the books and get in rate base, that there had to be proof by the utility that the costs were prudently incurred. So financial integrity is circumscribed by and subject to the prudence call, and the prudence call is what we understand the court has construed our order to mean.

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DAY: Judge Owen if I could begin by trying to help you understand or get a response to your question about whether it's a final order or not in light of the company's failure to write-off. That is an accounting convention. It is solely in the company's discretion. For instance: Texas Utilities Company which had a disallowance of close to $1.4 billion, that company in that situation chose to immediately write it off, the entire disallowance in spite of the fact that it continued to go forward on appeal. And indeed this court has recently considered the appeal of the Texas Utilities case, and has sent that back to the commission for reconsideration of some portion of that disallowance, which will mean that that company will get a windfall in essence money that's already off its books, yet the money will come back to it if indeed the commission has to reconsider the minority on a buy back case, in the Texas Utilities case. In this situation, Gulf States Utilities even though it had a final order _____ convention and said: We don't have to write off this disallowance until we have exhausted our appeals. And so it has nothing to do with whether or not the order is final.

OWEN: Well there was no disallowance by the commission. Is there any conclusion of law in the order that says this is disallowed?

DAY: Your honor let me take you to Conclusion of Law 18. It states as follows: $1,453,520,982. of GSU's share of_____ River Bend capital costs should not be included from GSU's rate base as invested capital used and useful in rendering service to the public pursuant to PURA §§ 38, 39, and 41. 18(a) then goes on to set the reasonable amount of that River Bend investment that can come into rates. This commission had to make a final decision in order to set rates. The rates that were set included a disallowance of $1.453 billion. The error dealt with in Coalition of Cities is not as to the determination of that $1.453 billion, but rather what the commission wanted to do with that determination after the determination was reached.

Let me take you to one financial integrity type point. I will refer you to page 157a and 157b out of the examiner's report. Now I bring it to your attention for several reasons because GSU put on financial integrity analysis and testimony before the commission of write-offs. And indeed as you see the parties listed on this side GSU illustrated that there were 3 parties testifying before the commission that represented in their testimony in evidence that $1.4 billion ought to be written off. And GSU then goes on to present financial integrity analysis of what the result would be in light of that. So the commission had that testimony before it and indeed the commission in its finding of fact 191, as referred to by Mr. Ratliff indicates that a phase-in is not necessary given that the revenues generated by the rates which included a $1.43 billion disallowance were going to be adequate, and therefore, it was not necessary to give the company in that situation a rate moderation plan.

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REBUTTAL

RATLIFF: Justice Owen if I could I think you are to the nub of the controversy. And that is what the state is trying to say here is that the commission can make a "reasoned judgment" and enter a reasoned opinion in this case when they did not know at the time that they sought to defer that there was going to be a holding by this court that that exceeded their power and in fact exceeded their power to such an extent that it would be subject to a collateral attack. You are exactly right. The commission is the one that has to make that decision. And the reason that it has to make that decision is because contrary to what we are used to in the trial court, the commission is charged by the statute with the duty to take into account the effect that its order may have on the utility in its ability to serve the public. That clearly was not done in this proceeding.

Now Mr. Day just took you to the commission's finding 191, but he left out a part of it. And after it talks about the rate moderation plan is not necessary it says such a plan may be appropriate in the future if additional River Bend capital costs are found to have been reasonably and prudently incurred. Similarly, I find it passing strange that we have the commission itself now saying that they have made a conscious decision to disallow in light of the language that they used on the motion for rehearing in Coalition of Cities where they specifically said that the commission deliberately refused to make that disallowance decision in this _____.

I think if you look at the order, and I think the extracts of the final order meetings that we handed to the court are instructive in this regard. And those final orders meetings are incorporated in the order because the commission itself in this order says: For the reasons stated on the record in those meetings we do thus and so. You go through it. Commissioner Graytock says everybody should be aware this is not a disallowance. Commissioner Campbell says we are not disallowing it. We are setting it to the side for a later determination. Chairman Thomas at that time dissents. He dissents on the basis that we should not hold this issue in abeyance. We should not defer.

GONZALEZ: To get to the point you want this court to get to, and that is remand to the PUC for a prudency hearing, what do we do with Coalition of Cities?

RATLIFF: I think what you do with Coalition of Cities is I think that if all of this conversation about burden of proof in my judgment was beside the point in Coalition of Cities. If I may be so bold as to say it. And the reason I say that is once this court determined that the commission by granting the severance had so far exceeded its power that this court would intervene in a collateral proceeding, and could uphold an injunction, I think the hunt was over once you decide that they have exceeded their power in attempting to set a second hearing.

GONZALEZ: So we would have to overrule Coalition of Cities to some extent?

RATLIFF: I think that you certainly would have to look at the burden of proof discussion in my judgment as being superfluous to the decision. Because I think the fact of the matter is is that you don't ever have to reach that question of burden of proof. Because as this court well knows once you are faced

with an order that at least appears on its face to be final, and once it appears that it deals with a subject matter which is not susceptible to separate treatment in two different proceedings it seems to me that under Scurlock you then have an order to the extent you are going to apply res judicata and collateral estoppel principles to administrative orders you then have an order that precludes a subsequent proceeding considering that same matter. It does not preclude a reversal and a remand in a direct attack such as this. But it occurs to me that some of the language dealing with burden of proof in Coalition I think that the court may well have to simply distinguish it on the basis that it wasn't absolutely necessary to the decision. I don't believe it was. And I think the whole problem with Coalition as interpreted by the 3d CA, the whole problem is is that as Justice Owen has pointed out you've got the court either this court of the CA or the DC making the determination that there has been a permanent disallowance. It is clear from the comments the commissioners in the final order made, that they understood the difference in impact on GSU of a permanent disallowance verses a deferral. It is also clear that they understood the financial situation that GSU found itself in at that time. So we believe that the only appropriate order is to allow the commission itself to utilize its powers to determine what goes in the rate base and go ahead and make the findings on exclusion. We have a finding here according to the respondents made by somebody a combination of the court and the commission I suppose that does away with the entire $1.45 billion. When even the staff and the other witnesses for the intervenors would admit that a portion of that $1.453 had been prudently and reasonably incurred.

ENOCH: It troubles me a little bit Mr. Ratliff if at the end of the trial of the case the judge says that I am not sure whether you've proved your case or not. So I am just not going to decide that issue, but I am going to render a judgment for X amount of dollars, which I can't calculate but for the fact I don't include the number that I am not sure whether you've proved it or not and just say we will go try that issue some other time. And now you've got a final judgment and goes up on appeal. My concern is what's the appellate function that's going on here? Do you have the burden if you have the burden of proof at trial to prove the TC erred in not awarding those damages. In other words did the PUC err in not including that in the rate base, or do you just send it back to the TC to recalculate its judgment based on what it understands the evidence to be? I guess my concern is this: You've got a final decision here that is set rates. And that can't have been calculated but for the PUC adding some figures and subtracting some figures and that sort of thing. In order to arrive at that they clearly didn't include the $1.453 billion in their calculation. Now the point that's being made is they didn't' include it because they say that Gulf States didn't show it was justified. We don't know. So we are just not going to allege it. We are saying well you can't defer that. You are going to have to decide it in this proceeding. We send it back to the PUC. Is it to send it back to say Gulf States take a second shot at proving this case? I mean is that what's going on here? GSU you didn't prove it the first time, we will give you a second shot to prove it, but doesn't that do violence with the Coalition of Cities which says PUC you can't be a in rate case you can't pick and choose what you are going to consider then and then put off for a future rate case stuff that should have been considered here.

RATLIFF: I do not believe it necessarily means a second bite. And that's the reason I was trying to be careful in answering your questions before. I think it ought to go back to the commission. If

the commission thinks they can make their decision on the basis of the record they currently have and can discharge their duty to the public as well as to GSU and to these parties, then I think that would be within the PUC's discretion. I think that's a part of their function. I think what happens in a situation you are talking about and we have some close analogies where the trial judge severs a cause and it is determined that he has severed a cause which is not severable. Well you don't in that case simply take the evidence that was adduced on the severed cause and try to sort it out. What you do is you say on the direct appeal from that order: Your honor you didn't have the right to sever; and therefore, we are going to reverse this case, we are going to remand it to you, and admittedly we are going to have to go back over some of the same ground, but you now are in a position to determine this appropriately with everything before you because you cannot sever. And I think that's the situation that we've got here.