No. 477A20

SUPREME COURT OF NORTH CAROLINA

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STATE OF NORTH CAROLINA ex rel. UTILITIES COMMISSION, Appellee, v. VIRGINIA ELECTRIC AND POWER COMPANY D/B/A DOMINION ENERGY NORTH CAROLINA, Appellant, ATTORNEY GENERAL JOSHUA H. STEIN, Cross-Appellant.	From the North Carolina Utilities Commission Docket No. E-22, Sub 562

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REPLY BRIEF OF APPELLANT VIRGINIA ELECTRIC AND POWER COMPANY D/B/A DOMINION ENERGY NORTH CAROLINA

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INTRODUCTION

The North Carolina Utility Commission's (the "Commission") legislative function in ratemaking is no defense for an arbitrary, capricious, and unconstitutional Order. Dominion Energy North Carolina ("DENC") agrees with Appellees that the legal doctrines of *stare decisis* or *res judicata* do not bind the Commission's ratemaking authority. Rather, DENC argues that the principles of fairness, trust, and efficiency are already embedded in the statutory limits the North Carolina Legislature has placed on the Commission's discretion.

Those statutory limits require the Commission to give more than a cursory recitation of its existing ratemaking policy before diverging from and reversing that policy. The Commission must confront its prior decisions head-on and meaningfully explain its decision-making. It runs counter to the regulatory compact and the General Assembly's policy to "promote the inherent advantage of regulated public utilities" to allow the Commission, as it has done here, to abruptly change its policy, not explain said change, and then expect that the new policy sticks. *See* N.C.G.S. § 62-2(a)(2). This Court should reverse and modify the Commission's arbitrary and capricious DENC Order to make it

consistent with the basic ratemaking treatment for coal ash costs the Commission adhered to in the most recent three rate case orders issued before the DENC Order at issue here.

ARGUMENT

I. EXERCISING THE "LEGISLATIVE FUNCTION" DOES NOT GIVE THE COMMISSION A LICENSE TO ENGAGE IN "ARBITRARY AND CAPRICIOUS" RATEMAKING.

Had this case been the first time the Commission addressed recovery of coal ash costs that were incurred to comply with the federal Coal Combustion Residuals Rule ("CCR Rule"), Appellees' brief might raise some compelling arguments. But it was the fourth time. In its three prior coal ash decisions, the Commission adopted a basic ratemaking policy that provides for a five-year amortization period with a return on the amortized balance. Rather than follow this basic ratemaking policy, the Commission attempted to reverse that policy with no explanation for its reversal. The Commission can change its policy, that is true; but it cannot suddenly change course without providing a reasoned basis for doing so. To allow otherwise would undermine the policy of the State of North Carolina to provide fair regulation of public utilities.

A. Appellees fail to show that the Commission's Order provided a reasoned basis for departing from its past treatment of Duke Energy's coal ash costs.

Appellees and DENC agree on two things. First, "[DENC] is correct that the Commission did not expressly distinguish [the 2018 Duke Orders]." Appellees' Br. 38. Second, the Commission's Order "broke with the different policy that it had adopted in the 2018 Duke Orders." *Id.* Therefore, it is undisputed that the Commission failed to provide any reasonable basis for departing from its policy in the 2018 Duke Order.

Appellees appear to acknowledge the Commission's omission, noting that "the Commission's failure to expressly distinguish its 2018 Duke orders could be error in other circumstances." *Id.* Yet, Appellees maintain the Commission's error was not error in *this* circumstance, because this Court's decision in *Stein*[1] and the subsequent settlement between Duke Energy and Appellees ("Duke Settlement") render this appeal futile. In essence, Appellees argue that the Commission's erroneous Order has been rescued by a later settlement between Appellees and Duke Energy that is less favorable to Duke Energy. Appellees' Br. 38-9.

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[1] *See State ex rel. Utilities Comm'n v. Stein*, 375 N.C. 870, 851 S.E.2d 237, 286 (2020).

i. *Stein* does not render this appeal futile.

Stein affirmed the basic ratemaking approach adopted by the Commission for coal ash costs, which allowed a five-year amortization period and authorized a return on the unamortized balance. *Stein*, 851 S.E.2d at 286. The Commission's error in the 2018 Duke Orders was that it adopted the basis ratemaking approach for Duke Energy without first considering the material facts offered in support of the Public Staff's recommended "equitable sharing." *Id.* at 276 (those material facts pertain to Duke Energy's "alleged environmental violations such as non-compliance with NPDES permit conditions, unauthorized discharges, and groundwater contamination from the coal ash basins in violation of 2L rules"). At the same time, this Court noted the Commission was "free. . . to reject the Public Staff's equitable sharing proposal" again on remand and maintain the status quo. *Id.* at 277.

Appellees contend that *Stein* is determinative of this case because this Court reversed the 2018 Duke Orders upon which DENC relies. Appellees' Br. 38 (framing *Stein* as reversing the 2018 Duke Orders because "the Commission had not adequately considered a proposal by the Public Staff, *which is similar to the ratemaking treatment that the*

Commission adopted in the present case") (emphasis added). Appellees appear to argue that, because this Court indicated that the Commission did not adequately consider and had the discretion to adopt "equitable sharing," the Commission's adoption of a "similar" ratemaking treatment here was necessarily appropriate. There are two major flaws with Appellees' analysis. First, *Stein* was not a single-issue decision.[2] Second, while the Public Staff advocated for, and the Commission rejected, "equitable sharing" in this case and in *Stein*, that is where the similarities end.[3] The Commission's decision to reject "equitable sharing" in this case is not on appeal.

To the extent Appellees are inferring that the Commission relied on the "material facts" relevant to "equitable sharing" as its rationale and somehow justifies its ratemaking treatment here, the record shows the opposite. DENC's alleged "culpability for non-compliance with

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[2] Several issues were on appeal in *Stein*, including (1) the appropriateness of deferring certain coal ash remediation costs, (2) inclusion of those deferred costs in retail rates, (3) the appropriateness of Duke earning a return on the unamortized balance of deferred coal ash remediation costs, and (4) approval of ab increased Basic Facilities Charge for Duke's residential retail customers. *See Stein*, 851 S.E.2d at 240.

[3] The Public Staff's "equitable sharing" concept involves randomly allocating coal ash costs between shareholders and ratepayers to address "culpability for non-compliance with environmental regulations that are meant to protect groundwater and surface water from contamination by" coal ash. T vol. 6 p 112; *compare Stein*, 851 S.E.2d at 274-5 (explaining the purpose of Public Staff's "equitable sharing" proposal was to address "culpability for extensive environmental violations resulting from its coal ash management").

environmental regulations" was not the basis for the Commission's Order. After considering the record, the Commission found "there is substantial evidence regarding DENC's compliance with legal requirements for handling and storing CCRs that tends to show that DENC was attentive to the applicable legal standards of the day, as well as evolving standards." (R p 204). Aside from one instance in the 1980s that was fully resolved contemporaneously, "there is no evidence of DENC having been the subject of notices of violation, NPDES permit revocations, other remediation orders, or enforcement actions by environmental regulators." (R p 204).

Stein is neither the sword nor the shield that Appellees think it is. Following *Stein*, any modification to ratemaking policy adopted on the 2018 Duke Orders would have been based on the Commission's further consideration of *Duke Energy's* environmental compliance history. DENC's environmental compliance history, on the other hand, was not the basis for the Commission's departure from the ratemaking policy it adopted in the 2018 Duke Orders. Thus, DENC was entitled to rely on the Commission's basic ratemaking policy, because there is no factual basis for diverging from that policy.

ii. Appellees' settlement with Duke Energy following *Stein* is irrelevant to this appeal.

Appellees suggest that DENC can no longer rely on the basic ratemaking policy articulated in the 2018 Duke Orders, because Duke Energy later entered a global coal ash settlement with "different terms less favorable to Duke." Appellees' Br. 39. Appellees are parties to the Duke Settlement. DENC is not. The Duke Settlement is not binding on DENC and does not (and cannot) retroactively justify the Commission's arbitrary and capricious treatment of DENC. Arguing that the Duke Settlement somehow is determinative for DENC and supersedes the Commission's basic ratemaking policy for coal ash is incorrect and overstates the effect of the Duke Settlement.

Moreover, there is no indication that the Commission approved the Duke Settlement to reverse the basic ratemaking policy it adopted in the 2016 DENC Order or the 2018 Duke Orders. To the contrary, the Duke Settlement approved by the Commission keeps the 2018 Duke Orders in place, provides a five-year amortization period, and allows a return on the unamortized balance. Add. 231-32.[4]

[4] The Duke Settlement is "less favorable" because Duke Energy agreed to forego recovery of a lump sum in its most recent rate cases and earn a lower rate of return in its future rate cases. Add. 231-32.

Parties settle cases for a variety of reasons, and the Commission approves settlements for a variety of reasons. Whatever the reasons for the Duke Settlement, they do not apply to DENC. In approving the Duke Settlement, the Commission noted that the settling parties aimed to "reduce costs that are passed on to customers, to avoid additional protracted litigation over [Duke Energy's] historical management practices, and to provide some closure to the debate that has been waged for several years." Add. 237-8. The Commission, however, takes no responsibility for its role in fueling the regulatory uncertainty and protracted litigation over Duke Energy's coal ash costs that made the Duke Settlement necessary. During the pendency of two new Duke Energy rate cases, and while the basic ratemaking policy in the 2018 Duke Orders was on appeal, the Commission issued its DENC Order and abandoned any regulatory certainty with respect to CCR costs. Despite this Court's ruling in *Stein* that would have allowed the Commission to affirm its 2018 Duke Orders, it is no surprise then that Duke Energy was willing to accept "less favorable" terms for its future coal ash costs. The Duke Settlement does not bind DENC and does not convert the Commission's unlawful DENC Order into a lawful order. Again, the

ratemaking treatment Duke Energy was willing to accept and the ratemaking treatment DENC is entitled to are two different things.

B. Appellees fail to show that the Commission's Order provided a reasoned basis for departing from its past treatment of DENC's coal ash costs.

Even if this Court agrees with Appellees' interpretation of the effect *Stein* and the Duke Settlement may have had on the 2018 Duke Orders, DENC should still prevail here because the Commission provided no reasoned basis for departing from the 2018 Duke Orders and the 2016 DENC Order. Appellees argue the Commission's failure to distinguish its prior orders should be excused because the Order provided an "extensive explanation for its treatment of [DENC]'s coal ash costs." Appellees' Br. 36. Appellees further point to the Commission's explanation that the factual record in DENC's 2016 rate case was "far less extensive" and that "the issues of prudence and reasonableness were [therefore] not fully litigated and no significant evidentiary record was developed." *Id.* at 37 (quoting R p 203).

As to Appellees' first argument, the Commission cannot escape its statutory duty to have a reasoned basis creating a new policy by merely concluding that its prior policy is not precedent. *See State ex rel. Utils.*

Comm'n v. Thornburg, 314 N.C. 509, 515, 334 S.E.2d 772, 776 (1985). The Commission's failure to explain why it departed from its prior policy is error on its face, which Appellees cannot minimize. *See* 2 Am. Jur. 2d *Administrative Law* § 360 (2020) (the Commission was required to "confront the issue squarely and explain why the departure is reasonable.").

Moreover, the Commission's ability to explain its new policy is not a justification for reversing its old policy. *Id.* (The Commission's failure to explain its change in policy is arbitrary and capricious "even if the record contains substantial evidence to support the determination made."). Appellees' argument attempts to merge two distinct requirements: (1) the Commission must explain its new policy and (2) the Commission must explain why it changed its policy. *Id.* At best, the Commission only satisfied the former. As discussed further below, however, even the Commission's explanation for its new policy is hollow.

i. The Commission's conclusory determination that the 2016 DENC Order lacked precedential value is not a reasoned basis for departing from that order.

The Commission's explanation for not following the 2016 DENC Order is a *non sequitur*. Appellees argue the Commission's departure

from its prior ratemaking treatment of DENC's coal ash costs is justified because the 2016 DENC Order was explicitly non-binding:

> Further, the Commission's determination in this case shall not be construed as determining the prudence and reasonableness of the Company's overall CCR plan, or the prudence and reasonableness of any specific CCR expenditures other than the ones deferred and authorized to be recovered.

(R p 203 (quoting 2016 DENC Order at 63)).

The above statement reveals that the Commission did not want to bind itself to prudency determinations regarding DENC's future coal ash costs or DENC's overall coal ash remediation plan. Thus, to the extent the 2016 DENC Order explicitly carved out room for different determinations in the future, it was limited to prudency determinations on DENC's future costs. In this case, the prudency of DENC's coal ash costs was not disputed, and the Commission concluded they were prudently incurred. (R p 94, 205). The 2016 DENC Order contains no such statement regarding the basic ratemaking treatment the Commission adopted for those costs. As DENC discussed at length in its opening brief, the Commission later concluded in the 2018 Duke Orders that the basic ratemaking treatment it adopted in the 2016 DENC Order had precedential value.

ii. The evidentiary record provided no reasoned basis for departing from the Commission's existing policy.

Regarding the evidentiary record, the Commission is attempting to disregard the 2016 DENC Order because more evidence was presented. But the Commission's focus on the quantity of the evidence ignores the quality of the evidence, which did not change the findings or assumptions underlying the 2016 DENC Order. Regardless, the Commission was required to explain why the new evidence should result in a different ratemaking policy, which it failed to do. Appellees offered four reasons justifying the Commission's Order, Appellees' Br. 29-34, but none of these reasons refute or invalidate the Commission's reasoning underlying the 2016 DENC Order.

1. DENC's coal ash costs in 2016 and 2019 were "extraordinary, large costs."

Appellees do not dispute that the 2016 DENC Order was premised on the "extraordinary, large" nature of the coal ash costs the Company has recently incurred and will continue to incur. *Id.* at 30. They argue that the Commission rightfully disregarded the 2016 DENC Order because it was not precedent. At the same time, the Commission was justified in relying on different, earlier decisions unrelated to coal ash because those were precedent. *Id.* This reasoning highlights the

Commission's arbitrary and capricious decision-making here: disregarding a more recent, analogous case in favor of earlier, factually dissimilar cases.

2. DENC's historical coal ash management practices did not change between 2016 and 2019.

At issue in this case and in DENC's 2016 rate case were costs DENC incurred to comply with the EPA's 2015 CCR Rule. (R p 203). These costs relate to efforts to remediate coal ash repositories put into service before 2015. Appellees argue that the Commission's new ratemaking approach was appropriate because the Commission stated "[a] number of material facts in evidence call into question the prudence of DENC's actions and inaction and the risks accepted by DENC management at several of its CCR sites." Appellees' Br. 32 (quoting R p 212). Those "material facts" consisted of an incident at Possum Point power station in the 1980s that was fully resolved at the time, and historical documents indicating the environmental risks of managing coal ash in unlined impoundments. (R p 212).

As to whether those risks were acceptable, the Commission ultimately concluded, though, that the "*substantial [material] evidence*" in the record "show[ed] that DENC was attentive to the applicable legal

standards of the day, as well as evolving standards" and that "unlined impoundments were the accepted repositories for storing CCRs prior to adoption of the CCR Rule." (R p 204); *compare* [2016 Order [62]] ("The cost of complying with federal and state CCR remediation requirements was a risk that was unknown to the Company prior to 2015."). Therefore, upon closer examination, the "material facts" that Appellees contend justify a different ratemaking treatment here, in no way contradict or rebut the basis for the 2016 DENC Order, which was that managing coal ash in unlined repositories was reasonable prior to the CCR Rule.

3. DENC's coal ash costs in 2016 and 2019 were associated with past generation.

In the 2016 DENC Order, the Commission rejected Appellee Attorney General's argument that current customers should not bear costs attributable to providing electric service to past customers. 2016 Order [62]. In this Order, the Commission now finds merit in that argument. But nothing about DENC's historical management of ash changed between 2016 and 2019. Like the costs at issue here, DENC's coal ash costs in 2016 were incurred to address the same coal ash repositories that served prior customers. The Commission's Order provides no explanation for reversing its position.

4. DENC did not seek recovery of coal ash costs before 2016.

Appellees argue the Commission's decision was justified because DENC failed to recover its coal ash costs in past rate cases. Appellees' Br. 35. To the extent DENC's failure applied to this case, it would also have applied to DENC's 2016 rate case. In other words, no new evidence in this "more developed" record would change the fact that DENC did not also recover coal ash costs prior to the 2016 rate case. This fact, therefore, cannot be a reasoned basis for departing from the 2016 DENC Order.

CONCLUSION

The Commission adopted a new ratemaking policy that effectively disallowed DENC's prudently incurred costs after previously allowing recovery of the same costs incurred for the same reasons when faced with the same or similar factual record. Not only did the Commission fail to articulate any rationale to support this abrupt departure from its past precedent, but the facts in the record, under any interpretation, do not support the harsh result the Commission reached given its finding that DENC's coal ash costs were prudently incurred. Accordingly, for all of the foregoing reasons and as set forth in DENC's Appellant Brief, DENC respectfully asks the Court to vacate the arbitrary and capricious DENC

Order and remand the case with instructions for the Commission to make it consistent with the basic ratemaking treatment for coal ash costs the Commission has three times declared to be fair and reasonable to utilities and their customers. Simply remanding the case, without further instructions, to the Commission would be insufficient to correct the error. As shown herein and in DENC's Appellant brief, there are no facts in the record that could support a more punitive result for DENC, here, than in the Commission's three previous orders on this issue. DENC, therefore, respectfully requests that this Court provide appropriate direction to the Commission to resolve, with finality, this contested matter.

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N.C. App. R. 33(b) Certification:
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CERTIFICATE OF SERVICE

I hereby certify that the undersigned counsel has this day served the foregoing **REPLY BRIEF OF APPELLANT VIRGINIA ELECTRIC AND POWER COMPANY D/B/A DOMINION ENERGY NORTH CAROLINA** in the above-captioned action on all parties to this cause by depositing the original and/or copy hereof, postage prepaid, in the United States Mail, addressed to the following:

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