

# Stipulations, the Consumer Advocate and Utility Regulation in Florida

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# Stipulations, the consumer advocate and utility regulation in Florida<sup>+</sup>

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## Abstract

Relatively little is known about the practice of settlement rather than litigation in US utility regulation, or about the activities of consumer advocates. This paper presents evidence from Florida. During 1976-2002, over 30 per cent of earnings reviews were settled by stipulations involving the Office of Public Counsel but only 5 per cent of other cases. Over three quarters of the rate reductions associated with earnings reviews derived from these stipulations, and in the decade 1976-86 the proportion was over 95 per cent. The average value of a rate reduction was seven times higher with a stipulation than without. Only 1 per cent of the rate increases associated with company requests derived from stipulations. In these few cases the stipulation typically provided for a lower proportion of the requested rate increase than a litigated outcome allowed (about one third compared to one half). A companion paper investigates the nature and effects of these stipulations. This research suggests that settlements deserve consideration in utility regulation generally, even outside the US context.

JEL classification: L51 Economics of regulation, L97 Utilities general, L94 Electric utilities, L 95 Gas utilities, pipelines, water utilities.

Key words: stipulations, settlements, consumer advocate, regulation.

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<sup>+</sup> This paper reports on research carried out some years ago, some outline results of which were given in Littlechild (2003). I am particularly indebted to Dale Mailhot of the Florida PSC for explaining the regulatory processes, allowing me access to the database, and patiently clarifying the details and background. I am grateful to Bonnie Davis, Jack Shreve and Scheff Wright for enlightening discussions in Tallahassee; to Dan Fessler and Steven Weissman for discussion of this topic in California; to Ashley Brown, Robert Burns, Joseph Doucet, Guy Holburn, Mark Jamison, Paul Joskow, Paul Sotkevitz, Pablo Spiller and James Wilson for related discussion and comments; and to a referee for helpful suggestions. For facilitating this research I thank Sanford Berg and Paul Sotkevitz at PURC, the Judge Business School and the TSEC grant to the Electricity Policy Research Group at Cambridge University. None of the above is responsible for views expressed herein.

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## **1. Introduction**

Traditionally, US and Canadian public utility commissions regulated utilities by a process of litigation, with periodic rate reviews involving hearings followed by decisions. However, over the last quarter century many commissions have replaced or supplemented this litigated process by endorsing negotiated settlements (sometimes called stipulations) agreed in previous discussions between the utilities and interested parties or intervenors and their appointed representatives. A number of questions naturally arise. How extensive has this practice been? What kinds of issues are most subject to settlements and stipulations of this kind? How different, if at all, are the provisions of the stipulations from the decisions that would otherwise have been made by the commissions themselves?

Over the same period, many US states created an office of consumer advocate to represent the interests of consumers before the utility commissions. This, too, raises obvious questions. What has been the extent and nature of the activities of such consumer advocates? What effect have they had on decisions of the regulatory commissions? To what extent have such consumer advocates been instrumental in the development or otherwise of negotiated settlements?

There are policy implications North America and beyond. Does the use of settlements indicate some inadequacy in the formal regulatory process or in the statutes that govern the commissions? Would it be feasible and sensible for European and other utility regulators to facilitate or encourage the use of settlements as an alternative or complement to their own proposals and decisions?

Relatively little seems to have been written on these matters, at least by economists. This paper presents evidence from the experience of the Public Service Commission (PSC) and the consumer advocate or Office of Public Counsel (OPC) in Florida. The data include details of over 300 dockets and orders of the PSC on revenue-related matters in the telephone, electricity and gas sectors from 1960 to 2002. Interest here focuses particularly on the extent and nature of the stipulations and settlements negotiated and signed by OPC after its creation in 1974. As it happens, the period 1976-2002 is essentially the period of office of a single person as Public Counsel, and therefore provides a sensible unit of analysis.

Section 2 of the paper reviews the relevant literature, sections 3 and 4 describe the institutional background in Florida, sections 5 and 6 discuss the data, section 7 provides background on the general pattern of utility rate regulation there from 1960 to 1975, section 8 explains Florida's policy on stipulations and settlements, section 9 discusses the motivations of the parties and establishes predictions as to where stipulations are most likely, section 10 tests these predictions against the evidence, section 11 examines stipulations involving PSC staff without the OPC, section 12 examines whether OPC policy has changed over time, section 13 examines whether OPC stipulations are more likely when rate reductions are hypothesized, and section 14 concludes.

The aim of the present paper is to document where and when settlements occur. A companion paper (Littlechild 2006) looks in detail at the content of the stipulations that have been made in the Florida electricity sector. The aim is to understand their purpose and effect, and to identify any differences in outcome compared to what would have happened had the decisions been left to the Commission and staff through the litigated process. This has implications for what would happen if settlements were encouraged in other jurisdictions too.

## 2. The economic and legal literature

A public utilities commission deals with rate cases that might be initiated by a regulated utility or (in the US) by the commission itself. The traditional litigated process has been for the commission to call for initial testimony, to require and test evidence via a series of formal hearings, then to make a decision in the form of an order that has the status of a judicial pronouncement in a court of law. Economists have studied, *inter alia*, the effects (or lack of them) that this process has on costs, prices and profits of the utilities (e.g. Stigler 1971, Peltzmann 1976, 1989), the effects of inflation and other factors on the regulatory process (e.g. Joskow 1974), various developments in regulation (e.g. Joskow and Schmalensee 1986, Joskow 1989), and the impacts of various pressure groups including consumer advocates (e.g. Holburn and Spiller 2002, Holburn and Vanden Bergh 2006).

During this period there has been interest, at least in administrative, legal and regulatory circles, in “alternative procedures that might be used by state public utility commissions in place of trial-type, adjudicatory procedures”.<sup>1</sup> One direction of development has been alternative dispute resolution (ADR) procedures, which often tend to focus on the resolution of customer complaints. Another direction (sometimes using the same term ADR) has been the development of a process of negotiated stipulations and settlements between the utility and interested parties, which might include the consumer advocate. As of the mid-1980s, “Negotiated and stipulated settlements in a judicial proceeding are used at many, but not all, state public utility commissions” and in “a wide variety of cases and issues”.<sup>2</sup>

On the face of it, this approach would seem to supercede, or at least to modify, a critical part of the traditional regulatory process, not least in such major issues as revenue determination and rate-making. Surprisingly, however, the development of stipulations does not seem to have attracted the attention of economists. Exceptions are some

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<sup>1</sup> “These are procedures that can lead to more efficient determination of routine commission decisions and procedures that can be used to consider forward-looking economic, financial, and other regulatory policy issues.” (Burns 1988 p. iii and references therein)

<sup>2</sup> Burns (1988), p. 42, referencing Petrusis (1985). The cases include “the effects of Tax Reform Act, water rate cases, fuel adjustment clause cases, prudence reviews, the treatment of overcapacity, competition in the telecommunications industry, customer service rule complaints, new telecommunications service offerings, the treatment of cancelled plant, the removal and deregulation of a plant from rate base, and the sale of an electric plant. (A list of examples of state commissions using stipulated or negotiated settlements is contained at appendix A.)” Interestingly, none of the 59 articles listed in that appendix refers to Florida.

unpublished research by Joskow (1972), an important study by Wang (2004), and some ongoing research involving the present author (Littlechild 2003, 2006, Doucet and Littlechild 2006 a,b).

In contrast, legal scholars and regulatory practitioners have followed the subject with interest. Initially, settlements were seen as a means of speeding up decisions (notably to reduce the backlog at the FPC)<sup>3</sup> and reducing costs and uncertainty. Some have been concerned about certain aspects of settlements, not least non-unanimous ones. More recently it has been suggested that settlements may reflect more accurately the views of the parties, and may allow more innovative and creative solutions than the regulatory commissions may be able to achieve by litigation. On this view, settlements are not so much, or not only, a way of reducing the transactions costs of achieving the same outcome as litigation. Rather, they can be a means of achieving a different outcome than litigation, and one that is preferred by the parties involved. Doucet and Littlechild (2006a) provide a survey of these literatures.

A critical participant in some of these negotiated settlements seems to be the consumer advocate or equivalent representative. This too seems to be an unexplored area: recent research by Holburn and Spiller (2002) claims to be “the first study to analyze, both theoretically and empirically, the effect of consumer advocates”.<sup>4</sup> Holburn and Vanden Bergh (2006) have studied the creation of consumer advocate bodies.

### **3. The Florida Public Service Commission**

The Florida Public Service Commission (FPSC or simply PSC) was established in 1887, abolished in 1891 and recreated in 1897.<sup>5</sup> It regulates the telephone, natural gas, electric power and water industries. Until 1979 it consisted of three elected commissioners. Since 1 January 1979 it consists of five members, each serving a four-year term, appointed by the Governor from nominees selected by the PSC Nominating Council; commissioners must also be confirmed by the Florida Senate.

The PSC has quasi-legislative and judicial responsibilities. In the former capacity it makes rules governing utility operations. In the latter capacity it hears and decides complaints, issues written orders similar to court orders, and may have its decisions appealed to the 1<sup>st</sup> District Court of Appeal and the Florida Supreme Court.

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<sup>3</sup> Stipulations and settlements are seen as one of the “procedural streamlining techniques ... that change procedures in a fundamental way so as to speed up the agency’s decision-making process”, and “Greater commission efficiency is the principal purpose of the procedural and substantive streamlining techniques”. Burns 1988, pp, iv, v, also 55-62. Substantive streamlining techniques include automatic fuel adjustment clauses, FERC’s generic benchmark rate of return on common equity, and price caps.

<sup>4</sup> Their main propositions are that participation of consumer advocates leads to lower allowed rates of return; that “consumer advocates are likely to be more influenced by interest groups reflecting industrial users than by consumer groups representing residential users. Thus consumer advocates may be associated with relatively lower industrial rates”; and that “utilities are less likely to initiate rate reviews in relatively pro-consumer regulatory environments, including those with a consumer advocate”. They present evidence from 1980-89 to support and quantify these conclusions. These claims are explored by Littlechild (2006).

<sup>5</sup> Information in these five paragraphs is from *Florida PSC Annual Report 2001*, pp. 9, 10.

The PSC must balance the needs of each utility and its shareholders with the needs of customers. Traditionally, the PSC sought this goal by establishing exclusive service territories, regulating the rates and profits of each utility, and imposing universal service obligations. More recently competition has become an issue. Legislative action during the 1995 session opened up the local telephone market to increased competition, and has required the PSC to facilitate entry of new firms into the market. There have also been regulatory debates about electricity competition.

In 2001 the PSC regulated 5 electric companies, 7 natural gas utilities and 207 water/waste water utilities, all investor-owned. These organisations varied greatly in size. The PSC also had regulatory authority and competitive market oversight for 10 incumbent local exchange telephone companies, over a thousand alternative local exchange and long-distance (inter-exchange) telephone companies, and many other telephone service providers. While the PSC does not regulate publicly owned, municipal or cooperative utilities, it does have jurisdiction in certain matters over 32 municipally owned electric systems, 18 rural electric cooperatives and 27 municipally owned natural gas utilities.

The PSC has an active workload. In 2001 it opened 1683 dockets, reopened 30 dockets, and closed 1833 dockets. It had 386 authorised staff positions and an annual budget of approximately \$27 million for fiscal year 2001-2.

#### **4. The Office of Public Counsel**

In the US generally, consumer advocates were mostly appointed during the 1970s and 1980s. The general aim was to give consumers a greater voice in the making of regulatory policies at a time when there was growing concern about rate increases.<sup>6</sup>

The State of Florida set up the Office of Public Counsel (OPC) in 1974.<sup>7</sup> Its duty is to represent the citizens of Florida in utility matters, mainly before the PSC.<sup>8</sup> It provides a

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<sup>6</sup> This was a time of rising fuel costs and general inflation. Whether regulatory commissions were indeed neglecting the interests of customers is beyond the scope of this paper.

<sup>7</sup> Florida was one of the earlier states to set up a consumer advocate. The order seems to be Indiana 1945, Maryland 1955, New York 1970, Kentucky 1972, Massachusetts and Montana 1973, New Jersey and Florida 1974, followed by 25 other states culminating in Tennessee 1994. (Holburn and Vanden Burgh 2006, Table 1)

<sup>8</sup> Florida Statute 350.06.01 provides that "The Joint Legislative Auditing Committee shall appoint a Public Counsel ... to represent the general public of Florida before the Florida PSC." The Public Counsel shall be an attorney. The duty of the Public Counsel is to provide legal representation for the people of the State in proceedings before the Commission. The powers of Public Counsel include

- to recommend the commencement of any proceedings
- to urge therein any position which he or she deems in the public interest (whether consistent or inconsistent with positions previously taken by the Commission)
- to utilize all forms of discovery available
- to have access to all files, records and data of the Commission available to any other attorney representing parties to a proceeding
- to seek review of determinations, findings and orders

balance to the utility in hearings before the PSC. The Public Counsel is appointed or reappointed annually. After three appointees served as Public Counsel in the first three years, a single incumbent (Mr Jack Shreve) held the office for over 25 years, until June 2003. The OPC presently has a staff of about 15, a little smaller than it was before telephone rate deregulation but said to be as experienced as FPSC staff, and an annual budget of about \$2.5 m.<sup>9</sup> This means that the OPC has less than one twentieth the staff of the PSC, and its budget is about one tenth that of the PSC. Consultants and expert witnesses are taken on for each case as needed.

The OPC does not publish annual reports, but in June 2003 issued a report on its activities over the period up to Mr Shreve's retirement.<sup>10</sup> Of the 26 pages, 3 ½ refer to its activities concerning telephone utilities, 7 to electricity and gas utilities, and 15 ½ to water and wastewater utilities.<sup>11</sup>

The normal procedure in revenue-related cases is for the utility to apply for a rate increase or for the PSC to order a review of a case, often but not always with a view to a rate decrease. The OPC and other interested parties such as customers or competitors can also press the PSC to review a case. Once the PSC opens a docket, the utility and the OPC and other parties that are accepted as intervenors normally file testimony.<sup>12</sup> All intervenors can challenge these testimonies and seek further information. There is then a formal hearing involving cross-examination of witnesses, after which the PSC makes its decision.

The role of the PSC staff is to develop the facts of the case and to raise relevant issues for investigation and discussion, then to advise the commissioners in the course of their deliberations. In earlier times staff would also have a quasi-advocacy role, but nowadays this role mostly falls to the OPC. Staff are required to be impartial as between the utility, the OPC and other interested parties. The evolving roles of OPC and staff in the settlements process are described below.

## 5. Data on utility revenue cases

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- to prepare and issue reports, recommendations and proposed orders to the Commission, Government and Legislature.

<sup>9</sup> This seems to be above average. "The typical consumer advocate office had a budget of \$0.9m in 1997, with a staff of 10 personnel." (Holburn and Vanden Bergh, 2006 fn 5)

<sup>10</sup> State of Florida Public Counsel *Activity Report*, June 30 2003 [henceforth *OPC Activity Report*].

<sup>11</sup> "It is the experience of the Public Counsel that customers are often far more concerned about and involved in water and wastewater cases than either electric or telephone cases. While the aggregate dollar effect of a water and wastewater case is far smaller than the much larger electric or telephone rate cases, the per customer effect is often on the same order of magnitude. In addition, the greater tangibility of the product and the local management that often characterizes these small utilities tends to generate a greater emotional response from customers. // As a result, the Office of the Public Counsel devotes a great deal of its energy and resource to water and wastewater cases, in spite of their smaller aggregate dollar impact." (*OPC Activity Report*, pp. 11-12)

<sup>12</sup> Florida Administrative Code 25-22.039 provides that persons who have a substantial interest in the proceedings, and who desire to become parties, may petition for leave to intervene. They must demonstrate that their substantial interests are subject to determination or will be affected through the proceedings.

The data consist of details of decisions in just over 300 dockets of Florida PSC over the period 1960-2002. The database records those decisions that have implications for the revenues of the electricity, gas and telephone utilities. These decisions relate to the largest investor-owned utility companies in Florida<sup>13</sup> from 1960 to 1967, and to all such utilities from 1968 to 2002. The decisions cover 13 telephone companies, 8 natural gas companies and 5 electric power companies.

300 dockets are evidently only a small fraction of the tens of thousands of dockets that have been opened and closed over the last forty years. However, most of the other dockets have limited economic significance. For example, there was a large increase in the number of dockets each year in the early 1980s with the allowance of payphone competition, and about a thousand dockets each year relate just to certificates for payphones and other telecommunications company activities. Many tariff changes each year have only a minor effect on terms or conditions, but have to be approved by the PSC. Water and wastewater are important sectors, but with over 200 investor-owned utilities in that sector, most of which are relatively small, the economic significance of any one decision is limited.

Some types of docket not included in the database would have economic significance. These would include the inter-company relationships in the telecommunications sector since the introduction of competition, and the restructuring of the electricity sector. Reportedly, parties typically have such different interests here that they seldom reach agreement, and find little to gain from devoting time to seeking a settlement, but this has not been investigated here. Commission decisions related to amortization, reserves, incentive plans and other issues are not included in the database unless they have implications for revenue. The impacts of fuel adjustment and other clauses (e.g. concerning conservation and the environment) are not included in the database.

The data are believed to cover all major revenue decisions in Florida utilities over the last quarter-century. In the period since 1976 they include allowed rate increases amounting to \$2.4bn (out of \$4.6bn requested) and permanent rate reductions of \$1.6bn plus a further \$1.3bn of one-time reductions.

## **6. Treatment of data**

Some dockets may comprise two or more orders. Some orders may comprise two or more items (each item being a line in the data base) describing the essential features. These different items variously reflect interim and final decisions, decisions for separate years, permanent and one-time reductions, reductions applied to different uses, a combination of issues in the rate case, and so on. In total there are just over 500 items.

I have generally consolidated the items and orders into one observation per docket. In a dozen cases, where a docket included orders of more than one type or where some orders

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<sup>13</sup> The eight large utilities in Florida are Southern Bell, General Telephone (Gentel), United, and Central Telephone (Centel) in telephones, and Florida Power and Light (FPL), Florida Power Corporation (FPC), Gulf Power and Tampa Electric (TECO) in electricity.



reflected stipulations and others did not, I have split them into two component parts (in one case three parts). This and other minor modifications<sup>14</sup> produced 318 observations. The observations are dated according to the first order in the docket so-defined.

For most purposes I have split the observations into two periods: 1960 to 1975 and 1976 to 2002. These are intended to reflect the periods before and after the operational effectiveness of the OPC following its establishment in 1974.<sup>15</sup>

The 85 observations in the period 1960 to 1975 have limited detail, and are relevant primarily as background to the subsequent period of interest. The remaining 233 observations pertaining to the period 1976 to 2002 have greater richness of detail, and allow more analysis of the role of negotiated settlements or stipulations.

Before 1978, all allowed rate increases and required rate reductions were in principle of a permanent nature. From 1978 onwards, there were some 60 such permanent rate reductions but also about 100 one-time rate reductions that variously took the form of refunds, rate base reductions, and applications to storm damage reserves, environmental clean-up costs, debt refinancing costs or an escrow account.<sup>16</sup>

For various purposes it is useful to aggregate permanent and one-time rate reductions. Unless indicated otherwise, the figures cited for rate reductions comprise the permanent reductions plus one-quarter times the one-time reductions.<sup>17</sup>

For the most part no distinction has been drawn here between the different types of one-time reductions. Section 13 examines whether stipulations are more likely with

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<sup>14</sup> Some further notes on data: 1) I have excluded the observations for one small company. Frontier Communications, formerly Southland Telephone Company, operates over the Florida-Alabama state line, with about 75% of its operations in Alabama. The company would file a rate case there, ask for the same rates in Florida as it received in Alabama, and usually receive them. The 7 dockets pertaining to this company were not included in the analysis. 2) I have counted Peoples Gas docket 980434 as a final settlement of WFNG docket 930091. 3) I have counted FPC dockets 891298 and 900935 as final settlements of docket 870220. 4) Three tax savings dockets actually cover 14 companies; I have left these as separate cases.

<sup>15</sup> It would be possible to draw the demarcation line a year or two earlier or later, depending on one's view of the initial situation at OPC. However, this would seem to make little difference to the results below since OPC's first signed stipulation (providing for only the second PSC rate reduction order in nearly ten years) did not occur until 1978. I have not sought to assess the impact (if any) of the change in 1979 from an elected Public Service commission to an appointed commission. Almost all the detailed data refer to the period with an appointed commission, and only two stipulations preceded that period.

<sup>16</sup> There were no one-time rate increases. In a couple of cases there were step (phased) increases that I have included as full increases without adjustment.

<sup>17</sup> A permanent reduction that did indeed last forever might be worth more than four times a one-time reduction. In practice, however, a permanent reduction would be subject to review at the time of the next rate review. A rough calculation suggests that this might be of the order of four years away on average. (The 233 cases derived from the database for 1976 to 2002 cover 26 companies, an average of 9 decisions per company over this period. This is an average of 3 years between decisions. However, some of the decisions refer to telephone and gas companies that merged during the period, and about fifty of the cases refer to tax decisions that did not reopen rate review issues or to ROE reviews that had no immediate impact on revenues. The remaining cases average about 4 years between decisions.)

hypothecated or unhypothecated rate reductions. Littlechild (2006) examines the allocation of rate reductions between customer classes.

## 7. Background: 1960 to 1975

Table 1 shows that, over the sixteen years 1960 to 1975, the utility companies initiated 50 dockets typically requesting a rate increase, while the PSC initiated 27 dockets typically leading to a rate decrease.<sup>18</sup> In total, this meant an average of about 5 dockets per year pertaining to revenue issues. The average requested increase was just over \$20m (much less for gas), of which the PSC allowed on average 63 per cent (a little less in electricity, a little more in the other two sectors). The average required rate decrease in PSC initiated cases was about \$2.5m (again much less for gas).

Table 1 Dockets decided by Florida PSC 1960-1975, by sector

Sector	Number of company requests	Average company request \$m	Average allowed request \$m	Proportion of request allowed %	Number of PSC initiated dockets	Average resulting reduction \$m	Total number of dockets
Electricity	14	37.1	14.6	54	14	3.8	28
Gas	13	0.6	0.4	75	3	0.1	16
Telephone	23	22.3	16.0	72	10	1.4	33
Total	50	21.3	13.4	63	27	2.5	77

Electricity and gas companies each accounted for about a quarter of these dockets, telephone companies for nearly half. The dockets differed sharply in size between sectors, with rate increases and reductions in gas being one to two orders of magnitude smaller than in telephones and electricity.<sup>19</sup>

Table 2 Dockets decided by Florida PSC 1960-75, by time period

Time period	Number of company requests	Average request \$m	Average allowed request \$m	Proportion of request allowed %	Number of PSC required reductions	Average PSC reduction \$m	Total number of dockets
1960-7	4	2.2	1.6	74	21	2.8	31
1968-9	9	2.1	1.3	62	5	1.7	16
1970-5	37	28.0	17.6	63	1	0.2	38
Total	50	21.3	13.4	63	27	2.5	85

<sup>18</sup> In addition, there were 6 cases between 1960 and 1967, and a further two in 1968-9, where companies are listed as making request but no amount is listed, and the outcome is a rate reduction. Most of these requests seem to have been for changes in rate structure where it was accepted that the company would need to reduce rates anyway. In one case FPSC requested the filing as a follow up to an earlier order requiring a rate reduction

<sup>19</sup> Although not shown in Table 1, there were great variations in size within each sector. For example, within telephones the amounts requested by companies varied from \$44,000 to \$216m.

Table 2 reclassifies the data to show the considerable variation over time. It divides the whole period into three sub-periods (of unequal length) to reflect the changing experience during the period as a whole.

The eight years 1960-67 were mainly a period of moderate rate reductions, averaging nearly \$3m each. Companies were also requesting rate increases, averaging only \$2m each, and on average three quarters of this was allowed, so the average rate increase was \$1.6m. There were five times as many orders to reduce rates as to increase them.

During the next two years 1968-69, the picture began to change. The average size of each reduction required by the PSC fell to \$1.7m. The average frequency of requests per year increased eightfold. There were now twice as many orders to increase rates as to reduce them.

From 1970-75, the picture was dominated by requested rate increases, now averaging nearly \$30m each. The average amount allowed (\$17.6m) was thirty times the average in the early 1960s. The PSC initiated only one rate reduction over this period, and that only for \$0.2m.

## **8. Stipulations and settlements**

In this context of large rate increases coming to replace moderate rate reductions, the State of Florida created the Office of Public Counsel to represent the interests of citizens. Amongst other activities, the OPC could discharge its role by analysis and argument in hearings before the PSC, which it did. Of present interest is how the OPC impacted on less formal practices such as settlements.

The PSC and its staff have an interest in reducing the time and costs of hearings where this can be achieved without compromising due process. To this end, until the mid-1970s PSC staff and companies negotiated many settlements that appeared simply as amounts in a subsequent order of the PSC. Other participants were seldom involved. There was no signed document and usually no reference to any meetings or agreements. The process was much less formal than today.

With the creation of the OPC, and the possibility of it participating in such settlements, a more formal process was needed to record the agreement between OPC, company and PSC staff. In addition, as the agreements became more complicated and included more than just an amount, putting the agreement in writing made clearer what everyone was agreeing to. For this purpose, settlements and stipulations were used. In Florida, a distinction does not seem to be drawn between these two terms.<sup>20</sup> The written agreements

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<sup>20</sup> Elsewhere, the California Public Utilities Code defines the terms as follows. “ ‘Settlement’ means an agreement between some or all of the parties to a Commission proceeding on a mutually acceptable outcome to the proceedings. ‘Stipulation’ means an agreement between some or all of the parties to a Commission proceeding on the resolution of any issue of law or fact material to the proceeding.” The Code further provides that “Parties to a Commission proceeding may stipulate to the resolution of any issue of law or fact material to the proceeding, or may settle on a mutually acceptable outcome to the proceeding, with or without resolving material issues.” California Public Utilities Commission, Rules of Practice and

variously refer to the document as a stipulation, settlement, stipulation and settlement, stipulation and agreement, and settlement agreement. The term stipulation is widely used in regulatory discussion, and for convenience is the term generally used in this paper.

There does not appear to be an explicit policy statement on stipulations and settlements in Florida, though the Commission cited a supportive Court observation in one particular stipulation.<sup>21</sup> In contrast, other jurisdictions have discussed this issue at some length.<sup>22</sup>

In principle, settlements and stipulations could be proposed and agreed at any time in the proceedings. In practice, discussions tend to take place after the opening filings and counter-filings of testimony, so that evidence is available on which to base discussion between the parties. If agreement is reached, this is frequently just before the hearing is scheduled.<sup>23</sup> If agreement is not reached, the parties testify as in a traditional contested hearing.

There seems to be no use of separate “settlement judges” in Florida as there is at FERC and in New York, for example.<sup>24</sup> In the early part of the period studied, FPSC staff often set up, or would be involved in, process meetings with the utilities and interested parties, with a view to facilitating an early and agreed settling of the case. There is no statutory prohibition on staff meeting with utilities and interested parties, whereas there is such a prohibition on commissioners meeting these parties. All parties must be notified of any such meeting, and have a right to attend.

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Procedure, Title 20 California Code of Regulations, April 2000, Article 13.5 Stipulations and Settlements, 51 (Rule 51) Definitions and 51.1 (Rule 51.1) Proposal of Settlements or Stipulations, pp 87-8.

<sup>21</sup> “ ‘It is the policy of the law to encourage and favor the compromise and settlement of controversies when such settlement is entered into fairly and in good faith by competent parties, and is not procured by fraud or overreaching. ... It is in the interest of the state as well as the parties themselves that there should be an end to litigation.’ 10 Fla. Jur. 2d Compromise, Accord and Release, §9. To the above criteria we would add: Is the Stipulation in the public interest and are the resulting rates fair and reasonable?” Docket 870220-El, Order 18627, In re: Request by Occidental Chemical Corporation for reduction of electric service rates charged by Florida Power Corporation. Issued 4 January 1988, p. 2

<sup>22</sup> Thus, the California Public Utilities Commission took the opportunity, in one of its judgements, “to address the role that “all-party” or unanimous settlements can play in assisting the Commission in discharging its regulatory responsibilities”. San Diego Gas and Electric Co, CPUC 1992, Summary; also Natural Gas and Procurement Issues, CPUC, 1991. This was nearly 15 years after OPC signed its first stipulation in Florida. See also the guidelines established by the State of New York Public Service Commission in Burns (1988, Appendix, pp. 137-140), the discussion of about 30 settlements by Goodman (1998), and the evolving guidelines obtaining in Canada (Doucet and Littlechild 2006b).

<sup>23</sup> A hearing is usually scheduled for about five months after a case begins. I am told that interested parties usually participate by the end of the first month: it is difficult to catch up and be a meaningful player thereafter. Parties usually get serious about settling a case during the fourth month, and settlements have sometimes been reached the night before the hearing. There is much less incentive to settle a case after a hearing is held.

<sup>24</sup> Burns (1988, p. 44)

Beginning in 1978, in the period to 2002, OPC entered into some 36 stipulations with revenue implications, as contained in the present database. OPC has also signed a few other stipulations.<sup>25</sup>

Initially, PSC staff would also sign the agreed settlement, along with the utility company and any other parties. Although this could not formally commit the PSC, it was thought a useful ingredient since commissioners would have a positive staff recommendation before them on each stipulation. Staff also signed a few additional stipulations without OPC.

At some time in late 1986, FPSC advised staff that it was not legally necessary for them to sign these agreements. This apparently followed a problem with one of the stipulations that staff had signed, even though a staff signature was not legally binding on the PSC.<sup>26</sup> From 1987 onwards, OPC and other parties negotiated without requiring the signature of PSC staff, or even the presence of staff in their meetings. Nevertheless, although staff did not have a power of veto over the content of the settlement, it was considered sensible to bear in mind staff views.

In practice, FPSC has almost invariably adopted negotiated settlements put to it.<sup>27</sup> For the PSC, a settlement avoids potential criticism from one or other of the parties and minimises the chance of a legal challenge. This is not to say that the PSC and staff have necessarily agreed with every aspect of each settlement (or with each other) as discussed in Littlechild (2006). However, unlike the practice in California and some other jurisdictions, FPSC has never sought to “cherrypick” by accepting some elements of the stipulation and rejecting others.

Since the meetings of interested parties are confidential, there is no public knowledge of what is said therein. As several commentators have pointed out, a consequence of adopting a settlement is that there is no public record of how the recommended solution was arrived at, in contrast to the procedure of hearings. However, stipulations tend to

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<sup>25</sup> These OPC stipulations not included in the database are thought to include the buy-out of the Tiger Bay Cogen plant and a nuclear outage at FPC, both of which limited the costs that could be recovered through the cost recovery clause. There were also three stipulations on quality of service where telephone companies implemented a service guarantee plan requiring them to make payments to individual customers if the company did not meet certain requirements such as getting a phone back in service within 48 hours after the customer notified the company.

<sup>26</sup> There is some uncertainty about precisely what was said and when. The first stipulation with OPC and without PSC staff is dated 29 September 1986 (Florida Power Corporation order 16862). Two stipulations were jointly signed after that (Centel order 17022 dated 24 December 1986 and Southern Bell order 17040 dated 31 December 1986). Staff subsequently signed two stipulations on their own without OPC (Gentel order 17382 dated 8 April 1987 and St Joe Natural Gas Co order 19793 dated 11 August 1988).

<sup>27</sup> There seems to have been only one case in which a negotiated settlement was overturned, and then only temporarily. In 1989 Gulf Telephone agreed with OPC to make a refund to customers. Part of this refund reflected pooling revenues from other companies and customers. FPSC took the view that the agreement would be unfair to competitors not party to the settlement, and inconsistent with FPSC policy for that industry, even though the competitors were not involved in the case. OPC went back to the company and signed a revised stipulation that removed the objectionable element. FPSC approved this revised stipulation. Burns (1988, p. 42) refers to a similar situation at FERC.

follow in time the filing of public testimony by the parties, which records their public positions beforehand. The parties sometimes put into the stipulation some indication of why they think the proposal is reasonable. There is generally a written record of the recommendations and analyses of staff. On occasion this records differences between members of staff, although staff were less inclined to be forthcoming after FPSC dealt rather impatiently with staff reservations in one case.<sup>28</sup> FPSC, which has to be satisfied that the proposed settlement is just and reasonable, will give some explanation of the reasons for its decision. Occasionally the formal FPSC order will simply replicate the (preferred) staff analysis.

## **9. Motivations of the parties and predictions on stipulations**

What are their likely motivations of the parties in considering stipulations? The utility companies may be presumed to seek to further the interests of their shareholders. The statutory duty of the OPC is to represent the interest of the citizens of Florida. In principle such representation could take many forms, and does not necessarily imply negotiating settlements and signing stipulations, though this is not precluded. OPC engages in many activities, and takes an active role in many cases, even where it does not sign a stipulation.<sup>29</sup>

The parties are only likely to enter an agreement and sign a stipulation where it is mutually beneficial to do so. This requires that the agreement can make a difference to the outcome that would otherwise ensue. This might be in terms of reducing the time or cost or risk associated with the predicted outcome if the case goes to litigation. This is typically what the parties affirm publicly.<sup>30</sup> Or, as commentators are beginning to

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<sup>28</sup> Florida Power and Light (FPL), Docket No. 990067-EI, 10 –17 March 1999.

<sup>29</sup> “During the current period, the Public Counsel has continued to pursue telephone-related dockets, to monitor proceedings and participate in workshops on issues of quality of service, violation of service standards, quality of service rules, the practices of cramming and slamming, late payment charges, area code use and number conservation measures, and area code relief.” (p. 1) “The office has also been actively involved in the Governor’s Energy 2020 Study Commission on which the Public Counsel, Jack Shreve, served as a ex officio member. The office also intervened and has taken an active role in the GridFlorida proceedings in which the PSC is considering the participation of Florida’s investor-owned electric utilities in a regional transmission organization (RTO) in response to the Federal Energy Regulatory Commission’s (FERC’s) Order No. 2000.” (p. 4) “The office continues to participate in the annual cost recovery dockets and intervenes in specific electric and gas utility matters as necessary to represent the customers’ interests. Routine activities include monitoring industry activities throughout the country, assistance for individual electric and gas utility customers, and frequent interaction with the press and investment companies.” (p. 5)

<sup>30</sup> E.g. “OPC and Southern Bell believe that it is in the best interests of the ratepayers of Southern Bell and the citizens of Florida to amicably settle the Southern Bell Rate Case without the expenditure of any further time, money and other resources in litigating these issues before the FPSC and the courts. ... The OPC and Southern Bell acknowledge that this stipulation and agreement is being entered into for the purposes of settlement only and that the parties are entering into this stipulation and agreement to avoid the expense and length of further legal proceedings, taking into account the uncertainty and risk inherent in any litigation.” Southern Bell, Docket 920660 and others, Order 94-0172, Stipulation and Agreement, 5 January 1994, pp. 2, 15. “This Stipulation and Settlement avoids the time, expense and uncertainty associated with adversarial litigation in keeping with the Florida Public Service Commission’s long-standing policy and practice of encouraging parties in contested proceedings to settle issues whenever possible.” Docket 990947-EI, Gulf Power Co., 1999

suggest, it might be in terms of finding a different and mutually preferred outcome to the one that would otherwise result from litigation via FPSC.

The likelihood of a stipulation may therefore depend on the issue involved. The database enables the 233 dockets in the period 1976-2002 to be classified into three types of issue:

- 93 earnings reviews (typically initiated by the PSC, sometimes at the request of the OPC, in the belief that earnings might be excessive and with the presumption that rate reductions or other benefits to customers might be called for);
- 82 company requests (typically for rate increases that the companies believe are necessary); and
- 58 'minor cases' (that may be further subdivided into dealing with tax changes, periodically reviewing the appropriate allowed Return on Equity (ROE), and Modified Minimum Filing Requirements (MMFRs) that require earnings to be filed every 4 or 5 years regardless of the level of the utility's profitability).<sup>31</sup>

Company requests accounted for just over one third (83/233) of all the revenue-related dockets in Florida during this period, PSC initiated dockets for the other two thirds.<sup>32</sup>

It seems plausible that the parties can 'make a difference' with respect to the earnings reviews and company requests, where there is a relatively high level of subjectivity about the factors involved. There is generally little if any scope for this with respect to the minor cases where it is more often a matter of ascertaining facts or following rules and applying automatic adjustments. There may be case-specific fixed costs and economies of scale with respect to regulatory issues, which would indicate focus on the more important cases, whether or not a stipulation was envisaged. It is also plausible that the incentives to save time and money and to reduce uncertainty are stronger, and that the time and effort associated with a settlement will be more productive, where the revenues at stake are higher than where they are lower.

Presentation may be an additional consideration. The OPC and the companies are likely to be interested not only in furthering the interests of their principals, but also in being seen to do so. They would therefore have an additional incentive to sign up publicly to those cases that represented "good news" for their principals, and to avoid signing up to those that, on the face of it, represented "bad news".

On this basis, both parties would be interested to sign stipulations that involved rate reductions. From the OPC's perspective, this is seen to bring tangible benefits to customers. From a company's perspective, this is more customer-friendly than having rate reductions forced upon it, and indicates to shareholders that the rate reduction is

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<sup>31</sup> Several dockets involved minor cases (either ROE reviews or tax changes) combined with earnings reviews, and have been classified here with the latter.

<sup>32</sup> It is not clear whether the 1980-89 data of Holburn and Spiller (2002) cover all rate cases or only those initiated by utilities, but reportedly only 10% of their cases involve rate decreases or no change in rate. (Private communication, Dr G L F Holbourn, 30 March 2003) By implication, 90% of their cases involve rate increases, presumably initiated by company requests. If rate cases initiated by the public utilities commission are not included, this may overlook a significant part of the work of the public utilities commissions and the consumer advocates, particularly since the volume of required rate reductions in Florida during this period was of comparable order of magnitude to the rate increases granted.

manageable and that the relationship with the regulator is good. Moreover, the greater the rate reduction, the more important it is for the parties to be associated with it.<sup>33</sup>

Interests are not so obviously congruent with respect to rate increases. A company might well be interested in showing that its rate increase is so reasonable as to be acceptable to the OPC. However, the OPC is unlikely to want to be associated with rate increases. It has to explain that, as a result of its negotiations, a rate increase is less severe than it otherwise would have been, which cannot always be clearly demonstrated. So, the greater the rate increase, the less attractive it is likely to be to OPC.

The net result is that stipulations are predicted to be more likely for earnings reviews, less likely for company requests, and unlikely for minor cases. Stipulations are predicted to be positively associated with the size of rate reductions following earnings reviews, and negatively associated with size of rate increases following company requests.

### 10. Evidence on types of stipulations signed

Table 3 shows, for each of the five types of docket, in how many cases the PSC decision reflected a stipulation signed by the company and OPC.<sup>34</sup> The evidence is consistent with the above hypotheses on the motivation of the parties. Of the 93 earnings review cases predicted to be more likely candidates, OPC and the utility signed a stipulation on 29 of them (31%). Of the 82 company requests and 58 minor cases, predicted to be less likely and unlikely candidates, respectively, they signed a stipulation on only 7% and 2% of them, respectively.<sup>35</sup>

Table 3 Dockets decided by Florida PSC 1976-2002, by type of case

Type of case	All cases	Stipulations signed by OPC		
	Number	Number	%	
Earnings review	93	29	31.2	
Company request	82	6	7.3	
Minor cases:				
Tax savings	33	0	0	
ROE review	16	1	6.3	
MMFRs	<u>9</u>	<u>0</u>	<u>0</u>	
Subtotal minor cases	<u>58</u>	<u>1</u>	<u>1.7</u>	
Total	233	36	15.5	

<sup>33</sup> A colleague comments that there may be different interests with respect to the calculation of the value of a settlement. The customer representative may want to maximise and publicise the undiscounted nominal dollar value of a rate reduction whereas the company will be more concerned about the real present value.

<sup>34</sup> As noted above, early stipulations included PSC staff, later ones did not. The 5 stipulations signed by staff and not by OPC are not included in the OPC figures. This is explored further below.

<sup>35</sup> The litigated cases where OPC did not agree a stipulation could be further divided into those that it contested and those that it did not. It would be interesting to compare the stipulated and contested cases directly, but data is not easily available to do this.



Tables 4, 5 and 6 look in more detail at each of these types of cases. Table 4 examines the 93 earnings reviews. As predicted, stipulations were associated with greater rate reductions. The average rate reduction in the 29 stipulations was \$49.6m contrasted with only \$6.7m in the 64 other (litigated) cases. The 29 stipulations accounted for under one third of the earnings review cases by number but they accounted for over three-quarters by value of the aggregate reduction in revenue associated with these cases.<sup>36</sup> How far the stipulations were the cause of these reductions is beyond the present paper. However, there is reason to believe that such reductions would not have been achieved to the same extent or so soon in the absence of settlements. (See Littlechild 2003, 2006)

Table 4 Florida PSC earnings review cases 1976-2002

	Number of dockets	Aggregate value of reduction \$m	% of total revenue reduction	Average value of reduction \$m
With OPC stipulation	29	1437.7	77.0	49.6
Without OPC stipulation	64	429.4	23.0	6.7
Total	93	1867.1	100	20.1

Table 5 examines the 82 company requests for rate increases. As predicted, stipulations are less likely the higher the rate increase involved. The average rate increase requested by the company (before the settlement negotiations began) was \$56.6m. But in those 6 cases where a stipulation followed the average requested increase was \$8.1m; in the other 76 cases it was \$60.4m. The allowed rate increase in the 6 stipulations was also smaller: \$2.9m compared to \$31.5m. On average the stipulations allowed a smaller proportion of the initially requested increase: 34.7% compared to 52.2%. Either the OPC had a stronger effect when negotiating a settlement than during litigation, or it was able to pick those cases for settlement where the companies' cases were weakest. In total, stipulations accounted for only 0.7% by value of the allowed rate increases.

<sup>36</sup> It is difficult to classify these 93 earnings review cases more finely. About one tenth, typically the earlier and smaller ones, are simply described as "Commission required" and lead to reductions not exceeding \$139,000 each. Just over half are associated with over-earnings in a particular year or years, resulting in rate reductions varying from \$8561 one-time to \$227.8m permanent plus \$249.4m one-time. The remainder have a variety of features, and may be associated with a particular year or several years, with rate reductions across the board or on particular charges, and with various other matters such as tax, ROE reviews, sharing arrangements and in one case a complaint, as well as over-earnings.

Table 5 Florida PSC company request cases 1976-2002

	Number of dockets	Total increases requested \$m	Average increase requested \$m	Total increases allowed \$m	%	Average increase allowed \$m	Average proportion allowed %
With OPC stipulation	6	49	8.1	17	0.7	2.9	34.7
Without OPC stipulation	76	4590	60.4	2396	99.3	31.5	52.2
Total	82	4639	56.6	2413	100	29.4	52.0

Table 6 shows that almost all of the 58 minor cases involved only small amounts of revenue reductions: in 18 cases none at all, and an average of \$5m in the other 40. OPC signed a stipulation for only one of these 58 cases. This was an ROE review that had no immediate outcome in terms of a rate reduction. Although this case might seem out of line with the hypothesis and with OPC practice, the circumstances were unusual.<sup>37</sup>

Table 6 Florida PSC minor cases 1976-2002

	Number of dockets	Number of dockets with non-zero revenue reduction	Total revenue reduction \$m	Average non-zero revenue reduction \$m
Tax	33	31	193.8	6.3
ROE	16	2	4.3	2.2
MMFR	9	7	2.4	0.3
Total	58	40	200.5	5.0

To summarise, over the period 1976 to 2002, stipulations involving the OPC have accounted for 31.2% by number, but 77.0% by value, of the earnings review cases where stipulations were predicted to be more likely. Over the same period, stipulations involving OPC have accounted for only 7.3% by number, and only 0.7% by value, of the company request cases where stipulations were predicted to be less likely. Among the 58

<sup>37</sup> Gulf Power Company, Docket No. 930139-EI, Order No. 93-0771, Discussion of issues, Agenda 4 May 1993. This case combined two types of minor case: an ROE review and an assessment of a tax change. The ROE review followed the company's filed intention to seek a rate increase, and the stipulation embodied an ROE reduction that avoided a potential rate increase.

## Rate increases & decreases by 5 year periods

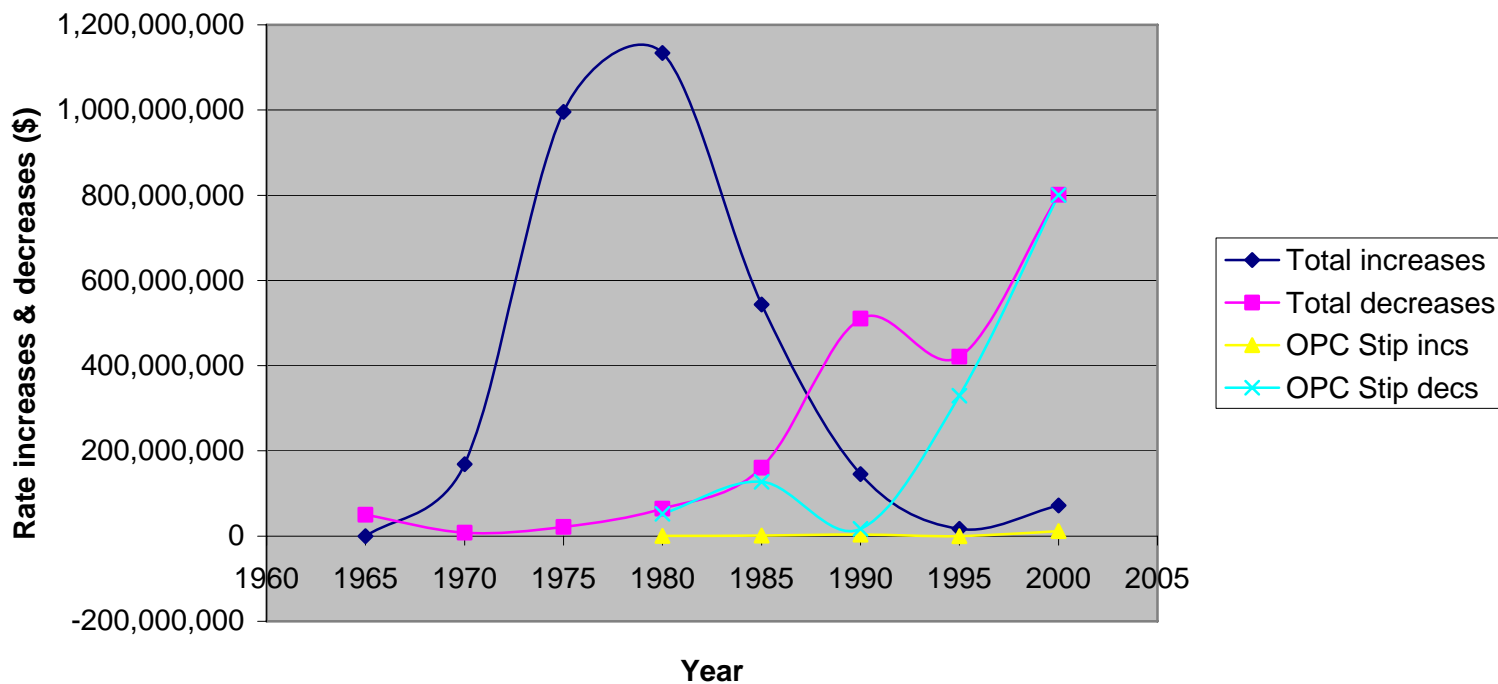


Figure 1 Revenue decisions at Florida PSC

minor cases where stipulations were predicted to be unlikely, OPC signed only one stipulation, which led to the withdrawal of a notified intention to file for a rate increase.

Figure 1 shows graphically the extent of rate increases and decreases over time. With the exception of the large case around 1990, a very high proportion of rate decreases is accounted for by OPC stipulations.

### 11. Stipulations involving PSC Staff only

During the period 1976 to late 1986 participants assumed that FPC staff agreement was necessary for any stipulation. Consequently staff co-signed all the OPC stipulations. In contrast, staff signed none of the OPC stipulations over the later period 1987 to 2002.

Staff signed five stipulations without OPC, three before 1986 and two shortly afterwards. Four of these are relatively straightforward. They involve gas companies, a sector in which the OPC was not particularly active, and/or relatively small amounts of revenue.<sup>38</sup> These stipulations are consistent with staff's presumed wish to minimise the time and cost of formal proceedings. The cases were evidently not sufficiently significant to attract OPC, or at least it felt that it could not make a useful impact there.

The remaining staff stipulation (General Telephone, 1987) approved a \$15.6m reduction in access charges, a \$1.5m reduction in zone charges, and a \$0.9m rate base reduction, all derived from tax savings. This is the most interesting stipulation of the five: given the

<sup>38</sup> The amounts involved were \$52,000 reduction (Indiantown Telephone Co, 1979), \$218,000 increase (South Florida Gas, 1983), \$3.8m increase (City Gas, 1984) and \$139,000 reduction (St Joe Gas, 1988).

size of rate reductions involved, why did OPC not sign as well? Perhaps OPC considered that tax reductions were not generally appropriate vehicles for a stipulation because they offered little scope for adding value, as discussed above. Also, the amount involved was still relatively small at a time when OPC was involved in larger reductions via earnings reviews. In addition, OPC may not have been attracted by staff's preferred use of the bulk of the tax savings to reduce access charges rather than to make general rate reductions (discussed below).

If stipulations signed by staff were useful in economising on the time and cost of hearings and litigation, have the benefits of this been lost since 1987? It seems not. Staff developed two alternative methods of avoiding unnecessary hearings when no other party is involved. In one method staff reach agreement with the company on how to resolve the earnings situation. The company then submits a written proposal that staff recommends to the PSC. In the other method, staff take a written position on all the issues. If the company agrees with staff this leaves no issues to be resolved in a hearing, and the PSC usually approves a document that has all the positions listed and agreed to. The latter method has been used for most of the gas utility rate increases.

## **12. Change over time? Earnings reviews**

FPSC decided in 1987 that it was no longer necessary or appropriate for its staff to co-sign stipulations. Is there any reason to believe that this would affect the extent or pattern of OPC stipulations, or any evidence that it did so?

It might be argued that having to get staff agreement would be a constraint on the OPC. Freed of this constraint, OPC would be able to sign more (or different) stipulations. It seems unlikely that staff would have had an interest in holding back stipulations supporting rate reductions that OPC might wish to sign, provided that these did not conflict with principles established in previous decisions. Possible areas of disagreement might be the structure of rates, the related question of how rate reductions should be applied, and the question of incentive mechanisms. These issues seem to have arisen mainly after the introduction of competition (in 1984 for telephones). They therefore seem unlikely to have caused staff to restrict OPC before 1987. Whether they would have done so after 1987 is another matter: it is certainly the case that staff objected to some of the later settlements signed by the OPC (Littlechild 2006).

It is nonetheless interesting to compare the number of OPC stipulations before and after 1987, particularly since some concern has been voiced about limitations on the OPC's funding (Common Cause Florida, n.d.). Of course, allowance has to be made for changes in other factors, such as the number and size of company requests and PSC earnings reviews. An interesting question is therefore whether the proportions of stipulations in each type of case remained about the same in the sub-period 1987-2002 as it had been in the sub-period 1976-1986, and what the outcomes of these stipulations were.

Table 7 gives details of the 93 PSC required rate reductions associated with earnings reviews, divided between the two successive sub-periods. In the first sub-period the

average frequency was 1.5 OPC stipulations per year, and in total stipulations covered 59.3% of these earnings review cases. The average amount involved in a stipulation was much greater than in non-OPC (litigated) cases: \$10.0m compared to \$0.6m. As a result, stipulations accounted for no less than 95.9% by value of these rate reductions in the first sub-period.

Table 7 Florida PSC Earnings review cases: pattern over time

	Number	Number	Whether	Total	As a	Average	Average
		per year	stipulation	required	proportion	required	value
	No.	No./yr	%	\$m	%	\$m	\$m/yr
1976-86							
OPC	16	1.5	59.3	160.1	95.9	10.0	14.6
Non-OPC	11	1.0	40.7	6.9	4.1	0.6	0.6
Total	27	2.5	100	167.0	100	6.2	15.2
1987-02							
OPC	13	0.8	19.7	1277.6	75.1	98.3	79.9
Non-OPC	53*	3.3	80.3	422.6*	24.9*	8.0*	26.4
Total	66	4.1	100	1700.2	100	25.8	106.3
Overall	93			1867.1			

\*If Southern Bell's 1988 case is excluded (see text), the total decrease and average decrease over the remaining 52 cases are \$132.4m and \$2.5m, respectively. On this basis, non-OPC (litigated) cases would account for only 9.4% of cases by value, and stipulations would account for 90.6%.

From the first to the second sub-period, the average frequency of earnings reviews increased from 2.5 to 4.2 per year, but the average frequency of OPC stipulations halved to 0.8 per year. As a result, OPC stipulations were only 19.7% of the total cases. The average rate reduction in each stipulation increased nearly ten-fold (from \$10.0m to \$98.3m), but the average size of litigated rate reductions increased by just over tenfold (from \$0.6m to \$8.0m). Nevertheless, because the average rate reduction in a stipulation was so much greater than in litigated cases, stipulations in the second sub-period still accounted for 75.1% by value of all rate reductions from earnings review cases.

The total value for the litigated cases in the second sub-period is crucially dependent on one single case.<sup>39</sup> OPC and the company sought to agree a stipulation but failed. The subsequently required rate reduction was \$227m on an ongoing basis plus \$249.4m one-time reduction (an effective total reduction of over \$290m using the weighting system in this study). This was quite exceptional in terms of size since the average non-stipulated

<sup>39</sup> Southern Bell, Docket No. 880069-TL, 1988.

rate reduction apart from this was only \$2.5m. It was by some margin the largest reduction ever ordered until that date, and since then was exceeded only once some eleven years later. Excluding this exceptional case, the average litigated rate reduction increased only fourfold from the first period, which is less than half the ten-fold rate at which the average value of OPC stipulations increased. And apart from this case, OPC stipulations would have accounted for 90.6% of rate reductions by value in the second period, which is only a little less than the proportion in the first period.

There is thus some evidence that OPC engaged in fewer stipulations in the second sub-period, and the proportion of earnings reviews settled by stipulation fell by two-thirds (from 59.3% to 19.7%). However, in terms of value the proportion accounted for by stipulation fell by only a fifth (from 95.9% to 75.1%). If the Southern Bell case is excluded, where OPC actively sought a stipulation, the proportion fell by only a fraction (from 95.9 to 90.6%). Moreover, the average value of each OPC stipulation increased by nearly ten-fold, and the average value of revenue reductions subject to stipulation each year increased four-fold.

Thus, although OPC signed fewer stipulations in the second sub-period, it seems to have concentrated just as successfully on the higher value ones as it did in the first sub-period. OPC was associated with over \$1.4bn of rate reductions from 1976 to 2002, and all but \$200m of that (15%) was achieved in the last 16 years. OPC's time and resources involved in stipulations were probably greater in the second sub-period rather than smaller. Whether it could usefully have deployed additional resources is unclear, but reportedly there was no obstacle to the provision of additional funds.

### **13. Change over time? Company requests**

The above discussion has focused on OPC stipulations with respect to earnings review type cases. It is worth looking briefly at possible changes over time in OPC stipulations on the 82 company requests for rate increases, even though the number of OPC stipulations in such cases was generally low during the period as a whole.

Table 8 shows that the underlying conditions were evidently quite different in one period compared to the other. The average frequency of requested rate increases fell from 4.9 to 1.8 per year, and the average size of each request fell from \$75m to \$21m.

OPC signed stipulations for the same low proportion of company requests (about 7%) in both periods. At first sight OPC policy did seem to change in other respects. The average size of the two requests for which stipulations were signed in the second sub-period was ten times the average size of the four stipulations in the first sub-period, even though the average size of all requests had fallen by two-thirds. In addition, the average proportion of the original request that the stipulations allowed increased from 23.8% in the first sub-period to 38.2% in the second, while for the other requests the average proportion allowed decreased from 53.9% to 40.0%. Was the OPC becoming more relaxed about agreeing rate increases?

Table 8 Requests for rate increases at Florida PSC : change over time

	Company requests			Requested			Allowed				
				Total	Average		Total	Average			
	No.	No/yr	%	\$m	\$m	\$m/yr	\$m	%	\$m	%	\$m/yr
1976-86											
OPC	4	0.4	7.4	8.2	2.1	0.7	2.0	0.1	0.5	23.8	0.2
Non-OPC	50	4.5	92.6	4042.8	80.9	367.5	2177.1	99.9	43.5	53.9	197.9
Total	54	4.9	100	4051.0	75.0	368.3	2179.0	100	40.4	53.8	198.1
1987-02											
OPC	2	0.1	7.1	40.6	20.3	2.5	15.5	6.6	7.8	38.2	1.0
Non-OPC	26	1.6	92.9	547.5	21.1	34.2	218.9	93.4	8.4	40.0	13.7
Total	28	1.8	100	588.1	21.0	36.8	234.4	100	8.4	39.9	14.7
Overall	82			4639			2413				

Such a conclusion would be premature. The numbers of stipulations are very small and both the stipulations in the second sub-period were unusual. One was presented as a rate reduction instead of an increase.<sup>40</sup> The other was agreed by intervenors at the last minute and OPC signed rather than appear to object.<sup>41</sup> It is therefore difficult to detect a change in OPC policy or activity over time.

#### 14. Hypothecated rate reductions

Of the 93 earnings review cases from 1976 to 2002, 65 cases led to across-the-board rate reductions or to reductions in the rate base that would lead to general rate reductions in future. In contrast, the other 28 cases involved reductions of particular rates, such as access charges and “Touchtone” charges in telephone cases. In some electricity cases the funds were earmarked for particular uses such as storm damage accrual and

<sup>40</sup> Centel docket 920310-TL order 93-0005 on 4 January 1993. The stipulation agreed an increase of \$3,485,000, but this was lower than the interim increase of \$4,591,194 l already agreed by FPSC on 11 September 1992. OPC could therefore present the stipulation as a rate reduction, and did so. Why the company agreed to this is discussed in Littlechild (2006).

<sup>41</sup> Peoples Gas System, docket 020384-GU, order PSC-03-0038-FOF-GU issued January 6, 2003, with reference to stipulation approved on 13 December 2002. (This is the last docket and stipulation in the database.) This stipulation allowed 53.3% of the requested amount, which was much above the 23.8% average for the three OPC stipulations in the first sub-period and the 19.4% proportion for the other stipulation in the second sub-period. Two other parties (Florida Industrial Gas Users and Auburndale Power Partners) were also involved as intervenors, and settled with the company at the last minute before entering court. (It is said that the stipulation was “handwritten on the table”. The formal record says that the settlement was approved at the hearing.) The OPC, which had been involved in the discussions and was hitherto not persuaded, was invited to join the stipulation and agreed to do so.

environmental clean-up costs. Is there reason to believe that OPC would prefer to sign one kind of stipulation or the other? That is, does it have a preference as between across-the-board and hypothecated rate reductions?

OPC’s statutory duty gives no indication of preference as to types of customers or services. My understanding is that OPC has been concerned as far as possible to protect all customer groups. It does not wish to advance the interests of particular groups of customers against others, or to get involved in issues of sharing costs and benefits between customer groups or types of services.<sup>42</sup> In addition, some hypothecations of revenues (an allocation to storm damage reserve, for example) would not lead to rate reductions and therefore might not be seen or appreciated by customers. There was also some fear by customers that a reduction in access charges paid by long-distance telephone companies (generally based out of state) to access the local networks might not be passed through to customers.<sup>43</sup> All this suggests that OPC would be more interested in stipulations with across-the-board rate reductions than those with hypothecated rate reductions.

Table 9 shows that of the 29 stipulations that OPC signed, only 4 had provisions on the nature of rate reductions, whereas of the 64 cases where it did not sign, 24 had such provisions. OPC stipulations covered 14.3% (=4/28) of the cases involving what we might call hypothecated reductions, which accounted for 54.4% (= \$371.4/\$683.0) by value of these cases. In contrast, OPC stipulations covered 38.5% (=25/65) of the cases not involving hypothecated reductions, accounting for 87.1% (= \$1066.3/\$1224.6) by value.

Table 9 PSC Earnings Review cases 1976-2002: provisions on rate reductions

	Hypothecated		Across the board		Total	
	Number	\$m	Number	\$m	Number	\$m
OPC stipulation	4	371.4	25	1066.3	29	1437.7
No OPC stipulation	24	311.6	40	117.8	64	429.4
Total	28	683.0	65	1224.6	93	1867.1

This evidence is consistent with the conjecture, but several qualifications should be made. First, there may be a relationship between size of rate reduction and whether it is

<sup>42</sup> In 2002 the South Florida Hospital and Health Care Association (SFHHA) appealed against a settlement agreed by OPC and FPL and endorsed by the PSC. OPC noted that “The Public Counsel cannot play favourites because it represents all customers, including the SFHHA.” OPC opposed the action on the basis that it might void the agreement or take the share of some other customer groups. *OPC Activity Report* p. 8.

<sup>43</sup> Rate structure issues became more important with the break-up of ATT on 1 January 1984. As competition developed across the networks, FPSC staff considered it important to reduce access charges in order to align network charges with costs. At the time, intra-state access charges regulated by FPSC were considerably higher than interstate access charges regulated by FCC.



hypothecated, so that the additional effect of hypothecation might be less than appears from the table. Second, the rate reductions that involve hypothecation do so to different extents, ranging from 15% to 100%. Third, other factors such as type of sector might be relevant. A simple regression analysis suggests that, after allowing for other factors, a hypothecated rate reduction is less likely to be subject to an OPC stipulation but not significantly so.<sup>44</sup> More research is therefore needed here.

## 15. Conclusions

In US utility regulation, relatively little seems to be known about the practice of settlement rather than litigation and about the activities of consumer advocates. This paper presents evidence from Florida during 1976-2002. In this period, over 30 per cent of earnings reviews were settled by stipulation involving the Office of Public Counsel but only 5 per cent of other cases. Over three quarters of the rate reductions associated with the earnings reviews derived from these stipulations. In the sub-period 1976-86 the proportion was over 95 per cent. The average value of a rate reduction was seven times higher with a stipulation than without. Only 1 per cent of the rate increases associated with company requests derived from these stipulations. On average a stipulation provided for a lower proportion of the requested rate increase than a litigated outcome allowed (about one third compared to one half).

This evidence suggests that settlements were an extremely important aspect of utility regulation in Florida during the last quarter century, that these settlements were particularly associated with rate reductions, and that the Public Counsel was instrumental in achieving them. The content of these stipulations, and how far the outcome was different from what a litigated outcome would have been, are important questions dealt with elsewhere. (Littlechild 2003, 2006) Questions for future research include whether the OPC's policy and record on stipulations have continued since the retirement of the person who held the office of Public Counsel during this whole 25 year period, and how far experience in Florida has been mirrored elsewhere in the US and Canada. More thorough econometric and/or game theory analysis would seem to be worthwhile, taking account of the causes and effects of OPC involvement and perhaps modelling the process as a two-stage regression or game.<sup>45</sup>

Even at this stage, however, it seems that settlements between utilities and consumer representatives are a feasible alternative or complement to traditional regulation, both within and beyond North America. Whether they are simply a quicker and more certain method of resolving regulatory issues, whether they typically achieve something that the regulator cannot offer or does not wish to offer, whether the traditional US regulatory system is unduly costly and inflexible, are important questions to resolve. In any event settlements have frequently been voluntarily chosen by market participants in preference to traditional regulation, and are therefore perceived to be beneficial to the parties

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<sup>44</sup> A regression analysis of these 93 cases suggests that 1) size of rate reduction is a very significant and positive determinant of whether a stipulation is signed, 2) a stipulation is significantly less likely after 1986, and 3) a stipulation is not more or less likely in the electricity or gas sectors than in telephones.

<sup>45</sup> E.g. Roberts et al (1978).

involved. Settlements deserve more active consideration by economists and policymakers than they have hitherto received. Outside of North America, the possibility of distinguishing more clearly between the roles of consumer advocate and regulatory adjudicator deserves consideration.

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