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Nov 06 2019

November 6, 2019

**VIA ELECTRONIC FILING**

Ms. Kimberley A. Campbell, Chief Clerk  
North Carolina Utilities Commission  
Dobbs Building  
430 North Salisbury Street  
Raleigh, North Carolina 27603

*Re: Joint Proposed Order of Virginia Electric and Power Company, d/b/a  
Dominion Energy North Carolina and the North Carolina Utilities  
Commission—Public Staff  
Docket No. E-22, Sub 562  
Docket No. E-22, Sub 566*

Dear Ms. Campbell:

Enclosed on behalf of Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina, is the *Joint Proposed Order of Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina and the North Carolina Utilities Commission—Public Staff* (“Joint Proposed Order”) for filing in the above-referenced proceedings. A Word version of the Joint Proposed Order is being provided via email to [briefs@ncuc.net](mailto:briefs@ncuc.net).

If you have any questions regarding this filing, please do not hesitate to call me. Thank you for your assistance with this matter.

Very truly yours,

/s/Mary Lynne Grigg

MLG:kjg

Enclosure

STATE OF NORTH CAROLINA  
UTILITIES COMMISSION  
RALEIGH

DOCKET NO. E-22, SUB 562  
DOCKET NO. E-22, SUB 566

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. E-22, SUB 562	)	
	)	
In the Matter of	)	
Application of Dominion Energy North	)	JOINT PROPOSED ORDER OF
Carolina for Adjustment of Rates and	)	VIRGINIA ELECTRIC AND POWER
Charges Applicable to Electric Service in	)	COMPANY, D/B/A DOMINION
North Carolina	)	ENERGY NORTH CAROLINA AND
	)	THE NORTH CAROLINA UTILITIES
DOCKET NO. E-22, SUB 566	)	COMMISSION—PUBLIC STAFF
	)	
In the Matter of	)	
Petition of Virginia Electric and Power	)	
Company, d/b/a Dominion Energy North	)	
Carolina for an Accounting Order to Defer	)	
Certain Capital and Operating Costs	)	
Associated with Greenville County	)	
Combined Cycle Addition	)	

HEARD:      Tuesday, July 30, 2019, at 7:00 p.m., Halifax County Historical  
                 Courthouse, 357 Ferrell Lane, Halifax, North Carolina

                 Wednesday, July 31, 2019, at 7:00 p.m., Martin County Courthouse, 305  
                 E. Main Street, Williamston, North Carolina

                 Wednesday, August 7, 2019, at 7:00 p.m., Dare County Courthouse, 962  
                 Marshall C Collins Drive, Manteo, North Carolina

                 Monday, September 23, 2019, at 2:00 p.m., Tuesday, September 24, 2019,  
                 at 9:00 a.m., and Wednesday, September 25, 2019, at 9:30 a.m., in  
                 Commission Hearing Room 2115, Dobbs Building, 430 North Salisbury  
                 Street, Raleigh, North Carolina

BEFORE:      Chair Charlotte A. Mitchell, Presiding  
                 Commissioner ToNola D. Brown-Bland  
                 Commissioner Lyons Gray  
                 Commissioner Daniel G. Clodfelter

APPEARANCES:

For Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina:

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BY THE COMMISSION: On February 27, 2019, pursuant to Commission Rule R1-17(a), Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina (DENC or the Company) filed a Notice of Intent to File a General Rate Application in Docket No. E-22, Sub 562.

On March 1, 2019, Carolina Industrial Group for Fair Utility Rates I (CIGFUR) filed a Petition to Intervene. The Petition was granted by the Commission on March 7, 2019.

On March 25, 2019, Nucor-Steel-Hertford (Nucor) filed a Petition to Intervene. The Petition was granted by the Commission on March 29, 2019.

On March 29, 2019, DENC filed an application for a general rate increase, pursuant to N.C. Gen. Stat. §§ 62-133 and 62-134 and Commission Rule R1-17 (Application), along with a Rate Case Information Report Commission Form E-1 (Form E-1), and the direct testimony and exhibits of Mark D. Mitchell – Vice President, Generation Construction, Richard M. Davis – Director of Corporate Finance and Assistant Treasurer, Robert B. Hevert – Managing Partner at ScottMadden, Inc., Bruce E. Petrie – Manager of Generation System Planning, Jason E. Williams – Director of Environmental Services, Paul M. McLeod – Regulatory Specialist, Robert E. Miller –

Regulatory Analyst, Paul B. Haynes – Director of Regulation, and Bobby E. McGuire – Director of Electric Transmission Project Development & Execution. Also on March 29, 2019, DENC filed an application for an accounting order to defer certain capital and operating costs associated with its Greenville County Power Station (Greenville County CC) in Docket No. E-22, Sub 566. The Company also requested that the Commission consolidate its consideration of this application with the Company’s application for general rate increase in Docket No. E-22, Sub 562.

On April 18, 2019, DENC made an errata filing.

On April 29, 2019, the Commission issued an Order Declaring General Rate Case and Suspending Rates.

On May 2, 2019, the Commission issued its Order Consolidating Dockets, which consolidated this general rate case with DENC’s pending petition for deferral accounting authority to defer post-in-service costs associated with commercial operations of the Greenville County CC in Docket No. E-22, Sub 566.

On May 30, 2019, the Commission issued an Order Scheduling Investigation and Hearings, Establishing Intervention and Testimony Due Dates and Discovery Deadlines and Requiring Public Notice.

On May 31, 2019, the Commission issued an errata order.

On August 5, 2019, DENC filed supplemental direct testimony and exhibits of Witnesses Davis, McLeod, Miller, Haynes, Petrie, and Deanna R. Kesler, as well as applicable supplemental NCUC Form E-1 information report items and supplemental Commission Rule R1-17 information.

On August 14, 2019, DENC filed additional supplemental direct testimony and exhibits of Witness Haynes.

On August 15, 2019, DENC filed its proof of notice.

On August 23, 2019, the North Carolina Utilities Commission—Public Staff (Public Staff) filed the testimony and exhibits of Sonja R. Johnson – Accountant, David M. Williamson – Utilities Engineer, Jack L. Floyd – Utilities Engineer, Michelle M. Boswell – Staff Accountant, Tommy C. Williamson – Utilities Engineer, Roxie McCullar – Consultant at William Dunkel and Associates, Dr. J. Randall Woolridge – Consultant, Jeffrey T. Thomas – Utilities Engineer, Michael C. Maness – Director of the Accounting Division, and Jay B. Lucas – Utilities Engineer. On the same date, Nucor filed the testimony and exhibits of Paul J. Wielgus and Jacob M. Thomas, and CIGFUR filed the testimony and exhibits of Nicholas Phillips, Jr.

On August 27, 2019, the North Carolina Office of the Attorney General (AGO) filed a Notice of Intervention.

On August 28, 2019, the Commission issued an Order Requesting Additional Information.

On September 10, 2019, DENC filed a Motion for Extension of Time to file its rebuttal testimony. The Motion was granted by the Commission on September 11, 2019.

On September 12, 2019, DENC filed second supplemental direct testimony and exhibits of Witness McLeod, supplemental Form E-1 items, and supplemental Commission Rule R1-17 information. Also on September 12, 2019, DENC filed the rebuttal testimony and exhibits of Witnesses Davis, Hevert, McLeod, Miller, Haynes, and Williams

On September 16, 2019, the Commission issued an Order Providing Notice of Commission Questions. Also on September 16, 2019, DENC filed its Witness List.

On September 17, 2019, DENC filed an Agreement and Stipulation of Partial Settlement with the Public Staff (Public Staff Stipulation). Also on September 17, 2019, the Public Staff filed Partial Settlement Joint Testimony of Witnesses Johnson and James S. McLawhorn – Director, Electric Division, and DENC filed testimony in Support of the Agreement and Stipulation of Partial Settlement of Witnesses Davis, Hevert, McLeod, Miller and Haynes.

On September 18, 2019, the Public Staff filed supplemental testimony of Witness Maness. Also on September 18, 2019, the Public Staff filed exhibits and supporting schedules for the joint testimony of Witnesses McLawhorn and Johnson filed on September 17, 2019.

On September 19, 2019, DENC, the Public Staff, and CIGFUR filed motions to excuse witnesses. The motions were granted on September 23, 2019.

On September 23, 2019, DENC filed an Agreement and Stipulation of Settlement with CIGFUR (CIGFUR Stipulation). Also on September 23, 2019, DENC filed a Revised Witness List and Late Filed Exhibits in response to the Commission's Order Providing Notice of Commission Questions.

The public hearings were held as scheduled. The following public witnesses appeared and testified:

Halifax: Tony Burnette, Dean Knight, Chuck Overton, Silverleen Alston.

Williamston: John Liddick, Patrick Flynn, Tommy Bowen, James Wiggins, and Glenda Barnes.

Manteo: Rhett White, Manny Medeiros, John Windley, and Brad Bernard.

Raleigh: No public witnesses appeared.

The matter came on for evidentiary hearing on September 23, 2019. DENC presented the testimony of Witnesses Mitchell, Davis, Hevert, McLeod, Haynes, Miller, and Williams. The testimony and exhibits of DENC Witnesses McGuire, Kessler, and Petrie were stipulated into the record. The testimony and exhibits of Nucor Witnesses Thomas and Wielgus were stipulated into the record. The testimony and exhibits of CIGFUR Witness Phillips were stipulated into the record. The Public Staff presented the testimony of Witnesses Maness, Johnson, Woolridge, and McLawhorn. The testimony and exhibits of Public Staff Witnesses David Williamson, Floyd, Boswell, Tommy Williamson, McCullar, Woolridge, and Thomas were stipulated into the record.

The pre-filed testimony of those witnesses who testified at the evidentiary hearing, as well as all other witnesses filing testimony in this docket, was copied into the record as if given orally from the stand, and their pre-filed exhibits were admitted into evidence.

The Public Staff and DENC filed Late-Filed Exhibits and responses to Commission questions on September 23, 2019, September 26, 2019, September 27, 2019, October 1, 2019, October 2, 2019, October 7, 2019, October 8, 2019, and October 23, 2019.

Proposed orders and briefs were filed by the parties on November 6, 2019.

Various filings made and orders issued in this proceeding are not discussed in this order, but are included in the record of this proceeding.

Based on the entire record in this proceeding, the Commission now makes the following:

### **FINDINGS OF FACT**

#### **Jurisdiction**

1. Virginia Electric and Power Company (VEPCO) is duly organized as a public utility operating under the laws of the State of North Carolina as Dominion Energy North Carolina and is subject to the jurisdiction of the North Carolina Utilities Commission. DENC is engaged in the business of generating, transmitting, distributing, and selling electric power and energy to the public in North Carolina for compensation. DENC is an unincorporated division of VEPCO and has its office and principal place of business in Richmond, Virginia. VEPCO is a wholly-owned subsidiary of Dominion Energy, Inc. (DEI).
2. The Commission has jurisdiction over the rates and charges, rate schedules, classifications, and practices of public utilities operating in North Carolina, including DENC, under Chapter 62 of the General Statutes of North Carolina.
3. DENC is lawfully before the Commission based upon its application for a general increase in its retail rates pursuant to N.C. Gen. Stat. §§ 62-133, 62-133.2, 62-134, and 62-135 and Commission Rule R1-17.
4. The appropriate test period for use in this proceeding is the 12 months ended December 31, 2018, adjusted for certain known changes in revenue, expenses, and rate base.

### The Application

5. In summary, by its general rate case Application, supporting testimony, and exhibits filed on March 29, 2019, in this docket, DENC sought an increase in its non-fuel base rates and charges to its North Carolina retail customers of \$26,958,000, along with other relief, including cost deferrals and changes to its rate design. The Application was based upon a requested rate of return on common equity (ROE) of 10.75%, an embedded long-term debt cost of 4.451%, and DENC's actual capital structure of 53.01% common equity and 46.99% long-term debt, as of December 31, 2018. DENC submitted supplemental filings and testimony after its initial Application and the effect of the Company's supplemental filings was to change its proposed annual base non-fuel revenue requirement increase to \$24,195,000.

### The Stipulation with Public Staff

6. On September 17, 2019, DENC and the Public Staff (Stipulating Parties) entered into and filed the Public Staff Stipulation, resolving all of the issues in this proceeding among the Stipulating Parties aside from issues associated with coal combustion residuals (CCR) costs.

7. After carefully reviewing the Public Staff Stipulation, the Commission finds that the Public Staff Stipulation is the product of give-and-take in settlement negotiations among the Stipulating Parties, and is material evidence entitled to be given appropriate weight by the Commission.

### The Stipulation with CIGFUR

8. On September 23, 2019, DENC and CIGFUR entered into and filed the CIGFUR Stipulation, resolving rate of return and certain cost allocation, rate design, and terms and conditions issues in this proceeding.

9. After carefully reviewing the CIGFUR Stipulation, the Commission finds that the CIGFUR Stipulation is the product of give-and-take in settlement negotiations among DENC and CIGFUR, and is material evidence entitled to be given appropriate weight by the Commission.

### Capital Structure, Cost of Capital, and Overall Rate of Return

10. The capital structure set forth in Section III.A. of the Public Staff Stipulation, consisting of 52.00% common equity and 48.00% long-term debt, is reasonable and appropriate for use by DENC in this case.

11. The embedded cost of debt set forth in Section III.A. of the Public Staff Stipulation of 4.442% is reasonable and appropriate for use by DENC in this case.

12. The overall rate of return that the Company should be allowed the opportunity to earn on the cost of the Company's used and useful property is 7.20%, as set forth in Section III.A. of the Public Staff Stipulation is reasonable and appropriate for use in this docket.

13. The rate of return on common equity that the Company should be allowed the opportunity to earn in this docket is 9.75%, as set forth in Section III.A. of the Public Staff Stipulation, and is reasonable and appropriate for use in this docket.

14. The authorized levels of overall return and rate of return on common equity set forth above are supported by competent, material, and substantial record

evidence, are consistent with the requirements of N.C. Gen. Stat. § 62-133 in light of changing economic conditions, and will allow the Company to maintain its facilities and services in accordance with the reasonable requirements of the Company's customers.

15. With respect to the foregoing findings on the appropriate overall rate of return on rate base and allowed rate of return on common equity for use in this proceeding, the Commission makes the following more specific findings of fact:

a. The overall rate of return on rate base and allowed rate of return on common equity underlying DENC's current base rates are 7.367% and 9.90%, respectively.<sup>1</sup>

b. DENC's current base rates became effective for service rendered on and after January 1, 2017, and have been in effect since that date.

c. In its Application, DENC sought approval for rates which were based on an overall rate of return on rate base of 7.79% and an allowed rate of return on common equity of 10.75%.

d. In the Public Staff Stipulation, the Stipulating Parties seek approval of an overall rate of return on rate base of 7.20% and an allowed rate of return on common equity of 9.75%.

e. The reduction in overall return and return on equity from both DENC's existing base rates and the Application, as reflected in the Public Staff Stipulation, is a substantial economic benefit to DENC's customers.

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<sup>1</sup> Order Approving Rate Increase and Cost Deferrals and Revising PJM Regulatory Conditions, Docket No. E-22, Sub 532 (December 22, 2016) (Sub 532 Order).

f. As reported by Regulatory Research Associates (RRA), the median ROE authorized for vertically integrated electric utilities during the first half of 2019 was 9.73% (compared to 9.57% in 2018). The authorized ROE for vertically integrated electric utilities is in the top third of all jurisdictions rated by RRA in terms of constructive and less risky regulatory environments range from 9.37% to 10.55%, with an average of 9.93%, and a median of 9.95% from 2016 through early September of 2019.

g. The stipulated rate of return on common equity of 9.75% is equal to the lowest rate of return on common equity granted by the Commission for a major electric utility in the last 10 years.

h. The currently authorized allowed rate of return on common equity underlying the base rates of Public Service Company of North Carolina, Inc. (PSNC) and Piedmont Natural Gas Company, Inc. (Piedmont) is 9.70%.<sup>2</sup> The currently authorized allowed rate of return on common equity for Duke Energy Carolinas, LLC (DEC), and Duke Energy Progress, LLC (DEP), is 9.90%.<sup>3</sup>

i. The stipulated allowed rate of return on common equity of 9.75% is consistent with the allowed rates of return on common equity identified above.

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<sup>2</sup> Order Approving Rate Increase and Integrity Management Tracker, Docket No. G-5, Sub 565 (October 28, 2016), and 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 (October 31, 2019).

<sup>3</sup> Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, Docket No. E-7, Sub 1146 (June 22, 2018), and Order Accepting Stipulations, Deciding Contested Issues and Granting Partial Rate Increase, Docket No. E-2, Sub 1142 (Feb. 23, 2018) (2017 DEP Rate Case).

j. The stipulated overall rate of return on rate base of 7.20% and allowed rate of return on common equity of 9.75% are supported by competent, material, and substantial evidence.

k. The evidence indicates that the overall economic climate in North Carolina (and nationally) remains strong, including data and projections from reliable sources that demonstrate: (i) generally consistent with the national rate of unemployment, the rate of unemployment has fallen substantially in North Carolina, peaking at 10% in late 2009 and early 2010 and falling to 3.70% by December of 2018; (ii) unemployment in the DENC counties peaked in late 2009 – early 2010 at 13.41% and had fallen to 4.95% by December 2018; growth in the Gross Domestic Product (GDP) is relatively strongly correlated between North Carolina and the national economy, and has been growing at a moderate pace since 2016; (iii) median household income in North Carolina has grown since 2009 at an annual rate of 2.32%; and (iv) residential electric rates in North Carolina since 2018 remain approximately 13% below the national average.

l. Irrespective of the economic conditions being experienced in North Carolina at this time, which are positive, some customers of DENC will struggle to pay their utility bills under the rate increases authorized herein.

16. The capital structure and rates of return on rate base and common equity set forth in the Public Staff Stipulation and approved by the Commission herein result in a cost of capital which appropriately balances DENC's interest in maintaining both its credit ratings and its ability to obtain equity financing on reasonable terms, and its customers' interest in receiving electric utility service at the lowest possible rate.

### Adjustments to Cost of Service

17. The Public Staff Stipulation provides for certain accounting adjustments, which are set forth in detail at Settlement Exhibit I. The Stipulating Parties agree that the settlement regarding those issues will not be used as a rationale for future arguments on contested issues brought before the Commission. The accounting adjustments outlined in Settlement Exhibit I are just and reasonable to all parties in light of all the evidence presented.

### Federal Excess Deferred Income Taxes – Rider EDIT

18. In this proceeding, the Company is adjusting rates to pass along to North Carolina jurisdictional customers the benefit of excess deferred federal income taxes (federal EDIT) resulting from the Federal Tax Cuts and Jobs Act of 2017. The system-level federal EDIT balance as of December 31, 2017, was \$2.0 billion, of which \$94.7 million was allocable to the North Carolina retail jurisdiction. Company Witness McLeod discusses the Company's proposal to begin amortizing federal EDIT on January 1, 2018.

19. The Public Staff Stipulation provides that DENC should implement a rider, Rider EDIT, to allow for the recovery of federal EDIT of \$1,214,000 (on a pre-income tax basis). This amount includes all unprotected federal EDIT allocable to the North Carolina jurisdiction totaling approximately \$8.0 million partially offset by the refund of approximately \$6.8 million associated with North Carolina jurisdictional protected federal EDIT amortization attributable to the 22-month period of January 1, 2018 through October 31, 2019.

20. DENC shall implement Rider EDIT to recover certain federal EDIT from customers over a two-year period on a levelized basis, with a return. As reflected on Settlement Exhibit II, the appropriate amount to be recovered from customers is a total of \$1,299,369. Rider EDIT should be calculated and reviewed using the methodology presented in the testimony of Company Witness Haynes.

21. The Company's fully-adjusted cost of service includes the income tax benefit arising from the annual amortization of protected EDIT during the test year, thereby incorporating a going-level of federal EDIT amortization in base non-fuel rates.

22. The ratemaking treatment of federal EDIT, including Rider EDIT as set forth in the Public Staff Stipulation, is just and reasonable to all parties in light of all the evidence presented.

#### Base Fuel Factor

23. The Public Staff Stipulation provides for a total decrease in DENC's annual base fuel revenues of \$2.155 million from its North Carolina retail electric operations, based on a base fuel factor of 2.092 cents per kilowatt-hour (kWh) (including regulatory fee), which is just and reasonable to all parties in light of all the evidence presented.

24. The base fuel factor should be differentiated between customer classes as provided on Company Additional Supplemental Exhibit PBH-1, Schedule 1, Page 2.

25. The Company has proposed to adjust its base fuel and non-fuel expenses to reflect 71% as a proxy for the fuel cost component of energy purchases for which the actual fuel cost is unknown (Marketer Percentage), with the remaining 29% of the cost of energy purchases being recovered by DENC in base rates. This represents a reduction

from the Company's current Marketer Percentage of 78%. The 71% Marketer Percentage is reasonable and appropriate for use in this proceeding, and shall remain in effect until the Company's 2021 annual fuel factor filing or next general rate case, whichever comes first.

#### Cost of Service Allocation Methodology

26. The Public Staff and CIGFUR Stipulations provide for the use of the Summer-Winter Peak and Average (SWPA) methodology calculated using the system load factor to weight the average component and  $(1 - \text{system load factor})$  to weight the peak demand component to allocate the Company's cost of service to the North Carolina jurisdiction and among the customer classes in this case. The Stipulating Parties and CIGFUR agree that use of the SWPA methodology for allocation between jurisdictions and among customer classes shall not be a precedent for, and may be contested in, future general rate case proceedings. The Stipulating Parties further agree that the Company's proposed adjustments i) to DENC's recorded summer and winter peaks to recognize the peak demand contributions of non-utility generators (NUGs) interconnected to the Company's distribution system, and ii) to remove the demand and energy requirements of three customers, one wholesale customer, NCEMC, and two large industrial customers, in the Company's Virginia jurisdiction for whom the obligation to provide generation service has ended or will end during 2019 are appropriate and reasonable. The SWPA cost of service methodology, adjusted as described, is appropriate for determining the Company's North Carolina jurisdictional and retail customer class cost allocation and responsibility for purposes of this case.

27. DENC's adjustment to the peak component of SWPA appropriately recognizes the impact that NUGs have on DENC's utility system and is appropriate for use in this proceeding.

28. DENC's adjustment to remove the demand and energy requirements of customers whose service has ended or will end during 2019 is appropriate for use in this proceeding.

29. The SWPA cost of service methodology, as adjusted by DENC, has been used in this Order to determine the appropriate levels of rate base, revenues, and expenses for North Carolina retail service.

30. DENC's continued use of the SWPA methodology in this proceeding properly assigns production plant costs to all customer classes, including the Schedule NS Class, in recognition of its significant use of the Company's generation throughout the year.

#### Rate Design

31. For purposes of apportioning and assigning the approved increase in base non-fuel and base fuel revenues between the North Carolina customer classes in this proceeding, the apportionment shall be consistent with the principles described in the testimony of Public Staff Witness Floyd and the rate design presented by Company Witness Haynes in his direct testimony, as adjusted by and as referenced in Section VI of the Public Staff Stipulation, which are reasonable, appropriate, and nondiscriminatory. The Public Staff Stipulation further provides that in developing rates based upon the foregoing class apportionment, the Company consider the rate of return indices for the LGS and 6VP classes and an appropriate rate of return index for the Schedule NS class.

Finally, the Public Staff Stipulation provides that all classes should share in the total base revenue increase.

#### Terms and Conditions

32. The rate design principles and service regulations proposed by the Company, as filed and updated throughout this proceeding, are reasonable.

#### Quality of Service

33. Consistent with Section IX of the Public Staff Stipulation, the overall quality of electric service provided by DENC is good.

#### Acceptance of Stipulations

34. Based upon all of the evidence in the record, including consideration of the public witness testimony and the evidence from parties who have not agreed with the Public Staff and CIGFUR Stipulations, the provisions of the Stipulations are just and reasonable to the customers of DENC and to all parties to this proceeding, and serve the public interest. Therefore, the Stipulations should be approved in their entirety. In addition, the Stipulations are entitled to substantial weight and consideration in the Commission's decision in this docket.

35. The base non-fuel and base fuel revenues approved herein are just and reasonable to the customers of DENC, to DENC, and to all parties to this proceeding, and serve the public interest.

#### Revenue Requirement

36. After giving effect to the approved Stipulations and the Commission's decision on contested issues, the annual revenue requirement for DENC will allow the Company a reasonable opportunity to earn the rate of return on its rate base.

37. As soon as practicable following the issuance of this Order, DENC should calculate and file the annual revenue requirement with the Commission, consistent with the findings and conclusions of this Order. The Company should work with the Public Staff to verify the accuracy of the filing. DENC should file schedules summarizing the gross revenue and the rate of return that the Company should have the opportunity to achieve based on the Commission's findings and determinations in this proceeding.

Just and Reasonable Rates

38. The base non-fuel and base fuel revenues approved herein are just and reasonable to the customers of DENC, to DENC, and to all parties to this proceeding, and serve the public interest.

**EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1-4**

The evidence supporting these findings of fact and conclusions is contained in the verified Application and Form E-1 of DENC, the testimony and exhibits of the witnesses, and the entire record in this proceeding. These findings and conclusions are informational, procedural, and jurisdictional in nature, and are not contested by any party. In addition, the Commission finds and concludes that the Company's use of a test period of the 12 months ended December 31, 2018, with appropriate adjustments for certain known changes in revenue, expenses, and rate base, comports with the requirements of N.C. Gen. Stat. § 62-133 and Commission Rule R1-17, and is appropriate for use in this proceeding.

## EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence supporting this finding of fact and conclusions is contained in the verified Application and Form E-1 of DENC, the testimony and exhibits of the witnesses, and the entire record in this proceeding.

### Summary of the Evidence

On February 27, 2019, pursuant to Commission Rule R1-17(a), DENC filed notice of its intent to file a general rate case application.

On March 29, 2019, DENC filed its Application and initial direct testimony and exhibits, seeking a net increase of \$26,958,000 in its annual base non-fuel rate revenue from its North Carolina retail electric operations. The Application is based on a requested ROE of 10.75%, an overall rate of return of 7.79%, an embedded long-term debt cost of 4.451%, and DENC's actual capital structure of 53.01% common equity and 46.99% long-term debt, as of December 31, 2018. Further, the Application states that DENC's 2018 return on equity was 7.52% and its overall rate of return was 6.08%.

The Company's last general rate case was in 2016 in Docket No. E-22, Sub 532 (2016 Rate Case or Sub 532). By Order issued on December 22, 2016, the Commission approved an increase in DENC's base non-fuel revenues of \$34,732,000, and a decrease of \$8,942,000 in its base fuel revenues. DENC's current authorized ROE is 9.9%, its authorized overall rate of return is 7.367%, and its authorized capital structure for ratemaking purposes is 51.75% common equity and 48.25% long-term debt. On March 4, 2019, the Commission approved a base non-fuel revenue reduction of \$14,349,000 in Docket No. E-22, Sub 560, due to the net reduction in the Company's revenue requirement (i.e., the income tax expense component in then-current base rates)

associated with the reduction in the federal corporate income tax rate pursuant to the Federal Tax Cuts and Jobs Act of 2017.

In its present Application, the Company proposed to implement the non-fuel base rate increase on a temporary basis subject to refund effective on November 1, 2019, along with an accelerated implementation of its new lower base fuel rate – to be filed in August 2019 – as part of any temporary rates (subject to refund) proposed to become effective November 1, 2019. The Company also proposed a methodology for returning certain federal EDIT to customers through a decrement rider, Rider EDIT, over a one-year period. Further, DENC proposed to amortize the post-in-service costs of the Greenville County CC it had requested to defer in Docket No. E-22, Sub 566.<sup>4</sup>

In its supplemental testimony filed on August 5, 2019, DENC updated the increase sought in its non-fuel base rates and charges to its North Carolina retail customers to \$24.9 million.

In its second supplemental testimony filed on September 12, 2019, DENC updated the increase sought to \$24.2 million.

#### Discussion and Conclusion

The Commission finds and concludes that DENC's Application satisfies the requirements of N.C. Gen. Stat. § 62-133, et seq., and Commission Rule R1-17. Further, DENC is a public utility within the meaning of N.C. Gen. Stat. § 62-3(23). Therefore, pursuant to N.C. Gen. Stat. § 62-30, et seq., the Commission has jurisdiction to consider and decide DENC's Application for a rate increase and other relief.

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<sup>4</sup> Consolidated into Docket No. E-22, Sub 562 by Commission *Order Consolidating Dockets* (May 2, 2019).

## EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 6-7

The evidence supporting these findings of fact and conclusions is contained in the testimony of DENC Witnesses Davis, McLeod, Hevert, Miller, and Haynes, Public Staff Witnesses McLawhorn and Johnson, and the entire record in this proceeding.

### Summary of the Evidence

On September 17, 2019, the Stipulating Parties filed the Public Staff Stipulation resolving all issues except the recovery of the Company's CCR costs. The Public Staff Stipulation is based on the same test period as the Company's Application. In summary, the Public Staff Stipulation provides:

- the revenue requirement increase of \$24,879,000 proposed by the Company in its August 5, 2019, supplemental filing should be reduced by at least \$13,517,000, based on the Company's position of an increase in the revenue requirement of \$6.428 million, consisting of an increase of \$8.583 million in non-fuel revenues and a decrease of \$2.155 million in base fuel revenues, and the Public Staff's position of an increase in the revenue requirement of \$2.037 million, consisting of an increase in \$4.192 million in non-fuel revenues and a decrease of \$2.155 million in base fuel revenues, with the difference between the Company's and the Public Staff's positions resulting from the unresolved issues identified at Section II.A.i of the Public Staff Stipulation (cost recovery of the Company's CCR costs, the recovery amortization period, and return during the amortization period);
- an ROE of 9.75% and an overall rate of return on rate base of 7.20%;

- a capital structure for ratemaking purposes consisting of 52% equity and 48% long-term debt;
- an embedded cost of debt of 4.442%;
- agreement on numerous adjustments to the Company's cost of service;
- a \$2.155 million decrease in DENC's annual base fuel revenues and a base fuel factor of \$0.02092 per kWh, including regulatory fee;
- a decrement Rider A1, equal to (\$0.00375) per kWh on a jurisdictional basis, calculated as the difference between the currently approved Rider B Experience Modification Factor (EMF) of \$0.00388 per kWh and the proposed Rider B EMF in the Company's 2019 Fuel Case (Docket No. E-22, Sub 579) of \$0.00013 per kWh;
- a Rider EDIT allowing for the recovery of \$1,214,000 of federal EDIT, which includes the amortization of all unprotected federal EDIT totaling approximately \$8.0 million partially offset by the refund of approximately \$6.8 million associated with federal EDIT amortization attributable to the 22-month period of January 1, 2018, through October 31, 2019;
- allocation of the Company's cost of service based on the SWPA method, including adjustments to recognize the peak demand contributions of NUGs interconnected to the Company's distribution system and to remove the demand and energy requirements of three customers in DENC's Virginia jurisdiction for whom the obligation to provide generation service has ended or will end during 2019;

- inclusion of certain wet-to-dry conversion costs at the Chesterfield Power Station (Chesterfield) in the revenue requirement, subject to a similar dispute pending in the Company's Virginia jurisdiction; and
- agreement that the overall quality of electric service provided by DENC is good.

In support of the Public Staff Stipulation, Company Witness McLeod testified that DENC, the Public Staff, and intervenors engaged in substantial discovery regarding the matters addressed in the Public Staff Stipulation. Witness McLeod further testified that the Public Staff Stipulation is the result of give-and-take negotiations in which each party made substantial compromises on individual issues in order to obtain a compromise from the other parties on other issues. He stated that the Stipulating Parties believe the results reached are fair to the Company and its customers. Witness McLeod also noted that the Public Staff Stipulation resolves all but one contested issue in the case between the Stipulating Parties without the necessity of contentious litigation. With respect to the contested issue not resolved by the Public Staff Stipulation, Witness McLeod explained that \$4.3 million of the CCR costs would be resolved outside of the Public Staff Stipulation as the Company would not support the "equitable sharing" methodology for these remaining CCR costs. (Tr. Vol. 4 at 334-341).

Company Witness Hevert also filed testimony in support of the Public Staff Stipulation and testified that the 9.75% ROE agreed to in the Public Staff Stipulation reflects negotiations among the Stipulating Parties and, taken as a whole with the rest of the Public Staff Stipulation, would be viewed by the financial community as constructive and equitable. Witness Hevert acknowledged that the 9.75% Stipulation ROE falls below

his recommended range of 10.00% to 11.00%, but noted that the Stipulated ROE is a reasonable resolution of a complex and frequently contentious issue. (Tr. Vol. 4 at 115-119).

Company Witness Davis' testimony in support of the Public Staff Stipulation's capital structure of 52.00% equity and 48.00% long-term debt stated that while differing from the recommendation in his direct testimony, the stipulated capital structure represents a reasonable compromise when considered within the context of the Public Staff Stipulation taken as a whole. (Tr. Vol. 4 at 231-233).

Company Witness Miller's testimony in support of the Public Staff Stipulation supported the cost of service issues agreed upon in the Public Staff Stipulation and provided updated schedules with a fully adjusted cost of service study showing the effects of all adjustments and rate changes to the North Carolina classes based on the Public Staff Stipulation. (Tr. Vol. 4 at 538-542).

Finally, DENC Witness Haynes' testimony in support of the Public Staff Stipulation explained the cost allocation, revenue apportionment, rate design, and cost of service studies agreed upon in the Public Staff Stipulation. Witness Haynes testified that the Public Staff Stipulation presents a just and reasonable approach to establishing the cost of service for the Company's North Carolina jurisdiction using the SWPA allocation methodology. He also explained that the SWPA methodology used the system load factor to weight the average component and the peak demand component, which was the same approach proposed in the Company's direct and rebuttal testimony, as well as the approach supported by Public Staff Witness Floyd. Witness Haynes also explained that

the Company still proposed to include decrement Rider A1 to mitigate the effect of the November 1, 2019, base non-fuel increase. (Tr. Vol. 4 at 485-490).

Public Staff Witnesses McLawhorn and Johnson filed joint testimony in support of the Public Staff Stipulation. They testified to the Public Staff's perception of several benefits provided by the Public Staff Stipulation, including a reduction in the base non-fuel revenue increase initially requested by DENC and the avoidance of protracted litigation between the Stipulating Parties. Similar to DENC Witness McLeod, Witnesses McLawhorn and Johnson stated that the CCR costs issue was not resolved in the Public Staff Stipulation and therefore the accounting and ratemaking adjustments cannot be finalized until the Commission makes a determination on that issue. (Tr. Vol. 6 at 52).

#### Discussion and Conclusions

As the Public Staff Stipulation has not been adopted by all of the parties to this docket, the Commission's determination of whether to accept or reject the Public Staff Stipulation is governed by the standards set out by the North Carolina Supreme Court in *State ex rel. Utilities Commission v. Carolina Utility Customers Association, Inc.*, 348 N.C. 452, 500 S.E.2d 693 (1998) (*CUCA I*), and *State ex rel. Utilities Commission v. Carolina Utility Customers Association, Inc.*, 351 N.C. 223, 524 S.E.2d 10 (2000) (*CUCA II*). In *CUCA I*, the Supreme Court held that

[A] stipulation entered into by less than all of the parties as to any facts or issues in a contested case proceeding under Chapter 62 should be accorded full consideration and weighed by the Commission with all other evidence presented by any of the parties in the proceeding.

The Commission must consider the nonunanimous stipulation along with all the evidence presented and any other facts the Commission finds relevant to the fair and just determination of the proceeding. The Commission may even adopt the recommendations or provisions of the nonunanimous stipulation as long as the Commission sets forth its reasoning and makes "its own independent conclusion" supported by

substantial evidence on the record that the proposal is just and reasonable to all parties in light of all the evidence presented.

348 N.C. at 466, 500 S.E.2d at 703.

However, as the Court made clear in *CUCA II*, the fact that fewer than all of the parties have adopted a settlement does not permit the Court to subject the Commission's Order adopting the provisions of a non-unanimous stipulation to a "heightened standard" of review. 351 N.C. at 231, 524 S.E.2d at 16. Rather, the Court said that Commission approval of the provisions of a non-unanimous stipulation "requires only that the Commission ma[k]e an independent determination supported by substantial evidence on the record [and] ... satisf[y] the requirements of chapter 62 by independently considering and analyzing all the evidence and any other facts relevant to a determination that the proposal is just and reasonable to all parties." *Id.* at 231-32, 524 S.E.2d at 16.

The Commission gives substantial weight to the testimony of DENC Witness McLeod regarding the Stipulating Parties' efforts in negotiating the Public Staff Stipulation. Further, the Commission gives significant weight to the settlement testimony of Public Staff Witnesses McLawhorn and Johnson, which in their discussion of the benefits that the Public Staff Stipulation will provide to customers and their testimony describing the compromise reflected in the Public Staff Stipulation's terms, indicate the Public Staff's commitment to fully represent the using and consuming public.

As a result, the Commission finds and concludes that the Public Staff Stipulation is the product of the give-and-take between the Stipulating Parties during their settlement negotiations in an effort to appropriately balance DENC's need for increased revenues and its customers' needs to receive safe, adequate, and reliable electric service at the lowest possible rates. In addition, the Commission finds and concludes that the Public

Staff Stipulation was entered into by the Stipulating Parties after substantial discovery and negotiations, and that it represents a proposed negotiated resolution of the matters in dispute in this docket. As a result, the Public Staff Stipulation is material evidence to be given appropriate weight in this proceeding.

### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8-9**

The evidence supporting these findings of fact and conclusions is contained in the testimony of DENC Witnesses Davis, Hevert, Miller, and Haynes, CIGFUR Witnesses Wielgus and Thomas, and the entire record in this proceeding.

#### Summary of the Evidence

On September 23, 2019, DENC and CIGFUR (CIGFUR Stipulating Parties) filed the CIGFUR Stipulation resolving certain issues related to rate of return and cost allocation, rate design, and terms and conditions. In summary, the CIGFUR Stipulation provides:

- the Company's SWPA methodology calculated using the system load factor to weight the average component and (1 - system load factor) to weight the peak demand component is appropriate for use in allocating the Company's per books cost of service to the North Carolina jurisdiction and between customer classes in this case;
- DENC and CIGFUR agree to the two adjustments the Company made in the course of calculating the SWPA;
- in the next general rate case, the Company should file the results of a class cost of service study with production and transmission costs allocated on the basis of the Summer/Winter Coincident Peak method in addition to the

SWPA used in this proceeding and consider such results for the sole purpose of apportionment of the change in revenue to the customer classes; and

- considering that no customers have taken service under the pilot Real Time Pricing (RTP) rates filed by the Company and approved by the Commission in Sub 532, the Company will work with CIGFUR to consider whether certain provisions within those rates should be modified. If there is mutual agreement between CIGFUR and DENC to such modifications, and CIGFUR indicates that at least one of its member customers is willing to take service under such rates, DENC agrees to re-file such rates with the Commission for approval with the modifications agreed upon within 60 days of such agreement.

At the hearing, Company Witnesses Haynes and Miller stated their support for the CIGFUR Stipulation in the summaries of their testimonies. Witness Haynes stated that the CIGFUR Stipulation presents a just and reasonable approach to establishing the Company's North Carolina jurisdictional cost of service and class cost of service for the allocation of production and transmission plant costs and related expenses based on the SWPA allocation methodology. He indicated that the Company believes the CIGFUR Stipulation represents a reasonable compromise of the allocation and rate design issues in this case, is fair to all parties, and should be approved by the Commission. Mr. Miller stated that the CIGFUR Stipulation represents a reasonable compromise of the cost of service issues in this case, is fair to all parties, and should be approved by the Commission. (Tr. Vol. 4 at 497, 545).

## Discussion and Conclusions

As with the Public Staff Stipulation, because the CIGFUR Stipulation has not been adopted by all of the parties to this docket, the Commission's determination of whether to accept or reject the CIGFUR Stipulation is governed by the standards set out by the North Carolina Supreme Court in *CUCA I* and *CUCA II*.

The Commission gives weight to the testimony of DENC Witnesses Haynes and Miller regarding the Company's support for the CIGFUR Stipulation. The Commission also gives weight to CIGFUR's agreement to the issues identified in the Stipulation.

As a result, the Commission finds and concludes that the CIGFUR Stipulation is the product of the give-and-take between the CIGFUR Stipulating Parties during their settlement negotiations in an effort to appropriately balance DENC's need for increased revenues and CIGFUR's interest in advocating for its member customers. In addition, the Commission finds and concludes that the CIGFUR Stipulation was entered into by the CIGFUR Stipulating Parties after discovery and negotiations, and that it represents a proposed negotiated resolution of the matters in dispute in this docket. As a result, the CIGFUR Stipulation is material evidence to be given appropriate weight in this proceeding.

## **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 10-11**

### Capital Structure

The evidence supporting this finding of fact and conclusions is contained in the testimony and exhibits of Company Witness Davis, Public Staff Witness Woolridge, CIGFUR Witness Phillips, and the Public Staff and CIGFUR Stipulations, as well as testimony and exhibits presented at the hearing of this matter.

In his prefiled direct testimony, DENC Witness Davis proposed a capital structure consisting of 53.01% common equity and 46.99% long-term debt, DENC's capital structure as of December 31, 2018. He discussed the Company's significant capital needs going forward, and explained how the Company plans to finance those capital needs, based on a balance of debt and common equity that DENC believes will support the Company's credit ratings going forward, and continue to enable the Company to access a number of markets, under a wide range of economic environments, on reasonable terms and conditions. Witness Davis stated that this market access is critical to fund the ongoing infrastructure capital expenditure programs that will be necessary to meet the Company's public service obligations in North Carolina and throughout its system. (Tr. Vol. 4 at 204-209, 214-217).

In his supplemental testimony, Mr. Davis updated the Company's proposed capital structure to its actual structure as of June 30, 2019, which reflected a long-term debt component of 46.351% and an equity component of 53.649%. Based on the Company's proposed updated cost rates for long-term debt and common equity, Mr. Davis' proposed updated capital structure produced an updated overall weighted-average cost of capital of 7.826%. (Tr. Vol 4 at 219-220).

Public Staff Witness Woolridge testified that the Company's proposed capital structure included more common equity than the average of the proxy group he used in conducting his analysis. He stated that it is appropriate to use the common equity ratios of the parent holding companies and that the high debt ratio and low equity ratio of DEI is a credit negative for DENC as evaluated by Moody's. He noted, however, that because DENC is a regulated business, it is exposed to less risk and can carry relatively more debt

in its capital structure than most unregulated companies, like DEI. Dr. Woolridge further testified that DENC should take advantage of its lower business risk to employ cheaper debt capital at a level that will benefit its customers through lower revenue requirements and, as a result, recommended a capital structure of 50.0% common equity and 50.0% debt based on a 9.0% rate of return on common equity. Dr. Woolridge also made an alternative capital structure recommendation of the Company's actual capital structure as of December 31, 2018, of 46.35% long-term debt and 53.65% common equity based on an 8.75% return on equity. (Tr. Vol. 6 at 552-562).

CIGFUR Witness Phillips testified that DENC's proposed capital structure includes more equity and less debt than other electric utilities and recommended a capital structure not to exceed 52.00% common equity. In support of his recommendation, Witness Phillips analyzed the proxy groups that he claimed met the various jurisdictional regulatory capital structures of a comparable group of electric utility companies. He referenced groups that consisted of all electric utilities nationwide with equity ratios determined in the first half of 2019 and North Carolina gas and electric utilities that have had authorized ROEs approved in recent years. Witness Phillips concluded that the Company's proposed capital structure was inconsistent with those authorized by the Commission in recent rate cases. (Tr. Vol 6 at 412, 416, 429-431).

In his rebuttal testimony, Mr. Davis testified that Mr. Phillips' recommendation ignores the Company's actual capital structure as of June 30, 2019, as well as DENC's capital structure at year-end of each of the previous three years in favor of arbitrarily developed structures. Mr. Davis stated that it is important that the Company's actual capital structure be considered in determining the appropriate capital structure for

purposes of this rate case because imputing the structure of other peer utilities in different jurisdictions can lead to erroneous conclusions. He also explained that the Company's financing plan is structured to maintain the Company's current credit ratings, which provide the greatest benefit to customers in the long-term. Mr. Davis stated that an arbitrarily derived capital structure could be viewed negatively by the Company's credit agencies. Finally, Witness Davis explained that using the Company's actual capital structure helps to support the significant capital spending program the Company has and continues to undertake to enhance and improve DENC's generation and transmission infrastructure. (Tr. Vol. 6 at 221-229).

Under Section III.A of the Public Staff Stipulation, the Stipulating Parties proposed a capital structure of 52% common equity and 48% long-term debt. In their stipulation testimony, Company Witness Davis and Public Staff Witnesses Johnson and McLawhorn testified that the capital structure reflected in the Public Staff Stipulation represents a compromise by both parties in an effort to reach agreement and is in the public interest. Witness Davis testified that the capital structure represented in the Stipulation provides an equity ratio that is 165 basis points lower than the Company's request of 53.649%, 200 basis points higher than the Public Staff's initial recommendation presented in Witness Woolridge's testimony, and 25 basis points higher than the equity ratio authorized in the 2016 Rate Case. Mr. Davis stated that he, like the Public Staff witnesses, believes the end result of the settlement is fair and reasonable with respect to both ratepayers and shareholders, and that such a ratio will allow the Company to continue providing safe and reliable service to its customers. (Tr. Vol. 6 at 51-52, Vol. 4 at 231-233).

In the CIGFUR Stipulation, CIGFUR and DENC stipulated that it was appropriate to use a capital structure consisting of 52% equity and 48% long-term debt.

In evaluating the evidence on capital structure in this proceeding, the Commission first notes that the equity/debt ratios reflected in the Stipulation of 52.00% equity and 48.00% long-term debt are consistent with and well within the prior experience of the Commission.<sup>5</sup> These are not determinative factors from the Commission's perspective, but they do provide some context supporting the reasonableness of the stipulated capital structure.

Based upon its own review and independent analysis of the evidence, the Commission concludes that a capital structure of 52.00% equity and 48.00% long-term debt, as is reflected in the Public Staff Stipulation, is just and reasonable and appropriate for use in this proceeding on several grounds.

First, this capital structure is very close, i.e., 25 basis points, to the capital structure authorized for DENC in its last rate case. Second, this capital structure was accepted by CIGFUR in the CIGFUR Stipulation. Third, while the Commission recognizes that Public Staff Witness Woolridge recommended a 50% common equity and 50% debt capital structure based on a 9.00% ROE as his primary recommendation, he also proposed use of the actual capital structure as of December 31, 2018, of 46.351%

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<sup>5</sup> See Sub 532 Order (51.75% common equity and 48.25% debt); Order Approving Rate Increase and Integrity Management Tracker, Docket No. G-5, Sub 565 (October 28, 2016) (52.0% common equity, 44.62% long-term debt, 3.38% short-term debt); 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 (October 31, 2019) (52.00% equity, 47.15% long-term debt, 0.85% short-term debt); Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, Docket No. E-7, Sub 1146 (June 22, 2018) (52% common equity and 48% long-term debt); and Order Accepting Stipulations, Deciding Contested Issues and Granting Partial Rate Increase, Docket No. E-2, Sub 1142 (Feb. 23, 2018) (52% common equity and 48% long-term debt).

long-term debt and 53.649% common equity based on an 8.75% return on equity.

Fourth, Section X. of the Public Staff Stipulation provides that:

[T]his Stipulation is in the public interest because it reasonably balances customer interests in mitigating rate impacts with investor interests in providing for reasonable recovery of investments, thereby providing the necessary level of revenue requirement to allow the Company to maintain its financial strength and credit quality and continue to provide high quality electric utility service to its customers.

Fifth, Section IV. of the CIGFUR Stipulation contains this same language. Sixth, we give substantial weight to Company Witness Davis' testimony regarding the Company's effort to find the appropriate balance between equity and debt financing. As Mr. Davis noted, Mr. Phillips relies primarily on the averages of his respective proxy groups without providing any further rationale in support of his recommended capitalization ratios. Seventh, we place substantial weight as well on Mr. McLawhorn's and Ms. Johnson's conclusion that the end result of the settlement is fair and reasonable with respect to both ratepayers and shareholders, and that customers will benefit from lower rates as a result of a negotiated settlement that, if approved, will reduce the Company's proposed rate increase by at least \$13 million. Eighth, the Commission also gives weight to the Public Staff Stipulation and the benefits that it provides to DENC's customers, which the Commission is obliged to consider as an independent piece of evidence under *CUCA I* and *CUCA II*. Each party to the Public Staff Stipulation gained some benefits that it deemed important and gave some concessions for those benefits. Based on the Application and pre-filed testimony, it is apparent that the Public Staff Stipulation ties the 52/48 capital structure to substantial concessions the Company made to reduce its revenue requirement.

Accordingly, based on the matters set forth above, and in the exercise of its independent judgment, the Commission finds that the weight of the evidence in this proceeding favors using the stipulated capital structure and that such capital structure is just, reasonable, and appropriate for use in setting rates in this docket.

#### Cost of Debt

The evidence supporting this finding of fact and conclusions is contained in the testimony and exhibits of Company Witness Davis, and Public Staff Witness Woolridge, the Public Staff and CIGFUR Stipulations, and the entire record of this proceeding.

In its Application and supporting testimony, the Company proposed a long-term debt cost of 4.45% at the end of the test year. In his supplemental testimony, Company Witness Davis updated the debt cost to 4.442% as of June 30, 2019. The Public Staff and CIGFUR Stipulations accept the 4.442% cost of debt proposed by the Company in Mr. Davis' supplemental testimony. No party contested the cost of debt proposed by the Company or agreed upon in the Public Staff and CIGFUR Stipulations.

The Commission therefore finds and concludes that the use of a debt cost of 4.442% is just and reasonable to all parties in light of all the evidence presented.

#### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 12-16**

The evidence for these findings and conclusions is contained in the Application, the direct testimony and exhibits of Witnesses Hevert, Woolridge, Phillips, the Public Staff and CIGFUR Stipulations, the testimony of public witnesses, the rebuttal testimony of Witness Hevert, the settlement testimony of Witnesses Hevert, McLawhorn and Johnson, and finally in the hearing testimony of Witness Hevert.

The Public Staff and CIGFUR Stipulations both state that an allowed rate of return on equity of 9.75% is reasonable for use in this proceeding, a decrease from the 9.9% level authorized by the Commission in the Company's last rate case. No other party presented evidence on the appropriate rate of return on equity. The Commission's consideration of the evidence and decision on this issue is set out below and is organized into three sections. The first is a summary of the record evidence on rate of return on equity. The second is a summary of the law applicable to the Commission's decision on rate of return on equity. The third is an application of the law to the evidence and a discussion and explanation of the Commission's ultimate decision on rate of return on equity.

I. Summary of Record Evidence on Return on Equity

In its Application, the Company requested approval for its rates to be set using an overall rate of return of 7.79% and a rate of return on equity of 10.75%. This request was based upon and supported by the direct testimony of DENC Witness Hevert. These rates of return compare to an overall return of 7.367% and rate of return on equity of 9.90% underlying DENC's current rates. DENC Witness Mitchell also filed testimony supporting the approval of the ROE recommended by Mr. Hevert. Witnesses for the Public Staff and CIGFUR also filed direct testimony on the appropriate rate of return on equity. This evidence was followed by the Public Staff and CIGFUR Stipulations, rebuttal testimony filed by Witness Hevert, settlement testimony filed by DENC Witness Hevert and Public Staff Witnesses McLawhorn and Johnson, and finally testimony of Mr. Hevert at the hearing of this matter. In addition to this expert testimony, the Commission received the testimony of a number of public witnesses on DENC's proposed rate

increase as well as numerous statements of consumer position. All of this evidence is summarized below.

*Direct Testimony of Mark Mitchell (DENC)*

DENC Witness Mitchell testified that the Company was facing significant capital investment needs. He stated that in order to attract the capital to meet these substantial future needs, the Company must achieve an adequate authorized ROE in this proceeding, and that the 10.75% ROE proposed by DENC would allow the Company to attract capital on reasonable terms in the capital markets. He explained that the ability to attract capital on favorable terms is important to DENC's ability to maintain its current credit ratings and, ultimately, minimize the cost of capital for customers. An adequate return also ensures DENC's ability to commit capital to future construction projects to provide safe, reliable, and cost-effective electric service to North Carolina customers without eroding the Company's shareholders' interests. (Tr. Vol. 4 at 168, 177-182).

*Direct Testimony of Robert B. Hevert (DENC)*

Mr. Hevert, DENC's primary cost of equity witness, filed direct testimony and exhibits in support of DENC's request for a 10.75% ROE. He explained that the cost of equity is the return that investors require to make an equity investment in a company, that it should reflect the return that investors require in light of the company's risks and the returns available on comparable investments, and that it differs from the cost of debt because it is neither directly observable nor a contractual obligation. In his direct testimony and exhibits, Mr. Hevert discussed the specific analyses he conducted in support of DENC's rate filing and provided a detailed description of the results of these analyses and resulting cost of equity recommendations. He applied the Constant Growth

Discounted Cash Flow (DCF) model, the Capital Asset Pricing Model (CAPM), the Empirical Capital Asset Pricing Model (ECAPM), the Bond Yield Plus Risk Premium approach, and the Expected Earnings Analysis to develop his ROE recommendation. He stated that the Commission's decision should result in providing DENC with the opportunity to earn an ROE that is: (1) adequate to attract capital at reasonable terms; (2) sufficient to ensure its financial integrity; and (3) commensurate with returns on investments in enterprises having corresponding risks. He discussed the need to select a group of proxy companies to determine the cost of equity, and how he selected the proxy group for this case. Mr. Hevert also noted that the regulatory conditions approved by the Commission in the merger of DENC's parent company, DEI, and SCANA Corporation were designed to ensure that the Company has "sufficient access to equity and debt capital at a reasonable cost to adequately fund and maintain their current and future capital needs and otherwise meet their service obligations to their customers." (Tr. Vol. 4 at 22-32).

According to Mr. Hevert, the results of his Constant Growth DCF analysis produced an ROE range of 8.34% to 10.38%. The results of Mr. Hevert's CAPM analysis showed a range of 8.25% to 11.34% in market risk premiums. The results of his ECAPM analysis showed a range of 9.61% to 12.76% in market risk premiums. The results of his Bond Yield Risk Premium analysis indicated an ROE range from 9.93% to 10.17%. The results of his Expected Earnings Analysis showed an average ROE of 10.38% and a median ROE of 10.52%. Based on his analyses, Mr. Hevert concluded that a rate of return on common equity in the range of 10.00% to 11.00% represents the ROE required by equity investors for investment in integrated electric utilities in today's

capital markets. Within that range, he recommended an ROE for DENC of 10.75% in both his direct and rebuttal testimony. (Tr. Vol. 4 at 45-56).

Mr. Hevert explained that his ROE recommendation also took into consideration several additional factors, including (1) DENC's need to fund its substantial planned capital investment program, (2) the regulatory environment in which the Company operates, and (3) flotation costs. With regard to the regulatory environment, he noted that North Carolina is generally considered to be a constructive regulatory jurisdiction, and that authorized ROEs tend to be correlated with the degree of regulatory supportiveness (utilities in jurisdictions considered to be more supportive tend to be authorized somewhat higher returns). He did not, however, make any specific adjustment to his ROE estimates for the effect of these factors. (Tr. Vol. 4 at 56-67).

Mr. Hevert also addressed the capital market environment and testified that it is important to assess the reasonableness of any financial model's results in the context of observable market data. In particular, he discussed the fact that investors see a probability of increasing interest rates based on near-term forecasts of the 30-year Treasury yield. (Tr. Vol. 4 at 77-81).

In this case, all parties had the opportunity to present the Commission with evidence concerning changing economic conditions as they affect customers. The testimony of Witnesses Hevert and Woolridge, which the Commission finds entitled to substantial weight, addresses changing economic conditions at some length. Witness Hevert provided detailed data concerning changing economic conditions in North Carolina as well as nationally, and concluded that the North Carolina-specific conditions are "highly correlated" with conditions in the broader nationwide economy. As such,

Witness Hevert testified that changing economic conditions, both nationally and specific to North Carolina, are reflected in his rate of return on equity estimates. (Tr. Vol. 4 at 67-77).

Mr. Hevert also considered the economic conditions in North Carolina in arriving at his ROE recommendation. He noted that the rate of unemployment has fallen substantially in North Carolina and in the U.S. generally since late 2009 and early 2010, with December 2018 rates of 3.70% in the State. He noted that since the Company's last general rate filing in March 2016, unemployment in the counties served by DENC has fallen by 1.4%. Mr. Hevert also noted that since the second quarter of 2013, the State has generally matched the national rate for real GDP, but that since 2009, median household income in North Carolina has grown at a somewhat slower annual rate than the national median income annual rate than the national median income. Total personal income, disposable income, personal consumption, and wages and salaries were generally on an increasing trend. Finally, he noted that since 2018, residential electricity costs in North Carolina remain approximately 13% below the national average. Based on all of these factors, Mr. Hevert opined that North Carolina and the counties contained within DENC's service area have experienced steady economic improvement since the Company's last rate case and that improvement is projected to continue. In his opinion, DENC's proposed ROE is fair and reasonable to DENC, its shareholders and its customers, in light of the impact of changing economic conditions on DENC's customers. (Tr. Vol. 4 at 67-77).

*Direct Testimony of J. Randall Woolridge (Public Staff)*

Public Staff Witness Woolridge performed DCF and CAPM analyses for both his and Witness Hevert's proxy groups of electric utilities. Dr. Woolridge developed his DCF growth rate after reviewing 13 growth rate measures including historic and projected growth rate measures and evaluating growth in dividends, book value, earnings per share (EPS), and growth rate forecasts from Yahoo, Reuters, and Zack's. Dr. Woolridge testified that it is well known that long-term EPS growth rate forecasts of Wall Street securities analysts are overly optimistic and upwardly biased. Public Staff Witness Woolridge determined a DCF equity cost rate of 8.55% for his proxy group, and 8.95% for the Hevert proxy group. (Tr. Vol. 6 at 534-537).

In Dr. Woolridge's CAPM analysis, he used for the risk free interest rate the top end of the range of yields on 30-year U.S. Treasury bonds over the 2013-2019 time period, 4.0%. He used the Value Line Investment Survey betas of 0.60 for his proxy group and 0.58 for Witness Hevert's proxy group. Witness Woolridge's market risk premium was 5.50%, based in part on the June 2019 CFO survey conducted by CFO Magazine and Duke University, which included approximately 200 responses, in which the expected market risk premium was 4.05%. He testified that thus, his 5.50% value is a conservatively high estimate of the market risk premium. Dr. Woolridge also testified that Duff & Phelps, a well-known valuation and corporate finance advisor that publishes extensively on cost of capital, recommended on December 31, 2018, using a 5.5% market risk premium, for the U.S. Witness Woolridge's CAPM equity cost rate was 7.3% for his proxy group and 7.2% for Witness Hevert's proxy group. (Tr. Vol. 6 at 591-604).

Witness Woolridge concluded that the appropriate equity cost rate for companies in his and Mr. Hevert's proxy groups is in the 7.20% to 8.95% range. He gave primary weight to his DCF results based on his belief that risk premium studies, including the CAPM, are a less reliable indicator of equity cost rates for public utilities. Dr. Woolridge also indicated that he found the DCF model to provide the best measure of equity cost rates considering the investment valuation process and the relative stability of the utility business. (Tr. Vol. 6 at 531, 604-605).

While noting that his equity cost rate studies indicated an ROE between 7.20% and 8.95%, Dr. Woolridge took into account the fact that his range was below the authorized ROEs for electric utilities nationally and made a primary recommendation of a 9.0% ROE assuming a 50.00% common equity ratio. Dr. Woolridge also provided an alternative recommendation of an 8.75% ROE based on the Company's originally recommended equity ratio of 53.649%. (Tr. Vol. 6 at 532-533).

Dr. Woolridge did not perform an ECAPM analysis and testified that the ECAPM is an ad hoc version of the CAPM and has not been theoretically or empirically validated in refereed journals. He also took issue with Mr. Hevert's Bond Yield Plus Risk Premium analysis and argued that it is inflated, gauges commission behavior rather than investor behavior, and overstates the actual ROE. (Tr. Vol. 6 at 612-613, 640-644).

Dr. Woolridge also expressed concerns with Mr. Hevert's Expected Earnings analysis and argued that the approach is inappropriate for several reasons: (1) it is accounting based and does not measure market based investor return requirements; (2) book equity does not change with investor return requirements as do market prices; (3) there is a negative relationship between the Return on Common Equity and Common

Equity ratios; (4) the approach is circular; and (5) the data partially reflect earnings of non-regulated operations. (Tr. Vol. 6 at 613, 644-648).

Dr. Woolridge also testified as to current capital market conditions as of the date of his testimony in August 2019. He stated that although the Federal Reserve increased the Federal Funds rate between 2015 and 2018, interest rates and capital costs remained at low levels. Witness Woolridge also pointed out that the 30-year Treasury yields are at historically low levels and are accompanied by slow economic growth and low inflation. (Tr. Vol. 6 at 548, 591, 610).

Dr. Woolridge responded to Witness Hevert's assessment of the economic conditions in North Carolina. He generally agreed with Witness Hevert's review of several measures of economic conditions, including the rate of unemployment, real GDP growth, median household income, residential electricity rates, and broad measures of income and consumption, as well as Mr. Hevert's general conclusion that economic conditions in North Carolina have improved since the Company's last rate case. Dr. Woolridge argued, however, that although economic conditions generally have improved, other conditions such as the higher unemployment rate in the DENC service territory as opposed to the whole state, and the median household income in North Carolina that is lower than the national norm, as well as the over 100 basis point difference in DENC's requested ROE and the average authorized ROEs for electric utilities in 2018-2019, do not support the Company's proposed rate of return. (Tr. Vol. 6 at 652-655).

*Direct Testimony of Nicholas Phillips, Jr. (CIGFUR)*

CIGFUR Witness Phillips did not perform cost of capital analyses. In his testimony, Mr. Phillips found the Company's proposed ROE to be excessive based on his

review of authorized ROEs for the first half of 2019, which averaged 9.57%, as reported by RRA. Mr. Phillips recommended that the Commission authorize a rate of return on equity that does not exceed the national average of 9.57%. (Tr. Vol. 6 at 427-431).

*Rebuttal testimony of Robert B. Hevert (DENC)*

In his rebuttal testimony, Company Witness Hevert responded to the arguments raised by CIGFUR Witness Phillips. Mr. Hevert explained that he analyzed the authorized ROE for vertically integrated electric utilities based on the jurisdiction's ranking by RRA, which provides an assessment of the extent to which regulatory jurisdictions are constructive from investors' perspectives. Witness Hevert stated that according to RRA, less constructive environments are associated with higher levels of risk, but North Carolina currently is ranked "Average/1," which falls approximately in the top-third of the 53 jurisdictions ranked by RRA. Witness Hevert testified that authorized ROEs for vertically integrated electric utilities in jurisdictions rated in the top third of all jurisdictions, like North Carolina, range from 9.37% to 10.55%, with an average of 9.93%, and a median of 9.95%. Finally, Mr. Hevert pointed to Company Rebuttal Exhibit RBH-16, which shows that the mean and median authorized returns for 2019, updated through August 16, 2019, are 9.61% and 9.73%, respectively. (Tr. Vol. 4 at 107-112).

*Public Staff and CIGFUR Stipulations*

In both the Public Staff and the CIGFUR Stipulations, DENC and the Public Staff, and DENC and CIGFUR agreed that the appropriate overall rate of return and rate of return on equity for use in this proceeding were 7.20% and 9.75% respectively. These agreements represent substantial movement by the parties from the positions on overall

return and return on equity articulated in testimony. This stipulated overall return of 7.20% and return on equity of 9.75% was supported by settlement testimony filed by Company Witness Hevert. The overall reasonableness of the stipulated rates of return was also addressed by Public Staff Witnesses McLawhorn and Johnson in their settlement testimony.

*Settlement Testimony of Robert Hevert (DENC)*

In his testimony supporting the Stipulations, Mr. Hevert noted that although the 9.75% stipulated ROE is somewhat below the lower bound of his recommended range, he recognized that the Stipulations reflect negotiation on many issues between the parties. Mr. Hevert stated that the terms of the Stipulations, when taken as a whole, would be regarded favorably by the financial community. He noted that the median ROE authorized in 2019 at the time of his testimony was 9.73%, only two basis points from the stipulated ROE. Mr. Hevert testified that the stipulated ROE fell below his Risk Premium model results, it fell in the 69th percentile of the mean and median of his DCF results, the 32th percentile of his CAPM and ECAPM results, and the 40th percentile of his Expected Earnings analysis. Thus, Mr. Hevert concluded that the stipulated ROE was supported by returns in other jurisdictions and fell within the range of his model results, though at the lower end. (Tr. Vol. 4 at 116-119).

*Hearing Testimony of Robert Hevert (DENC)*

Under cross-examination by the AGO, Mr. Hevert defended the use of projected treasury yields in his CAPM analysis by pointing out that there was only about a 21 basis point difference between the current and projected treasury yields, which was not a material difference. He noted that the CAPM results based on the current yield also

support his recommendation. Mr. Hevert also pointed out that using projected yields gave an important perspective, especially in light of the fact that in the recent market, the 30-year Treasury yield fell 71 basis points in 34 trading days. He also pointed out that in the 2017 DEP Rate Case and a recent Virginia case the commissions found his DCF analysis to produce unreasonably low ROE results, even using only earnings estimates. Mr. Hevert did not dispute that of the 32 data points he considered in determining his range and recommended ROE, 24 were lower than his recommended ROE. Nonetheless, Mr. Hevert noted that a mean of these results would not necessarily provide an appropriate estimate of DENC's cost of equity, as various qualitative factors should also be considered, such as capital expenditure plans and the regulatory environment. (Tr. Vol. 4 at 143-147).

*Public Witness Testimony/Statements of Consumer Position*

In addition to the direct prefiled testimony of the expert witnesses for the parties, a number of public witnesses also gave testimony suggesting that DENC customers would experience difficulty paying the increased rates requested in the Application and opposing the rate increases proposed by DENC. The Commission also received numerous statements of consumer position in regards to this docket, many of which expressed concern about DENC's proposed rate increase.

II. Law Governing the Commission's Decision on Return on Equity

Rate of return on equity is often one of the most contentious issues to be addressed in a rate case, even in a case such as this one in which Stipulations between DENC and the Public Staff and DENC and CIGFUR have been reached. In the absence of a settlement agreed to by all the parties, the law of North Carolina

requires the Commission to exercise its independent judgment and arrive at its own independent conclusion as to the proper rate of return on common equity. *See CUCA I*. In order to reach an appropriate independent conclusion regarding the rate of return on equity, the Commission must evaluate the available evidence, particularly that presented by conflicting expert witnesses. *State ex rel. Utils. Comm'n v. Cooper*, 366 N.C. 484, 491-93, 739 S.E.2d 541, 546-47 (2013) (*Cooper I*). In this case, the expert witness evidence relating to the Company's cost of equity capital was presented by Company Witness Hevert, Public Staff Witness Woolridge, and CIGFUR Witness Phillips. No return on equity evidence was presented by any other party.

The baseline for establishment of an appropriate rate of return on common equity is the constitutional constraints established by the decisions of the United States Supreme Court in *Bluefield Water Works & Improvement Co., v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679 (1923) (*Bluefield*), and *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) (*Hope*) which establish that:

To fix rates that do not allow a utility to recover its costs, including the cost of equity capital, would be an unconstitutional taking. In assessing the impact of changing economic conditions on customers in setting an ROE [rate of return on equity], the Commission must still provide the public utility with the opportunity, by sound management, to (1) produce a fair profit for its shareholders, in view of current economic conditions, (2) maintain its facilities and service, and (3) compete in the marketplace for capital.

Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, Docket No. E-7, Sub 1146, p. 50 (June 22, 2018). *See also State ex rel. Utils. Comm'n v. General Telephone Co. of the Southeast*, 281 N.C. 318, 370, 189 S.E.2d 705, 738 (1972) (*General Telephone*). As the North Carolina Supreme Court

held in *General Telephone*, these factors constitute “the test of a fair rate of return declared” in *Bluefield* and *Hope. Id.*

It is also important for the Commission to keep in mind that the rate of return on equity is, in fact, a cost. The return that equity investors require represents the cost to the utility of equity capital. In his dissenting opinion in *Missouri ex rel. Southwestern Bell Tel. Co. v. Missouri Pub. Serv. Comm’n*, 262 U.S. 276 (1923), Justice Brandeis remarked upon the lack of any functional distinction between the rate of return on equity (which he referred to as a “capital charge”) and other items ordinarily viewed as business costs, including operating expenses, depreciation, and taxes:

Each is a part of the current cost of supplying the service; and each should be met from current income. When the capital charges are for interest on the floating debt paid at the current rate, this is readily seen. But it is no less true of a legal obligation to pay interest on long-term bonds. . . and it is true also of the economic obligation to pay dividends on stock, preferred or common.

*Id.* at 306. (Brandeis, J. dissenting) (emphasis added). Similarly, the United States Supreme Court observed in *Hope*, “[f]rom the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business . . . [which] include service on the debt and dividends on the stock.” 320 U.S. at 591, 603.

Leading academic commentators also define rate of return on equity as the cost of equity capital. Professor Charles Phillips, for example, states that “the term ‘cost of capital’ may be defined as the annual percentage that a utility must receive to maintain its credit, to pay a return to the owners of the enterprise, and to ensure the attraction of capital in amounts adequate to meet future needs.” Phillips, Charles

F, Jr., *The Regulation of Public Utilities* (Public Utilities Reports, Inc. 1993), at 388.

Professor Roger Morin approaches the matter from the economist's viewpoint:

While utilities enjoy varying degrees of monopoly in the sale of public utility services, they must compete with everyone else in the free open market for the input factors of production, whether it be labor, materials, machines, or capital. The prices of these inputs are set in the competitive marketplace by supply and demand, and it is these input prices which are incorporated in the cost of service computation. This is just as true for capital as for any other factor of production. Since utilities must go to the open capital market and sell their securities in competition with every other issuer, there is obviously a market price to pay for the capital they require, for example, the interest on capital debt, or the expected return on equity.

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[T]he cost of capital to the utility is synonymous with the investor's return, and the cost of capital is the earnings which must be generated by the investment of that capital in order to pay its price, that is, in order to meet the investor's required rate of return.

Morin, Roger A., *Utilities' Cost of Capital* (Public Utilities Reports, Inc. 1984), at 19-21 (emphasis added). Professor Morin adds:

The important point is that the prices of debt capital and equity capital are set by supply and demand, and both are influenced by the relationship between the risk and return expected for those securities and the risks expected from the overall menu of available securities.

*Id.* at 20.

In addition, the Commission is and must always be mindful of the North Carolina Supreme Court's command that the Commission's task is to set rates as low as possible consistent with the dictates of the United States and North Carolina Constitutions. *State ex rel. Utils. Comm'n v. Pub. Staff-N. Carolina Utils. Comm'n*, 323 N.C. 481, 490, 374 S.E.2d 361, 370 (1988) (*Public Staff*). Further, and echoing the discussion above concerning the fact that rate of return on equity represents the cost of equity capital, the Commission must execute the Supreme Court's command

“irrespective of economic conditions in which ratepayers find themselves.” Order Granting General Rate Increase, Docket No. E-2, Sub 1023 (May 30, 2013) (2013 DEP Rate Order). The Commission noted in that Order:

The Commission always places primary emphasis on consumers’ ability to pay where economic conditions are difficult. By the same token, it places the same emphasis on consumers’ ability to pay when economic conditions are favorable as when the unemployment rate is low. Always there are customers facing difficulty in paying utility bills. The Commission does not grant higher rates of return on equity when the general body of ratepayers is in a better position to pay than other times, which would seem to be a logical but misguided corollary to the position the Attorney General advocates on this issue.

*Id.* Indeed, in *Cooper I* the Supreme Court emphasized “changing economic conditions” and their impact upon customers. *Cooper I*, 366 N.C. at 484, 739 S.E.2d at 548.

The Commission further noted in the 2013 DEP Rate Order that:

While there is no specific and discrete numerical basis for quantifying the impact of economic conditions on customers, the impact on customers of changing economic conditions is embedded in the rate of return on equity expert witnesses’ analyses. The Commission noted this in the 2013 DEP Rate Order: “This impact is essentially inherent in the ranges presented by the return on equity expert witnesses whose testimony plainly recognizes economic conditions – through the use of economic models – as a factor to be considered in setting rates of return.”

2013 DEP Rate Order, at 38.

Finally, under long-standing decisions of the North Carolina Supreme Court, the Commission’s subjective judgment is a necessary part of determining the authorized rate of return on equity. *Public Staff*, 323 NC at 490, 374 S.E.2d at 369. As the Commission has previously noted:

Indeed, of all the components of a utility’s cost of service that must be determined in the ratemaking process, the appropriate

ROE is the one requiring the greatest degree of subjective judgment by the Commission. Setting an ROE for regulatory purposes is not simply a mathematical exercise, despite the quantitative models used by the expert witnesses. As explained in one prominent treatise,

Throughout all of its decisions, the [United States] Supreme Court has formulated no specific rules for determining a fair rate of return, but it has enumerated a number of guidelines. The Court has made it clear that confiscation of property must be avoided, that no one rate can be considered fair at all times and that regulation does not guarantee a fair return. The Court also has consistently stated that a necessary prerequisite for profitable operations is efficient and economical management. Beyond this is a list of several factors the commissions are supposed to consider in making their decisions, but no weights have been assigned.

The relevant economic criteria enunciated by the Court are three: financial integrity, capital attraction and comparable earnings. Stated another way, the rate of return allowed a public utility should be high enough: (1) to maintain the financial integrity of the enterprise, (2) to enable the utility to attract the new capital it needs to serve the public, and (3) to provide a return on common equity that is commensurate with returns on investments in other enterprises of corresponding risk. These three economic criteria are interrelated and have been used widely for many years by regulatory commissions throughout the country in determining the rate of return allowed public utilities.

In reality, the concept of a fair rate of return represents a “zone of reasonableness.” As explained by the Pennsylvania commission:

There is a range of reasonableness within which earnings may properly fluctuate and still be deemed just and reasonable and not excessive or extortionate. It is bounded at one level by investor interest against confiscation and the need for

averting any threat to the security for the capital embarked upon the enterprise. At the other level it is bounded by consumer interest against excessive and unreasonable charges for service.

As long as the allowed return falls within this zone, therefore, it is just and reasonable. . . . It is the task of the commissions to translate these generalizations into quantitative terms.

Charles F. Phillips, Jr., The Regulation of Public Utilities, 3d ed. 1993, pp. 382. (notes omitted).

2013 DEP Rate Order at 35-36.

Moreover, the North Carolina Supreme Court has interpreted N.C. Gen. Stat § 62-133 as requiring the Commission to make findings regarding the impact of changing economic conditions on customers when determining the proper rate of return on equity for a public utility. *Cooper I*, at 495, 739 S.E.2d at 548. The Commission must exercise its subjective judgment so as to balance two competing rate of return on equity-related factors—the economic conditions facing the Company’s customers and the Company’s need to attract equity financing in order to continue providing safe and reliable service.

2013 DEP Rate Order at 35-36.

In addition to adhering to the broad controlling legal principles on the allowed rate of return discussed above, the Commission must adhere to the multi-element formula set forth in N.C. Gen. Stat. § 62-133 when it sets rates. The rate of return on cost of property element of the formula in N.C. Gen. Stat. § 62-133(b)(4) is a significant, but not an independent element. Each element of the formula must be analyzed to determine the utility’s cost of service and revenue requirement. The Commission must make many subjective decisions with respect to each element in

the formula in establishing the rates it approves in a general rate case. The Commission must approve accounting and pro forma adjustments to comply with N.C. Gen. Stat. § 62-133(b)(3) and must approve depreciation rates pursuant to N.C. Gen. Stat. § 62-133(b)(1). The subjective decisions the Commission makes as to each of these elements have multiple and varied impacts on the decisions it makes on other rate-affecting elements, such as the decision it must make on the rate of return on equity.

Pursuant to N.C. Gen. Stat. § 62-133, rates in North Carolina are set based on a modified historic test period.<sup>6</sup> A component of cost of service equally important as the return on investment component is test year revenues.<sup>7</sup> The higher the level of test year revenues, the lower the need for a rate increase, all else remaining equal. Historically, and in this case, test year revenues are established through resort to regression analysis, using historic rates of revenue growth or decline to determine end of test year revenues. Economic conditions existing during the test year, at the time of the public hearings, and at the date of this Order will affect not only the ability of DENC's customers to pay electric rates, but also the ability of DENC to earn the authorized rate of return during the period rates will be in effect. Thus, in accordance with the above-discussed applicable law, the Commission's duty under N.C. Gen. Stat. § 62-133 is to set rates as low as reasonably possible without impairing the Company's ability to attract investors to raise the capital needed to provide reliable electric service and recover its cost of providing service.

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<sup>6</sup> N.C. Gen. Stat. § 62-133(c).

<sup>7</sup> N.C. Gen. Stat. § 62-133(b)(3).

In fixing rates, the Commission is also cognizant that when a utility's costs and expenses grow at a faster pace than revenues during the period when rates will be in effect, it will experience a decline in its realized rate of return on investment to a level below its authorized rate of return. Differences exist between the authorized return and the earned, or realized, return. Components of the cost of service must be paid from the rates the utility charges before the equity investors are paid their return on equity. Operating and administrative expenses must be paid, depreciation must be funded, taxes must be paid, and the utility must pay interest on the debt it incurs. To the extent revenues are insufficient to cover the entire cost of service, the shortfall reduces the return to the equity investor, last in line to be paid. When this occurs, the utility's realized, earned return is less than the authorized return, an occurrence commonly referred to as regulatory lag. In setting the rate of return, just as the Commission is constrained to address the impact of difficult economic times on customers' ability to pay for service by establishing a lower rate of return on equity in isolation from the many subjective determinations that must be made in a general rate case, it likewise is constrained to address the effect of regulatory lag on the Company by establishing a higher rate of return on equity. Instead, the Commission sets the rate of return considering both of these negative impacts in its ultimate decision fixing a utility's rates.

It is against this backdrop of overarching principles and law that the Commission turns to the evidence present in this case.

III. Discussion and Application of Law to the Facts of this Case Regarding the Issue of Return on Equity

The Commission has examined the Company's Application and supporting testimony and exhibits and Form E-1 filings seeking to justify its requested increase. DENC's updated request prior to entering into the Stipulations was a retail revenue increase of \$24.2 million in annual revenues. The Public Staff, who in this docket represents all users and consumers of the Company's electric service, and DENC entered into a Stipulation that resulted in reducing the retail revenue increase sought by the Company. CIGFUR and DENC entered into a separate Stipulation that provided for the same reduction in the revenue increase, as well as a 9.75% ROE. As with all settlement agreements, each party to the Stipulations gained some benefits that it deemed important and gave some concessions for those benefits. Based on DENC's Application, it is apparent that the Stipulations tie the 9.75% rate of return on equity to substantial agreed upon concessions made by DENC. As noted above, since the AGO and Nucor, parties in this docket, did not agree to the settlements, the Commission is required to examine the Stipulations and exercise its independent judgment to arrive at its own independent conclusion as to the proper rate of return on common equity.

The starting point for an examination of what constitutes a reasonable rate of return on equity begins with the various economic and financial analyses provided by the parties' expert witnesses. In this proceeding, those analyses were provided in the testimonies of three different witnesses: Witness Hevert for DENC; Witness Woolridge for the Public Staff; and Witness Phillips for CIGFUR. These testimonies, as summarized above, provide a relatively broad range of methods, inputs, and recommendations regarding the proper rate of return on equity determination for DENC.

For example, Witness Hevert relied in his direct testimony on four different analyses to arrive at his rate of return on equity recommendation. These analyses were a Constant Growth DCF Analysis, a Capital Asset Pricing Model analysis, a Bond Yield plus Risk Premium analysis, and an Expected Earnings analysis. By way of comparison, Public Staff Witness Woolridge relied upon a DCF analysis and a Capital Asset Pricing Model analysis in reaching his conclusions; however, the inputs utilized by Witness Woolridge in his analyses are different from those utilized by Witness Hevert. Witness Phillips looked at the average allowed rates of return on equity for both vertically integrated and distribution-only electric utilities for the first and second quarters of 2019 of 9.57% and recommended that average as a cap to the allowed rate of return on equity.

These varying analyses, as is typical, produced varying results. Witness Hevert's analyses prompted him to propose a rate of return on equity range of 10.00% to 11.00% with a specific rate of return on equity recommendation of 10.75%. Witness Woolridge's analyses resulted in a recommended rate of return on equity range of 7.20% to 8.95% with a primary recommendation of a 9.00% rate of return on equity with a 50.00% common equity capital structure and a secondary recommendation of an 8.75% ROE if DENC's actual capital structure of 46.351% long-term debt and 53.649% common equity, as proposed in the supplemental testimony of Company Witness Davis, was approved. Finally, as noted above, Witness Phillips recommended a cap on rate of return on equity of 9.57%.

The Commission finds the cost of equity analyses helpful in reaching its conclusion on an appropriate rate of return on equity for DENC, but notes that the ranges of the various analyses span a range from 7.20% to 12.76% and the specific rate of return

on equity recommendations of the witnesses span a range from 7.20% on the low end to 11.00% on the high end.

The Commission finds that the DCF, CAPM, ECAPM, and Bond Yield Plus Risk Premium analyses of DENC Witness Hevert, and the Stipulations are credible, probative, and entitled to substantial weight.

DENC Witness Hevert in his direct testimony provided his constant growth DCF analyses, as shown on Exhibit RBH-1, pages 1, 2, and 3: 30-day dividend yield mean 9.24%, median 9.18%; 90-day dividend yield mean 9.31%, median 9.25%; and 180-day dividend yield mean 9.39%, median 9.38%. Although the Commission, as stated in previous Commission general rate case orders, does not approve of Witness Hevert's sole use of analysts' predicted earnings per share to determine the DCF growth rate, the Commission finds Witness Hevert's constant growth DCF analyses mean and median rate of return on equity results credible, probative, and entitled to substantial weight.

Witness Hevert's CAPM analysis for his Proxy Group Average Value Line Beta Coefficient, as shown on Exhibit RBH-4, page 1, includes current 30-year treasury rates to calculate the risk free rate of 3.04%, producing what Witness Hevert described as a Value Line Market DCF Derived rate of return on equity of 9.78%. Witness Hevert's ECAPM analysis for his Proxy Group Average Bloomberg Beta Coefficient, as shown on Exhibit RBH-4, page 1, produces what Witness Hevert described as a Bloomberg Market DCF Derived rate of return on equity of 9.61%. The Commission approves of the use of current risk-free rates rather than predicted near-term or long-term rates. The Commission finds the above-described CAPM and ECAPM analyses credible, probative, and entitled to substantial weight.

DENC Witness Hevert's Bond Yield Plus Risk Premium, as shown on Exhibit RBH-5, using the current 30-year Treasury yield of 3.04% and applying it to the approved rates of return on equity in 1,581 electric utility rate proceedings between January 1980 and February 28, 2019, results in a rate of return on equity of 9.93%. As previously stated, the Commission approves the use of current interest rates, rather than projected near-term or long-term interest rates. The Commission finds Witness Hevert's updated Bond Yield Plus Risk Premium analysis using the current 30-year Treasury yield to be credible, probative, and entitled to substantial weight.

The Commission has carefully evaluated the DCF analysis recommendation of Witness Woolridge. As shown on Mr. Hevert's settlement testimony Exhibit RBH-S-1, from 2016 – 2019, there were 81 vertically integrated electric utility decisions by public service commissions resulting in a mean approved 9.74% rate of return on equity. The mean year-to-date 2019 rate of return on equity is 9.61%, and the median rate of return on equity is 9.73%.

As shown on Exhibit RBH-S-1, during this period there was only one public service commission (the South Dakota Public Service Commission) decision approving a rate of return on equity below 9.00% for a vertically integrated electric utility (8.75% in May 2019). Public Staff Witness Woolridge's DCF analysis produced a rate of return on equity ranging from 8.55 – 8.95%, adjusted upward for a specific rate of return on equity recommendation of 9.00% with a 50.00% common equity capital structure component. As shown on Exhibit JRW-8, page 1, the result of the CAPM analysis for the Electric Proxy Group and the Hevert Proxy Group were 7.3% and 7.2%, respectively. These DCF

and CAPM results are substantially below the mean allowed rate of return on equity of 9.74% from 2016 through mid-September 2019.

In summary, the Commission concludes there is substantial evidence supporting the reasonableness of a rate of return on equity of 9.75%. First, that rate of return is well within the range of recommended returns by the economic experts in this docket of 7.20% to 11.00%. Second, it falls just 36 basis points above the 9.39% mean results of DENC Witness Hevert's DCF analysis and below the mean high results of his DCF analysis. Third, it falls within the range of DENC Witness Hevert's CAPM results. Fourth, it falls within the results of DENC Witness Hevert's ECAPM results. Fifth, it falls only 18 basis points below the lower end of the range of DENC Witness Hevert's Bond Yield Plus Risk Premium analysis results. Sixth, it is slightly below the recommended range of DENC Witness Hevert (10.00% to 11.00%). Seventh, it falls squarely within the range and very close to the average of recent vertically integrated electric utility allowed returns on equity nationally.<sup>8</sup> Eighth, it is equal to the lowest rate of return on equity awarded by this Commission in general rate cases for major electric utilities in at least the last 10 years.<sup>9</sup> Ninth, it is 15 basis points lower than DENC's current allowed rate of return on equity. Tenth, it is supported as the appropriate rate of return on equity for DENC by all of parties filing rate of return testimony in this

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<sup>8</sup> The Commission determines the appropriate rate of return on equity based upon the evidence and particular circumstances of each case. However, the Commission believes that the rate of return on equity trends and decisions by other regulatory authorities, as well as other recent decisions of this Commission, deserve some weight, as (1) they provide a check or additional perspective on the case-specific circumstances, and (2) the Company must compete with other regulated utilities in the capital markets, meaning that a rate of return on equity significantly lower than that approved for other utilities of comparable risk would undermine the Company's ability to raise necessary capital, while a rate of return on equity significantly higher than other utilities of comparable risk would result in customers paying more than necessary.

<sup>9</sup> See Docket Nos. E-2, Subs 1023 and 1142; E-7, Subs 909, 989, and 1146; and E-22, Subs 459, 479, and 532.

proceeding in lieu of the recommendations made by their respective witnesses on this subject, and the stipulated return on equity of 9.75% is supported by credible filed settlement testimony by the cost of capital witness for DENC. Finally, and without expressly adopting his methodology, it is consistent with Witness Phillips' notion that DENC's return should be capped at the average rate of return on equity approved by other state commissions for the first two quarters of 2019.<sup>10</sup>

These factors lead the Commission to conclude that a 9.75% rate of return on equity is supported by the substantial weight of the evidence in this proceeding. However, to meet its obligation in accord with the holding in *Cooper I*, the Commission will next address the impact of changing economic conditions on customers.

In this case, all parties had the opportunity to present the Commission with evidence concerning changing economic conditions as they affect customers. The testimony of Witnesses Hevert and Woolridge, which the Commission finds entitled to substantial weight, addresses changing economic conditions at some length. Witness Hevert provided detailed data concerning changing economic conditions in North Carolina, as well as nationally, and concluded that the North Carolina-specific conditions are "highly correlated" with conditions in the broader nationwide economy. As such, Witness Hevert testified that changing economic conditions, both nationally and specific to North Carolina, are reflected in his rate of return on equity estimates.

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<sup>10</sup> Witness Phillips' proposal was a cap at 9.57% based on the first and second quarter average rates of return reported by RRA. However, Mr. Phillips included distribution-only electric utilities, which are not appropriate. DENC witness Hevert's rebuttal testimony explained that the results reported by Mr. Phillips were skewed by the Otter Tail decision, and a better measure was the median return of ROEs authorized for vertically integrated utilities in 2019 through August 2019 of 9.73%, as opposed to the mean of 9.61%. The Commission finds the use of vertically integrated electric utilities to be a more comparable measure, as well as the more current data.

Public Staff Witness Woolridge agreed with DENC Witness Hevert that economic conditions have improved in North Carolina. He pointed out that while the State's unemployment rate has fallen by one-third since its peak in the 2009-2010 period and is slightly below the national average of 3.90%, the unemployment rate in DENC's service territory is 4.95%, over 100 basis points higher than the national and North Carolina averages. Dr. Woolridge also noted that North Carolina's residential electric rates are below the national average; however, its median household income is more than 10% below the U.S. norm.

Based upon the general state of the economy and the continuing affordability of electric utility service, and after weighing and balancing factors affected by the changing economic conditions in making the subjective decisions required, the Commission concludes that the stipulated rate of return on equity of 9.75% will not cause undue hardship to customers even though some will struggle to pay the increased rates resulting from the Stipulations. When the Commission's decisions are viewed as a whole, including the decision to establish the rate of return on equity at 9.75%, the Commission's overall decision fixing rates in this general rate case results in lower rates to consumers in the existing economic environment.<sup>11</sup>

The many Commission-approved adjustments reduced the revenues to be recovered from customers and the return to be paid to equity investors. Some adjustments reduced the authorized rate of return on investment financed by equity

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<sup>11</sup> The Commission notes that consumers pay "rates," a charge in cents per kilowatt-hour ("kWh") for the electricity they consume. They do not pay a "rate of return on equity," though it is a component of the Company's cost of providing service which is built into the charge per kWh. Investors are compensated by earning a return on the capital they invest in the business. Per the Commission determination of the rate of return on equity in this matter, investors will have the opportunity to be paid in dollars for the dollars they invested at the rate of 9.75%.

investors. These adjustments have the effect of reducing rates and providing rate stability to consumers (and return to equity investors) in recognition of the difficulty some consumers will have paying increased rates in the current economic environment. While the equity investor's cost was calculated by resort to a rate of return on equity of 9.75% instead of 10.75%, this is only one approved adjustment that reduced ratepayer responsibility and equity investor reward. Many other adjustments reduced the dollars the investors actually have the opportunity to receive. Therefore, nearly all of the adjustments reduce ratepayer responsibility and equity investor returns in compliance with the Commission's responsibility to establish rates as low as reasonably permissible without transgressing constitutional constraints, and thus, inure to the benefit of consumers' ability to pay their bills in this economic environment.

For example, to the extent the Commission made downward adjustments to rate base, disallowed test year expenses, increased test year revenues, or reduced the equity capital structure component, the Commission reduced the rates consumers will pay during the future period when rates will be in effect. Because the compensation owed to investors for investing in the Company's provision of service to consumers takes the form of return on investment, downward adjustments to rate base, disallowances of test year expenses, increases to test year revenues, or reduction in the equity capital structure component will reduce investors' return on investment irrespective of the determination of rate of return on equity.

Considering the changing economic conditions and their effects on DENC's customers, the Commission recognizes the financial difficulty that an increase in DENC's rates may create for some of DENC's customers, especially low-income customers. As

shown by the evidence, relatively small changes in the rate of return on equity have a substantial impact on a utility's base rates. Therefore, the Commission has carefully considered changing economic conditions and their effects on DENC's customers in reaching its decision regarding DENC's approved rate of return on equity.

The Commission also recognizes that the Company is in a significant construction mode, and much of the associated investment is for generation, transmission, and distribution infrastructure to benefit DENC's customers, as well as in response to recent increases in environmental compliance costs and other operating expenses. The need to invest significant sums to serve its customers requires the Company to maintain its creditworthiness in order to compete for large sums of capital on reasonable terms. The Commission must weigh the impact of changing economic conditions on DENC's customers against the benefits that those customers derive from the Company's ability to provide safe, adequate, and reliable electric service. Safe, adequate, and reliable electric service is essential to the well-being of the people, businesses, institutions, and economy of North Carolina. Thus, the Commission finds and concludes that such capital investments by the Company provide significant benefits to all of DENC's customers.

The Commission concludes in the exercise of its independent judgment and discretion that a 9.75% rate of return on equity is supported by the evidence and should be adopted. The hereby approved rate of return on equity appropriately balances the benefits received by DENC's customers from DENC's provision of safe, adequate, and reliable electric service in support of the well-being of the people, businesses, institutions, and economy of North Carolina (which benefits are symbiotically linked to the Company's ability to compete in the equity capital market to access capital on

reasonable terms that will be fair to ratepayers) with the difficulties that some of DENC's customers will experience in paying DENC's adjusted rates. The Commission further concludes that a 9.75% rate of return on equity will allow DENC to compete in the market for equity capital, providing a fair return on investment to its investor-owners and, the lowering of the rate from the requested 10.75% to 9.75% has the effect of lowering the cost of service which forms the basis the rates the ratepayers must pay for service. Accordingly, the Commission concludes, taking into account changing economic conditions and their impact on customers that the approved rate of return on equity will result in the lowest rates constitutionally permissible in this proceeding.

Finally, in approving the 9.75% rate of return on equity, the Commission gives significant weight to the Stipulations and the benefits that they provide to DENC's customers, which the Commission is obliged to consider as an independent piece of evidence under the Supreme Court's holding in *CUCA I*.

#### **EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 17**

The evidence supporting this finding of fact and conclusions are contained in DENC's verified Application and Form E-1, the testimony and exhibits of the witnesses, the Public Staff Stipulation, and the entire record in this proceeding.

##### Summary of the Evidence

The Company and the Public Staff agreed to certain cost of service adjustments addressed in the testimony of Public Staff Witness Johnson and the rebuttal testimony of Company Witness McLeod and as further negotiated by the Stipulating Parties. These adjustments are shown on Settlement Exhibit I of the Public Staff Stipulation and are each described below. The resolution of the various adjustments as reflected in the

Public Staff Stipulation are to be viewed holistically as the result of give and take negotiations between the Stipulating Parties rather than the agreement of each Stipulating Party on the amount adjusted in each adjustments.

#### Executive Incentive Compensation

In his direct testimony, Witness McLeod testified that the Annual Incentive Plan (AIP) represents at-risk compensation paid out to Company employees only upon meeting certain operation and financial goals during the plan year. He stated that the Company made an adjustment that provided for 100% of the plan target instead of the 120% payout that occurred during the Test Year. (Tr. Vol. 4 at 267).

In her testimony, Public Staff Witness Johnson described the Company's AIP and Long-Term Incentive Plan (LTIP) and how eligible employee's performance is evaluated by the Company and what metrics are used in determining an employee's compensation under one or both of the plans. Witness Johnson testified that she adjusted the allowable costs of AIP to exclude incentive amounts that were based on financial metrics, which are closely tied to EPS, as the AIP as a whole is funded based on a consolidated EPS. Witness Johnson removed amounts related to all executive-level employees because she claimed that those employees' goals align with shareholders' interests. Finally, Witness Johnson adjusted the LTIP costs allowed to exclude Performance Shares because the Public Staff believes that the metrics used in calculating Performance Shares provide direct benefits to shareholders rather than ratepayers. (Tr. Vol. 6 at 19-20).

The Public Staff Stipulation provides for the removal of 50% of the costs associated with the Company's executive incentive plan that were based on financial metrics and otherwise retained the Company's proposal. The Commission finds and

concludes that the Public Staff Stipulation's treatment of the incentive plan costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Employee Severance Program Costs

In his direct testimony, Witness McLeod testified that the Company made an adjustment to include a normalized level of employee severance costs in the cost of service based on the Company's historical experience over the past 24 years. He explained that since 1994, there were five major corporate-wide severance programs which resulted in an average of approximately one every five years. (Tr. Vol. 4 at 266-267).

In his supplemental testimony, Witness McLeod explained that in March 2019, the Company announced the Voluntary Retirement Program (VRP) for employees that meet certain age and service requirements. Witness McLeod stated that the VRP was offered to employees of nearly all DEI affiliates, including DENC and Dominion Energy Services, Inc. (DES), and is expected to reduce total workforces during the remainder of 2019 and 2020. He also testified that the VRP is expected to result in a cost savings due to efficiencies gained and confirmed that the Company's supplemental filing incorporated the VRP severance costs as well as the savings through adjustments to employee salaries and wages, benefits, and AIP costs. Witness McLeod further testified that the revenue requirement presented in the Company's supplemental filing has comprehensively incorporated the severance costs and savings associated with the VRP. Additionally, Witness McLeod updated the employee severance program normalization adjustment to include VRP-related severance costs. During the period 1994 through 2019, there were

six major corporate-wide severance programs instituted by the Company, resulting in an average of approximately one every 4.17 years. (Tr. Vol. 4 at 305, 311).

In her testimony, Witness Johnson stated that the Public Staff would typically include a normalized level of employee severance program costs and use the actual costs of the Company's latest corporate-wide severance program, amortized over a reasonable period of time. However, the circumstances in this docket are distinguishable. Public Staff Witness Johnson took exception with using VRP severance costs in the employee severance program cost adjustment because she claimed these costs "appear to be closely linked" to the DEI and SCANA merger approved by the Commission on November 19, 2018, in Docket Nos. E-22, Sub 551 and G-5, Sub 585 ("SCANA Merger Order").

Witness Johnson acknowledged that the Company reflected a reduction to salaries and wages, benefits, AIP, and payroll taxes in its supplemental filing as a result of the VRP, but disagreed with including the VRP severance costs in the normalized employee severance program calculation. Witness Johnson claimed that the VRP severance costs should be considered "integration costs" as defined in the SCANA Merger Order and pursuant to that Order, integration costs should not be included for ratemaking purposes. Witness Johnson proposed retaining the existing normalized level of employee severance costs that was calculated and approved in the 2016 Rate Case. (Tr. Vol. 6 at 20-24).

For purposes of this proceeding, the Public Staff Stipulation provides for a reduction in the revenue requirement in the amount of \$304,000 to reflect a downward adjustment for the costs related to the employee severance program requested in this case and a normalization of those costs over 4.5 years. The Commission finds and concludes that the Public Staff Stipulation's treatment of the severance costs is appropriate and

reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### VRP Employee Backfill Costs

In his supplemental testimony, Witness McLeod testified that the Company made an adjustment that offset a portion of the VRP savings incorporated in the employee labor and benefits adjustments with a calculated value of salaries and wages for backfilled positions. (Tr. Vol. 4 at 317).

In her testimony, Public Staff Witness Johnson made an adjustment to remove the 582 planned positions for both DENC and DES that the Company intended to fill as a result of the VRP. Witness Johnson explained that because these positions have not actually been filled, the costs of those positions should not be included in this proceeding. Witness Johnson explained that should the Company hire any of these employees and provide supporting documentation, up to the close of the hearing in this docket, then she would update her testimony accordingly after investigation and verification that the employees had been hired. (Tr. Vol. 6 at 24).

For purposes of this proceeding, the Public Staff Stipulation provides for an adjustment to the requested revenue requirement for the employee severance program as described above and for the Public Staff's withdrawal of its proposed adjustment for the related VRP backfill costs. The Commission finds and concludes that the Public Staff Stipulation's treatment of the employee backfill costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Storm Restoration Expense

In his direct testimony, Witness McLeod explained that it is appropriate to include a normalized level of storm expense in the cost of service for ratemaking purposes given the unpredictable nature of storm activity that can cause a material level of expense in a short period of time. The Company used a historical average of storm activity and cost during the nine years of 2010–2018 in determining its normalized level of expense. (Tr. Vol. 4 at 268).

In her testimony, Public Staff Witness Johnson made an adjustment to the Company's normalized level of major storm restoration expenses by calculating the average costs for the last ten years instead of nine as used by the Company. Witness Johnson stated that a ten-year average was consistent with the method used in the most recent rate cases for DEC and DEP) in Docket Nos. E-7, Sub 1146 and E-2, Sub 1142, respectively. (Tr. Vol. 6 at 25-26).

For purposes of this proceeding, the Public Staff Stipulation provides for a reduction in the revenue requirement in the amount of \$81,000 to reflect a downward adjustment for the storm costs requested in this case. The Commission finds and concludes that the Public Staff Stipulation's treatment of the storm restoration costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Advertising Expense

In his direct testimony, Witness McLeod testified that the Company made an adjustment to eliminate all promotional advertising expenses from the Test Year. (Tr. Vol. 4 at 269).

In her testimony, Public Staff Witness Johnson testified that the Company included instructional advertising that appears to be related to public notices specifically related to Virginia jurisdictional matters. The Public Staff made an adjustment to eliminate those public notices that do not appear to relate to DENC ratepayers. (Tr. Vol. 6 at 26).

For purposes of this proceeding, the Public Staff Stipulation provides for a reduction in the revenue requirement in the amount of \$12,000 to reflect a downward adjustment for the advertising costs request in this case. The Commission finds and concludes that the Public Staff Stipulation's treatment of the advertising costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Executive Compensation

In his direct testimony, Witness McLeod testified that the Company made an adjustment to remove 50% of the compensation of the three executives with the highest level of compensation allocated to DENC during the Test Year. (Tr. Vol. 4 at 267).

In her testimony, Public Staff Witness Johnson made an adjustment to also remove 50% of the compensation and benefits of the fourth executive with the highest level of compensation allocated to DENC during the Test Year. She claimed that executives' duties and compensation encompass a substantial amount of activities related to shareholder interests and therefore some of their compensation and benefits should be borne by shareholders. (Tr. Vol. 6 at 26-28).

For purposes of this proceeding, the Public Staff Stipulation provides that the Stipulating Parties agreed to accept the Public Staff's proposed adjustment to executive

compensation costs. The Commission finds and concludes that the Public Staff Stipulation's treatment of the executive compensation costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Non-Fuel Variable Operation and Maintenance Expense Displacement

In his direct testimony, Witness McLeod testified that the Greenville County CC began commercial operation in December 2018 and the Company then began incurring ongoing operation and maintenance (O&M) expenses associated with running the facility. The Company proposed an adjustment to annualize non-labor O&M expense based on projected average monthly expenses during 2019. Witness McLeod also explained the Company's adjustment to amortize the deferred costs, including a return on investment, associated with the facility as requested in the Company's petition filed on March 29, 2019, in Docket No. E-22, Sub 566. Witness McLeod stated that the Company is requesting that the incremental costs incurred from the time the facility was placed into service until the time costs will be reflected in the base non-fuel rates approved in this proceeding be deferred and amortized over a three-year period beginning with the effective date of rates approved in this proceeding. (Tr. Vol. 4 at 266, 276).

In her testimony, Public Staff Witness Johnson adjusted the non-fuel variable O&M expenses to prevent the inclusion in cost of service of more than an annual level of these types of expenses as the Company made pro forma adjustments to include the full cost of Greenville County CC in the cost of service, including adding incremental non-fuel variable O&M expenses to reflect a full year of operations. Witness Johnson testified that, with the addition of Greenville County CC, other plants in DENC's fleet will operate less frequently, and thus incur fewer non-fuel variable O&M expenses.

Therefore, the Public Staff adjusted non-fuel variable O&M expenses to prevent the inclusion in cost of service of more than an annual level of these types of expenses. (Tr. Vol. 6 at 29-30).

The Public Staff Stipulation provides for a reduction in the revenue requirement in the amount of \$142,000, representing non-fuel variable O&M expense displacement. The Commission finds and concludes that the Public Staff Stipulation's treatment of these non-fuel O&M costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Lobbying Expenses

In her testimony, Public Staff Witness Johnson made an adjustment to remove internal and external lobbying expenses recorded above the line. She explained that she reviewed job descriptions of employees, both registered and non-registered lobbyists, that performed lobbying activities and applied a "but for" test for reporting lobbying costs as used in a State Ethics Commission opinion dated February 12, 2010. As a result, Witness Johnson stated that she excluded not only costs for direct contact with legislators, but also costs for other activities such as preparing for or surrounding lobbying that would not have occurred but for the lobbying itself. (Tr. Vol. 6 at 30-31).

For purposes of this proceeding, the Public Staff Stipulation provides for a reduction in the revenue requirement in the amount of \$42,000 to reflect a downward adjustment for the lobbying costs requested in this case. The Commission finds and concludes that the Public Staff Stipulation's treatment of the lobbying costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Uncollectible Expense

In his direct testimony, Witness McLeod testified that the Company adjusted its uncollectible expense based on a historical average uncollectible expense rate. (Tr. Vol. 4 at 269).

In her testimony, Public Staff Witness Johnson testified that the Company used data from 2014-2018 to calculate its average uncollectibles amount. Public Staff Witness Johnson stated that in 2014 the Company changed its write-off and collections policies for customers with medical certifications, and prior to 2014 the Company did not include these customers in its determination of the reserve for uncollectibles. Witness Johnson explained the result of including these customers now created a \$12.1 million credit accounting adjustment in 2014, on a total system level, to its reserve for uncollectibles accounts, with a charge to uncollectibles expense, in order to establish an initial reserve for customers with medical certificates. Witness Johnson testified that the Public Staff adjusted this amount by only calculating the average uncollectibles based on 2015–2018 data. (Tr. Vol. 6 at 31-32).

For purposes of this proceeding, the Public Staff Stipulation provides that the Company accepted the Public Staff's proposed adjustment to uncollectibles costs, resulting in a reduction of \$238,000 in the Company's revenue requirement. The Commission finds and concludes that the Public Staff Stipulation's treatment of the uncollectibles costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Skiffes Creek

Company Witness Bobby McGuire testified on direct that DENC invests in its electric transmission system to ensure reliability and ongoing compliance with the North American Electric Reliability Corporation (NERC) reliability standards and requirements, address load growth, and repair or replace aging infrastructure, and explained that these investments ensure the Company's continued ability to provide safe, reliable, and economical power to all of its customers. He stated that DENC has invested approximately \$268 million in electric transmission projects located in North Carolina during the period of 2016–2018. Witness McGuire further explained that the Company's electric transmission system investments completed in Virginia also provide benefits to North Carolina customers. (Tr. Vol. 6 at 366-369.)

In his testimony, Public Staff Witness David Williamson provided an overview of the Surry-Skiffes Creek 500 kV transmission project that crosses the James River in Virginia, including the need for the project and the regulatory approvals needed for the project from the Virginia State Corporation Commission, the Army Corps of Engineers, and others. Mr. Williamson stated that the Public Staff takes the position that the mitigation costs for the project were not incurred for the purpose of constructing or operating the project and do not provide additional benefits to the Company's North Carolina retail customers, so those costs should not be recovered from the Company's North Carolina customers. Specifically, Mr. Williamson asserted that the mitigation costs, which are predominantly reflected in a Memorandum of Agreement signed by multiple stakeholders that participated in the project's permitting process, should be excluded from the Company's revenue requirement consistent with Commission

precedent set in the Company's 2012 Rate Case, Docket No. E-22, Sub 479, involving a disallowance of the incremental costs associated with undergrounding three transmission lines in northern Virginia largely for aesthetic purposes. (Tr. Vol. 6 at 447-461).

In her testimony, Public Staff Witness Johnson made an adjustment to remove the costs of the Skiffes Creek project mitigation as explained by Witness Williamson. (Tr. Vol. 6 at 33).

The Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$153,000 to reflect a downward adjustment for the Skiffes Creek mitigation costs requested in this case. The Commission finds and concludes that the Public Staff Stipulation's treatment of the Skiffes Creek mitigation costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Chesterfield Units 3 and 4

In his direct testimony, Company Witness Williams discussed DENC's compliance strategy for complying with federal and state environmental regulations. Witness Williams testified that, to comply with the CCR<sup>12</sup> and the Environmental Protection Agency's (EPA) effluent limitations guideline (ELG)<sup>13</sup> rules, Chesterfield underwent a number of wastewater and environmental improvements in 2017 to transition from wet sluicing coal ash to a dry ash management system. In order to manage the dry coal ash, DENC constructed an onsite, permitted landfill. Witness Williams stated that the onsite landfill has been receiving dry ash since 2017. Overall,

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<sup>12</sup> Hazardous and Solid Waste Management System; Disposal of Coal Combustion Residuals From Electric Utilities, 80 Fed. Reg. 21,301 (Apr. 17, 2015).

<sup>13</sup> Effluent Limitations Guidelines and Standards for the Steam Electric Power Generating Point Source Category, 80 Fed. Reg. 67,837 (Nov. 3, 2015).

Witness Williams testified that the Company's actions to close its ash facilities have been reasonable and prudent. (Tr. Vol. 5 at 90, 93).

In his testimony, Public Staff Witness Jay Lucas testified that in 2015 the Company began making investments to comply with the CCR and the ELG rule, referred to by the Company as the Chesterfield Integrate Ash (CHIA) project. He explained that the CHIA project included wet to dry conversion of several units, among other things, and in June 2015 the Company executed an agreement with a contractor to design and build dry ash handling facilities for Chesterfield Units 3, 4, 5, and 6. Mr. Lucas stated that in its 2015 Integrated Resource Plan (IRP), the Company indicated that Units 3 and 4 would be retired in 2020, but these units were actually retired in March 2018. Mr. Lucas opined that the investment made to convert these two units was not prudent and recommended a disallowance of \$25.7 million, which is 20.7% of the total investment. (Tr. Vol. 6 at 189-191).

In her testimony, Public Staff Witness Johnson made an adjustment to remove the costs associated with the common plant related to Chesterfield Units 3 and 4 based on the recommendation of Witness Lucas. (Tr. Vol. 6 at 33).

The Public Staff Stipulation provides that the costs of the wet-to-dry conversion for Units 3 and 4 at the Chesterfield Power Station should be included in the stipulated revenue requirement, pending resolution of a similar dispute in Virginia.<sup>14</sup> If the final resolution in Virginia results in such costs being removed from the Virginia Rider E revenue requirement, the Company will establish a regulatory liability for estimated

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<sup>14</sup> *Virginia Electric and Power Company, For approval of a rate adjustment clause, designated Rider E, for the recovery of costs incurred to comply with state and federal environmental regulations pursuant to § 56-585.1 A 5 e of the Code of Virginia*, Case No. PUR-2018-00195, Final Order (Aug. 5, 2019); Order Granting Reconsideration (Aug. 26, 2019).

amounts recovered from North Carolina customers associated with the project costs beginning November 1, 2019, and ending on the effective date of rates established in the Company's next general rate case. The amortization of the regulatory liability balance will be incorporated into the revenue requirement developed in the Company's next general rate case. The Commission finds and concludes this resolution of the Chesterfield issue to be appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Outside Services

In her testimony, Public Staff Witness Johnson testified that the Public Staff reviewed costs for outside services, and the Public Staff's investigation revealed charges that were related to legal services for certain expenses that were allocated to DENC that should have been directly assigned to other jurisdictions. Witness Johnson stated that DENC ratepayers should be charged only the reasonable costs of providing electric service to North Carolina retail customers. (Tr. Vol. 6 at 33-34).

The Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$177,000 to reflect a downward adjustment for the outside services costs requested in the case. The Commission finds and concludes that the Public Staff Stipulation's treatment of the outside services costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Mount Storm Fuel Flexibility Project

In his supplemental testimony, Company Witness McLeod proposed to defer as a regulatory asset costs associated with the abandoned Coal Yard Fuel Flexibility Project (CYFFP) at the Company's Mount Storm Power Station (Mount Storm) that was

canceled due to changing market conditions, decreased power prices, and lower capacity factors, and coal consumption at Mount Storm. The Company abandoned the project in May 2019, resulting in an impairment of construction costs incurred on the project totaling \$62.4 million (system-level). Mr. McLeod proposed to defer the portion of the CYFFP costs allocable to the Company's North Carolina jurisdiction to be amortized over a three-year period. (Tr. Vol. 6 at 316).

In his testimony, Public Staff Witness Thomas provided an overview of the Mount Storm CYFFP, which was undertaken to allow the facility to receive 100% of its coal supplies by rail in the event of problems with truck deliveries. Due to quality differences between truck and rail delivered coal and the emissions limits established by Mount Storm air permits, as well as the specific boiler design characteristics of the Mount Storm units, coal blending facilities were required. Witness Thomas testified that DENC originally planned to construct four coal stacking tubes and a dry coal storage enclosure, and to make significant changes to its rail system, along with supplementary fire suppression systems. He testified that not until the adjustment was included in DENC's supplemental filing did the Public Staff become aware of the project and then had an opportunity to review the costs and underlying analyses. Witness Thomas testified that the Public Staff analyzed the Company's financial analyses used in determining the viability of the CYFFP and expressed concerns with the Company's decision-making with respect to future coal prices used in its analyses, contract negotiations with the local trucked coal supplier, and the projected capacity factor of the Mount Storm facility used in its analyses. He also expressed concerns that significant commitments and associated expenditures with the project appear to have been made

prior to completion of detailed engineering work, and relatively little cost-benefit analyses were performed until 2014, three years and \$2.1 million into the project. Witness Thomas concluded that based on his review of forecast data in the Company's past IRPs, the Company should have been more aware of market conditions within both the natural gas and coal markets, and the increased risk that the project would not deliver the expected benefits. In addition, the Public Staff believes that the 2014 cost-benefit analysis justifying the project had significant shortcomings and was not a reasonable or prudent analysis to justify a project that, at the time, had an estimated cost of \$116 million. Witness Thomas recommended that expenditures on the CYFFP after this 2014 analysis should be disallowed for a total of \$60,179,000 system-wide. (Tr. Vol. 6 at 504-526).

In her testimony, Public Staff Witness Johnson made an adjustment to remove certain costs associated with the project as recommended by Public Staff Witness Thomas that are allocable to the Company's North Carolina jurisdiction. (Tr. Vol. 6 at 34-35).

The Public Staff Stipulation provides that 50% of the Mount Storm impairment costs should be removed with the remaining portion amortized over 2.75 years. The Commission finds and concludes that the Public Staff Stipulation's treatment of the Mount Storm CYFFP costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### NUG Contract Termination Expense

In his supplemental testimony, Witness McLeod testified that the Company had a long-term power and capacity contract with a coal-fired NUG with an aggregate summer

generation capacity of approximately 218 MW. Witness McLeod stated that the plant had been, and was expected to remain, generally uneconomical in the PJM Interconnection, LLC (PJM) energy market, and therefore, ran infrequently and was not a key resource for DENC nor does it continue fit within DENC's portfolio of increasingly cleaner generation resources. In May 2019, the Company entered into an agreement and paid \$135.0 million to terminate the contract, effective April 2019. Given the magnitude of the termination fee and the significant capacity savings going-forward, Witness McLeod proposed to defer the North Carolina jurisdictional portion of the termination fee to be amortized over the original remaining term of the contract (32 months—April 2019 through November 2021).

In her testimony, Public Staff Witness Johnson testified that the Public Staff made an adjustment to remove approximately \$21.4 million from the NUG contract termination expense payment associated with the Company's early contract termination. Witness Johnson explained that her adjustment accounts for the "net amount" of capacity revenue that the Company will be receiving from the PJM capacity market as well as the estimated replacement power costs that will be incurred as a result of the termination of the contract. (Tr. Vol. 6 at 35-36).

The Public Staff Stipulation provides that the Company accepted the Public Staff's proposed adjustment to the NUG contract termination expense. The Commission finds and concludes that the Public Staff Stipulation's treatment of the NUG contract termination expense is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Impact on Expenses of Changes in Usage and Number of Customers

In her testimony, Public Staff Witness Johnson testified that the Company adjusted revenues for the change in kWh sales and the number of customers due to customer growth, changes in usage, and weather normalization, but did not make a corresponding adjustment to recognize the changes in the non-fuel variable O&M expenses, which vary due to the change in kWh sales. She also explained that the Company did not make a corresponding adjustment to customer-related expenses to reflect the change in the number of customers. Witness Johnson adjusted these expenses to reflect the changes in kWh sales and the number of billings proposed by the Company in its customer growth, usage, and weather normalization adjustments. (Tr. Vol. 6 at 36-37).

The Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$90,000 to reflect updated and corrected customer growth, usage, and weather normalization numbers. The Commission finds and concludes that the Public Staff Stipulation's treatment of these costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Inflation

In his direct testimony, Witness McLeod testified that the Company adjusted O&M expenses in the cost of service not adjusted elsewhere by increasing them with an inflation factor. He explained that the inflation factor was measured as the difference of the Producer Price Index – Finished Goods less Food and Energy (PPI) between the midpoint of the Test Year and the end of the period from January 1, 2019 – June 30, 2019 (Update Period). (Tr. Vol. 4 at 270).

In his supplemental testimony, Witness McLeod updated the inflation adjustment to reflect the actual PPI for June 2019. (Tr. Vol. 4 at 313).

Public Staff Witness Johnson stated in her testimony that she made additional adjustments in the calculation of the inflation adjustment to reflect the Public Staff's adjustments to the O&M expenses subject to inflation. (Tr. Vol. 6 at 37).

For purposes of this proceeding, the Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$7,000 to reflect updated data related to inflation. The Commission finds and concludes that the Public Staff Stipulation's treatment of the inflation expense is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Customer Growth, Usage, and Weather Normalization

In his direct testimony, Witness McLeod testified that the Company annualized base non-fuel tariff revenues based on projected customer levels and weather-normalized usage as of June 30, 2019. He explained that this adjustment was a net reduction to revenue, primarily reflecting the annualized impact of a return to normal weather on customer usage. In his direct testimony, Company Witness Haynes testified that the adjustments for customer growth, increased usage, and weather normalization are incorporated in Form E-1 Item 42.a, and that the methodologies used to calculate these adjustments are consistent with those approved by the Commission in the 2016 Rate Case. (Tr. Vol. 4 at 259, 411).

In their supplemental testimony, Witnesses McLeod and Haynes updated the calculations based on actual customer growth and usage during the Update Period. Witness Haynes testified that the weather normalization and usage adjustments should

not include Basic Customer Charge revenues in the calculation of the average revenue per kWh applied to the sum of these kWh adjustments. Witness Haynes stated that he made this change in the calculation. (Tr. Vol. 4 at 307, 420).

In his second supplemental testimony, Witness Haynes presented an additional update to the customer growth and usage adjustments to the level of customers used in the calculation. The update is consistent with how customer levels were calculated in the 2016 Rate Case. In his second supplemental testimony, Witness McLeod updated the calculations based on the annualized level of customer usage presented in Witness Haynes' second supplemental testimony. (Tr. Vol. 4 at 430).

The Public Staff Stipulation provides that the Stipulating Parties agreed to increase the revenue requirement in the amount of \$49,000 to reflect the Company's updated and revised kWh sales. The Commission finds and concludes that the Public Staff Stipulation's treatment of these costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Cash Working Capital

In his direct testimony, Witness McLeod testified that the Company made an adjustment to its cash working capital (CWC) based on a lead/lag study prepared using calendar year 2017 data. He further explained that the CWC requirement included in the cost of service per books is adjusted based on the adjusted CWC requirement as determined for regulatory purposes. (Tr. Vol. 4 at 279).

In his supplemental testimonies, Witness McLeod proposed updates to the CWC adjustment to reflect changes in lead/lag days, and the impacts of the various accounting adjustment revisions and updates to the cost of services. (Tr. Vol. 4 at 297, 329).

Public Staff Witness Johnson testified that the Public Staff adjusted CWC under present rates by (1) showing the working capital impact of revenues separate from expenses for presentation purposes, and also (2) reflecting all of the other Public Staff adjustments. Witness Johnson also adjusted CWC for the effect of the Public Staff's proposed revenue decrease. (Tr. Vol. 6 at 38-39).

For purposes of this proceeding, the Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$83,000 and \$282,000 to reflect changes in CWC under present and proposed rates, respectively. The Commission finds and concludes that the Public Staff Stipulation's treatment of these costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### DES Office Building

In his direct testimony Witness McLeod testified that during the second quarter of 2019, the Company planned to occupy a new office building, 600 Canal Place, and made an adjustment to annualize the amount of costs for DENC's direct occupancy of the new building, as well as DENC's billable portion of expenses from DES based on DES' existing methodology to bill its office space and equipment expenses to affiliates. He explained that the Company planned to cease occupying its existing office space after the move and the adjustment reflects the net effect of the increased annual expenses between the two offices. (Tr. Vol. 4 at 267-268).

In his supplemental direct testimony, Witness McLeod testified that, at the time of the of the Application, occupation of 600 Canal Place by DENC and DES employees was expected to begin during the second quarter of 2019. Witness McLeod explained that

DES and the Company began occupying the new building in July 2019 and DES will begin making lease payments in August 2019. The Company's adjustment updated the new lease expense budget for calendar year 2019 and Witness McLeod stated that the expense will be updated again in September 2019 after the actual lease payment is incurred for August 2019. Mr. McLeod's second supplemental testimony updated this accounting adjustment based on the actual corporate-level costs for the month of August 2019, the month in which the lease payments commenced. (Tr. Vol. 4 at 312, 331).

In her testimony, Public Staff Witness Johnson testified that the Public Staff was awaiting additional documentation pertaining to the Company's adjustment to reflect the new office building. Witness Johnson explained that the Public Staff will need additional time to review the adjustments once filed by the Company as they relate to the new office building. (Tr. Vol. 6 at 40-41).

For purposes of this proceeding, the Public Staff Stipulation provides that the revenue requirement should be reduced in the amount of \$720,000 to reflect the updated, actual costs of the Company's new office building. The Commission finds and concludes that the Public Staff Stipulation's treatment of the office building costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

#### Depreciation

In his direct testimony, Witness McLeod testified that the Company made an adjustment to annualize the depreciation expense based on projected plant in service as of June 30, 2019, and the composite depreciation rate from the Company's most recent depreciation study. (Tr. Vol. 4 at 274).

In his supplemental testimony, Witness McLeod updated the depreciation expense based on actual plant in service at the end of the update period. (Tr. Vol. 4 at 317).

In her testimony, Public Staff Witness McCullar testified that she participated in field visits of several DENC facilities or project locations, analyzed the Company's most recent depreciation study, and presented the Public Staff's proposed depreciation rates. Ms. McCullar's Table One provides a comparison of annual depreciation accrual amounts as proposed by the Company versus as proposed by the Public Staff. The table indicates that the Public Staff and the Company are aligned with respect to steam production plant, nuclear production plant, hydraulic production plant, combined cycle production plant, simple cycle production plant, and general plant. The two parties differed, however, with respect to solar production plant, transmission plant, and distribution plant. Ms. McCullar explained that for solar production plant, the Public Staff used updated depreciation schedules that changed the probable retirement year for several solar facilities from 2041 to 2051. Ms. McCullar also explained that the differences in transmission plant and distribution plant depreciation as a difference between the Public Staff's and the Company's proposed future net salvage accrual amounts, as the Public Staff proposed less accelerated future net salvage amounts than the Company. (Tr. Vol. 6 at 476-494).

For purposes of this proceeding, the Public Staff Stipulation provides that the Public Staff accepted the Company's proposed depreciation rates as filed in its Application. The Commission finds and concludes that the Public Staff Stipulation's treatment of the depreciation costs is appropriate and reasonable in this case when considered within the context of the Public Staff Stipulation as a whole.

### Retirement of Cold Reserve Units

In his direct testimony, Company Witness Mitchell testified that, in an effort to reduce costs, uneconomical units that were previously placed in a cold reserve state and are not currently operating will be retired by the end of March 2019. According to Mitchell, these older, less efficient units are unable to compete in the current energy market and have been displaced by cleaner burning natural gas facilities, as well as utility-scale solar. Witness Petrie explained in his direct testimony that ten of these units were older, less efficient units that were placed in a “cold reserve” state in 2018. These units included Bellemeade Power Station, Bremo Power Station units 3 and 4, Chesterfield Power Station units 3 and 4, Mecklenburg Power Station units 1 and 2, Pittsylvania Power Station, and Possum Point Power Station units 3 and 4, all of which were retired from service effective March 31, 2019. Witness Petrie also testified that the Company plans to retire Possum Point unit 5 on May 31, 2021.

In his supplemental testimony, Witness McLeod explained that, as a result of these early retirements, the Company recorded an impairment charge of \$307.1 million, representing the remaining net book value of the units. Related balances in construction work in progress and materials and supplies inventory were written-off as well. Witness McLeod proposed that the Company amortize the impairment cost for the ten units formerly in cost storage over a ten-year levelized basis and the materials and supplies inventory over a three-year period. He also proposed eliminating the O&M expense and materials and supplies inventory for the ten units formerly in cold reserve. Finally, Witness McLeod proposed reestablishing the Possum Point unit 5 net book value and depreciation expense for ratemaking purposes as the unit has not yet been physically

retired from service. He requested that any costs incurred during the decommissioning of these facilities after the Update Period be deferred for review in the Company's next base rate case, consistent with the treatment of decommissioning costs for the Chesapeake Energy Center in the 2016 Rate Case. (Tr. Vol. 4 at 302-304, 348).

The Commission finds and concludes that the Company's treatment of costs associated with the retirement of cold reserve units is appropriate and reasonable in this case.

### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 18-22**

The evidence supporting these findings of fact and conclusions is found in the Company's verified Application and Form E-1, the exhibits and testimony of Company Witnesses McLeod and Haynes, the exhibits and testimony of Public Staff Witness Boswell, the exhibits and testimony of CIGFUR Witness Phillips, and the entire record in this proceeding.

#### Summary of the Evidence

In his direct testimony, Company Witness McLeod described the 2017 Tax Cuts and Jobs Act (TCJA) and the primary elements of the TCJA that impact DENC including a reduction in the federal corporate income tax rate from 35% to 21%. Mr. McLeod explained that the Commission initiated a new proceeding in January 2018 in Docket No. M-100, Sub 148 to address how North Carolina utilities should adjust their North Carolina jurisdictional cost of service and rates in response to the TCJA. Mr. McLeod testified that the Commission directed the Company to collect the federal corporate income tax expense component of rates on a provisional basis beginning January 1, 2018, pending a final order from the Commission in its *Order Addressing the Impacts of the*

*Federal Tax Cuts and Jobs Act on Public Utilities on October 5, 2018*, (TCJA Order).

Mr. McLeod described the filings and orders in that docket and explained that the Company implemented a Commission-approved rate reduction to address certain impacts of the TCJA. Mr. McLeod testified that this included an annual revenue reduction of \$14.3 million and approval of a one-time bill credit to reflect a return of amounts collected provisionally for income taxes at the higher tax rate through existing base rates since January 1, 2018, which will be delivered to customers beginning in the April 2019 billing period for amounts collected provisionally through March 2019. (Tr. Vol. 4 at 282-284).

Mr. McLeod testified that for purposes of federal EDIT, the Company established an overall regulatory liability and began amortizing plant-related federal EDIT on its books and records at a system level as a reduction to income tax expense with an effective date of January 1, 2018. Mr. McLeod explained that this amortization is being deferred to a regulatory liability account in accordance with the Commission's TCJA Order. Mr. McLeod provided a general overview of federal EDIT and explained that the predominant amount of federal EDIT is associated with utility property depreciation and related book-tax timing differences, which are subject to the Internal Revenue Code's normalization rules. This EDIT is referred to as "protected" and the Company is required to use the average rate assumption method (ARAM) for purposes of amortizing such EDIT. Mr. McLeod then presented the federal EDIT balances as of December 31, 2017, at a system level and the portion allocable to the North Carolina retail jurisdiction for plant-protected, plant-unprotected, and non-plant unprotected. The total amount allocable to the North Carolina jurisdiction was \$94.1 million. (Tr. Vol. 4 at 284-288).

Mr. McLeod testified that for ratemaking purposes, the Company has proposed that the effective date of federal EDIT amortization begin on January 1, 2018. He further explained that because the Company is proposing to implement new rates beginning November 1, 2019, that the federal EDIT amortization attributable to the 22-month period of January 1, 2018 through October 31, 2019, would be credited to customers through a one-year decrement rider, Rider EDIT, of \$6,909,000. Finally, Mr. McLeod testified that for periods thereafter, the Company's fully adjusted cost of service includes the income tax benefit arising from annual federal EDIT amortization during the test period, thereby incorporating a going-level of federal EDIT amortization in base non-fuel rates. Mr. McLeod proposed an ARAM method to amortize plant-related federal EDIT (both protected and unprotected) and a 30-year amortization period for non-plant, unprotected federal EDIT. Mr. McLeod presented the proposed annual amount of federal EDIT amortization for the North Carolina jurisdiction of \$2.7 million. Witness McLeod explained that the base non-fuel revenue requirement reflects this amortization providing the customers with an annual revenue benefit of approximately \$3.6 million (\$2.7 million / 74% retention factor). (Tr. Vol. 4 at 290-291).

In Mr. Haynes' direct testimony, he explained the Company's proposal that Rider EDIT credit should be allocated to customer classes based upon North Carolina basic (non-fuel) rate revenue annualized based upon current rates for 2018. Witness Haynes testified that the decrement rate will be applied to customer usage beginning with the effective date of the rider and will be in effect for 12 months. Witness Haynes proposed that, prior to the tenth month from the effective date of the rider, the Company will provide an analysis to the Public Staff to evaluate if the total rider credit will be provided

at the end of the 12 months. If there is a derivation between the total rider credit and the projected credit provided to customers, the Company and the Public Staff will work together to develop an adjustment to the Rider EDIT to minimize the deviation over the remaining months of Rider EDIT being in effect. (Tr. Vol. 4 at 288-289, 401-402).

In his supplemental testimony, Mr. McLeod summarized corrections to the allocation of system-level federal EDIT balances and amortization to the North Carolina jurisdiction resulting from revisions to DENC's cost of service study presented by Witness Miller. As a result of the corrections, the North Carolina jurisdictional federal EDIT balance was revised to \$94.7 million. Witness McLeod explained that the total Rider EDIT rate credit, as revised, reflects a slight \$1,000 increase from \$6,909,000 to \$6,910,000. (Tr. Vol. 4 at 296-297, 325-326).

In his testimony, CIGFUR Witness Phillips acknowledged DENC's proposal to credit to customers through a one-year rider the federal EDIT amortization attributable to the period January 1, 2018 through October 31, 2019, and stated that excess deferred taxes are overpayments that should be returned as soon as possible. (Tr. Vol. 6 at 431).

In her testimony, Public Staff Witness Boswell recommended three adjustments to the Company's proposed treatment of federal EDIT. First, Ms. Boswell stated that she agreed with the Company's proposed ARAM utilization for federal protected EDIT, but could not calculate this amortization due to a lack of a breakout between protected and unprotected EDIT. Ms. Boswell recommended the Company file schedules illustrating this breakout. Second, Ms. Boswell stated that she disagreed with the Company's adjustment to include a portion of unprotected EDIT labeled as "plant-unprotected" to be recovered utilizing the ARAM calculation. Instead, Witness Boswell recommended

including the “plant-unprotected” balance with the unprotected EDIT and collecting the balance on a levelized basis over a five-year period. Finally, Ms. Boswell testified that the entire unprotected EDIT balance should be removed from rate base and be placed in a rider to be collected from ratepayers over a five-year basis. Ms. Boswell testified that the Public Staff does not, in theory, object to the Company’s proposal to flow back federal protected and unprotected amortization since January 1, 2018, as a one-year levelized rider. (Tr. Vol. 6 at 440-443).

In his Stipulation testimony, Mr. McLeod testified that the Stipulating Parties agreed that the Company would implement Rider EDIT to allow for recovery of federal EDIT of \$1.2 million, comprised of the amortization of all unprotected federal EDIT totaling \$8.0 million, partially offset by the refund of approximately \$6.8 million associated with federal EDIT amortization attributable to the 22-month period January 1, 2018 through October 31, 2019. (Tr. Vol. 4 at 340).

#### Discussion and Conclusions

In its TCJA Order, the Commission ordered:

That excess deferred income taxes related to the decrease in the federal corporate income tax rate to 21% under the Tax Act for Cardinal, DENC, DEP, Piedmont, and PSNC, as appropriate, shall be held in a deferred tax regulatory liability account until they can be addressed for ratemaking purposes in each utility’s next general rate case proceeding or in three years, whichever is sooner. These amounts will ultimately be returned to customers with interest reflected at the overall weighted cost of capital approved in each Company’s last general rate case proceeding. Therefore, the Commission concludes that if Cardinal, DENC, DEP, Piedmont or PSNC have not filed an application for a general rate case proceeding by October 5, 2021, each Company shall file its proposal by that date to flow back to its ratepayers both the protected and the unprotected EDIT generated due to the Tax Act. The federal EDIT flow back proposal should include all workpapers that support the proposed calculations... These utilities are hereby required to maintain the deferred tax regulatory liability account previously established and shall not begin amortization of

amounts recorded in such accounts pending further order of the Commission (Ordering Paragraph 6).

This proceeding is the first general rate case filed with the Commission by DENC since the TCJA Order was issued. DENC has complied with the Commission's directive by submitting a proposal to address all federal EDIT related to the decrease in the federal corporate including all workpapers that support the proposed calculations. The Company has also complied with the Commission's directive not to begin amortization of North Carolina jurisdictional federal EDIT until further order of the Commission. DENC meets this requirement given the Company's proposal to begin amortization on January 1, 2018, by proposing to credit amortization during the 22-month period from January 1, 2018 through October 31, 2019, the effective date of rates in this case, to customers through a decrement rider, Rider EDIT. In addition, for periods thereafter, the Company's cost of service for ratemaking purposes includes the income tax benefit arising from annual federal EDIT amortization during the test period, thereby incorporating a going-level of federal EDIT amortization in base non-fuel rates.

The Public Staff, through Witness Boswell, recommended including the "plant-unprotected" balance with the unprotected EDIT and collecting the balance through a rider to be collected from ratepayers over five years on a levelized basis, with carrying costs. Ms. Boswell testified that this treatment is consistent with the same methodology previously recommended by the Public Staff.

The Stipulating Parties agree that the Company shall implement Rider EDIT to allow for recovery of certain federal EDIT. The Public Staff Stipulation provides that the appropriate level of federal EDIT to be recovered by the Company in this case is \$1,214,000 (on a pre-income tax basis), which includes 1) the amortization of all

unprotected federal EDIT totaling approximately \$8.0 million partially offset by 2) the refund of approximately \$6.8 million associated with federal EDIT amortization attributable to the 22-month period January 1, 2018 through October 31, 2019. Rider EDIT will be implemented to recover certain federal EDIT from customers over a two-year period on a levelized basis, with a return. As reflected on Settlement Exhibit II, the appropriate amount to be recovered from customers is a total of \$1,299,369. Rider EDIT should be calculated and reviewed using the methodology presented in the testimony of Company Witness Haynes.

On September 25, 2019, the Commission issued an *Order Requesting Additional Information* and ordered that the Public Staff make a filing providing an explanation of why DENC's total unprotected EDIT has a debit balance as the Commission has not yet seen a debit balance in its consideration of EDIT issues related to the TCJA. On October 7, 2019, the Public Staff filed a response to this request. The response referenced the testimony and exhibits of Company Witness McLeod which provided details regarding the Company's balance of unprotected federal EDIT. Specifically, Mr. McLeod's testimony and exhibits demonstrate that the largest debit balance for non-plant unprotected EDIT related to pension benefits. The Public Staff reviewed the causation of the debit balance for the aforementioned account and determined the debit balance was due to the status of funding for the Company's pension plan. As of December 31, 2017, the Company's projected benefits obligation from its pension plan was larger than the amount that had been funded for the plan, resulting in a net pension liability on the Company's books. This in turn resulted in a deferred tax asset on the Company's books, and thus an EDIT asset. The Public Staff also analyzed how the Company divided its

plant-related protected and unprotected EDIT during the discovery process. The Public Staff ultimately agreed with the Company's division of plant-related EDIT between protected and unprotected components, which resulted in the unprotected portion having a relatively small debit balance.

The Commission finds and concludes that DENC has met the directives specified in the TCJA Order with regard to federal EDIT. The ratemaking treatment of federal EDIT, including Rider EDIT presented in the Public Staff Stipulation, is just and reasonable to all parties in light of all the evidence presented.

#### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 23-25**

The evidence supporting these findings of fact and conclusions is found in the verified Application, the direct testimony and exhibits of Company Witnesses Petrie and Haynes, the supplemental testimony of Witnesses Petrie, Haynes, and McLeod, the additional supplemental testimony of Witness Haynes, the testimony and exhibits of Public Staff Witness Floyd, the Public Staff Stipulation, and the entire record in this proceeding.

##### Summary of the Evidence

In his direct testimony, Company Witness Petrie presented an estimate of DENC's adjusted system fuel expense for the period July 1, 2018 – June 30, 2019, of \$1.803 billion, which was used by Company Witness Haynes to estimate the anticipated reduction in the fuel factor rate. He also estimated a cumulative fuel under-recovery position for the 12-month test period ending June 30, 2019, of approximately \$1–3 million, and described DENC's forecasted fuel expense over-recoveries for the second

half of 2019 and how those over-recoveries could offset the expected under-recovery as of June 30, 2019. (Tr. Vol. 6 at 345-350).

Witness Haynes calculated the projected normalized North Carolina jurisdictional average fuel factor and differentiated that rate by voltage for each class. These calculations were consistent with the methodologies used in the Company's 2018 fuel case, except that he updated the class expansion factors for 2018. Mr. Haynes also presented DENC's projected EMF and total projected change in its fuel factor to be filed in its 2019 fuel proceeding. (Tr. Vol. 4 at 397-400).

Witness Petrie also testified that the Company evaluated the current Marketer Percentage calculation and updated the calculation based on the PJM State of the Market Reports for 2017 and 2018 using the same averaging method applied in the 2018 Fuel Case and the 2016 Rate Case. Using this method, Mr. Petrie calculated an updated Marketer Percentage of 71%. (Tr. Vol. 6 at 345-350).

In his direct testimony, Witness McLeod testified that adjustments to purchased energy expenses reflect an updated Marketer Percentage of 71% supported by Company Witness Petrie. Mr. McLeod stated that the base fuel rate revenue requirement in the supplemental filing will reflect the 71% Marketer Percentage. (Tr. Vol. 4 at 245).

In his supplemental testimony, Mr. Petrie presented an updated adjusted total system fuel expense for the twelve-month period ending June 30, 2019, of \$1.78 billion, based on the 71% Marketer Percentage proposed in the Company's Application. (Tr. Vol. 6 at 355-356).

In his direct testimony, Company Witness Haynes testified that while the Company's fuel factor is adjusted annually by the Commission between general rate

cases, the Commission also resets the Company's base fuel factor in each base rate case as required by subsection (f) of the North Carolina fuel factor statute, N.C. Gen. Stat. § 62-133.2. Company Witness Haynes proposed to initially set a placeholder base fuel rate for each class based on the fuel factor approved in the Company's 2018 fuel adjustment case, Docket No. E-22, Sub 558 (2018 Fuel Case). He further testified to the Company's proposal to set Rider A – Fuel Cost Rider to zero beginning November 1, 2019, and to use the fuel rate as approved in the 2018 Fuel Case, differentiated by class, as the placeholder base fuel rate in each of the rate schedules. Mr. Haynes stated that the Company planned to update the placeholder base fuel rate after the Company filed its annual fuel factor application in August 2019. (Tr. Vol. 4 at 397-398).

In his supplemental testimony, Mr. Haynes updated the placeholder base fuel rate and proposed a new rider, decrement Rider A1, which the Company planned to file in its August 2019 fuel factor application. Mr. Haynes testified that because the Company was anticipating an over-recovery of fuel expenses for the period of July 2019 to December 2019, and to mitigate the effect of the November 1, 2019, non-fuel base rate increase on customers' rates, the Company was proposing to implement a three-month decrement rider, Rider A1. Mr. Haynes testified that Rider A1 would allow for a seamless, no impact transition of total fuel rates between November 1, 2019, and February 1, 2020, based on the Company's anticipated fuel factor filing. Finally, he explained that the Company anticipated making an additional supplemental update in this proceeding to calculate the revised base fuel rates by customer class using the information in the Company's August 2019 fuel factor application. (Tr. Vol. 4 at 416, 423-424).

In his additional supplemental testimony, Witness Haynes used the updated adjusted total system fuel expense presented in the Company's 2019 fuel factor filing to calculate an average fuel factor of \$0.02092/kWh. He also used the revised Rider A rate of zero, to be effective on November 1, 2019, consistent with the Company's 2019 fuel factor filing. Finally, Witness Haynes explained that the amount used for decrement Rider A1 was based on an estimation that the Company will over-recover fuel expenses from July through December 2019 by approximately \$11.8 million, with the rider being the difference between the proposed February 1, 2020, Fuel Rider B EMF Rate and the current EMF Rider B rates that became effective on February 1, 2019. Mr. Haynes stated that including the proposed base fuel rate, the proposed Fuel Rider A re-set to \$0.000000/kWh, the proposed Rider A1 rates, and the present EMF Rider B, the Company proposed to implement a total jurisdictional average fuel rate of \$0.02105/kWh on November 1, 2019, a decrease of \$0.00425 compared to the present total jurisdictional average fuel rate of \$0.02530/kWh. (Tr. Vol. 4 at 428-431).

Public Staff Witness Floyd testified the Public Staff did not have any concerns with the Company's proposed fuel rates for purposes of this proceeding and that the Public Staff would address any concerns with fuel rates in the 2019 Fuel Case proceeding in Docket No. E-22, Sub 579. Mr. Floyd also stated that the Public Staff did not oppose implementing the Company's proposed total fuel rate as part of the interim rates on November 1, 2019, along with the proposed decrement Rider A1. (Tr. Vol. 6 at 81-83).

In her testimony, Public Staff Witness Johnson adjusted the fuel clause expense to reflect the base fuel rate and Rider A as set forth in the Additional Supplemental Testimony of DENC Witness Haynes and recommended by Public Staff Witness Jack

Floyd, subject to the outcome of the Company's currently ongoing fuel proceeding in Docket No. E-22, Sub 579. Witness Johnson stated that this adjustment resulted in a decrease of \$2.155 million from the fuel expense originally included in the Company's Application. (Tr. Vol. 6 at 39).

Section V.A of the Public Staff Stipulation provides that a decrease of \$2.155 million in the Company's base fuel revenue requirement, incorporating the base fuel rate and Rider A as set forth in the Additional Supplemental Testimony of Company Witness Haynes and recommended by Public Staff Witness Floyd, was appropriate to be included in the Company's base rates, subject to any adjustment based on the outcome of the Company's ongoing 2019 Fuel Factor proceeding. The Stipulating Parties also agreed that decrement Rider A1, equal to (\$0.00375) per kWh on a jurisdictional basis, is appropriate to become effective on November 1, 2019.

#### Discussion and Conclusions

Based on all of the evidence in this proceeding, the Commission finds and concludes that the stipulated base fuel factor of \$0.02105/kWh is just and reasonable for DENC in this case. This reflects the proposed base fuel rate, proposed Fuel Rider A, the proposed Rider A1, and the present EMF Rider B and is subject to any adjustments made in the Company's 2019 fuel factor application.

No party opposed the Company's proposed Marketer Percentage. Based on all of the evidence in this proceeding, the Commission finds and concludes that effective February 1, 2020 a Marketer Percentage of 71%, to be applied to appropriately determine the fuel cost component of energy purchased for which the fuel cost is unknown, and

shall remain in effect until approval of a new Marketer Percentage in the Company's 2021 fuel factor filing or next general rate case, whichever is earlier.

### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 26-30**

The evidence supporting these findings of fact and conclusions is found in the verified Application and exhibits, the Stipulation, and the testimony of Company Witnesses Miller and Haynes, Public Staff Witness Floyd, Nucor Witnesses Thomas and Wielgus, CIGFUR Witness Phillips, and the entire record before the Commission in this proceeding.

#### Summary of the Evidence

The Company's Application, as supported by Company Witnesses Miller and Haynes, used the SWPA cost of service methodology to allocate production and transmission plant costs for both the North Carolina jurisdiction and the North Carolina retail customer classes. The SWPA method recognizes two components of providing service to customers – peak demand and average demand – when determining the responsibility for costs of production and transmission plant and related expenses. The peak demand component takes into account the hour when the load on the system is highest during both the summer months and the winter months. The average demand component recognizes that there is a load incurred by the system over the course of all hours during the year. The average demand is determined based upon the total energy provided to the customers during the year divided by the total number of hours in the year. The average component is then weighted by the system load factor, and the peak component is weighted by 1 minus the system load factor. The load factor is calculated

by taking the Company's actually experienced average demand divided by its actually experienced peak demand during the test year.

Witness Miller explained that DENC developed and presented in its Form E-1, Item 45, the "per books," annualized, and "fully-adjusted" jurisdictional and customer class cost of service studies for the test year ended December 31, 2018. Witness Haynes explained that in developing the SWPA cost of service study (COSS), the Company also made two adjustments in the course of calculating the SWPA allocation factors. The first is an adjustment to the Company's recorded summer and winter peaks to recognize and add back the kW generated by NUGs interconnected to DENC's distribution system that are not included in those values. Mr. Haynes testified that this adjustment was approved by the Commission in the Company's 2016 Rate Case. The second is an adjustment to remove the demand and energy requirements of three customers, one wholesale customer, NCEMC, and two large industrial customers in the Company's Virginia jurisdiction, for whom the obligation to provide generation service has ended or will end during 2019. (Tr. Vol. 4 at 374, 509).

Witness Miller testified that the objective of jurisdictional and customer class cost of service studies is to determine the allocation of a share of the system's revenues, expenses, and plant related to providing service across multiple jurisdictions. Certain items can be assigned directly to the jurisdiction and classes based on the utility's records, but other items are not directly assignable and must be allocated. Witness Miller stated that in this proceeding, the Company allocated its production and transmission plant and expenses using the SWPA cost of service methodology. He noted that the Commission has approved DENC's use of the SWPA method in DENC's last six general

rate cases, dating back to 1983, including the 2016 Rate Case. Witness Haynes testified that the SWPA allocation method is consistent with the manner in which DENC plans and operates its system. Specifically, the “Summer and Winter” peak component recognizes the total level of generation resources necessary to serve the system peaks, while the average component recognizes the type of generation serving customers’ energy needs year-round. (Tr. Vol. 4 at 371-373, 502-510).

Witness Haynes also emphasized that use of a single peak or other peak-only methodology could allow certain customer classes that have zero demand during the peak hour(s) of the year to fully avoid responsibility for production plant costs. Mr. Haynes explained that a common example is streetlights that normally do not operate during peak hours. Mr. Haynes also highlighted the NS Class as another example unique to DENC’s North Carolina jurisdictional load. Mr. Haynes explained that Nucor, the only customer in the NS Class, has an average annual demand throughout the year of approximately 106 megawatts (MW), while Nucor’s average of its summer (July 2, 2018) and winter (January 7, 2018) coincident peak demands is approximately 42 MW. Witness Haynes explained that without recognizing an average component in the cost allocation, this customer class would “pay” for only 42 MW and escape cost responsibility for an average of 64 MW for the rest of the year (i.e., the average demand of 106 MW less the allocated demand of 42 MW). Mr. Haynes explained that by recognizing both the energy needed to serve load at the peak hour, as well as energy consumed throughout the year, the SWPA method allocates some portion of these system costs to all customers, including those customers that can reduce their peak demand and those that may not place a demand on the system during the respective summer and winter peak hours. Such

customers still use and receive the benefit of the Company's investments in production assets by paying lower energy costs, specifically fuel costs, during all other hours. (Tr. Vol. 4 at 371-374).

Public Staff Witness Floyd agreed with the Company's use of the SWPA cost of service methodology in this proceeding because it appropriately allocates the Company's production plant costs in a way that most accurately reflects the Company's generation planning and operation. He testified that unlike other methodologies that allocate all of the production plant costs based on a single coincident peak or on a series of monthly peaks, the SWPA methodology recognizes that a portion of plant costs, particularly for base load generation, is incurred to meet annual energy requirements throughout the year and not solely to meet peak demand at a particular time. Witness Floyd also stated that the Public Staff agrees with DENC's proposed adjustments to the COSS as appropriately recognizing the impact of distribution connected NUGs and the removal of wholesale contract load in 2020 on DENC's utility system. (Tr. Vol. 6 at 68-72).

CIGFUR Witness Phillips testified that the SWPA method is inconsistent with both DENC's method of planning for future capacity requirements, and the increase in the portion of its generating mix represented by natural gas, as outlined in its 2018 IRP. Mr. Phillips also claimed that the SWPA method over-allocates cost to large, high load factor customers without a symmetrical fuel cost allocation. Mr. Phillips advocated for the use of the Summer/Winter Coincident Peak (S/W CP) cost of service methodology as consistent with system planning and cost causation principles, arguing that the S/W CP corrects over-allocations of costs to large, energy intensive industrial customers, such as those on the Company's Schedule 6VP. (Tr. Vol. 6 at 422-425).

Nucor Witness Wielgus did not recommend that the 1-Coincident Peak (1-CP) methodology be used in the cost of service study in this proceeding, but he did recommend that the Commission examine in a formal proceeding whether using a 1-CP or 5-CP method instead of the Company's proposed SWPA would be most appropriate for DENC given the way that PJM uses coincident peaks and that Duke Energy conducts its cost of service studies for its North Carolina jurisdiction. Mr. Wielgus argued that the SWPA fails to properly recognize the system's need for generation and is not consistent with the Company's primary need for generation capacity, which is to serve its annual peak demand. Mr. Wielgus also argued that the SWPA method fails to recognize the system benefits associated with the NS Class. In particular, Mr. Wielgus noted that Nucor's facility comprises approximately 20% of the Company's load, has a high load factor that is beneficial to the Company's system operations and corresponding costs, and the service to Nucor is not firm and Nucor must curtail if called upon to do so. Mr. Wielgus calculated a value of the capacity that is avoided when Nucor is curtailed based on its peak load of 172 MW and its load during the summer and winter peak hours of 42 MW and claimed that if Nucor were a firm customer, the Company would have to secure an additional 129 MW of capacity every day of the year at an annual cost of \$5.7 million. (Tr. Vol. 6 at 378-400).

Nucor Witness Thomas presented two variations on the allocation of production costs using a 1-CP model and a re-weighted Summer Winter Peak and Average (reweighted SWPA) model. Witness Thomas explained that for the 1-CP model he replaced the SWPA allocator with the single highest coincident peak demand, which in this proceeding was the winter peak demand net of North Anna. In the reweighted

SWPA, Witness Thomas explained that he used a 60% weight for the summer/winter peak demand component and a 40% weight for the average demand (energy) component. Witness Thomas concluded that under the 1-CP scenario, Nucor would have a relative rate of return (ROR) index before the revenue increase of 3.10, which is significantly higher than the 0.84 index computed by the Company under its SWPA scenario. In the reweighted SWPA, Nucor has a relative ROR of 1.20 before the revenue increase. Finally, he explained that to achieve a ROR index of 0.80 for Schedule NS, as the Company's SWPA methodology does, Nucor's base revenue would have to decrease by nearly \$10.5 million under the 1-CP scenario and \$2 million under the reweighted SWPA scenario. (Tr. Vol. 6 at 404-408).

Company Witness Haynes extensively addressed and rebutted the cost of service arguments of Witness Phillips on behalf of CIGFUR and Witness Wielgus on behalf of Nucor in his rebuttal testimony. Witness Haynes explained that the SWPA method reasonably and appropriately recognizes the two components of providing service to customers, peak demand and average demand, and is consistent with the manner in which the Company's planning department plans for and meets DENC's system needs, taking into consideration the need both to meet peak demands and to provide resources that can be operated to serve customers throughout the year. The Company's SWPA cost of service study followed the same approach for Schedule NS (as well as all other classes) used in the cost of service studies filed and approved in DENC's three most recent rate cases, Sub 532, Docket No. E-22, Sub 479 in 2012, and Docket No. E-22, Sub 459 in 2010. Specifically, as described by Company Witness Haynes, the Company used both a summer and winter peak demand for the NS Class that reflected Nucor's measured

demand and recognized the interruptible nature of Nucor's arc furnace pursuant to the confidential terms and conditions of the Company's contract with Nucor. The 42 MW of peak demand assigned to the NS Class represents the average of the winter and summer peaks of the NS Class at the time of the test year system winter and summer peaks.

These peak demands were used to develop the production plant and transmission related demand allocation factors.

Mr. Haynes explained that the "Summer and Winter" peak component recognizes the total level of generation resources necessary to serve the system peaks, while the average component recognizes the dispatch of different types of generation providing the system with low cost energy year-round. Mr. Haynes pointed to the Company's recent addition of the 1,588 MW Greenville County CC, as well as the Company's historical investments in its baseload fleet as production-related plant operated throughout the year to provide baseload energy to the Company's customers. Mr. Haynes also specifically pointed to the Company's investment in nuclear plant at the end of 2018 that represented approximately 26% of the total production plant invested. He also reiterated the Commission's consistent support for the Company's continued use of the SWPA methodology as the proper method to assign production plant costs to all customer classes, including the Schedule NS Class. (Tr. Vol. 4 at 436-447).

Witness Haynes testified that the S/W Coincident Peak methodology advocated by CIGFUR Witness Phillips is not reasonable or appropriate for DENC because its reliance on only the two hours of DENC's summer and winter peaks is inconsistent with the way DENC plans and operates its system to meet the system peaks and deliver low

cost energy throughout the year. He also explained that use of the S/W CP would result in a significant shift of costs to the residential class. (Tr. Vol. 4 at 437-438).

Witness Haynes also testified that Witness Wielgus' recommendation that the Commission examine in a formal proceeding whether using a 1-CP or 5-CP method instead of the SWPA would be most appropriate for DENC is misplaced. Witness Haynes argued that such a method would increase the total North Carolina jurisdictional revenue requirement and significantly shift costs to the residential class while benefitting Nucor and the LGS and 6VP classes. Mr. Haynes testified that regardless of the methodology approved by the Commission for use by Duke Energy, it is appropriate for the Commission to consider the usage characteristics of customers and the generation system's planning and operation for each utility to determine an appropriate allocation method, rather than not uniformly applying a particular method to all utilities. (Tr. Vol. 4 at 437-466).

With respect to Mr. Wielgus' recommended modifications to the weighting of the peak demand and average components in the SWPA method as proposed by the Company, Mr. Haynes stated that the modifications are not consistent with the way customers use the Company's production and transmission systems and would result in a shift in cost responsibility from Nucor and other non-residential classes to the residential class, resulting in a higher increase in rates for residential customers than proposed by the Company. (Tr. Vol. 4 at 437-466).

Mr. Haynes also responded to Witness Wielgus' claims regarding the benefits provided by Nucor to the Company's system, stating that the service arrangement with Nucor only requires a partial curtailment of its furnace load but not its total load and the

Company is restricted in the number of hours such load can be curtailed. He noted that while Nucor's load factor may be considered higher than load factors for residential and small general service classes, it is not in the range of higher load factor customers in the LGS class. Witness Haynes also performed analyses of the value of Nucor's avoided capacity to the Company, concluding that while there was considerable value of curtailment to be considered in setting rates, the value was not as high as calculated by Witness Wielgus. Witness Haynes also analyzed the benefit to the North Carolina jurisdiction and Nucor of recognizing Nucor's actually-curtailed peak load under the SWPA method. He concluded that recognizing Nucor's curtailed demand in developing the allocation methodology provides a significant and properly recognized financial benefit to Nucor, as well as a lower overall allocation of system costs to the North Carolina jurisdiction. He explained that the Company's SWPA allocation factors were calculated in a reasonable manner – consistent with the principles approved in DENC's 2016 Rate Case – that appropriately recognizes the value of Nucor's interruptibility to the system and does not overstate cost or understate returns for the North Carolina jurisdiction and its customer classes. (Tr. Vol. 4 at 437-466).

In the Public Staff Stipulation, the Stipulating Parties agreed that the Company's SWPA methodology calculated using the system load factor to weight the average component and  $(1 - \text{system load factor})$  to weight the peak demand component is appropriate for use in allocating the Company's per books cost of service to the North Carolina jurisdiction and between the customer classes in this case. The Public Staff Stipulation also agreed to the two adjustments made in the course of calculating the SWPA as described above.

The CIGFUR Stipulation states that, for purposes of settlement only, the parties agreed that the Company's SWPA methodology, calculated using the system load factor to weight the average component and  $(1 - \text{system load factor})$  to weight the peak demand component is appropriate for use in allocating the Company's per books cost of service to the North Carolina jurisdiction and between customer classes in this case. The CIGFUR Stipulation also provides that the parties agree to the two adjustments the Company made in the course of calculating the SWPA. The parties did not reach a compromise on the total base revenue increases the Company proposed to assign to the LGS and 6VP customer classes or the Company's proposed rates of return for the customer classes. The parties agreed that in the next general rate case, the Company would file the results of a class cost of service study with production and transmission costs allocated on the basis of the Summer/Winter Coincident Peak method in addition to the SWPA used in this proceeding and consider such results for the sole purpose of apportionment of the change in revenue to the customer classes. They also agreed that considering that no customers have taken service under the pilot RTP rates filed by the Company and approved by the Commission in Sub 532, the Company will work with CIGFUR to consider whether certain provisions within those rates should be modified. If there is mutual agreement between CIGFUR and DENC to such modifications, and CIGFUR indicates that at least one of its member customers is willing to take service under such rates, DENC agrees to re-file such rates with the Commission for approval with the modifications agreed upon within 60 days of such agreement.

At the hearing and on redirect examination, Mr. Haynes testified that under the alternative cost allocation methodologies proposed by Nucor and CIGFUR, Nucor would

receive a rate decrease, and the residential class would receive rate increases ranging from approximately \$20 million to \$63 million, as compared to the \$17 million increase provided in the Company's supplemental filing. (Tr. Vol. 5 at 48-50).

### Discussion and Conclusions

The Commission finds and concludes that DENC has carried its burden of proof to show that the Company's SWPA methodology is the most appropriate cost of service methodology to use in this proceeding to assign cost responsibility for production plant to the North Carolina jurisdiction and the Company's customer classes. On this issue, the Commission gives substantial weight to the testimony of Company Witnesses Haynes and Miller and Public Staff Witness Floyd, and both Stipulations. The cost of service methodology employed in establishing an electric utility's general rates should be the one that best determines the cost causation responsibility of the jurisdiction and various customer classes within the jurisdiction based on the unique characteristics of each class' peak demands and overall energy consumption. Witness Haynes testified extensively that the Company's investments in generating plant, including the recently placed in service Greenville County CC, are designed to meet the Company's system peaks and to deliver low cost energy throughout the year. Witness Haynes explained that the SWPA methodology appropriately recognizes that DENC's system planning is designed to meet both the Company's peak and average system demands and energy needs of customers throughout the year. Both Company Witnesses Haynes and Miller and Public Staff Witness Floyd testified that the SWPA method appropriately matches allocation of production plant with DENC's generation planning and operations. The Commission finds that, for purposes of this proceeding, the SWPA cost of service methodology

properly recognizes the manner in which DENC plans and operates its generating plants to provide utility service to customers in North Carolina.

Based on the facts in this case, a methodology that does not properly consider the effect of overall energy consumption, but focuses mainly on peak responsibility, such as the 1-CP methodology, would not properly represent the way in which the Company plans for and provides its utility service and the way customers use that service. The Commission is not persuaded that either the S/W CP methodology or the 1-CP methodology is appropriate for the Company in this proceeding, nor does the Commission see the need to open a formal proceeding to investigate the implementation of a 1-CP or 5-CP methodology for DENC in future rate cases. The disparity between allocation factors for peak demand-related factors and energy-related factors is apparent for each methodology, with the SWPA resulting in the most equitable sharing of the rate of return among DENC's customer classes in this case. Because the Commission finds that the SWPA method is not unreasonable or flawed, the Commission does not find Nucor Witness Wielgus' arguments as to the inappropriateness of the SWPA methodology proposed by the Company in this proceeding persuasive. The Commission also continues to find and conclude that cost allocation does not lend itself to a one size fits all approach, and the specific circumstances of each utility must be considered when determining the appropriate cost allocation methodology for that utility.

Based on the Stipulations and the testimony on the record, the Commission also finds that including the distribution-interconnected NUG generation in the average portion of the SWPA, but not including this NUG generation in the Company's recorded summer and winter peaks creates a mismatch between the peak and average components

of the Company's SWPA COSS. The Commission concludes that the Company's adjustment to the summer and winter peaks to recognize the NUG generation at the distribution level appropriately recognizes the impact those NUGs have on DENC's utility system and is approved.

Based on the Stipulations and the testimony on the record, the Commission also finds that the adjustment to remove demand and energy requirements of three customers for whom the obligation to provide generation service has ended or will end in 2019 is appropriate.

Based on the evidence in this proceeding, including the Stipulations, the Commission finds and concludes that the greater weight of the evidence shows that the SWPA cost of service methodology provides the most appropriate methodology to assign fixed production costs by incorporating DENC's seasonal peak demands at the two single hours they occur and by incorporating the total energy consumed by the jurisdiction and customer classes over all the other hours of the year. In addition, the Commission finds good cause to require that the Company should continue to file a cost of service study using the SWPA methodology annually with the Commission.

Moreover, as a result of the opposing testimony between the DENC and CIGFUR witnesses, the Commission finds and concludes that the CIGFUR Stipulation is the product of the give-and-take between the parties during their settlement negotiations in an effort to appropriately balance DENC's usage of the SWPA and CIGFUR's desire to investigate a different methodology for the sole purpose of apportionment of the change in revenue to the customer classes in the next general rate case. The Commission finds and concludes that the CIGFUR Stipulation was entered into by the parties after

substantial discovery and negotiations, and that it represents a proposed negotiated resolution of the matters in dispute in this docket. As a result, the CIGFUR Stipulation is material evidence to be given appropriate weight in this proceeding.

Finally, based on the entire record in this proceeding, the Commission is persuaded that the Company has treated the NS Class and Nucor appropriately in its cost of service study and that no additional recognition of the benefits associated with the Nucor contract should be made in this proceeding. The facts and evidence in this proceeding show that the Company has consistently followed the same approach in this case of recognizing the benefits of Nucor's interruptibility – to both Nucor and the North Carolina jurisdiction – consistent with DENC's approach in the Company's past three rate case proceedings. Further, the curtailment provisions in the Nucor agreement have not been modified since last reviewed by the Commission in 2016. Nucor's contract with the Company provides Nucor with flexibility in deciding how and when it consumes energy for the vast majority of hours in the year and the Company's treatment of Nucor through its SWPA methodology is reasonable and appropriate.

### **EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 31**

The evidence supporting this finding of fact and conclusions is found in the verified Application, the testimony of Company Witness Haynes, Public Staff Witness Floyd, CIGFUR Witness Phillips, Nucor Witness Wielgus, the Public Staff Stipulation, and the entire record in this proceeding.

#### Summary of the Evidence

The Application and the testimony and exhibits of Company Witness Haynes explain how DENC proposed to apportion the jurisdictional revenue requirement

established using the Company's SWPA jurisdictional and class COSS among the customer classes. Witness Haynes' testimony and exhibits assigned the revenue requirement to specific rate schedules and then calculated the percent increase that customers on each rate schedule would experience.

In apportioning the revenue requirement among the customer classes, Witness Haynes identified general and class-specific principles that the Company used to equitably distribute the base rate revenue increase, including: (1) all classes should share in the nonfuel base rate revenue increase in a manner that moves each class of customers closer to parity with the North Carolina jurisdictional ROR; (2) generally, if a customer class has a ROR index less than 1.00, such class should receive a percentage increase that is greater than the overall jurisdiction percentage base rate increase. If a customer class has a ROR index greater than 1.00, such class should receive a percentage increase that is less than or equal to the overall jurisdiction percentage base rate increase; (3) for classes outside of a reasonable return index range of 0.90 and 1.10 (Parity Index Range), an effort must be made to more reasonably align the rates customers pay with their responsibility for cost, even if the index achieved after apportionment still remains outside of the Parity Index Range; (4) for purposes of apportioning the increase for the LGS, 6VP, and NS classes, which include the Company's large non-residential customers, in addition to the class rates of return and resulting indices, consideration should also be given to the appropriate increase for these customer classes based upon certain non-cost factors that support a lesser increase for large industrial customers with high load factors; and (5) for purposes of apportioning the increase to the NS Class, the Company recognized the need to equitably address the unique nature of the Company's

electric service arrangement with its largest and most energy-intensive customer, Nucor. (Tr. Vol. 4 at 384-387).

Specific to the non-cost considerations that DENC took into account in apportioning the revenue increase among the industrial customer classes, Witness Haynes testified that he considered the quantity and timing of large industrial manufacturing customers' electric usage in their industrial operations, as well as factory utilization and the economic vitality of the Company's North Carolina service territory, as it relates to these industrial customers. Witness Haynes then presented a summary table of the Company's allocated rate base, class rate of returns, apportionment of the non-fuel base rate increase, and the class rates of return after apportionment. Mr. Haynes then detailed the proposed apportionment by class, and explained that while the Company's customers would experience an increase in non-fuel base rates, this increase would be substantially moderated after taking into account certain reductions, like that anticipated for the fuel component of rates. (Tr. Vol. 4 at 378-395).

After explaining how the proposed non-fuel base revenue increase was apportioned across customer classes, Witness Haynes discussed how the components of the rate schedules are adjusted to achieve the non-fuel base rate increases. Mr. Haynes stated that the target percentage increase listed by class in his summary table is applied to the total present revenue to calculate the target revenue increase for the rate schedule. Then, Mr. Haynes explained, a factor is used to adjust each rate component and applied to the present rates to develop a proposed rate that would result in the propose revenue requirement. Mr. Haynes noted that this information is included in Columns (7) through (14) of the Company's Form E-1 Item 42a summary sheet. Finally, Mr. Haynes noted

that the rate design method used in this proceeding generally produced a proposed customer charge less than the fully-supported customer charges presented by Mr. Miller. (Tr. Vol. 4 at 395-397).

In his testimony, Public Staff Witness Floyd disagreed with the Company using only the base non-fuel revenue to calculate class rate of returns and instead recommended that DENC use both base fuel and base non-fuel revenues to determine base revenue assignment. Witness Floyd testified that, consistent with past rate cases, several principles should be taken into account when apportioning any combined base fuel and base non-fuel revenues among the various classes, all of which attempt to assign the revenue requirement to each customer class in an equitable and fair manner and to minimize rate shock to any individual class. Finally, Witness Floyd explained that because the Public Staff recommended a total revenue decrease, all of the traditional principles the Public Staff rely on in apportioning the revenue requirement are not necessarily applicable. Mr. Floyd testified that it is still appropriate to focus on addressing any disparities in the class rate of returns when apportioning the decrease, but any individual customer class revenue decrease should be limited so that no individual customer class sees an increase in its assigned revenue requirement. (Tr. Vol. 6 at 72-77).

In his testimony, Nucor Witness Wielgus disagreed with Witness Haynes' rate design as it relates to Nucor and the proposed 0.80 rate of return index for the Schedule NS class. Mr. Wielgus recommended that the percentage increase in base rates to Schedule NS should not exceed the average of the percentage increases applied to rate schedules in the LGS and 6VP classes. (Tr. Vol. 6 at 393-396).

In his testimony, CIGFUR Witness Phillips noted that the Company's proposed distribution of the revenue increase moves the rate of return for the 6VP and the LGS classes closer to cost and the system average rate of return. Mr. Phillips recommended that because the Company's proposed method of distributing the requested increase to classes moves rates closer to cost in a meaningful manner, it should be implemented as proposed. (Tr. Vol. 6 at 417-422).

In his rebuttal testimony, Witness Haynes noted that Witness Phillips' comment that the 6VP class has been providing "excess returns" to DENC, and pointed out that the same is true for the LGS class and that both classes are important to the Company's North Carolina service territory, with rate of return indices well above the Parity Index Range at 1.33 for the LGS class and 1.22 for the 6VP class. Mr. Haynes explained that the Company considered the nature of these customers' usage, as well as concerns about the economic competitiveness of industrial customers and the need to maintain the economic vitality of the Company's North Carolina service territory. He pointed out that in the 2016 Rate Case, the Company gained approval of Rate Schedule 6L to help large high load factor customers who may utilize their plant efficiently in multiple daily shifts. (Tr. Vol. 4 at 481-483).

Witness Haynes also disagreed with Mr. Wielgus' recommendation that Schedule NS should not exceed the average of the percentage increase applied to rate schedules in the LGS and 6VP classes. He stated that the rate of return index for the LGS and 6VP classes is well above the Parity Index Range and, given other non-cost factors, these two large industrial classes should receive a very low percentage increase. Mr. Haynes further noted that the Company modified its position on the apportionment of the revenue

increase to Schedule NS and that the Company believes that the Schedule NS class should have a lower rate of return index. Specifically, Witness Haynes stated that in the 2016 Rate Case, the Schedule NS class' rate of return index moved from 0.43 to 0.74, which represented a move of two-thirds of the way toward the low end (90% of jurisdictional rate of return) of the Parity Index Range, and he noted that prior to the 2016 Rate Case a deficiency had existed for a number of years. Witness Haynes explained that in the Company's Application, the Schedule NS class had a rate of return index of 0.80, but, after considering the operational benefit to the system that Nucor provides as a result of its partially interruptible service, the Company believed a rate of return index of 0.75 is more appropriate. (Tr. Vol. 4 at 479-484).

In his Stipulation testimony, Witness Haynes testified that Section VI<sup>15</sup> of the Public Staff Stipulation presents a just and reasonable approach to establishing the Company's North Carolina jurisdictional cost of service and class cost of service for the allocation of production and transmission plant costs and related expenses based on the SWPA allocation methodology. (Tr. Vol 4 at 486-488).

Pursuant to Section III.D of the CIGFUR Stipulation, at the hearing counsel for CIGFUR cross-examined Company Witness Haynes on the rate of return index provided for the LGS and 6VP classes under the Public Staff Stipulation. He agreed that these classes will be paying rates above cost and beyond the range of reasonableness, but agreed with CIGFUR counsel that the increases for these classes are very small. He also pointed out that the terms of the Public Staff Stipulation result in a reduction in the increase in base non-fuel revenue from these classes from the Company's initial request.

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<sup>15</sup> At the hearing, Witness Haynes corrected this statement in his testimony, which had referenced Section V of the Public Staff Stipulation. (Tr. Vol. 4 at 362).

(Tr. Vol. 5 at 40-43). On redirect examination, he also testified that when all factors are considered, including Rider EDIT and the proposed Rider A-1, the overall impact for the North Carolina jurisdiction will be a 2.37% reduction, with all classes except residential and lighting having a decrease. He also agreed that the Company is working with a reduced revenue requirement under the Public Staff Stipulation as compared to the revenue requirement used to develop its proposed rate of return indices filed with its Application. (Tr. Vol. 5 at 54-58).

#### Discussion and Conclusions

Based on the Public Staff Stipulation and the evidence in the record, the Commission concludes that for purposes of this proceeding it is appropriate to apportion the proposed base fuel and non-fuel revenue increase approved in this Order using the methodology recommended by DENC as consistent with the Public Staff Stipulation. As the Public Staff Stipulation recognizes, the rate of return indices for the LGS and 6VP classes are above 1.20. However, based on the evidence presented, the Commission concludes that the rate of return indices for these and all of the classes are reasonable and should be accepted. In reaching this conclusion, the Commission relies on the following: the very small increase in rates that these classes will receive; the principles that the Public Staff and the Company have identified as important for apportioning the revenue increase, which the Commission finds reasonable; the fact that when all factors are considered, the overall impact for the North Carolina jurisdiction will be a 2.37% reduction with all classes except residential and lighting having a decrease; and the significantly reduced revenue requirement resulting from the Public Staff Stipulation. The Commission concludes that based on the terms of the Public Staff Stipulation, which

it has found to be just and reasonable to the customers of DENC and to all parties to this proceeding, and to serve the public interest, the rate of return indices for all of the Company's classes provided by the Public Staff Stipulation are appropriate for purposes of this proceeding.

### **EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 32**

The evidence supporting this finding of fact and conclusions is found in the Company's Form E-1 and the direct testimony of Company Witness Haynes.

#### Summary of the Evidence

In his direct testimony, Company Witness Haynes testified that Item 39 of the Company's Form E-1 shows the Company's proposed changes to each section of the terms and conditions. Specifically, he referenced the proposed changes to several miscellaneous service fees to cover the updated cost of service, excess facilities charge percentages, and minor wording changes. Witness Haynes stated that each change is accompanied by "comments" that provide a description of the relevant proposed change. He also testified that the Company proposed to wait to implement these changes until permanent rates become effective and the changes are approved by the Commission. Finally, Witness Haynes confirmed that the non-fuel base rate revenue increase includes the Company's proposed changes for the miscellaneous charges. (Tr. Vol. 6 at 383, 408-409).

No other party testified in opposition to the Company's proposed changes to the terms and conditions, and Mr. Haynes was not cross examined on this issue at the hearing.

## Discussion and Conclusions

The Commission finds and concludes that the Company's proposed changes included in Item 39 of its Form E-1 are reasonable and appropriate and should be approved.

### **EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 33**

The evidence supporting this finding of fact and conclusions is found in DENC's verified Application and Form E-1, the testimony and exhibits of Company Witness Mitchell and Public Staff Witness Tommy Williamson, the Public Staff Stipulation, and the entire record in this proceeding.

#### Summary of the Evidence

Company Witness Mitchell provided testimony regarding DENC's performance with regard to customer service. He testified that the Company's generating fleet has demonstrated excellent performance results. He also stated that DENC continues to provide excellent customer service, and that the Company has improved its North Carolina System Average Interruption Duration Index (SAIDI) excluding major storms performance by over 20% since 2007, and maintained consistent performance below 120 minutes since 2016. Mr. Mitchell also testified that the Company continues to achieve excellence in customer service by offering innovative solutions in response to customer expectations, including leveraging technology to perform quick, seamless customer transactions. He noted that DENC customers completed more than 16 million online transactions during 2018 and that usage of online transactions has increased by 12% since 2017. He described the Company's promotion of social media interactions with customers, including its messages to educate customers on important issues such as

energy conservation and service reliability. Mr. Mitchell also testified about recognition for outstanding performance that the Company's parent, DEI, had received during the past several years. (Tr. Vol 6 at 169-170, 178-181).

Public Staff Witness Tommy Williamson testified that the Public Staff had reviewed service-related complaints received by the Public Staff's Consumer Services Division, the Company's call center operation reports filed with the Commission and SAIDI, and System Average Interruption Frequency Index (SAIFI) statistics. Mr. Williamson testified that the data for non-Major Event Days showed that SAIDI and SAIFI results have been stable and slightly improving. He also testified that the vast majority of inquiries made by DENC customers through the Public Staff's Consumer Services Division were requests to establish or modify payment arrangements and no other category of inquiry exceeded 4% of the total. Based on this information, Mr. Williamson found the overall quality of electric service provided by DENC to retail customers to be adequate. (Tr. Vol. 6 at 466-467).

#### Discussion and Conclusions

Under Section IX of the Public Staff Stipulation, the Stipulating Parties agreed that the quality of DENC's service is good. Therefore, consistent with Section IX of the Public Staff Stipulation, and based on the testimony of Company Witness Mitchell and Public Staff Witness Williamson, the Commission finds and concludes that the overall quality of electric service provided by DENC is good.

## EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 34-35

The evidence supporting these findings of fact and conclusions is found in the testimony and exhibits of the Company and the Public Staff, and in the Public Staff and CIGFUR Stipulations.

Pursuant to N.C. Gen. Stat. § 62-133(a), the Commission is required to set rates that are “fair both to the public utilities and to the consumer.” In order to strike this balance between the utility and its customers, the Commission must consider, among other factors, (1) the utility’s reasonable and prudent cost of property used and useful in providing adequate, safe and reliable service to ratepayers, and (2) a rate of return on the utility’s rate base that is both fair to ratepayers and provides an opportunity for the utility through sound management to attract sufficient capital to maintain its financial strength. *See* N.C. Gen. Stat. § 62-133(b).

As fully discussed above, the provisions of the Stipulations are the product of the give-and-take of settlement negotiations between DENC and the Public Staff and between DENC and CIGFUR.

The result is that the Stipulations strike a fair balance between the interests of DENC and its customers. As discussed above, the Commission has fully evaluated the provisions of the Stipulations and concludes, in the exercise of its independent judgment, that the provisions of the Stipulations are just and reasonable to all parties to this proceeding in light of the evidence presented, and serve the public interest. The provisions of the Stipulations strike the appropriate balance between the interests of DENC’s customers in receiving safe, adequate, and reliable electric service at the lowest possible rates, and the interests of DENC in maintaining the Company’s financial

strength at a level that enables the Company to attract sufficient capital. As a result, the Commission concludes that the provisions of the Stipulations, as established by this Order, are just and reasonable under the requirements of the Public Utilities Act. Therefore, the Commission approves the Stipulations in their entirety.

### **EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 36-37**

The evidence supporting these findings of fact and conclusions is contained in the Company's verified Application and Form E-1, the testimony and exhibits of the witnesses, the Public Staff Stipulation, and the entire record in this proceeding.

#### Summary of the Evidence

In the Application and initial direct testimony and exhibits, DENC provided evidence supporting an increase of approximately \$27 million in its annual non-fuel revenues from its North Carolina retail electric operations. With regard to fuel, in his direct testimony Company Witness McLeod testified that the Company annualized fuel clause revenue by applying the current base fuel rate plus Rider A to the annualized and normalized customer usage at June 30, 2019. He also explained that an adjustment was made to fuel clause expense to make fuel clause expense equal to fuel clause revenue, net of the regulatory fee. (Tr. Vol. 4 at 260).

On August 5, 2019, the Company filed supplemental direct testimony and exhibits updating several cost of service adjustments. These updated adjustments decreased the Company's revenue requirement by approximately \$2.1 million, for a revised increase in North Carolina retail revenue of \$24.9 million, which was reduced again in the Company's additional supplemental testimony filed on September 12, 2019, to \$24.2 million.

On August 23, 2019, the Public Staff filed the direct testimony of Ms. Johnson, presenting her recommended accounting and ratemaking adjustments to the Company's proposed revenue requirement. Accounting for these adjustments, she recommended a decrease in the Company's annual base non-fuel operating revenue of \$8,112,000.

Witness Johnson also testified that the Public Staff adjusted the fuel clause expense to reflect the base fuel rate and Rider A as set forth in the Additional Supplemental Testimony of DENC Witness Haynes and recommended by Public Staff Witness Jack Floyd, subject to the outcome of the Company's currently ongoing fuel proceeding in Docket No. E-22, Sub 579. Witness Johnson stated that this adjustment resulted in a decrease of \$2.155 million from the fuel expense originally included in the Company's Application. (Tr. Vol. 6 at 39).

On September 17, 2019, the Company and the Public Staff entered into and filed the Public Staff Stipulation. Also on September 17, 2019, the Company filed the testimony of Witnesses McLeod, Miller, Hevert, Davis, and Haynes in support of the stipulated revenue increase. These witnesses testified in support of the accounting and ratemaking adjustments agreed upon in the Public Staff Stipulation. They also testified that the Public Staff Stipulation is the result of negotiations between the Stipulating Parties. Also on September 17, 2019, the Public Staff filed the Joint Stipulation testimony of Ms. Johnson and Mr. McLawhorn, recommending and supporting the stipulated adjustments to the Company's requested revenue increase while also noting the unresolved issues related to CCRs.

The Public Staff Stipulation, as reflected on Settlement Exhibit I, reflects the Company's proposed increase in the revenue requirement of \$6.428 million, consisting of

an increase of \$8.583 million in non-fuel revenues and a decrease of \$2.155 million in base fuel revenues, and the Public Staff's proposed increase in the revenue requirement of \$2.037 million, consisting of an increase in \$4.192 million in non-fuel revenues and a decrease of \$2.155 million in base fuel revenues. The difference between the Company's and the Public Staff's proposals in the Public Staff Stipulation result from the unresolved issues identified at Section II.A.i of the Public Staff Stipulation (cost recovery of the Company's CCR costs, the recovery amortization period, and return during the amortization period).

#### Discussion and Conclusions

As discussed in the body of this Order, the Commission approves the Public Staff Stipulation in its entirety and makes its individual rulings on the unresolved issues as discussed herein. As the unresolved issues pertaining to CCR cost recovery were not addressed by the Public Staff Stipulation and accompanying testimony and exhibits, the Commission requests that DENC recalculate the required annual revenue requirement consistent with all of the Commission's findings and rulings herein as soon as practicable following the issuance of this Order. The Commission further orders DENC to work with the Public Staff to verify the accuracy of the recalculations. Once the Commission receives this filing, the Commission will work promptly to verify the calculations and will issue an Order with final revenue requirement numbers.

#### **EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 38**

The evidence supporting this finding of fact and these conclusions is contained in the verified Application, the testimony and exhibits of the DENC and Public Staff witnesses, the Public Staff Stipulation, and the record as a whole.

Pursuant to N.C. Gen. Stat. § 62-133(a), as described earlier, the Commission is required to set rates that are “fair both to the public utilities and to the consumer.” In order to strike this balance between the utility and its customers, the Commission must consider, among other factors, (1) the utility’s reasonable and prudent cost of property used and useful in providing adequate, safe and reliable service to ratepayers, and (2) a rate of return on the utility’s rate base that is both fair to ratepayers and provides an opportunity for the utility through sound management to attract sufficient capital to maintain its financial strength. *See* N.C. Gen. Stat. § 62-133(b). DENC’s continued operation as a safe, adequate, and reliable source of electric service for its customers is vitally important to DENC’s individual customers, as well as to the communities and businesses served by DENC. DENC presented credible and substantial evidence of its need for increased capital investment to, among other things, maintain and increase the reliability of its system and comply with environmental requirements.

For example, DENC Witness Mitchell testified that during the last three years, the Company invested \$1.3 billion to bring online a total of 1,588 MW of new generation in the Greenville County CC. Witness Mitchell stated that this new generation is cleaner and highly-efficient combined cycle generating capacity that has the potential to create substantial fuel savings due to very favorable current natural gas prices. Witness Mitchell also noted that the Company has invested \$132 million to bring on-line three regulated solar facilities totaling 56 MW and between 2019 and 2020 plans to invest approximately \$410 million to bring on-line an additional 240 MW of nameplate solar capacity. Mr. Mitchell also testified that the Company has received a Certificate of Public Convenience and Necessity to construct the 12 MW Coastal Virginia Offshore

Wind Project that is expected to come on-line in 2020. Finally, Witness Mitchell explained that the Virginia Grid Modernization and Security Act specified that up to 5,000 MW of solar and wind generation facilities constructed by a utility such as the Company are in the public interest and the Company has committed to have approximate 3,000 MW placed in service or under development by the end of 2022. (Tr. Vol. 4 at 171-172).

Witness Mitchell further testified that DENC has spent approximately \$268 million on transmission improvements in North Carolina during the last three years. He stated that these improvements support improved reliability of the transmission system and local economic growth. He also testified that the Company plans to invest an additional \$200 million in transmission improvements in North Carolina over the next five years. (Tr. Vol. 6 at 173-174).

In addition, Witness Mitchell testified that DENC has invested over \$29 million in its distribution system in North Carolina during the last three years. He stated that these investments balance the need for reliable service with prudent spending. (Tr. Vol. 6 at 174).

Witness Mitchell also testified regarding the impact of current and proposed environmental regulations on the Company's operations. He stated that during the last decade electric utilities have been required to address compliance with a suite of new environmental standards adopted by the EPA. He testified that compliance with these standards has directly impacted DENC's operation of its coal-fired generating plants, citing as an example the EPA's Mercury Air Toxics Standards Rule, which led to the retirement of over 900 MW of coal-fired generating capacity. Witness Mitchell also

stated that the enactment of the CCR Final Rule in April 2015 created a legal obligation for the Company to retrofit or close all of its inactive and existing ash ponds, as well as perform required monitoring, corrective action, and post-closure activities as necessary. (Tr. Vol. 6 at 170-176).

Moreover, Witness Mitchell testified that DENC plans to invest \$11.1 billion over the next three years for generation, transmission, and distribution investments in order for the Company to continue to fulfill its obligations of providing reliable, cost-effective service in an environmentally responsible manner for DENC's customers. (Tr. Vol. 6 at 177).

These are representative examples of the capital investments that have been made and are planned to be made by DENC in order to continue providing safe, reliable, and efficient electric service to its customers. Based on all of the evidence, the Commission finds and concludes that the rates established herein strike the appropriate balance between the interests of DENC's customers in receiving safe, reliable, and efficient electric service at the lowest possible rates, and the interests of DENC in maintaining the Company's financial strength at a level that enables the Company to attract sufficient capital. As a result, the Commission concludes that the rates established by this Order are just and reasonable under the requirements of N.C. Gen. Stat. § 62-30, et seq.

IT IS, THEREFORE, SO ORDERED, as follows:

1. That the Stipulation filed by DENC and the Public Staff is hereby approved in its entirety.
2. That the Stipulation filed by DENC and CIGFUR is hereby approved in its entirety.

3. That, as soon as practicable following the issuance of this Order, DENC shall file with the Commission, the annual revenue requirement and accompanying rate schedules and terms and conditions that are consistent with the findings and conclusions of this Order and the Public Staff Stipulation. The Company shall work with the Public Staff to verify the accuracy of the filing. DENC shall file schedules summarizing the gross revenue and the rate of return that the Company should have the opportunity to achieve based on the Commission's findings and determinations in this proceeding.

4. That DENC is hereby authorized to adjust its rates and charges in accordance with the Stipulations and findings in this Order effective for service rendered on and after the following day after the Commission issues an Order accepting the calculations required by Ordering Paragraph 3.

5. That the Commission shall issue an Order approving the final revenue requirement numbers once received from DENC and verified by the Public Staff as soon as practicable.

6. That the proper aggregate base fuel factor for this proceeding is 2.089 cents per kWh, excluding regulatory fee, and 2.092 cents per kWh, including regulatory fee. The Company shall replace the voltage-differentiated base fuel factors approved in Sub 532, with the following voltage-differentiated base fuel factors, including gross receipts tax, effective February 1, 2020:

Customer Class	Base Fuel Factor
Residential	2.118 c/kWh
SGS & PA	2.115 c/kWh
LGS	2.098 c/kWh
NS	2.036 c/kWh
6VP	2.065 c/kWh
Outdoor Lighting	2.118 c/kWh
Traffic	2.118 c/kWh

7. That the jurisdictional and class cost allocation, rate design principles, and service regulations proposed by the Company are approved and shall be implemented.

8. That DENC shall implement Rider EDIT as described in Section VIII of the Public Staff Stipulation.

9. That as soon as practicable after the date of this Order, DENC shall file for Commission approval five copies of rate schedules designed to comply with the rate design approved in this Order accompanied by calculations showing the revenues that will be produced by the rates for each schedule. This shall include a schedule comparing the revenue produced by the filed schedules during the test period with the revenue that will be produced under the rate schedules to be approved herein and a schedule illustrating the rates of return by class based on the revenues produced by the rates for each schedule.<sup>16</sup>

10. That as soon as practicable after the issuance of the last Commission Order in DENC's four pending rate-related proceedings, which are this proceeding, the Sub 579 fuel charge adjustment proceeding, the Sub 578 renewable energy and energy efficiency portfolio standard (REPS) cost recovery proceeding, and the Sub 577 demand-side management (DSM) proceeding, DENC shall file a consolidated proposed customer notice addressing the rate changes associated with the non-fuel base and base fuel rate changes approved in this proceeding (Sub 562), the Fuel Rider B in the Sub 579 proceeding, the REPS Rider RP and RPE rate changes in Sub 578, and the DSM Rider C and Rider CE rate changes in Sub 577. Such notice shall include the effect of each rate-

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<sup>16</sup> If necessary, the Commission will address in a subsequent order any refund due based on any differences in the rates approved in this Order and the Company's temporary rates implemented on November 1, 2019.

related proceeding on a residential customer using 1,000 kWh and the combined effect of all four rate-related proceedings on a residential customer using 1,000 kWh. Upon approval by the Commission, DENC shall notify its North Carolina retail customers of the foregoing rate adjustments by including the approved notice as a bill insert with customer bills rendered during the next regular scheduled billing cycle.

11. That the Company shall continue to annually file a cost of service study with the Commission using the Summer/Winter Peak and Average methodology.

12. That in its next general rate case, the Company shall file the results of a class cost of service study with production and transmission costs allocated on the basis of the Summer/Winter Coincident Peak method in addition to the SWPA used in this proceeding and consider such results for the sole purpose of apportionment of the change in revenue to the customer classes.

13. That the Company shall work with CIGFUR to consider whether certain provisions within its RTP rates should be modified and, if there is mutual agreement between CIGFUR and DENC to such modifications, and CIGFUR indicates that at least one of its member customers is willing to take service under such rates, DENC shall re-file such rates with the Commission for approval with the modifications agreed upon within 60 days of such agreement.

ISSUED BY ORDER OF THE COMMISSION.

This the \_\_\_\_ day of \_\_\_\_\_, 2019.

NORTH CAROLINA UTILITIES COMMISSION

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of the foregoing Joint Proposed Order of Virginia Electric and Power Company, d/b/a Dominion Energy North Carolina and the North Carolina Utilities Commission—Public Staff, as filed in Docket No. E-22, Subs 562 and 566, was served electronically or via U.S. mail, first-class, postage prepaid, upon all parties of record.

This, the 6<sup>th</sup> day of November, 2019.

/s/Mary Lynne Grigg

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