WIGGINS & VILLACORTA, P.A.
ATTORNEYS AT LAW
POST OFFICE DRAWER 1657
TALLAHASSEE, FLORIDA 32302
2145 DELTA BOULEVARD, SUITE 200
TALLAHASSEE, FLORIDA 32303
TELEPHONE (850) 385-6007
FACSIMILE (850) 385-6008
INTERNET: wiggvill@nettally.com

July 14, 1999

VIA HAND DELIVERY

Ms. Debbie Causseaux, Clerk
Supreme Court of Florida
Supreme Court Building
500 South Duval Street
Tallahassee, Florida 32399-1925

970808-TL

Re: Case No. 94,656 - GTC, Inc. v. Joe Garcia, etc., et al.

Dear Ms. Causseaux:

Enclosed for filing in the above referenced case are the original and seven (7) copies of GTC, Inc.'s Initial Brief and Request for Oral Argument.

Thank you for your assistance in this matter.

Sincerely,

Susan Davis Morley

SDM:plk
Enclosures
cc: Parties of Record

AFA
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DOCUMENT NO.
08358-99
July 14

IN THE SUPREME COURT OF FLORIDA

GTC, INC.,	)	
	)	
Appellant,	)	
	)	
v.	)	Case No. 94,656
	)	
JOE GARCIA, ETC., ET AL.,	)	
	)	
Appellee.	)	
	)	

REQUEST FOR ORAL ARGUMENT

Pursuant to Florida Rule of Appellate Procedure 9.320, Appellant GTC, Inc. respectfully requests oral argument in this proceeding.

Respectfully submitted this 14th day of July, 1999.

WIGGINS & VILLACORTA, P.A.

Patrick Knight Wiggins (FBN 212954)
Susan Davis Morley (FBN 612006)
2145 Delta Blvd., Suite 200
Post Office Drawer 1657
Tallahassee, FL 32302
(850) 385-6007

Attorneys for GTC, Inc.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and accurate copy of the foregoing was furnished by hand or overnight delivery to the following this 14th day of July, 1999.

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Division of Records & Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Beth Keating
Division of Legal Services
Florida Public Service Commission
Division of Legal Services
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Charles J. Beck
Deputy Public Counsel
Office of Public Counsel
c/o The Florida Legislature
111 W. Madison Street, Ste. 812
Tallahassee, FL 32399-1400

Tracy Hatch, Esquire
AT&T Communications of the
Southern States, Inc.
Suite 700
101 North Monroe Street
Tallahassee, FL 32301

Chris Moore
Division of Appeals
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Mark R. Ellmer
GTC, Inc.
502 Fifth Street
Suite 400
Port St. Joe, FL 32456

Nancy B. White, Esquire
c/o Nancy H. Sims
BellSouth Telecommunications,
Inc.
150 S. Monroe Street, Ste. 400
Tallahassee, FL 32301-1556

John H. Vaughan
GTCOM
502 5th Street
Port St. Joe, FL 32456

Susan Davis Morley
Florida Bar Number 612006

Case No. 94,656

IN THE SUPREME COURT OF FLORIDA

GTC, INC.,

Appellant,

v.

JOE GARCIA, ETC., ET AL.

Appellee.

F.P.S.C. Docket No. 970808-TL

INITIAL BRIEF OF GTC, INC.

WIGGINS & VILLACORTA, P.A.

Patrick Knight Wiggins
Susan Davis Morley
2145 Delta Blvd., Suite 200
Post Office Drawer 1657
Tallahassee, FL 32302
(850) 385-6007

Attorneys for GTC, Inc.

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FLORIDA PUBLIC SERVICE COMMISSION

JURISDICTION

This Court's jurisdiction over this appeal is mandated by Article V, Section 3(b)(2), Florida Constitution, and Section 364.381, Florida Statutes (1998).

STATEMENT OF THE CASE AND FACTS

GTC, Inc. (d/b/a GTCom, Inc., and formerly St. Joseph Telephone and Telegraph Company "GTC") is a small incumbent local exchange carrier located in Port St. Joe, Florida. In the early 1980's, at the onset of long distance competition, the Florida Public Service Commission ("Commission") established a system of uniform access charges for calls between Florida local access transport areas (LATAs). See Modified Final Judgment, U.S. v. AT&T, 552 F. Supp. 131 (D.D.C. 1982); In re: Intrastate telephone access charges for toll use of local exchange services, 83 F.P.S.C. 12:100 (1983). The Commission's original access charge plan required interexchange carriers ("IXCs") to compensate local exchange carriers ("LECs") such as GTC for interLATA calls originating or terminating over the LEC facilities, and required carriers collecting these charges to pool the resulting revenues. However, in 1985, the Commission terminated the pooling arrangement in favor of a "bill and keep" system for collection of access charges. See In re Intrastate access charges for toll use of local access charges, 85 F.P.S.C. 6:69 (1985). Under the bill and keep system, each local exchange carrier would keep the revenue it received for use of its local facilities. Because the Commission had established uniform access charges across the state, and costs and volumes of traffic within each LATA varied, the new system favored some carriers over others. The interLATA subsidy ensured that all LECs would be compensated for use of their facilities without changes in local rates. As a result, GTC currently receives an annual interLATA subsidy of $1,223,000, (Tr. Ex. 2), which is collected by BellSouth Telecommunications, Inc. ("BellSouth") from IXC long distance carriers as access charge revenues and remitted to GTC. (Tr. 99, 120, 123-24).

In 1995, the Florida Legislature passed Chapter 95-403, Laws of Florida ("the Act"), which substantially altered the existing regulation of incumbent local exchange carriers such as GTC. The

Act included new price cap statutes, which offered small local exchange carriers the option of discontinuing traditional rate regulation of their operations, in exchange for an agreement to freeze their basic local rates for a period of several years. On June 25, 1996, GTC notified the Commission of its decision to operate as a price cap regulated local exchange company pursuant to Section 364.051(1)(b), Florida Statutes, and its rates for basic local exchange services were frozen at that time. (BellSouth Revised Pet., R.7, at 3.) BellSouth later notified GTC that it intended to discontinue payment of the interLATA subsidy due to GTC's price cap election. When GTC responded that the subsidy could not be terminated in this manner, BellSouth filed its July 1, 1997 petition asking the Commission to remove the subsidy. (R. 1, 7). A hearing was held on May 20, 1998 before the full Commission, and on August 28, 1998, the Commission issued Order No. PSC-98-1169-FOF-TL ("Order"), terminating the subsidy and directing BellSouth to institute specified rate reductions. That Order is the subject of GTC's Appeal.

SUMMARY OF THE ARGUMENT

The Commission's Order terminating the interLATA subsidy and requiring a rate reduction by BellSouth violates the new regulatory bargain established by the Florida Legislature in 1995. Through its 1995 price cap statutes, the Legislature intended local exchange carriers opting for price cap regulation to be free from further rate of return regulation, in exchange for the LECs' agreement to freeze their basic local rates and to open their service areas to competition by other carriers. Central to this bargain is the premise that while future revenues may be gained or lost at each LEC's peril, each begins the new competitive regulatory bargain with fixed rates and revenues specifically identified by the Legislature in the price cap statutes. For small LECs such as GTC who elected price cap regulation prior to July 1, 1996, this means that basic local rates frozen at that time are presumed to be fair and reasonable, and not subject to subsequent earnings review or reduction.

Nothing in the price cap statutes suggests that the Legislature intended to limit only the LEC's ability to raise rates, but to permit the Commission continued discretion to eliminate underlying revenues as it may see fit. Rather, the Act establishes a starting line for competition in the provision of basic local exchange services, which may not be altered by the Florida Commission. Nevertheless, the Commission has declared in this case its belief that it is appropriate to terminate subsidy revenues to companies electing price cap regulation, as a result of that election.

It is true that the Florida Statutes regulating local exchange telephone companies now include two fundamentally incompatible regulatory schemes. Under the old rate of return scheme, LECs receiving the interLATA subsidy at issue in this case were subject to periodic earnings review, and the subsidy was gradually reduced or eliminated as overearnings occurred. Each decision to reduce or eliminate the subsidy was grounded in the principle of revenue neutrality, preventing an

unconstitutional taking of the LECs' property. However, the 1995 price cap regulation statutes preclude continued application of an earnings analysis to price cap regulated companies such as GTC, so that there is no basis for elimination of the interLATA subsidy.

Faced with the inability to apply its pre-Act test for termination of the subsidy, the Commission declared that GTC's price cap election created a "changed circumstance" justifying the elimination of $1,223,000 of GTC's revenues. The Commission then suggested that GTC may initiate a hearing to regain these revenues, but in an evidentiary proceeding which may well prove similar to a rate case. Finally, the Commission applied the old principle of revenue neutrality to BellSouth, also a price cap regulated LEC, directing BellSouth to reduce its rates to offset the termination of its obligation to remit the interLATA subsidy amount to GTC.

Perhaps as an institution the Commission is simply geared toward an averaging process where the amorphous public interest standard is satisfied by averaging extremes. And in many situations, blending is a lot like moderation and passes for wisdom. But two distinct statutory schemes cannot be blended to create a new statutory scheme as the Commission has done in this case. The Commission's order exceeds the scope of its authority under Chapter 364, and must be reversed.

ARGUMENT

I. THE 1995 FLORIDA TELECOMMUNICATIONS ACT CREATES A NEW REGULATORY BARGAIN BETWEEN GTC AND THE STATE OF FLORIDA, UNDER WHICH THE FLORIDA PUBLIC SERVICE COMMISSION HAS NO STATUTORY AUTHORITY TO DISCONTINUE THE INTERLATA SUBSIDY.

At issue in this case is the effect of the Florida Legislature's 1995 telecommunications legislation upon an interLATA subsidy which GTC has received since 1985. Prior to the 1995 legislation, when the interLATA subsidy was established, GTC was operating under a rate regulation scheme in which the company was required

- to operate as a common carrier within its territory,
- to provide nondiscriminatory service among customers and locations,
- to establish universal service, and
- to price its services only as authorized by the Public Service Commission.

See generally Sections 364.03-364.05, Fla. Stat. (1994) and related sections. In exchange, the company was afforded an exclusive right to serve its territory, and an opportunity to earn a fair rate of return on its investments used and useful in the provision of telecommunications service. See, e.g., Permian Basin Area Rate Cases, 390 U.S. 747, 792 (1968), cited in United Tel. Co. of Fla. v. Mann, 403 So.2d 962 (Fla. 1981), Keystone Water Company, Inc. v. Bevis, 278 So.2d 606, 609 (Fla. 1973), Gulf Power Company v. Bevis, 289 So.2d 401 (Fla. 1974). As the Court is fully aware, under this scheme if a utility was underearning because the authorized rates were inadequate, then the utility could seek rate increases through a rate case. Conversely, if the utility were overearning, the Commission could impose a rate reduction in a rate case. Absent overearning, the Commission typically could not force the company to lower a particular rate without providing for an offset to

assure revenue neutrality, to ensure that the company's property was not taken without due process of law. Id. The principle of revenue neutrality was honored in non-rate case adjustments to a company's rates, so that the fundamental regulatory bargain was not breached by the State.

With the 1995 Act and its price cap statutes, Sections 364.051 and 364.052, Florida Statutes, the Legislature has established a new regulatory bargain. Under the new bargain, as a price cap regulated local exchange company, GTC has agreed to freeze its basic local rates for a period of three to five years,[1] and to limit price increases thereafter to the rate of inflation less one percent. See Section 364.051(4), Fla. Stat. (1995). In exchange for this rate guarantee, GTC is relieved from rate base, rate of return regulation and the related requirements of Sections 364.03, 364.035, 364.037, 364.05, 364.055, 364.14, 364.17 and 364.18, Florida Statutes.[2] GTC is no longer protected from competition in its service area, and is not guaranteed a rate correction to offset changing market conditions or its own managerial decisions. But the Company is now free to make its investment and operational decisions based on the emerging market, not regulatory accounting principles, and it is free to reap any resulting profits without an overearning correction and "success tax" by the Commission.

Comparing the two regulatory bargains, under the traditional approach, business risk effectively was placed on the ratepayers because of the guaranteed opportunity for the utility to earn

[1] In 1998, the Legislature amended its original price cap statute, extending the initial freeze period by one year. See Section 364.051(2)(a), Fla. Stat. (1998).

[2] These statutes address topics including: reasonableness of rates, performance of service, and maintenance of telecommunications facilities (§ 364.03); rate fixing and criteria service complaints (§ 364.035); telephone directory advertising revenues (§364.037); changing rates, tolls, rentals, contacts or charges (§ 364.05); rentals, contacts or charges (§ 364.05); interim rates and procedure (§ 364.055); readjustment of rates, charges, tolls or rentals and orders or rules requiring facilities to be installed (§ 364.14); forms of reports, accounts, records and memoranda (§ 364.17) and access to company records (§ 364.18).

a fair rate of return. This guarantee was the shareholder's fundamental protection, while the ratepayers were protected through continued Commission surveillance of the utility's operations. Under the new bargain, the business risk moves to the shareholder, and the ratepayer is protected by frozen rates. There is no guarantee of future earnings to protect the shareholder; rather, it must find its protection in the acumen of its business decisions. However, one essential element of the bargain serves as a guarantee to the shareholder – the guarantee of statutory entitlement to the revenue the utility was receiving at the time it elected price cap regulation.

Nothing in the new price cap statutes suggests that the Legislature considered the loss of subsidies in place at the time of price cap election to be a cost of the new regulatory bargain. Nevertheless, the Commission has concluded that a small LEC's election of price cap regulation under the Act triggers termination of the interLATA subsidy. Now that GTC has frozen its basic local rates, the Commission has ordered that an annual interLATA subsidy of $1,223,000 which GTC has relied upon in setting those frozen rates should be discontinued.

Because the subsidy was a part of the revenues received by GTC at the time of its price cap election, GTC is statutorily entitled to the continued receipt of the subsidy amount. These revenues served as the agreed upon starting line for the Company's decision to enter the competitive race, and the statute guarantees that once the race has begun, the starting line will not be changed. Or perhaps more apt, once GTC agreed to enter the race based on the amount of fuel in its tank, the Commission may not siphon off a portion of the tank just as competitors are preparing to shift into high gear. The Commission's reduction of GTC's "starting line" revenues through termination of the interLATA subsidy violates the new regulatory bargain created by the new price cap statutes, and should be reversed.

II. THE LEGISLATURE HAS DELEGATED TO THE COMMISSION THE AUTHORITY TO IMPLEMENT EITHER ONE OF TWO DISTINCT REGULATORY SCHEMES BASED ON THE ELECTION OF THE LEC; HOWEVER, THE LEGISLATURE DID NOT AND COULD NOT DELEGATE TO THE COMMISSION THE AUTHORITY TO BLUR THE DISTINCTIONS BETWEEN THESE SCHEMES THROUGH THE FICTION OF "CHANGED CIRCUMSTANCES."

As a result of the 1995 Act, there now exist in Chapter 364, Florida Statutes, two fundamentally incompatible schemes for the economic regulation of local exchange telephone companies. Rate regulated companies who do not elect price cap regulation would be subject to Commission review of the entire scope and depth of their operations, to ensure that certain policy objectives such as universal and non-discriminatory service are achieved, while insuring the companies an opportunity to earn a fair rate of return. Any failure to afford that opportunity would amount to an unconstitutional taking of the companies' property. Thus, when revenue streams to these companies are terminated outside a rate case, typically an offset is provided to assure "revenue neutrality" of the regulatory action. In this context, "revenue neutrality" is an overarching principle in earnings regulation.

The new regulatory bargain, however, abandons earnings review in favor of capping prices. There is nothing subtle or complex about this scheme. Neither the utility nor the Commission may tinker with basic local rates without some extraordinary justification, and the Commission may not take a regulatory action that deprives the utility of revenues to which the utility is entitled absent some extraordinary justification. Because the utility's "starting line" revenues are not subject to being diminished by the stroke of the Commission's pen, the fact that the utility's rates are frozen does not trigger the problem of unconstitutional taking of property. In other words, because the

Commission may not take the first action, there is no need to allow for an opposite and equal reaction, as contemplated under the principle of revenue neutrality.

The interLATA subsidy at issue in this case was originally created under the old rate regulation scheme, in an effort to maintain a revenue neutral "wash" when bill and keep was implemented. Order 14452, 85 F.P.S.C. 6 at 79-82. Consistent with this approach, and prior to the enactment of the price cap regulation statute, the Commission reduced or terminated each of the interLATA subsidies paid to local exchange carriers on a case by case basis, when it was determined that those companies were overearning. (Order at 6; Tr. Ex. 1). By the same token, in each case where a subsidy payment was terminated to a LEC, the payor of the subsidy was required to reduce a rate or set aside a corresponding amount. As a result, the elimination of the subsidy was a revenue neutral event.[3]

In the instant case, however, the Commission made no finding that GTC was overearning—and could not do so. The 1995 Act prohibits application of an overearnings test to price cap regulated companies on a going forward basis. In addition, because of the short period between the effective date of the Act and the applicable price cap deadline, the earnings of companies electing price cap regulation prior to the July 1, 1996 are considered just and reasonable, and not subject to a "final" overearnings review as part of the price cap election.[4] Accordingly, GTC did not provide

[3] As the Commission staff's Witness Mailhot observed, access charges began to vary between companies by late 1988, and have continued to vary since that time. (Tr. at 120.) The Commission could have adjusted each company's access charges to eliminate the subsidy system in a generic proceeding, once access charges became non-uniform. However, the Commission chose instead to gradually eliminate each company's subsidy by reviewing earnings on a case by case basis. (Tr. at 120.) As the Commission observed in its order, "**this policy was designed to keep all the subsidy participants revenue neutral.**" (Order at 6, emphasis added).

[4] Although the rates of companies electing price cap regulation **after** July 1, 1996 are subject to a final overearnings analysis, GTC filed its price cap notice on June 25, 1996. See § 364.052(2), Fla. Stat. and BellSouth Revised Petition at 3. Accordingly, GTC's rates as of July 1, 1996 are not subject to an after-the-fact overearnings

earnings data for review below, and no specific data in the record below address GTC's current earning situation.

Even if the Commission simply intended to apply the traditional principle of revenue neutrality in this proceeding, without an earnings analysis, its end result is internally inconsistent. The Commission was careful to direct BellSouth to reduce its rates in an amount which would offset the discontinued subsidy, (Order at 16-17), suggesting through this ruling that the revenue neutrality requirement continues to be applicable to BellSouth, a price cap regulated LEC. However, the Order completely disregards the impact of the lost revenue upon GTC's rates and revenues, which were presumed to constitute a fair rate of return at the point of price cap election.

The Commission staff's own witness apparently recognized this problem, suggesting that since BellSouth is receiving the access charge revenue essentially on behalf of GTC, the Commission could offset termination of subsidy by allowing GTC to collect the funds directly through access charges. (Mailhot, Tr. at 126.) This would keep the parties in the position they are in today, effecting a revenue neutral solution. (Mailhot, Tr. at 129.) Nevertheless, the Commission rejected this proposal.[5]

Instead, faced with a situation in which the new statute prohibited previous methods of analysis, the Commission adopted a new standard for termination of GTC's interLATA subsidy. Relying upon the fact that all parties understood the "temporary" nature of the subsidy, the

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analysis for purposes of the 1995 Act .

[5] In its Order, the Commission expressed concern that the access charge adjustment suggested by GTC and the Commission staff's witness appeared to be contrary to Section 364.163, Florida Statutes, which caps each LEC's intrastate access rates. (Order at 13.) However, as stated by Witness Mailhot, the proposed adjustment would not result in a real increase in access charge revenues for GTC, just a change in the party collecting those charges. (Tr. at 126-127.)

Commission stated that the access subsidy was to last

> only until a company experienced some change in circumstances that we found justified terminating the subsidy. We believe that it is appropriate for **changed circumstances** to continue to be the criterion for determining if the subsidy should be eliminated.
>
> Order at 6 (emphasis added).

As discussed above, prior to this proceeding, the only "changed circumstance" warranting termination of the interLATA subsidy was overearning. However, the Commission went on to conclude that because GTC had "demonstrated a desire to take on the opportunities of the competitive arena by electing price regulation," (Order at 12) and frozen its rates, the Company's revenues should be reduced by $1,223,000. Under this analysis, GTC's own commitment to cap its basic local rates is the "changed circumstance " triggering confiscation of revenues underlying those frozen rates. This test finds absolutely no support in the 1995 Act.

The Commission suggests in its order that "[i]f GTC believes that termination of the subsidy payment to GTC amounts to a changed circumstance that justifies a rate increase, GTC may seek relief pursuant to Section 364.051(5), Florida Statutes." (Order at 12.) That section permits price cap regulated LECs who believe circumstances have changed substantially, justifying an increase in their frozen rates for basic local service, to petition the Commission for a rate increase; however, the Commission is directed to grant such a petition "only after an opportunity for hearing and a compelling showing of changed circumstances." Section 364.051(5), Fla. Stat. (1995). Requiring a price cap regulated company to engage in a special hearing in order to regain revenues identified by the Legislature as the starting point for price regulation clearly violates the intent of the Act. The hearing proposal alluded to by the Commission merely shifts the burden to GTC to

compensate for the Commission's unlawful act.

As a practical matter, if the hearing simply involved (1) a finding as a matter of law that the removal of the interLATA subsidy by the Commission constitutes a "changed circumstance" for purposes of Sections 364.051(5), and (2) an order granting GTC authority to raise rates for basic local service to offset the amount of the lost subsidy, then perhaps GTC would be willing to pursue this option, to obviate the need for this appeal. Unfortunately, because no "changed circumstances" proceeding has been initiated under the new price cap statute, no one knows what the standard or scope of proceeding will be.

In an effort to answer this question, GTC filed a Petition for Declaratory Statement with the Commission on March 11, 1999. See In re: Petition for Declaratory Statement by GTC, Inc. d/b/a GTCom regarding Section 364.051, F.S., F.P.S.C. Order No. PSC-99-1194-FOF-TL (June 9, 1999). Through its petition, GTC sought a declaration that:

- the removal of the interLATA subsidy effected by the Final Order constitutes grounds under Section 364.051(5), Florida Statutes, for the Commission to grant GTC authority to raise rates for basic local service;

- in determining whether to grant authority to raise rates for basic local service the Commission may not inquire beyond the narrow issues of (1) the amount of the subsidy eliminated and (2) the adjustments to basic local rates necessary to generate the subsidy amount; and

- In determining whether to grant authority to raise rates for basic local service, no party to the proceeding may seek discovery from GTC beyond (1) the amount of subsidy eliminated and (2) the adjustments to basic local rates needed to generate the subsidy amount.

Order No. PSC-99-1194-FOF-TL at 2.

The Commission refused to issue a declaratory statement clarifying these points.

It its response opposing GTC's petition, the Office of the Public Counsel clearly communicated its vision of a Section 364.051(5) hearing in which

> all of the circumstances affecting a company, **including evidence that may offset the circumstances** presented by the company, should be considered. The OPC further asserts that any proceeding under the statute would be very fact dependent in order to determine if the circumstances were as compelling or as substantial as alleged by the company.
>
> Order No. PSC-99-1194-FOF-TL at 2 (emphasis added).

The Commission did not disagree. In its Order Denying Petition for Declaratory Statement, the Commission simply stated:

> We agree that an evidentiary proceeding is required to determine whether changed circumstances justify an increase in rates for basic local telecommunications services. We do not believe that a declaratory statement proceeding is the right kind of proceeding in which to determine whether the compelling showing required by Section 365.051(5), Florida Statutes, has been made. Declaring that we may not inquire beyond the narrow issues that GTC requests would be tantamount to finding that a compelling showing has been made without the opportunity for any party to challenge whether there is a change in circumstances.
>
> Id.

The Commission goes on to say that

> We believe that a Section 120.57(1) hearing is the proper proceeding in which to determine whether GTC's circumstances have changed substantially to justify a rate increase under Section 364.051(5). The scope of the issues and evidence to be considered and the scope of discovery should be determined in that proceeding, with the specific facts before us, and not by declaratory statement...The questions posed should be answered in the proceeding initiated by filing a petition under Section 364.051(5), Florida Statutes.
>
> Id.

Another proceeding is required. The Commission has declared GTC's price cap election a "changed circumstance" justifying the reduction of the Company's "starting line" revenues, but has

refused, without a Section 120.57(1) hearing, to conclude that this reduction in revenue creates a "compelling change in circumstances" permitting GTC to offset its loss. The amount of the subsidy does not appear to be in question, nor does the fact that this amount was part of GTC's revenues at the point of its price cap election. Nevertheless, the Commission has concluded that an evidentiary proceeding is required in order to determine whether the changed circumstance finding by the Commission justifies a corresponding increase in GTC's local rates. It is difficult to see what other evidence could be necessary or appropriate for consideration in such a proceeding, unless the Commission intends to undertake the OPC's proposed review of "all circumstances affecting a company, including evidence that may offset the circumstances presented by the company"—an approach which sounds remarkably similar to a traditional rate case, without the accompanying statutory standards.

The Commission's order in this case signals its intent to create a hybrid method of regulation combining two fundamentally incompatible regulatory schemes. Under the Commission's view, it can reduce the "starting line" revenues of price cap companies at will and require those companies to participate in what is potentially a de facto rate case to regain them. The Commission makes this position clear in the Order, stating that "[w]e agree with BellSouth's witness Lohman that it seems quite appropriate that we should remove a revenue support instituted when a company was under rate of return regulation once a company has become price regulated." (Order at 8-9.) In other words, when a company elects price cap regulation, any subsidy in place at that time affords the Commission delegated authority to modify the Legislature's price cap regulation scheme through rate regulation, in violation of the new regulatory bargain.

Under the Commission's analysis, if a company's revenues include money generated by a subsidy, the company will always be subject to the burden of earnings regulation with respect to those revenues, but none of the benefits. If this were the statutory scheme as enacted by the Legislature, it would be unconstitutional. There is, however, not one word to be found in Chapter 364 to even suggest such an approach. Moreover, no principle in any mature view of economic regulation supports a scheme in which a regulatory burden is placed on a company without any offset or corresponding regulatory benefit.

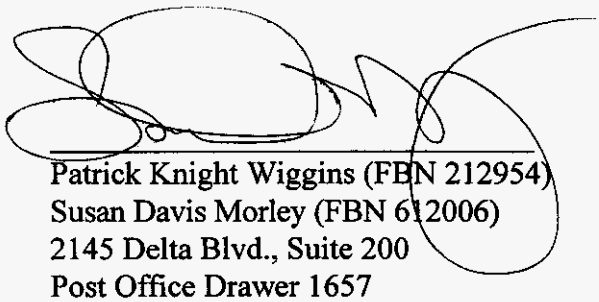
The Commission's job is to follow and implement the law, not to invent it. The Commission's decision below must be reversed.

CONCLUSION

For the reasons stated above, GTC respectfully requests that F.P.S.C. Order No. PSC 98-1169-FOF-TL, terminating GTC's interLATA subsidy, be reversed.

Respectfully submitted this 14th day of July, 1999.

WIGGINS & VILLACORTA, P.A.



Patrick Knight Wiggins (FBN 212954)
Susan Davis Morley (FBN 612006)
2145 Delta Blvd., Suite 200
Post Office Drawer 1657
Tallahassee, FL 32302
(850) 385-6007

Attorneys for GTC, Inc.

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Tallahassee, FL 32399-0850

Chris Moore
Division of Appeals
Florida Public Service Commission
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Beth Keating
Division of Legal Services
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Division of Legal Services
2540 Shumard Oak Boulevard
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Mark R. Ellmer
GTC, Inc.
502 Fifth Street
Suite 400
Port St. Joe, FL 32456

Charles J. Beck
Deputy Public Counsel
Office of Public Counsel
c/o The Florida Legislature
111 W. Madison Street, Ste. 812
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Suite 700
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Tallahassee, FL 32301

John H. Vaughan
GTCOM
502 5th Street
Port St. Joe, FL 32456

Susan Davis Morley
Florida Bar Number 612006