STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. E-7, SUB 1214
DOCKET NO. E-7, SUB 1213
DOCKET NO. E-7, SUB 1187

DOCKET NO. E-7, SUB 1214 In the Matter of Application by Duke Energy Carolinas, LLC, for Adjustment of Rates and Charges Applicable to Electric Utility Service in North Carolina DOCKET NO. E-7, SUB 1213 In the Matter of Petition of Duke Energy Carolinas, LLC, for Approval of Prepaid Advantage Program DOCKET NO. E-7, SUB 1187 In the Matter of Application of Duke Energy Carolinas, LLC for an Accounting Order to Defer Incremental Storm Damage Expenses Incurred as a Result of Hurricanes Florence and Michael and Winter Storm Diego	)	POST-HEARING BRIEF OF APPLE INC., FACEBOOK, INC., and GOOGLE LLC (TECH CUSTOMERS)

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Intervenors Apple Inc., Facebook, Inc., and Google LLC (collectively, "Tech Customers"), by and through counsel, submit this Post-Hearing Brief in the above-captioned matters.

INTRODUCTION

This proceeding concerns the rates to be charged by Duke Energy Carolinas, LLC (DEC or Company), for electricity service in the future and raises a number of significant policy concerns, including how the Commission should handle rate issues during the unprecedented and ongoing COVID-19 pandemic and its associated economic turmoil, how DEC and its customers should pay for infrastructure investments to improve the electrical grid, the appropriate balance to be struck between the interests of ratepayers in paying low rates and the impact on the utility's credit ratings, how much scrutiny should be applied to DEC's continued operation and retirement of coal-fired power plants, and how the Commission should handle the effects of the federal Tax Cuts and Jobs Act. The Commission's decisions on these issues will have substantial effects on the rates charged by DEC, which will significantly impact DEC's customers and, more broadly, the economy of the state.

Each of the Tech Customers is a provider of online services and products. In connection with these business operations, the Tech Customers, through their respective affiliates, own and operate data centers and related infrastructure in the service territory of DEC. Data centers are high load factor facilities that use energy on a 24-hours-a-day, seven-days-a-week basis. Each of the data centers owned and operated by the Tech Customers in DEC's service territory uses electricity sold by DEC and is affected by DEC's operation of its electric generation, transmission and distribution facilities. The availability of an adequate supply of electricity at a reasonable rate is critically important to the viability of the Tech Customers' data center operations.

SUMMARY OF ARGUMENT

This brief addresses legal and factual issues related to (1) DEC's request for approval of deferred accounting for certain Grid Improvement Plan expenses; (2) DEC's claims regarding the potential impairment of its credit metrics, (3) the appropriate return on equity that should be awarded, (4) DEC's request for recovery of certain costs associated with coal plants that are slated for early retirement, and (5) the return of Excess Deferred Income Taxes (EDIT). The Tech Customers urge the Commission to deny a number of DEC's requests related to these issues in order to establish just and reasonable rates.

As an overarching consideration, the Tech Customers urge the Commission to consider the context of DEC's request for a rate increase: the ongoing COVID-19 pandemic. This novel and (at least in "modern" times) unprecedented public health crisis has caused significant disruption to the State's economy, harming residential, commercial, and industrial customers and impairing their ability to pay higher electric rates. These "changing economic circumstances" strongly militate against increases in rates for essential utility services—especially those charged by the dominant provider, by far, in North Carolina. Such increases would exacerbate the economic harms experienced already by too many North

Carolina consumers and impair the State's ability to "restart" the economy in these trying times.

As to DEC's request for approval of deferral accounting for Grid Improvement Plan expenses, the request should be denied—irrespective of the legitimacy of any individual expense—as inconsistent with North Carolina's ratemaking process, noncompliant with the Commission's established test for deferral accounting, and noncompliant with the Commission's instructions on this same issue in the last rate case. A grant of deferral accounting in this case risks creating precedent that will encourage utilities to seek special rate treatment for what should be considered the normal costs of doing business, thus eroding the ratepayer protections established by the General Assembly in N.C. Gen. Stat. § 62-133 and otherwise in Chapter 62.

With regard to credit metrics, DEC's witnesses repeatedly argued that the Commission should make decisions for the sole purpose of protecting DEC's credit ratings. Not only does the Commission have no legal duty to protect the Company's credit metrics as an independent regulatory goal, the evidence adduced at hearing shows that DEC's warnings about protecting its credit ratings are a false alarm. DEC has also failed to prove that a credit downgrade, even if one should occur, would have any adverse impact on the Company's ability to access needed capital.

With respect to return on equity, DEC has failed to justify its requested return on equity, including the rate of 9.6% recommended in the Second Stipulation between DEC and the Public Staff. DEC relies entirely on the subjective judgment of its witness D'Ascendis, but data and empirical analysis show that the return sought by DEC is not reflective of its risk relative to comparable utilities but rather is at the high end of the range of reasonableness. The only reliable expert testimony in this case supports a return on equity (ROE) below 9.6%.

With respect to coal plant retirements, the evidence presented in the case suggests the Commission should apply additional scrutiny to the timing and reasons provided for coal plant retirements in order to ensure that DEC's decision-making is driven by the need to provide electricity at the lowest possible cost rather than the desire to increase value for DEC's shareholders.

Finally, the Tech Customers support the proposed return of EDIT as agreed to by DEC and the Public Staff in their Second Stipulation as a reasonable and expeditious mechanism for the return of over-collected taxes.

I. The Commission Should Consider the Unprecedented Circumstances Relating to the COVID-19 Pandemic in Establishing Going-Forward Rates.

DEC is a **public** utility. Its primary mission under its certificate and under its "regulatory compact" is to serve the public—not its investors. This core mission has particular importance in times of economic crisis such as caused by the ongoing pandemic, which makes the Company's current request for increased rates particularly untimely and, potentially, counterproductive to economic recovery efforts.

By all measures, the novel and unprecedented public health crisis resulting from the COVID-19 pandemic has caused significant and ongoing disruption to the State's economy—with uncertain prospects and impacts going forward. *E.g.,* Order Suspending Utility Disconnections for Non-Payment, Allowing Reconnection, and Waiving Certain Fees, Docket No. M-100, Sub 158 (Mar. 19, 2020) (recognizing "the potentially devastating health and financial impacts on [utilities'] customers' lives"); *see also* Joint Petition of DEC and DEP for Approval of Accounting Order to Defer Incremental Covid-19 Expenses, Docket Nos. E-7, Sub 1241, E-2, Sub 1258 (Aug. 7, 2020) at 1 ("The Pandemic continues to significantly impact economic activity throughout the state and country[.]"). Other state regulatory commissions have made similar findings.

The Nevada Public Utilities Commission:

> The Commission finds that the economic recession and financial crisis caused by the ongoing COVID-19 global pandemic presents a unique set of circumstances that require that the Commission take unique action. . . . [I]t is apparent that the COVID-19 global pandemic has had a major financial impact on NPC's ratepayers.[1]

The Virginia State Corporation Commission:

> [The] unprecedented socioeconomic crisis inflicted on the United States and the Commonwealth of Virginia by the coronavirus (COVID-19) . . . . [W]e do not minimize the continuing hardships faced by many Virginians due to the economic devastation caused by the COVID-19 crisis, nor do we presume to predict when our economic situation will return to the low unemployment rates just before the COVID-19 pandemic hit the United States. . . . While there are some signs of economic recovery, hundreds of thousands of Virginians are still suffering from lost jobs and income caused by the crisis.[2]

[1] *Application of Nevada Power Co. d/b/a NV Energy for Auth. to Adjust Its Annual Revenue Requirement for Gen. Rates Charged to All Classes of Elec. Customers & for Relief Properly Related Thereto*, No. 20-06003, 2020 WL 5577011, at *10 (Sept. 9, 2020) (approving refund of earnings sharing regulatory liability in the form of one-time bill credit).

[2] *Commonwealth of Virginia, Ex Rel. State Corp. Comm'n*, No. PUR-2020-00048, 2020 WL 3304397, at *1 (June 12, 2020) (extending moratorium on service disconnections

The Michigan Public Service Commission:

> Michigan is facing an unprecedented situation with the novel coronavirus (COVID-19) pandemic threatening human health and disrupting the economy.[3]

The significance and impact of this crisis has not been lost on Duke's Executive Leadership Team, as the following statements demonstrate:

Statement of Lynn Good, Chief Executive Officer

> This pandemic has no barriers - it has permeated the globe, our country and the state in which we operate. It has altered our day-to-day lives from how we interact to the way we operate and serve our customers.[4]

Statement of Steve Young, Chief Financial Officer

> This is an extraordinary time that has and will continue to require our utilities to incur cost on behalf of our customers and the employees who operate our business. Similar to what others are doing across the country, we will work with our regulators to identify the best solutions to recover these costs, to support the ongoing financial health of our utilities, while also recognizing the unique needs of our customers during this unprecedented time.[5]

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until August 31, 2020). *See also Commonwealth of Virginia State Corp. Comm'n*, No. PUR-2020-00048, 2020 WL 5577355, at *1 (Sept. 15, 2020) (extending moratorium through October 5, 2020).

[3] *In the Matter, on the Commissions Own Motion, to Review Its Response to the Novel Coronavirus (Covid-19) Pandemic, Including the Statewide State of Emergency, & to Provide Guidance & Direction to Energy & Telecommunications Providers & Other Stakeholders*, No. U-20757, 2020 WL 4402047, at *1 (July 23, 2020) (requiring further reports on COVID-related impacts on utilities and establishing parameters for cost recovery).

[4] Edited Transcript: Q1 2020 Duke Energy Corporation Earnings Call, May 12, 2020, (De May Tech Customers Cross Exhibit 1), at 2-3, 5.

[5] *Id.*

While DEC took prompt action to mitigate immediate impacts on consumers by, among other things, not disconnecting customers for nonpayment[6]—matters subsequently mandated by Orders of the Commission[7] and Executive Order of the Governor[8]—DEC is now seeking special accounting treatment of pandemic-related expenses, such as lost revenue from customer write-offs and waived fees and other safety-related concerns, so that its investors are held harmless from the direct and indirect economic impacts of the pandemic.[9] In the meantime, according to the Commission's data, some three-hundred thousand households in DEC's territory were considered delinquent on their utility account as of June 30, 2020. *See* North Carolina Utilities Commission, Letter to Gov. Cooper re: Implementation by the North Carolina Utilities Commission of Executive Order No. 142, Docket No. M-100, Sub 158 (July 15, 2020).

Notwithstanding this backdrop and in the midst of the continuing pandemic, DEC is requesting average increase of approximately 8.4% in its rates. *See* McManeus Second Settlement Exhibit 1, Schedule 1. In addition, DEC seeks to defer $800 million in grid improvement expenses for future recovery in rates—expenses which are discretionary in nature. On cross-examination, DEC's North

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[6] *See Customer Response to COVID-19 and Request for Expedited Approval for the Companies to Waive Late-Payment and Reconnect Fees for their Customers*, Docket No. E-7, Sub 1236 (Mar. 19, 2020).

[7] *See*, *e.g.,* Order Suspending Utility Disconnections for Non-Payment, Allowing Reconnection, and Waiving Certain Fees, Docket No. M-100, Sub 158 (Mar. 19, 2020).

[8] *See*, *e.g.,* Executive Order No. 124 (Mar. 31, 2020).

[9] J*oint Petition of Duke Energy Carolinas, LLC and Duke Energy Progress, LLC for Approval of Accounting Order to Defer Incremental Expenses as a Result of COVID-19*, Docket No. E-7, Sub 1213 (Aug. 7, 2020).

Carolina President, Mr. De May, conceded that the pandemic is a factor to be considered by the Commission in its review of the Company's rate request, (Tr. vol. 11, 1013), but, ultimately, he dismissed these concerns: "The pandemic notwithstanding, our customers want cleaner energy, they want more convenience and control over their usage, and they want relief for those among us who are least able to afford their power bills." (Tr. vol. 11, 891-92.) Put another way, DEC takes the position that its customers—"the pandemic notwithstanding"—want the Company to raise their rates.[10] Of course, DEC put on no such evidence of consumer preferences "notwithstanding the pandemic," so no such assumption is justified under this record. To the contrary, as conceded by DEC, the Commission is obligated to consider the obvious exacerbation of ongoing harms that will be caused by raising electric rates in the midst of a pandemic.

Section 62-133 requires the Commission to set rates that "shall be fair both to the public utilities and to the consumer." N.C. Gen. Stat. § 62-133(a). Similarly, Section 62-133(b)(4) requires the Commission to set a rate of return to "enable the public utility . . . to produce a fair return for its shareholders, considering changing economic conditions and other factors . . . ." *Id.* § 62-133(b)(4).

The North Carolina Supreme Court has emphasized the importance of the "changing economic conditions" factor:

> We have explained that [Section 62-133(b)(4)] advances the Legislature's "twin goals of assuring sufficient shareholder

[10] Mr. De May contended, on cross-examination, that Duke had responded to concerns "in its rate application" and "through its settlement agreements." (Tr. vol. 11, 1013.) However, merely agreeing to accept less of a rate increase than initially proposed, and offering to put $6 million in a low income fund, does not being to address the magnitude of the ongoing pandemic and its impact on consumers and the economy.

> investment in utilities while simultaneously maintaining the lowest possible cost to the using public for quality service."
> ...
> [I]t is clear that the Commission must take customer interests into account when making an ROE determination. . . . [In a previous case,] we concluded that the Commission had not made sufficient findings regarding the impact of changing economic conditions on consumers.
> ...
>
> We previously have stated that "[t]he Commission's concern about an 'extreme fluctuation' between the rate of return allowed in [the company's] last general rate case and that allowed here ... is an improper consideration in determining rate of return. It has nothing to do with the [c]ompany's existing cost of equity." *State ex rel. Utils. Comm'n v. Public Staff*, 331 N.C. 215, 225, 415 S.E.2d 354, 361 (1992) (citing N.C.G.S. § 62–133(b)(4) (1989)). There does not appear to be any evidence in the record indicating that the economic conditions facing Dominion, its shareholders, and its consumers today are comparable to the conditions facing other utilities over the last thirty years. Fundamentally, the Commission's reliance on past ROE determinations authorized for other utilities, without evidence tying those determinations to the facts of the case sub judice, prevented the Commission from fairly considering current economic conditions.

State ex rel. Utils. Comm'n v. Attorney General Cooper, 367 N.C. 430, 440-42, 758 S.E.2d 635, 641-42 (2014). Without question, the ongoing pandemic and related economic distress is the sort of "changing economic condition" contemplated by the General Assembly.

While DEC certainly could not have foreseen the pandemic when it filed its rate case in September 2019, the scope of this crisis and its potential impacts on DEC's ratepayers were evident well before this matter came on for hearing and remain evident as DEC presses on for a substantial rate increase. Due consideration must be given to the overall context in which DEC's current request has been made. The Commission should make every effort to avoid increasing electricity rates during the ongoing pandemic and resulting economic crisis.

II. The Commission Should Deny DEC's Request for Deferred Accounting Treatment for "Grid Improvement Plan" Expenses.

The Commission should reject DEC's request for deferral accounting for the proposed Grid Improvement Plan (GIP) spending.

DEC initially sought deferral accounting for approximately $1.3 billion to support its proposed GIP. In the Second Agreement and Stipulation of Partial Settlement between DEC and the Public Staff (Second Stipulation), DEC agreed to withdraw its request for deferral accounting for all GIP programs other than Self-Optimizing Grid (SOG), Integrated Volt Var Control (IVVC), Integrated System and Operations Planning (ISOP), Transmission System Intelligence, Distribution Automation, Power Electronics, DER Dispatch Tool, and Cyber Security. DEC witness McManeus confirmed that the Company was withdrawing its deferral request for programs other than those listed in the Second Stipulation. (Tr. vol. 11, 583-84.)

The programs for which deferral is sought are estimated to cost more than $800 million (Tr. vol. 4, 128) over the next three years, with substantial variation from this estimate possible. DEC has not agreed to any cost capping (Tr. vol. 6, 33), and DEC's request—although presented with a proposed budget, Oliver Exhibit 10—is for pre-approved deferral of <u>unlimited costs</u>.

In DEC's last rate case, DEC put forward its ten-year, $13 billion Power/Forward Carolinas plan for grid investment—a plan that DEC's witness conceded was "part of Duke Energy's corporate policy intended, as quoted in a

Duke investor earnings call, 'to drive 4 to 6 percent earnings growth.'" *See* Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, *In re Application of Duke Energy Carolinas, LLC, for Adjustment of Rates and Charges Applicable to Electric Utility Service in North Carolina*, Docket No. E-7, Subs 1146, 819, 1152, 1120, at 128-29 (June 22, 2018) (2018 DEC Rate Order). DEC sought a rider and deferral accounting for Power/Forward expenses, but the Commission rejected both requests. 2018 DEC Rate Order at 149. In doing so, as discussed in more detail below, the Commission provided guidance to DEC on how best to present a future deferral accounting request for grid modernization costs. *Id.* at 148-49.

DEC's request for deferral accounting spending should be rejected because it is inconsistent with North Carolina's ratemaking process, fails to satisfy the test for deferral accounting set forth in the Commission's prior orders, and fails to follow specific guidance provided by the Commission in DEC's last rate case regarding an appropriate way for DEC to bring a request for deferral of grid modernization costs before the Commission. A grant of deferral accounting in this case—even for expenditures otherwise in the public interest—risks creating precedent that will encourage DEC to return repeatedly in the future to ask for special rate treatment for what should be considered the normal costs of doing business as a regulated electric utility. The Commission should also specifically reject the provision of the Second Stipulation that approval of deferral accounting constitutes approval of DEC's "decision to incur" grid modernization costs.

A. DEC's GIP deferral accounting request fails to satisfy the Commission's test for deferral accounting.

DEC's request for deferral accounting is a request that the Commission forgo the statutory process for fixing rates established by the General Assembly in N.C. Gen. Stat. § 62-133.

The Commission has set out clear guideposts for when deferral accounting should, and should not, be used, and recently described those principles at length. Order Granting Partial Rate Increase and Requiring Customer Notice, Docket No. W-354, Sub 363 (Mar. 31, 2020) (Carolina Water). There, the Commission noted that "deferral accounting must not be used routinely or frequently," and should only be used "when the costs at issue 'were reasonably and prudently incurred, unusual or extraordinary in nature, and of a magnitude that would result in a material impact on the Company's financial position (level of earnings).'" Carolina Water at 42 (quoting Order Denying Request to Implement Rate Rider and Schedule Hearing to Consider Request for Creation of Regulatory Asset Account, Docket No. E-7, Sub 849 (June 2, 2008) at 19). Requests for deferral accounting

> must be examined and resolved on a case-by-case fact-specific basis and will be approved only where the Commission is persuaded by clear and convincing evidence that the costs in question are unusual or extraordinary in nature and that, absent deferral, would have a material impact on the utility's financial condition.

Id. The two-prong test thus requires (1) extraordinary costs and (2) a material impact on the utility's financial condition, absent deferral. Furthermore, whether the costs are extraordinary in nature is the Commission's primary concern:

> The issue of whether an event or change results in revenues or costs that would materially impact a utility's financial condition, while in some cases may be dispositive, it is secondary to the first prong of the test historically relied on by the Commission to determine

> whether deferral accounting should be permitted or required. If it is determined that the subject of a deferral request is not unusual or extraordinary, that decision is dispositive and the materiality issue is not reached.

Order Approving Amended Schedule NS and Denying Deferral Accounting, Docket No. E-22, Sub 517 (Mar. 29, 2016) at 11.

As to whether costs are "extraordinary," the Commission examines whether the "costs in question represent major non-routine, infrequent, non-regularly occurring investments of considerable complexity and significance or were beyond the control of the utility such as storm costs or new operating requirements/standards imposed by newly-enacted legislation or other governmental action." Carolina Water at 42. Thus, the Commission may consider "whether costs were unanticipated, unplanned, beyond the control of the utility, and of an infrequent, non-recurring nature." *Id.* The costs must be extraordinary in type and magnitude. 2018 DEC Rate Order at 148.

As to whether there is a material impact on the utility's financial condition, the Commission "often examines whether and to what extent the costs incurred will have a significant impact on the level of company earnings and the company's ability to achieve its currently authorized rate of return on common equity." Carolina Water at 43. For example, in Carolina Water, the Commission authorized deferral accounting for wastewater treatment plant investments that would "result in a 434-basis point rate of return on common equity reduction." *Id.* at 44.

"The clear and convincing standard requires evidence that should fully convince." *Scarborough v. Dillard's, Inc.*, 363 N.C. 715, 721, 693 S.E.2d 640, 643 (2009) (internal quotations omitted). "This burden is more exacting than the 'preponderance of the evidence' standard generally applied in civil cases, but less than the 'beyond a reasonable doubt' standard applied in criminal matters." *Id.* at 721, 693 S.E.2d at 643.

DEC has failed to meet either prong of the deferral test.

First, DEC has not shown that the costs are extraordinary by clear and convincing evidence.

The GIP program costs are not "beyond the control of the utility," do not reflect "operating requirements/standards imposed by newly-enacted legislation or other governmental action," and were not "unanticipated" or "unplanned." On the contrary, the set of programs identified for inclusion in the GIP were selected by DEC and packaged into a multi-year proposed plan, with DEC ultimately agreeing in the Second Stipulation to request deferral accounting for only a subset of the programs. In other words, the GIP costs are *discretionary*, *planned* future costs.

The GIP program costs cannot fairly be described as "non-routine, infrequent, [or] non-regularly occurring." Instead, these kinds of costs are simply the costs of doing business as an electric utility. (*See* Tr. vol. 7, 17-18 (Public Staff Witness T. Williamson acknowledging a utility's obligation to "modernize" as part of good utility practice).) The so-called Megatrends contributing to the need for grid modernization are not new and are not expected to abate in the foreseeable future. (*E.g*., Strunk Exhibit KGS 10 at 2; Strunk Exhibit KGS 11 at 2.) DEC is not facing a "new normal" that requires significant changes to its business and North Carolina's regulatory environment; rather, DEC is simply faced with "normal." Indeed, DEC has already deployed many of the technologies that make up the

GIP, including self-optimizing grid, transmission system intelligence, distribution automation, and cyber security. (*E.g.*, Tr. vol. 17, 310-14.)

There is nothing unique or extraordinary contributing to the Megatrends DEC has identified to justify its request. In DEC's last rate case, DEC sought deferral of Power/Forward program costs, which DEC argued were necessary to

> improve the reliability and hardiness of the system while making it smarter, build a foundation for customer-focused innovation and new technologies, comply with prescriptive federal transmission reliability and security standards, address maintenance requirements for aging assets, further integrate and optimize intermittent distributed renewable energy generation, and address physical and cyber security, worsening weather, customer disruption, and wear and tear on equipment.

Id. at 128. These issues are materially indistinguishable from the Megatrends identified by DEC witness Oliver in this case. But as the Commission recognized when it rejected DEC's Power/Forward proposal,

> the reasons DEC says underlie the need for Power Forward are not unique or extraordinary to DEC, nor are they unique or extraordinary to North Carolina. Weather, customer disruption, physical and cyber security, DER, and aging assets are all issues the Company (and all utilities) have to confront in the normal course of providing electric service.

2018 Order DEC Rate at 146. The same conclusion is inescapable here. DEC witness Oliver confirmed that the Megatrends are not unique to North Carolina; indeed, witness Oliver's testimony regarding the existence of these trends relies on national data and on Duke Energy's experience in numerous other states. (*See* Tr. vol. 11, 612-14.)

Tech Customers witness Strunk explained that the GIP investments are "similar, if not identical, to the type of investment that DEC routinely makes in its transmission and distribution systems." (Tr. vol. 16, 122-23.) Witness Strunk also pointed out that the electric sector has undergone and will continue to undergo change, and that the Megatrends are neither new nor likely to be temporary. (Tr. vol. 16, 126-27.) Responding to such trends is simply "part of . . . prudent utility planning." (Tr. vol. 16, 127.) The Public Staff likewise "would not characterize a number of these trends as new, novel, or outside the scope of normal business." (Tr. Vol. 17, 317.) Far from a "clear and convincing" showing that the proposed GIP spending is extraordinary, the evidence is, at best, equivocal. GIP expenditures are already part of the revenue requirement for which DEC seeks approval in this proceeding, confirming that DEC is pursuing them in the normal course of business.

Second, DEC has not provided clear and convincing evidence of any material impact on its financial condition, absent deferral. To be clear, the question before the Commission is not "would DEC's GIP spending, if implemented as proposed, have a material negative financial impact on DEC if deferral is denied," but rather "will DEC's GIP spending, as actually implemented, have a material negative financial impact on DEC if deferral is denied."

Importantly, rather than seeking deferral for known, already-incurred expenses or mandatory future expenses such as storm recovery or regulatory compliance, DEC's request is for limitless spending over a three-year period on a set of optional modifications to its grid technology. DEC never considered what its implementation of the programs lumped together to form the GIP would look like in the absence of deferral. DEC cannot say what the financial impact of a denial of the deferral request would be; its own witnesses described doing so as "impossible." (*E.g.*, Tr. vol. 5, 46.; Tr. vol. 11, 706-07.) That is because, if the Commission denies deferral, the proposed costs may be delayed, may be incurred in smaller increments over longer periods of time, or may simply evaporate if DEC determines not to pursue any particular program. (Tr. vol. 5, pp. 45-52.) DEC could also mitigate any impact by filing a rate case. Thus, an entirely plausible result of a deferral denial is little or no financial impact.

Moreover, DEC's attempts to offer some quantification of the financial impact of the GIP, absent deferral, are significantly flawed. DEC witness McManeus calculated an impact of the GIP as-filed of 100 basis points by 2022. However, as pointed out by Tech Customers witness Strunk, witness McManeus's calculation "assumes that the Company's grid improvement investments will be the same amount (and on the same timeframe) irrespective of whether the Commission approves the deferral." (Tr. vol. 16, 23; *see also* Tr. vol. 6, 102 (witness McManeus testifying that the 100 basis point impact assumes "if [DEC] did not receive the deferral and [DEC] went forward" with GIP spending).) Witness McManeus also testified that DEC later recalculated the financial impact of implementing only those projects identified in the Second Stipulation, and arrived at a value of 70 basis points in the aggregate over three years—or 13 basis points in year one and 29 basis points in each of years two and three. (Tr. vol. 9, 36, 85-86.) This equates to an average of 23.67 basis points per year, which would not typically support grant of deferral accounting treatment. (*See*, *e.g.*, Tr. vol. 20, 537 (Maness testifying that, in regards to his calculation of a 20.33 basis-point impact per year, "[u]nder normal circumstances, the Public Staff would not recommend deferral of an investment with basis point impacts so small.")).) Regardless, DEC's calculation is subject to the same flaws as McManeus's original calculation; namely, that it assumes DEC would go forward with the same level of GIP spending in the absence of deferral.

But DEC's witness Oliver conceded that, if deferral is denied, DEC will *not* go forward with the GIP plan as proposed. Indeed, according to witness Oliver, it is unknown which programs DEC would implement, or when, if deferral is denied, and DEC considers the exercise of predicting such implementation "impossible." (Tr. vol. 5, 46.) Through at least December of 2019, DEC had given no serious consideration whatsoever to what would happen if its deferral request were denied. (*E.g.*, Exhibit KGS 12.) DEC witnesses Oliver and McManeus also offered joint testimony purporting to show the financial impacts of denial of deferral accounting, but that testimony itself admits that the calculation is "purely hypothetical in nature" and that it "[p]robably [does] not" "reflect reality," and that the analysis "likely does not reflect decisions the Company will actually make during the period 2020-2023." (Tr. vol. 11, 708-09.)

Moreover, as discussed by Tech Customers witness Strunk, DEC's analysis of potential financial impacts of deferral denial inappropriately isolates the impact from DEC's overall cost of service. (Tr. vol. 16, 129-30.) DEC's analysis of financial effects does not account for potential savings or any other changes to its cost of service, including the possibility that DEC could seek rate relief if a negative impact on earnings materializes. (Tr. vol. 16, 129-31.) As anticipated in the Commission's order in DEC's last general rate case, DEC could also make a request for deferral accounting if it were to proceed with GIP and were to demonstrate that the non-discretionary GIP expenditures threatened its ability to earn its authorized return. Instead, DEC is asking the Commission to assume a future negative effect on earnings without knowing how DEC's cost of service will evolve, which amounts to inappropriate regulatory policy.

DEC has provided no evidence that withstands even modest scrutiny regarding the financial impact of a deferral denial in this case. Importantly, *not even DEC is convinced* that its prediction of financial impacts is correct. Although DEC has presented evidence of an average annual basis points impact of 23.67 basis points for the programs included in the Second Stipulation with Public Staff (Tr. vol. 6, 108; Tr. vol. 9, 85-86), witness McManeus also agreed on cross-examination that the estimated basis point impact "doesn't reflect the real-world impact of a decision not to grant deferral." (Tr. vol. 6, 119.) DEC witness Oliver agreed on cross-examination that, absent deferral, DEC would implement GIP programs "at a much smaller scale and a much slower pace." (Tr. vol. 5, 51.) The most that can be said, then, is that the financial impact on DEC of a deferral denial will be "much smaller" than the claimed aggregate 70 basis points and will accrue over a much longer period than three years (because they will be implemented at a "much slower pace")—suggesting a potentially insignificant financial impact. And because any financial impact incurred as a result of deferral denial in this case could be mitigated by filing a future rate case or a concrete, backward-looking deferral request, any financial impact of a deferral denial must be considered purely hypothetical. This leaves the second prong of the deferral test entirely unanswered, let alone met by clear and convincing evidence.

Denial of deferral accounting for the GIP is precisely in line with the expectation of investors and the credit markets. The GIP is simply a repackaging of Power/Forward, for which the Commission already denied deferral accounting in the 2018 DEC Rate Order. Thus, a denial of deferral accounting here will have no adverse impact on the outlook of Duke Energy's investors or the credit markets from which DEC may seek to borrow. Indeed, with regard to grid modernization investments, the markets already have an "expectation that the utility will continue to recover its capital expenditures as part of its rate proceedings" and that "there will likely be some regulatory lag." (Young Rebuttal Exhibit No. 4, at 3.)

Finally, as addressed in more detail in the following section, the settlement agreements entered into by DEC with some of the parties to this proceeding do not support a grant of deferral accounting. At most, the settlement agreements are merely indicia of some support for certain programs *so long as all the other items in the settlement agreements are fulfilled by DEC*. Moreover, not all parties have joined the settlement agreements. Such qualified and limited support of deferral accounting is not part of the general ratemaking principles set forth in Section 62-133, nor is it part of the Commission's traditional test for deferral. In light of DEC's failure to show (1) that the proposed costs are extraordinary, (2) that, absent deferral, DEC risks financial harm, or even (3) that the programs themselves have widespread support among stakeholders, the settlement agreements can be taken at most as evidence that deferral accounting for some programs would be acceptable to some parties under some circumstances.

In sum, DEC has failed to support its claim for deferral accounting for the GIP under the standard applied by the Commission, and its request should be denied.

B. The Commission provided specific guidance related to deferral of grid modernization costs, but DEC failed to follow that guidance.

DEC and the Public Staff, in supporting the Second Stipulation, seek to invoke guidance offered by the Commission in the 2018 rate case as support for allowing deferral in this case. But the 2018 DEC Rate Order applied to a completely different set of facts, and, in any event, DEC did not follow any part of the Commission's guidance.

In 2018 order, the Commission instructed:

> [t]he Company may seek deferral at a later time outside of the general rate case test year context to preserve the Company's opportunity to recover costs, to the extent not incurred during a test period. In that regard, were the Company in the future *before filing its next rate case to request a deferral* outside a test year and *meet the test of economic harm*, the Commission is willing to entertain a requested deferral for Power Forward, as opposed to customary spend, costs. Should a *collaborative undertaking with stakeholders as addressed herein produce a list of Power Forward projects*, such designation would greatly assist the Commission in addressing a requested deferral. Were the Company to demonstrate that the costs can be properly classified as Power Forward and grid modernization, the Commission would seek to expeditiously address the request and to determine that the Company would meet the "extraordinary expenditure" test and conceptually authorize deferral for subsequent consideration for recovery in a general rate case.
>
> The Commission can authorize a test for approving a deferral within a general rate case with parameters different from those to be applied in other contexts. Consequently, with respect to demonstrated Power Forward *costs incurred by DEC prior to the test year in its next case*, the Commission authorizes expedited

> consideration, and to the extent permissible, reliance on leniency in imposing the "extraordinary expenditure" test.

2018 DEC Rate Order at 148-49 (emphases added); *see also id.* at Decretal Paragraphs 10-12. Notably, in that case, the Commission understood that DEC "would proceed with Power Forward as planned, within the same time frame, even without approval of the Grid Rider." *Id.* at 132-33. In that light, the Commission's guidance is clear: in order to obtain a deferral of grid modernization costs—which the Commission understood would be incurred regardless of the Commission's decision—DEC was to come back *prior to the next rate case* with *a list of projects produced through a collaborative stakeholder process*, which the Commission would use to determine whether expenses *that had already been incurred by that point* would be eligible for deferral. The Commission specifically did not offer leniency with respect to a deferral request for grid modernization costs proposed in *this* rate case.

The Public Staff, in its testimony—and presumably in reaching its settlement with DEC—has misinterpreted the 2018 DEC Rate Order. Public Staff witness Maness provided testimony regarding the application of "leniency" as "appearing to offer possible leniency regarding the magnitude of costs or financial impacts necessary to justify deferral." (Tr. vol. 6, 145-146; *see also* Tr. vol. 20, 537-39.) However, witness Maness's interpretation of the 2018 Order is incorrect. The Commission's offer of leniency was limited to the circumstance in which DEC, having incurred appropriate costs *prior to its next rate case*, applied for deferral accounting. The Commission was not commenting on the availability of leniency regarding the relief sought here: pre-approval of deferral accounting of *future* costs *during the next rate case*.

DEC also has not produced a list of grid modernization projects generated in a collaborative stakeholder process. While it is true that DEC undertook a stakeholder process, that process did not, by all uncontroverted accounts, generate any consensus regarding grid modernization projects that should be pursued by DEC. NC Justice Center *et al*. and NCSEA witness Alvarez noted that although the GIP planning process included changes based on critiques of Power/Forward, "it was made clear that there would be no further changes to the GIP based on stakeholder feedback." (Tr. vol. 16, 459.) Public Staff T. Williamson, a participant in the stakeholder conversations, agreed on cross-examination that "it would be fair to say that there was not global consensus on any grid improvement programs" at the end of the stakeholder process. (Tr. vol. 7, 20.) Vote Solar witness Fitch, who attended all three GIP stakeholder meetings, characterized the plan as "already baked" before it was presented to stakeholders, explaining that he

> cannot characterize the workshops as 'collaborative,' in the true definitional sense of a process where stakeholders would be expected to have more input on shaping the objectives or parameters of the process. In general, the prevailing feeling during workshops was unidirectional information-sharing by the Company. Stakeholders did not appear to play a role in choosing which investments should be selected, or shaping the process by which the Grid Improvement Plan was developed.

(Tr. Vol. 16, 221.)

DEC's evidence that the stakeholder process resulted in changes to the plan is less than convincing. DEC witness Oliver cites the addition of IVVC to the plan and the reduction of targeted undergrounding work and distribution hardening and resiliency work as the most notable changes to DEC's proposed plan, supposedly representing stakeholder feedback from a May 17, 2018 workshop. (Tr. vol. 11, 630-31.) However, the changes from Power/Forward to the GIP primarily represent reductions from a ten-year plan to a three-year plan. Furthermore, witness Oliver's explanation unconvincingly attributes these changes to "stakeholder" feedback rather than the intervening issuance of the Commission's June 22, 2018 Order, which heavily criticized both targeted undergrounding and distribution hardening and resilience. 2018 DEC Rate Order at 146-147. Duke did not propose cutting those programs until after Power/Forward had been rejected by Commission. In any event, despite serious questions raised by stakeholders regarding whether targeted undergrounding (TUG) should be included in grid modernization at all (Oliver Exhibit 11, at 13, 18), DEC told stakeholders it was proposing $57 to $93 million in TUG spending. (Oliver Exhibit 12, at 97.) Ultimately, DEC included nearly $115 million in TUG spending in its filed GIP proposal. (Oliver Exhibit 10, at 3.) It is difficult to see how the changes to the TUG program proposed by DEC actually reflect the stakeholder feedback received. On cross-examination, DEC witness Oliver also conceded that DEC was considering including IVVC in the GIP prior to the start of the stakeholder feedback process. (Tr. vol. 5, 28.) Vote Solar witness Fitch points out that these changes do not appear to have been driven by stakeholder feedback. (Tr. vol. 16, 222.)

Duke's failure to reflect stakeholder feedback in the GIP plan is shown in Oliver Exhibits 12 and 14. Comparing Oliver Exhibit 12, at 97, to Oliver Exhibit 14, at 9, it is clear that DEC made no changes to the GIP based on feedback received at the November 8, 2018 stakeholder meeting by the time of its May 16, 2019 workshop. Unsurprisingly, the summary of the May 16, 2019 workshop indicates significant stakeholder dissatisfaction with the ability of stakeholders to influence the GIP. (Oliver Exhibit 16, at 19-27.)

The reason DEC did not allow more stakeholder input into the GIP or the process of developing the plan was explained aptly by DEC's counsel:

> So when Duke Energy Carolinas and Duke Energy Progress started their stakeholder process, they were already a little pregnant, right? We were coming off Power/Forward proposals from the last rate case, so there were already proposals on the table.

(Tr. vol. 8, 86.)

The final GIP submitted as Oliver Exhibit 10, at 3, reflects a seemingly random set of alterations to the spending amounts proposed by DEC in its workshop materials. (*Compare* Oliver Exhibit 14, at 9, *with* Oliver Exhibit 10, at 3.) For instance, DEC informed workshop participants it was considering $25 to $39 million in spending on oil breaker replacements and then ultimately filed a plan seeking to spend more than $200 million on oil breaker replacements. The stakeholder meeting summaries reflect a proposal of $36 to $58 million for transmission bank replacement, but DEC ultimately proposed over $116 million. The stakeholder meeting notes do not reflect any stakeholder interest in these programs. Significant additions to proposed TUG spending also undercut the claim that the proposed GIP plan reflects stakeholder input. Meanwhile, the ISOP program, which received significant stakeholder support, saw its proposed funding reduced from $30 to $48 million to a final proposal of less than $7 million.

To support DEC's claim of stakeholder input, DEC witness Oliver touted the settlements reached by DEC with a number of parties. (Tr. vol. 4, 125-26.) In addition to the Second Stipulation with the Public Staff, DEC also entered into an Agreement and Stipulation of Settlement with CIGFUR (CIGFUR Settlement); a Settlement Agreement with the Commercial Group (Commercial Group Settlement); a Settlement Agreement with Harris Teeter (Harris Teeter Settlement); an Agreement and Stipulation of Settlement with NC Justice Center *et al*. and NCSEA (NC Justice Center *et al*. and NCSEA Settlement); and an Agreement and Stipulation of Settlement with Vote Solar (Vote Solar Settlement). But these settlements do not support a finding of substantial stakeholder support for the GIP plan as a whole or the individual programs that comprise it, nor do they provide any evidentiary support for the legal test that must be satisfied.

First, the settlements do not reflect the support of all the parties to this proceeding. Specifically, the settlements do not include the Attorney General, Tech Customers, CUCA, Center for Biological Diversity and Appalachian Voices, and NC WARN.

Second, as a general matter, settlement agreements, which resolve a number of issues simultaneously, provide little or no insight into the settling parties' respective stances with regard to any particular issue. Instead, each of the settlement agreements expressly refutes witness Oliver's suggestion that the settlements reflect actual support of the settling parties for the proposed GIP program or deferral accounting. Second Stipulation at 20 (noting "this Second Partial Stipulation reflects a give-and take of contested issues"); CIGFUR Settlement at 7 ("This Stipulation is the product of negotiation and compromise of a complex set of issues, and no portion of this Stipulation is or will be binding on any of the Stipulating Parties unless the entire Agreement and Stipulation is accepted by the Commission."); Commercial Group Settlement at 3 ("[T]his Stipulation . . . reflects a give-and take of contested issues . . . . The provisions of this Settlement do not reflect any position asserted by any of the Settling Parties but instead reflect the compromise and settlement between the Settling Parties as to all of the issued covered hereby."); NC Justice Center *et al*. and NCSEA Settlement at 8-9 ("The provisions of this Stipulation do not reflect any position asserted by any of the Stipulating Parties but reflect instead the compromise and settlement among the Stipulating Parties as to all the issues covered hereby."); Vote Solar Settlement at 5 ("[T]his Stipulation . . . reflects a give-and take of contested issues . . . ."); Harris Teeter Settlement at 2 ("The provisions of this Settlement do not reflect any position asserted by any of the Settling Parties but instead reflect the compromise and settlement between the Settling Parties as to all of the issued covered hereby."). More insight can be gleaned from these parties' witnesses. For instance, NC Justice Center *et al*. and NCSEA witness Stephens recommended the Commission impose cost controls on all GIP programs and indicated the SOG program should not be approved as proposed but rather should be significantly cut. (Tr. vol. 16, 497.) CIGFUR witness Phillips recommended the Commission reject DEC's request for deferral accounting, (Tr. vol. 22, 117), as did

NC Justice Center *et al*. and NCSEA witness Alvarez, (Tr. vol. 16, 425.), and Harris Teeter witness Bieber, (Bieber[11] at 19).

Third, as specifically indicated by the settlement agreements, DEC was not able to obtain consensus stakeholder support even among this limited set of parties for the GIP. Among the settling parties, only Harris Teeter fully supports the proposed plan. Harris Teeter Settlement at 1-2. NC Justice Center *et al.* and NCEA, and Vote Solar all support some, but not all, programs agreed to by the Public Staff. NC Justice Center *et al.* and NCSEA Settlement at 4; Vote Solar Settlement at 3. The Commercial Group "does not oppose or specifically support the approval of a Grid Improvement Plan deferral." Commercial Group Settlement at 2. CIGFUR agreed to support a deferral request "without taking a position on the appropriateness of the individual items comprising" the GIP. CIGFUR Settlement at 3. In sum, contrary to the suggestion of DEC witness Oliver, the settlements reflect limited or no support for the GIP programs proposed by DEC.

Finally, as discussed in section II.A above, DEC has failed to meet the test of financial harm for its requested GIP spending. The settlements do not provide any evidentiary value whatsoever regarding the two-pronged legal test that must be satisfied for the Commission to approve deferral accounting. To the contrary, the actual expert witness testimony sponsored by many of the settling parties does speak to the legal test and, in each case, this testimony helps to demonstrate that

[11] Witness Bieber's testimony was entered into the record, (Tr. vol. 16, 314), but was inadvertently omitted from the transcript. The testimony was added to the official transcript by an errata filing made on October 29, 2020, but was not paginated as part of any transcript volume. The citations for witness Bieber's testimony herein refers to the pagination in the testimony as filed.

DEC has not satisfied its legal burden. For instance, the NC Justice Center *et al.* and NCSEA witness Stephens recommended the Commission impose cost controls on all GIP programs and indicated the SOG program should not be approved as proposed but rather should be significantly cut. (Tr. vol. 16, p. 497.) CIGFUR witness Phillips recommended the Commission reject DEC's request for deferral accounting, (Tr. vol. 22, p. 117), as did NC Justice Center *et al*. and NCSEA witness Alvarez (Tr. vol. 16, 425), and Harris Teeter witness Bieber (Bieber at 19).[12] As illustrated by the following table, there was <u>no</u> expert testimony—other than by DEC's witnesses—fully supportive of DEC's proposal for deferral accounting for GIP expenditures:

Supports GIP Deferral	**Opposes GIP Deferral**	**Other**
Oliver / McManeus	Strunk O'Donnell Alvarez Stephens Phillips Bieber Powers	Maness[13] Von Nostrand and Fitch[14]

While it is true—and DEC places heavy reliance on this fact—that DEC was able to achieve support for (or non-opposition to) a modified GIP plan through individual negotiations with various intervenors, those settlements reflected negotiation and compromise on a range of issues, were based on the exchange of promises of

[12] While these witnesses did not oppose or take issue with the settlement stipulations entered into by their sponsoring clients, they also did not retract their testimony criticizing DEC's deferral accounting request.

[13] Supports deferral accounting based on misreading of 2018 DEC Rate Order.

[14] Offering no position on deferral accounting but critical of the process employed by DEC and deferral accounting in general.

value by DEC to the settling intervenor on matters unrelated to the GIP, and do not change the fact that many of the setting parties' own expert witnesses opposed deferral accounting for the GIP.

In sum, while the Commission indicated DEC should return with stakeholder buy-in prior to this rate case in order to seek deferral of grid modernization spending, along with evidence of financial harm, DEC did not follow that guidance. Instead, DEC returned with a plan with limited stakeholder support, having conducted a "stakeholder process" that many stakeholders apparently believe was mere window dressing. The support DEC is able to show was gained solely through multifaceted settlement agreements.

C. Granting deferral here will weaken the deferral test and encourage similar requests in the future.

Granting deferral in this case would set a bad precedent and provide little protection for ratepayers. As described below, a grant of deferral here will weaken the test for deferral and encourage repeated future use of the deferral mechanism for grid investment. Because deferral accounting shifts risks to ratepayers, the Commission should guard against such an outcome. The risk to ratepayers in this case is increased because there are no metrics by which to judge whether the GIP is successful. And DEC's GIP arrives at a time when grid technology is rapidly evolving and new technological choices are becoming rapidly available.

DEC's GIP proposal is a significant, but pared-down, successor to the $13 billion Power/Forward plan. Nevertheless, given Duke Energy's intent to drive future earnings through grid investment, the Commission should expect that a successful deferral request in this proceeding will invite DEC to submit similar, periodic requests for the "unusual" expenses of modernizing the grid. As NCSEA *et al.* witness Alvarez explained,

> My concern is that, once deferral accounting is approved for a program, the approval will be interpreted as tacit endorsement of the technical or economic merits of the program. This GIP may be only the first of several extraordinary grid investment proposals the Commission will be asked to consider in the next decade, and these proposals are likely to consist largely of continuations of previously approved programs. The fact that the GIP is, in many ways, a 3-year, $2.3 billion subset of the 10-year, $13 billion Power/Forward plan proposed in the last Duke Energy rate cases should cause the Commission significant concern in this regard.

(Tr. vol. 16, 433.)

Because, as shown above, DEC has failed to satisfy either prong of the Commission's test for deferral accounting, approval of deferral accounting in this case will result in significant reduction in the test's usefulness in checking utility spending. There are billions of dollars in grid investments waiting to be made if DEC believes it can obtain favorable rate treatment for those investments. If deferral is granted here, the Commission will be hard-pressed to reject future grid modernization deferral requests for such spending in a non-arbitrary manner.

As noted by Vote Solar witnesses Van Nostrand and Fitch, deferral accounting shifts risks to ratepayers because

> In general, ratepayers' interests are well-served by the reliance on traditional general rate cases for setting rates, and the associated regulatory lag that produces a strong incentive for a utility to hold down costs. Streamlining that process through the use of deferred accounting reduces the regulatory oversight that results from the general rate case process, and largely eliminates the economic incentive from regulatory lag to hold down costs.

(Tr. vol. 16, 297.) As Tech Customers witness Strunk explained, deferral accounting "transfers risks from DEC to its customers." (Tr. vol. 16, 133; *see also* Tr. vol. 20, 55 (CUCA witness O'Donnell describing risk shift to ratepayers).)

The shifting of risk to ratepayers is especially problematic because DEC has provided no metrics by which the Commission can judge if the GIP program is successful—a matter brought home in the Commissioners questions at the hearing. (Tr. Vol. 6, 18-19, 37-39; Tr. Vol. 8, 77-80.) Moreover, the meeting reports show that stakeholders repeatedly asked for the establishment of performance metrics (e.g., Oliver Exhibit 11, at 5-6, 14, 23, 25, 34; Oliver Exhibit 16, at 4, 16-17), but DEC did not incorporate any performance metrics in its plan, further illustrating the lack of stakeholder effect on the GIP. DEC witness Oliver suggested in his rebuttal testimony that DEC "intends to track project/program scope, schedule, costs and benefits as appropriate during implementation." (Tr. vol. 11, 681.) However, those are not metrics by which performance can be judged, and DEC has provided no specific measure for the Commission to consider or judge whether GIP implementation is successful. In fact, the Second Stipulation between DEC and Public Staff suggests that even reporting of the results of the GIP is still a work-in-progress. Second Stipulation at 10-11 (agreeing to "work together to develop biannual reporting requirements to track GIP expenditures"). Public Staff witness T. Williamson agreed that the Public Staff believes it will have better information to evaluate program effectiveness after the programs are implemented. (Tr. vol. 7, 95.)

The flaws in the settlement agreements as discussed above demonstrate the reason why they Commission gave the instructions regarding stakeholder input in the 2018 DEC Rate Order. Private one-on-one settlements in which each side is making trade-offs on unrelated items are not the appropriate venue for developing a plan for prudent expenditure of over a billion dollars.

D. The Commission should reject the Public Staff's agreement not to challenge DEC's "decision to incur" GIP costs.

If the Commission adopts section III.D of Public Staff's Second Stipulation, the Commission will forfeit its ability to review GIP expenses because it will not be able to review DEC's "decision to incur" GIP costs. The Commission should reject this portion of the Second Stipulation. Section III.D provides:

> The Stipulating Parties' agreement regarding deferral treatment of GIP costs constitutes only approval of the decision to incur GIP program costs. The Public Staff reserves the right to review costs for reasonableness and prudence.

Public Staff Second Stipulation at 10.

Despite the reservation of rights, as Public Staff witness Maness testified, the Public Staff believes acceptance of this provision forecloses a full prudence review of the costs incurred and would only allow consideration whether, later on, additional costs become imprudent. (Tr. vol. 7, 54-56.) Witness Maness explained:

> [T]he Public Staff's recommendation is basically consistent with the conclusion that, at this point in time, or at least at the point in time the testimony was filed in this case, that it was reasonable for the Company to start down this road. But subsequent to that point in time, and circumstances change, then the Commission could determine that their reaction to those circumstances should have caused them to depart from the plan that was established right at the first.

(Tr. vol. 7, 55.) Thus, the Commission's ability to reconsider DEC's initial decision to incur GIP program costs would be closed. (Tr. vol. 7, 56.) In response to a question as to whether the Commission's "hands would be tied if [the Second] Stipulation is accepted with respect to at least the decision to incur GIP program costs," DEC witness McManeus likewise testified that,

> I'm not sure if I would say it in exactly that language, but I think I have tried to communicate that it is important that the Commission's approval make clear that they are saying that they believe that the program -- the programs are appropriate and the electric costs that are the outcome of the programs are the types of costs that would be appropriate to recover from customers if they are reasonably and prudently incurred, again, because if we're going to have a regulatory asset on our books, I think, you know, we still bear all of the execution risk of these programs, but I would be -- *I think it would be inappropriate to get to a rate case and have the outcome be, well, you shouldn't have even undertaken these programs to begin with. So I would view the Commission's approval of the deferral accounting as an indication that, yes, these programs seem reasonable and the costs seem of the nature that customers should pay*, given the benefits of the programs, but not -- but, again, exact cost recovery and the ability to disallow cost is still determined in a future rate case, and the Company bears 100 percent of the risk of that execution of the programs.

(Tr. vol. 9, 88-89 (emphasis added).) Furthermore, in the context of N.C. Gen. Stat. § 110.7, DEC previously argued that approval of a "decision to incur" costs means "the Commission will not second guess the utility's decision to incur the necessary investments in project development." DEC Proposed Order, Docket No. E-7, Sub 1146, at 208. Thus, it is clear that both the Public Staff and DEC believe their stipulation—if accepted—would foreclose the Commission's future review of DEC's decision to begin incurring GIP costs. Public Staff witness Maness clarified that

> The Public Staff has taken the position that it is reasonable for the decision -- for them to make the decision to begin incurring costs, but

> I think that the decision to approve deferral accounting, although it's related to that, can be separated, and the Commission could caveat its approval of deferral accounting with any conditions it wishes, including a decision to revisit or possibly revisit the initial decision to begin incurring costs. It's not necessary that the Commission make any finding as to the prudence and reasonableness of that decision in order to approve deferral accounting for costs.

(Tr. vol. 8, 40.)

In the event the Commission approves deferral accounting for any or all of the proposed GIP programs, the Commission should take witness Maness's invitation to reject the Public Staff's approval of DEC's "decision to incur" GIP costs.

Although the Commission should be free to fully consider the prudence of any GIP costs at the time DEC seeks to collect them from ratepayers, the Commission has previously suggested that determination of whether the decision to incur costs was reasonable is part of the prudence analysis:

> When setting just and reasonable rates, the Commission must determine whether costs incurred by the utility were prudently incurred, which involves an examination of whether the utility's actions, inactions or decisions to incur costs were reasonable based on what it knew or should have known at the time the actions, inactions, or decision to incur costs were made.

Order Accepting Public Staff Stipulation in Part, Accepting CIGFUR Stipulation, Deciding Contested Issues, and Granting Partial Rate Increase, Docket No. E-22, Sub 562 (Feb. 24, 2020) at 121 (citing Order Granting Partial Increase in Rates and Charges, Docket No. E-2, Sub 537 (Aug. 5, 1988) at 14, *rev'd in part on other grounds and remanded, Utils. Comm'n v. Thornburg,* 325 N.C. 484, 385 S.E.2d 463 (1989)); *see also* Order Granting In Part and Denying In Part Motion to Strike, Docket No. E-7, Sub 2016 (July 3, 2013) at 4 ("The test for recovery of costs and expenses in a general rate case is whether the costs and expenses are reasonable and prudent. The facts and conditions relevant for determining reasonableness and prudence are those existing at the time that management made the decision to incur the costs and expenses.").

DEC should not be allowed to, and should not, base its decision regarding whether to pursue GIP program expenses upon the Commission's approval or disapproval of deferral accounting. The prudence or imprudence of such decisions should rise or fall on their own merits, not because DEC believes a decision has been made that makes recovery of such costs more likely. DEC has not asked the Commission to approve the prudence of the GIP investments.

Accordingly, any approval of deferral accounting for GIP costs should make clear that the Commission is not approving DEC's decision to incur such costs, leaving all questions of prudence open for future consideration.

III. The Commission Should Reject DEC's Request to Elevate the Company's Credit Metrics Above the Interests of DEC's Ratepayers.

The Commission should reject DEC's argument that the Company will not be able to access necessary capital unless the Commission grants DEC full recovery on all the contested items in this rate proceeding—particularly with regard to coal ash. The Commission has no obligation to cater to DEC's credit ratings, especially when doing so would harm DEC's ratepayers and would not impair DEC's access to the credit market.

During the hearing, DEC repeatedly admonished the Commission to avoid any rulings that might affect the Company's credit ratings, cautioning that any such ruling would harm ratepayers by raising the Company's cost of debt. DEC witness

Steve Young, DEC's Chief Financial Officer, testified of the "implications of the [Commission's] decision[s] on the capital markets." (Tr. vol. 3, 42–43.) Specifically, he cautioned that an adverse determination on coal ash recovery "will cause a lowering of [DEC's] credit ratings" which would make securing "future debt . . . more costly and more difficult" (Tr. vol. 3, 38, 40, 52) and "make it very difficult for [DEC] to get into these markets and have the flexibility that we need on the debt and equity side." (Tr. vol. 3, 71.) Echoing this theme, other DEC witnesses suggested that the Commission would "breach" the "regulatory construct" if it does not allow full recovery in this case. (*See* Tr. vol. 2, 67-68, 73, 74 (Newlin redirect).)

Despite DEC's novel views on the "regulatory construct," North Carolina law makes clear that the Commission has no duty to protect the Company's credit metrics, as DEC itself admitted (Tr. vol. 3, 42), especially at the expense of DEC's ratepayers. Moreover, cross-examination by the Public Staff revealed that DEC has built its case for protecting its credit ratings on a flawed cost-benefit analysis and speculation about its challenges in raising debt. As such, there is no legal or factual basis for DEC's request that the Commission prioritize preservation of its credit metrics as a primary decision-making tool in this proceeding.

A. The Commission is obligated to set rates no higher than what is necessary to allow DEC to obtain capital.

As is well-recognized, "the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the" constitution. *State ex rel. Utils. Comm'n v. Duke Power Co.*, 285 N.C. 377, 388, 206 S.E.2d 269, 276 (1974). Therefore, although the Commission must enable DEC to "compete in the market for capital," the Commission's "ultimate objective of rate making" is to set rates "which will enable the utility to do [this], *and no more*." *State ex rel. Utils. Comm'n v. Gen. Tel. Co. of Se.*, 281 N.C. 318, 370, 189 S.E.2d 705, 738 (1972); *see* N.C. Gen. Stat. § 62-133.

In other words, the Commission must set rates no higher than what is necessary for DEC to secure *adequate* debt; to raise rates further so that DEC can obtain *cheaper* debt would violate the Legislature's directives. As DEC witness Young himself admitted under questioning, the Commission has no duty to "set rates and make decisions so that a company has one of the highest credit ratings" and can secure the best interest rates. (Tr. vol. 3, 42.)

B. The evidence shows that the benefit to ratepayers of protecting DEC's credit rating is dwarfed by the costs in issue.

Witness Young's caution to the Commission that a downgrade to DEC's credit rating will cause customers to suffer from "future debt . . . [being] more costly" does not tell the whole picture.

As an example, witness Young conceded that DEP recently was successful in raising $700 million of debt with a 2.5% interest rate (Tr. vol. 3, 59; Tr. vol. 4, 47), notwithstanding DEP's lower credit ratings (Public Staff Newlin Rebuttal Cross-Examination Exhibit 2). Interest of 2.5% is lower than DEC's current cost of debt of 4.51% (McManeus Exhibit 1, at 2)—which means that if DEC were to secure debt at an interest rate of 2.5%, DEC would *reduce* its cost of debt. In other words, if DEC's debt ratings were downgraded to match DEP's current ratings, DEC could nevertheless secure debt at interest rates that would still *lower the cost of debt* for DEC's customers.

Given the reality of the current credit markets and the availability of very low interest rates, DEC's argument that the Commission should award DEC the full recovery it seeks ($86 million more in the case of coal ash) so that DEC can protect customers from "future debt . . . [being] more costly" misses the forest for the trees. (Tr. vol. 3, 40; *see id.* 70–71.)

Moreover, on cross-examination by the Public Staff, witness Young agreed that, should DEC suffer a downgrade, its cost of debt would increase a mere *five basis points*. (Tr. vol. 3, 69.) Based on DEC's forecast of its debt needs, this would result in an increase of $225,000 in annual interest. (*Id.*) Stated another way, DEC is, in essence, asking the Commission to allow it to recover some $86 million in costs from ratepayers so that it can save them from increased annual interest payments of approximately $225,000.

C. DEC's claim that a denial of full coal-ash recovery would result in higher rates for ratepayers amounts to speculation with little evidentiary value.

DEC's argument to protect its credit ratings is constructed from speculation that is of little evidentiary value. DEC has failed to establish that it will experience a decline in its debt ratings if full recovery is not permitted in this case nor has it established that if the Company's credit is downgraded it will have to pay more to secure debt.

As our Supreme Court has held, the best gauge of a utility's ability to secure debt is "the *actual experience* of [the] utility in the attraction of capital, *under the rates of which it complains*[.]" *State ex rel. Utils. Comm'n v. Gen. Tel. Co. of Se.*, 281 N.C. 318, 371, 189 S.E.2d 705, 739 (1972) (emphasis added). Therefore, the

Commission's should reject witness Young's warning of the debt market's *possible* reaction to a *possible* change to DEC's credit ratings. Two layers of speculation is an inadequate foundation for increasing the rates paid by consumers.

First, witness Young admitted it is not certain that DEC will experience a credit downgrade if full recovery is not granted in this proceeding. For example, Young argued that if DEC does not get a return on coal ash, Duke Energy's Funds from Operations (FFO)/Debt ratio would drop from 15% to 14%, which "will result in a down rating." (Tr. vol. 3, 45–46.) Young conceded, however, that Duke Energy's FFO/Debt ratio has been below 15% in several previous time periods (Tr. vol. 3, 48) with no apparent detrimental impact on Duke's credit rating. Indeed, when pressed on what action the credit agencies might take based on a drop in the FFO/Debt ratio, witness Young demurred—declining to "speak for the credit agencies" and refusing to "say what they will do." (Tr. vol. 3, 45.) DEC has presented no reliable evidence that it will experience a credit downgrade if its full requests for cost recovery in this proceeding are not granted.

There is also no evidence that, if DEC experienced a credit downgrade, it would have a meaningful impact on DEC's ability to raise debt. After the Public Staff's cross-examination disproved the claim that full recovery, particularly with regard to coal ash, would save DEC's customers money, DEC witness Young pivoted to emphasizing that "[t]he point is not what the delta is right now; the point is the ability to access markets over a long term." (Tr. vol. 3, 69.) Witness Young described such access as DEC having "flexibility" over "when [DEC] can go into the marketplace" to raise debt. (Tr. vol. 3, 54, 69.)

But on cross-examination, witness Young admitted that DEC is rather rigid in when it raises debt: "We try to come out of the gate and hit the financing early in the year." (Tr. vol. 3, 58.) Thus, despite the purported value that "flexibility" provides DEC's customers, DEC never established that it actually captures this value. It is speculation that DEC would ever use its "flexibility" when raising debt. Moreover, witness Young admitted that DEC, with a credit rating of Aa2, has one of the "very highest" credit ratings of all electric utilities (Tr. vol. 4, 46), including DEP (Public Staff Newlin Rebuttal Cross-Examination Exhibit 2), Duke Energy Corporation (Tr. vol. 3, 76), and most other comparable electric utilities (Tr. vol. 3, 42). Young conceded on cross-examination that these other utilities were able to access the credit markets on satisfactory terms despite their lower credit quality. (*Id.*) Witness Young further conceded that DEC could similarly operate with a lower credit rating. (*Id.*)

As further evidence that a credit downgrade will *not* imperil DEC's "flexibility" in successfully entering the credit markets, a month before witness Young's testimony, DEP raised $700 million in debt. (Tr. vol. 3, 59; Tr. vol. 4, 47.) Notably, witness Young did not testify that DEP, with its lower debt rating, had any difficulty in raising debt in the midst of a historic recession.

In summary, DEC's argument that the Commission should elevate concerns of maintaining the Company's existing credit metrics as a primary driver of its decisions in this proceeding are legally and factually deficient. Not only does the

Commission have no legal duty to protect the Company's credit metrics as an independent regulatory goal, the cross-examination of DEC witness Young shows that DEC's warnings of the risks of a credit downgrade are alarmist in nature and fail to account for the current low-interest economic environment which entails advantages for debt financing.

IV. The Commission Should Approve a Lower Return on Equity than Stipulated in the Settlement Agreements.

DEC has reached settlement agreements with several parties, including the Public Staff, agreeing to an ROE of 9.6% (the "Settlement ROE"). This Settlement ROE, though, is at the middle of the range of ROEs approved prior to the onset of the ongoing pandemic. As Tech Customers' expert witness Strunk showed in his testimony, the mean awarded ROE was 9.63% for vertically integrated electric utilities from January 1, 2019, to February 19, 2020, with the median being 9.65%. (Tr. vol. 16, 139–40.)

Three factors strongly weigh in favor of DEC receiving a below-average ROE. First, by objective metrics, DEC is less risky than other vertically integrated utilities and, therefore, should have a lower ROE. Second, the expert testimony of multiple parties in this case supports an ROE below 9.6%. Third, an ROE of 9.6% is in the middle of *pre-pandemic* ROEs; consideration of the current economic conditions and challenges warrants a lower ROE.

A. Because DEC is less risky than the average, comparable utility, DEC should have a below-average ROE.

Objective metrics establish that DEC is less risky than comparable electric utilities. DEC has an "Excellent" business risk ranking from Standard & Poor's, which is the highest possible score. (Tr. vol. 16, 142.) Almost half of DEC's proxy group have lower scores. (*Id.*) DEC also received an "Intermediate" financial risk ranking from Standard & Poor's, and all but two in the proxy group have lower rankings. (Tr. vol. 16, 143.) Furthermore, DEC has the "very highest" bond ratings of all electric utilities (Tr. vol. 4, 46), which reinforces the relatively high level of security DEC's investors have compared to other investors in utilities.

Notably, DEC did not attempt to rebut this showing and did not offer evidence to suggest that it might be as risky as or riskier than its peers. Because DEC presents a lower risk than comparable utilities, DEC's investors should be entitled to the opportunity to earn a corresponding lower-than-average ROE—otherwise, DEC's investors will be receiving returns comparable to those offered by riskier investments, from a *safer* investment.

B. The only expert analysis entitled to substantial weight supports an ROE below 9.6%.

An ROE below the stipulated rate of 9.6% is supported by the record. DEC's expert witness D'Ascendis is the lone expert to testify that it would be reasonable to award DEC an ROE as high as 9.6%; all other experts opined the ROE should be lower. But the financial models D'Ascendis used to support his recommended ROE include flaws that the Commission has previously recognized in other orders. Given these flaws, the only reliable evidence in the record supports an ROE below 9.6%.

DEC's witness D'Ascendis testified in support of an ROE above 9.6%—going so far as to advocate for an ROE in the range of 10% to 11%. (Tr. vol. 11, 57.) Every other expert who relied upon independent modeling to generate a proposed ROE opined that DEC's ROE should fall below the settlement ROE of 9.6%. Specifically:

- Public Staff witness Woolridge testified that DEC's ROE should be 9.0% if DEC had 50% equity (or 8.4% if DEC had 53% equity). (Tr. vol. 17, 89–90.)

- Attorney General witness Baudino testified in support of an ROE of 9.0%. (Tr. vol. 16, 318.)

- CUCA witness O'Donnell testified to an ROE of 8.75%. (Tr. vol. 22, 27.)

Not only is D'Ascendis's recommendation of an ROE above 9.6% an outlier among the various expert opinions offered in this proceeding,[15] the key models upon which D'Ascendis relies to support his recommendation—CAPM, ECAPM, and Expected Earnings—have several demonstrable flaws regarding their use of, and reliance on, data projections. In summary:

- D'Ascendis's CAPM and ECAPM models improperly rely on earnings-per-share (EPS) forecasts. The market-risk premium component of his CAPM and ECAPM models uses analyst projected EPS forecasts as the growth component. (Tr. vol. 11, 129–30, 132–33.) The Commission has given no weight to the CAPM analysis of DEC's expert in the past because it was "an outlier and upwardly biased due to [the] risk premium component of his CAPM . . . solely using analysts projected EPS forecasts as the growth component." 2018 DEC Rate Order at 63.

- D'Ascendis further inflates his CAPM and ECAPM models by incorporating projected Treasury rates. (Tr. vol. 11, 344.) The Commission has repeatedly disapproved of models that rely on predictions of future risk-free rates. *E.g.,* Order Accepting Public Staff Stipulation in Part Accepting CIGFUR Stipulation, Deciding Contesting Issues, and Granting Partial Rate Increase, Docket No. E-22, Subs 562 and 566 (Feb. 24, 2020) at 40–41 (2020 Dominion

[15] CIGFUR's witness Phillips testified that DEC's ROE should be below the national average of 9.73% for vertically-integrated utilities from January 1, 2019, to December 31, 2019. (Tr. vol. 22, 120–22.) However, Phillips did not employ independent modeling to support a specific ROE recommendation.

Order) ("approv[ing] of the use of current risk-free rates rather than predicted near-term or long-term rates"); Order Approving Stipulation, Granting Partial Rate Increase, Line 434 Revenue Rider, EDIT Riders, Provisional Revenues Rider, and Requiring Customer Notice, Docket No. G-9, Sub 743 (Oct. 31, 2019) at 41 (2019 Piedmont Order) (same)).

- D'Ascendis's Expected Earnings model also inappropriately relies on projections—i.e., projected earnings for 2022–2024. (D'Ascendis Rebuttal Exhibit DWD-6.) The Commission has rejected reliance on Expected Earnings models as unduly speculative given their reliance on future earnings forecasts. *E.g.,* 2019 Piedmont Order at 43 (ruling the expected earnings model was "entitled to no weight" because the model was "based entirely on projected earnings . . . for the years 2022-2024").

As with these three models that the Commission has rejected in prior rate cases, D'Ascendis's Bond Yield model also suffers from flaws. First, his Bond Yield model seeks merely to calculate the correlation between 30-year Treasury rates and the ROEs awarded by regulatory bodies. (Tr. vol. 11, 138–39.) Thus, this model does not provide empirical evidence of the marketplace returns that utility investors actually earn. (Tr. vol. 16, 373–74.) Second, D'Ascendis, yet again, uses *projected* Treasury rates to inflate the upper-end returns of this model. (Tr. vol. 11, 56.)

In contrast to the data produced by his CAPM, ECAPM, Expected Earnings, and Bond Yield models, witness D'Ascendis's Constant Growth Discounted Cash Flow (DCF) model produced results that are untainted by these analytical flaws; namely, his DCF model does not rely on projections. Accordingly, the Commission has repeatedly found the DCF model presented by utility experts to be highly probative of a reasonable ROE. *See*, *e.g.*, 2019 Piedmont Order at 41 (finding DCF model to be "credible, probative, and entitled to substantial weight"); 2020 Dominion Order at 40 (same).

Notably, the mean result of D'Ascendis's most recently updated DCF analysis is 8.82%—well below the Settlement ROE of 9.6%. (Tr. vol. 11, 344.)

In sum, the only reliable evidence of an appropriate ROE offered by D'Ascendis is his DCF analysis, which supports an ROE well below 9.6%. As stated, the appropriateness of an ROE below 9.6% is also supported by the other expert witnesses performing independent modelling in this case.

C. The ongoing economic recession supports award of an ROE that is below the pre-pandemic average ROE.

If the Commission were to award DEC the Settlement ROE of 9.6%, DEC would be receiving the average ROE that utilities have received in recent years. The onset of the coronavirus pandemic, however, has resulted in perhaps the worst economic recession since the Great Depression.

The Commission must make findings regarding the impact of changing economic conditions on customers when determining the proper rate of return on equity for a public utility. *State ex rel. Utils. Comm'n v. Cooper*, 366 N.C. 484, 495, 739 S.E.2d 541, 548 (2013). "Subsection 62-133(a) does emphasize that fairness to customers is a critical consideration in rate cases by including a directive that 'the Commission shall fix such rates as shall be fair both to the public utilities *and to the consumer*.' *Id.* (quoting N.C. Gen. Stat. § 62-133(a)) (emphasis in original).

As of today, nearly 13 million people are unemployed in the United States. After a modest economic uptick, unemployment rates have currently stalled at

7.9% at the national level.[16] In North Carolina, the seasonally adjusted unemployment rate was at 7.3% as of October 2020.[17]

As the Commission has previously concluded, "[T]he Commission always places primary emphasis on consumers' ability to pay where economic conditions are difficult." 2013 DEP Rate Order at 37. Raising consumers' electricity rates so that DEC—a company that possess less risk that its peers—can earn a ROE that is in line with what its peers earned before the pandemic is not fair to consumers. Indeed, as noted above, more than five-hundred thousand households served by Duke Energy—including some three-hundred thousand in DEC's territory—were considered delinquent on their utility accounts as of June 30, 2020. *See* North Carolina Utilities Commission, Letter to Gov. Cooper re: Implementation by the North Carolina Utilities Commission of Executive Order No. 142, Docket No. M-100, Sub 158 (July 15, 2020) (supporting data summary). With hundreds of thousands of North Carolinians unable to earn any income because of the pandemic-induced recession, the ROE for going-forward rates must be established with a goal of not exacerbating the ongoing crisis.

D. The empirical evidence and current economic conditions support an ROE of in the range of 9.35% to 9.45%.

In light of the guiding legal principles and the evidence before the Commission, a fair and reasonable ROE for DEC is in the range of 9.35% to 9.45%. A return in this range accounts for DEC's lower-than-average risk profile, the

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[16] *See* U.S. Bureau of Labor Statistics, *Employment Situation Summary* (Oct. 2, 2020), *available at* https://www.bls.gov/news.release/empsit.nr0.htm.

[17] *See* U.S. Bureau of Labor Statistics, *Employment and Unemployment Summary* (Oct. 2, 2020), *available at* https://www.bls.gov/news.release/laus.nr0.htm.

opinions offered by the parties' experts, current economic conditions, and the Settlement ROE.

- Objective evidence shows that DEC is less risky than its peers; as such, DEC's investors should earn a return below the average return of its peers. As witness Strunk testified, the mean awarded ROE was 9.63% for vertically integrated electric utilities from January 1, 2019, to February 19, 2020. An ROE of 9.4% is a modest reduction from this mean return and would be appropriate in light of current economic conditions.

- A return in the 9.4% range is roughly the midpoint of the ROEs offered by all of the experts. On the low end, Baudino, Woolridge, and O'Donnell testified that the ROE should be between 8.75% and 9.0%, with the average of their opinions being 8.92%. On the high end, D'Ascendis testified that the ROE should be between 10% and 11%; but, given his use of flawed and previously rejected models, only the low end of D'Ascendic's range should be given any weight. The midpoint of this range of 8.92% and 10% is 9.46%.

- A return in the 9.4% range is the midpoint of the low end of D'Ascendis's range of reasonable ROEs (10.0%) and his only reliable model, the DCF analysis that produced a median return of 8.82%.

- A return in the 9.4% range is a discount to the recent, pre-pandemic ROEs awarded to utilities. The mean return awarded to vertically integrated electric utilities since the beginning of 2019 through February 2020 is 9.63%. Given the economic difficulties ratepayers are now facing because of the pandemic, a discount of 23 basis points from the mean awarded ROE is fair and reasonable.

- A return in the 9.4% range places the Settlement ROE in the context of the empirical evidence before the Commission. The reliable models presented by the experts suggest that investors expect a return below 9.6%. A return of 9.4% gives due weight to the stipulations of many of the parties, while still accounting for the methodologies, opinions, and recommendations of the parties' financial experts.

Therefore, for these reasons, the award of an ROE in the range of 9.35% to 9.45% is supported by the evidence, reflective of the current economic conditions, and fair and reasonable.

V. DEC Has Failed to Properly Justify its Continued Investment in Coal Plants that It Now Seeks to Retire on an Accelerated Basis.

This rate case brings into stark relief an issue that the Commission will be faced with for the foreseeable future—the continued expenditure of significant capital on coal-fired facilities that are slated for early retirement. In this case alone, DEC seeks recovery of some $944 million in capital expenditures for its coal-fired plants during the 2017 and 2018 calendar years. (Tr. vol. 16, 111.)

Here evidence suggests that concerns about investor returns drove decisions regarding certain capital investments. [BEGIN CONFIDENTIAL] [redacted] [END CONFIDENTIAL]

The assessment of prudence is based on information available at the time of the management decision. As the Commission explained:

> [T]he standard for judging prudence is whether management decisions were made in a reasonable manner and at an appropriate time on the basis of what was reasonably known or reasonably should have been known at that time. … [T]his standard … must be based on a contemporaneous view of the action or decision under question.

2018 DEC Rate Order at 247 (internal quotation omitted).

[BEGIN CONFIDENTIAL] [redacted]

[redacted]

A. The Allen Station Presentation.

[redacted]

[redacted]

[redacted] [redacted]

[redacted]

[18] Note that, earlier, the 111th Congress, which had large Democrat majorities in the House and Senate, was unsuccessful in passing carbon legislation.

[redacted]

B. The Cliffside Presentation.

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted] **[END CONFIDENTIAL]** Indeed, only two years later, DEC decided to accelerate the retirements of these very units as part of this rate case. (Spanos Exhibit 1, at 40–41.) **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]**

The result was DEC customers paying for tens of millions of capital investments that could have been avoided. For Cliffside 5, Immel testified that, since 2017, DEC has invested tens of millions of dollars in converting the coal unit to dual fuel optimization. (Tr. vol. 12, 83.)[19] Witness Immel also testified that $150 million has been spent on Allen Units 4 and 5, of which $80 million could have been avoided by committing to an earlier retirement. (Tr. vol. 12, 100-01.) The

[19] Immel testified that DEC invested $125 million to convert Cliffside 5, Cliffside 6, and Belews Creek 1 to dual fuel optimization, plus an additional $120 million for gas pipelines to these units. (Tr. vol. 12, 82.)

expense to customers of DEC's delayed retirement of these coal units is substantial.

In its latest IRP filing, DEC has outlined plans for retiring all of its coal units over the coming decade. Duke Energy Carolinas, LLC 2020 Integrated Resource Plan Update and 2019 REPS Compliance Plan, Docket No. E-100, Sub 165 (Sept. 1, 2020), at 20-21. **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]**

VI. EDIT Should Be Promptly Returned to Customers.

The Tax Cuts and Jobs Act (2017 Tax Act) reduced the corporate tax rate applicable to DEC from 35% to 21%, effective January 1, 2018. Pub. L. 115-97, Title I, § 13001(a), Dec. 22, 2017, 131 Stat. 2096. As a result of the 2017 Tax Act DEC has accumulated some $783 million[20] in EDIT[21] which it is holding on behalf

[20] As originally filed. *See* McManeus Direct Testimony, Exhibit 4, at 1.

[21] EDIT results from the fact that in the early years of a given capital asset, the utility collects more in tax expense from ratepayers than it pays out to the Internal Revenue Service due to the difference in accelerated depreciation for tax purposes and straight-line depreciation for ratemaking purposes. This interest-free loan is reflected as a credit to the utility's accumulated deferred income taxes ("ADIT") liability account. Due to the 2017 Tax Act, DEC's future tax liabilities will be lower than originally anticipated. The

of its customers. In DEC's last rate case, the Commission denied DEC's request to employ $200 million of the EDIT as a cash flow mitigation measure and, instead, required DEC to maintain federal EDIT resulting from the 2017 Tax Act in a regulatory liability account "pending flow back with interest reflected at the overall weighted cost of capital approved in this case of 7.35% in three years or in DEC's next general rate case proceeding, whichever is sooner." 2018 DEC Rate Order, at 196-197.[22] It is this amount which is now before the Commission for disposition.

In their Second Stipulation, the Public Staff and DEC propose that unprotected federal EDIT (together with North Carolina EDIT and deferred revenues related to the provisional over-collection of federal income taxes) be returned to customers through a rider using the levelized rider methodology proposed by the Public Staff over a five-year amortization period. *See* Public Staff Second Stipulation, at 6. The Tech Customers are in accord with this approach, as this is the approach that best balances the need to expeditiously return over-collections to ratepayers and DEC's interest in managing its cash flow.

The Commission, of course, has discretion over how "unprotected" EDIT is returned to ratepayers because those deferred taxes are not subject to IRS normalization rules. Congress intentionally excluded unprotected EDIT because

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amount by which DEC's current ADIT balances exceeds its future income tax liability as a result of the 2017 Tax Act are the excess deferred income taxes ("EDIT") at issue.

[22] Subsequently, the Commission clarified this directive with regard to a separate interest accrual, finding that "all of the EDIT, including the total amount of the protected EDIT and the total amount of the unprotected EDIT resulting from the Tax Act, shall be reflected as a reduction to rate base thereby providing customers the benefit of a return on it in current rates and eliminating the need for a separate interest accrual." Order on Motions for Clarification, Docket No. E-7, Sub 1146 (July 2, 2020).

the assets associated with unprotected assets do not have normal useful lives.[23] The depreciation rates and "lives" referenced by DEC in its original proposal to return unprotected EDIT over twenty years merely reflect the accounting treatment DEC has given these accounts, not the useful life of actual PP&E. There is simply no logical connection between this class of assets and DEC's original proposal for a longer return period.

The longer the period customers are forced to wait for return of the over-collections, the longer the forced loan from ratepayers—which, as the Federal Energy Regulatory Commission has recognized, may be a "necessary evil . . . [b]ut . . . nonetheless an evil" to be mitigated wherever possible. *Buckeye Pipe Line Co.*, 13 FERC ¶ 61267, 61594 (1980) ("Millions of the Americans who use [electricity] live in poverty or on very tight budgets. Those people are in no position to lend money to anybody. A state of affairs that compels them to supply . . . electric companies with long-term credit in amounts that may sometimes seem minuscule on a per capita basis to the affluent but that are almost always material to the poor and to those who are just getting by cannot be viewed complacently."). Returning all unprotected federal EDIT over five years is a reasonable approach that appropriately balances the need to return the over-collections to ratepayers and

[23] For example, DEC previously (in the last rate case) identified the following among its "PPE Other" assets: "AFUDC Debt," "Casualty Loss," "Clearing Cost," "Coal Ash – Capital for tax," "Depreciation Lag," "Hardware Capitalized," "Mixed Service Costs 263A," "ORIG TAX ADJ FED," "Other Adj," "Pension Cost," "Percentage Repair Allowance," "Salvage Artificial Loss," "Salvaged Inventory Proceeds," "SOFTWARE EXPENSED," "TAX EXPENSING," and "WESTINGHOUSE CREDIT." *See* DEC response to NC Public Staff Data Request No. 155-3, Docket No. E-7, Sub 1146 (filed March 22, 2018).

the need to protect both DEC and ratepayers from the shocks that otherwise would result from significant rate decreases followed by rate hikes.

CONCLUSION

For the reasons discussed above, the Tech Customers respectfully request that the Commission issue an order consistent with the arguments and authorities herein and the Partial Proposed Order submitted contemporaneously herewith.

Respectfully submitted, this 4th day of November, 2020.

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Certificate of Service

I hereby certify that a copy of the foregoing *Post-Hearing Brief of the Tech Customers* has been served this day upon counsel for all parties of record in this proceeding by electronic mail.

This the 4th day of November, 2020.

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/s/ Craig D. Schauer