

STATE OF NORTH CAROLINA  
UTILITIES COMMISSION  
RALEIGH

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

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

DOCKET NO. E-7, SUB 1213 )  
)  
In the Matter of )  
Application for Approval of Proposed )  
Prepaid Advantage Program )  
)  
)  
DOCKET NO. E-7, SUB 1214 )  
)  
In the Matter of )  
Application of Duke Energy Carolinas, LLC )  
for Adjustment of Rates and Charges )  
Applicable to Electric Utility Service in North )  
Carolina )  
)  
)  
DOCKET NO. E-7, SUB 1187 )  
)  
)  
In the Matter of )  
Application of Duke Energy Carolinas, LLC )  
for an Accounting Order to Defer )  
Incremental Storm Damage Expenses )  
Incurred as a Result of Hurricanes Florence )  
and Michael and Winter Storm Diego )

PUBLIC STAFF  
POST-HEARING  
BRIEF ON  
UNPROTECTED EDIT  
OFFSET AGAINST  
CCR COMPLIANCE  
COSTS OR COAL  
PLANT RETIREMENT  
ACCELERATED  
DEPRECIATION

## I. Overview

The purpose of this brief is to address the issue of whether it would be appropriate to offset Duke Energy Carolinas, LLC's (DEC or Company) coal combustion residual (CCR) compliance costs approved in the herein rate case, or, in the alternative, DEC's Commission-approved calculation of accelerated depreciation associated with the early retirement of coal-fired electric generating plants, with unprotected federal excess deferred income tax (EDIT) refunds due DEC's retail customers.

## II. Background

On July 31, 2020, the Public Staff and DEC (collectively, Stipulating Parties) filed a Second Agreement and Stipulation of Partial Settlement (Public Staff Second Partial Stipulation), which among other things settled and reached agreement on the return of federal EDIT due to the Tax Cuts and Jobs Act (Tax Act). DEC and the Public Staff also filed testimony in support of the Public Staff Second Stipulation on July 31, 2020. The Company agreed to the Public Staff's recommended treatment of the return of unprotected federal EDIT, state EDIT, and deferred revenues related to the provisional overcollection of federal income taxes ("deferred revenues"), as well as to additional provisions pertaining to future tax changes. Both DEC and the Public Staff agreed that the provisions of the Public Staff Second Partial Stipulation were in the public interest and should be approved. The Stipulating Parties agreed to the following specific terms regarding the flowback of unprotected EDIT to DEC's customers:

- 1) The regulatory liabilities related to (a) unprotected federal EDIT (both the portion identified by the Company as related to property, plant, and equipment and the portion identified as not related to such) (collectively, “total unprotected federal EDIT”); (b) North Carolina EDIT, and (c) deferred revenues will be returned to customers through riders by using the levelized rider calculation methodology described and set forth in the testimony and exhibits of the Public Staff in this proceeding.
- 2) Total federal unprotected EDIT will be returned to customers over a five-year amortization period (the “Federal Unprotected EDIT Amortization Period”).
- 3) North Carolina EDIT will be returned to customers over a two-year amortization period (the “NC EDIT Amortization Period”).
- 4) Deferred revenues will be returned to customers over a two-year amortization period (the “Deferred Revenues Amortization Period”).

Under the terms of the Public Staff Second Partial Stipulation, as reflected in the revenue requirement recommended by the Public Staff, DEC’s revenue requirement for the first two years will be reduced by the State EDIT Rider and deferred revenues decrement, totaling approximately \$83.054 million for each year; and DEC’s revenue requirement for the first five years will be reduced by the Federal Unprotected EDIT Rider decrement of approximately \$240.875 million for

each year, to be reduced by the actual amount of EDIT refunded during DEC's implementation of interim rates.

On September 3, 2020, during the expert witness hearing held by the Commission in this docket, Commissioners Kimberly W. Duffley and Daniel G. Clodfelter requested late-filed exhibits reflecting the impact on the revenue requirement of using federal unprotected EDIT to offset certain costs. Commissioner Duffley requested schedules showing the impact on DEC's and the Public Staff's proposed revenue requirement amounts that reflect an offset of federal unprotected EDIT, and if needed State EDIT, against DEC's CCR compliance costs. Commissioner Clodfelter requested that DEC and the Public Staff provide a schedule reflecting the revenue requirement impact if federal unprotected EDIT, and if needed State EDIT, were used to offset DEC's calculation of accelerated depreciation associated with the early retirement of certain coal-fired electric generating plants, based on DEC's requested depreciation periods and amounts. On October 23, 2020, the Public Staff filed Public Staff Late-Filed Exhibit 3, which provided the Public Staff's analysis of the effects of an offset of CCR costs by federal unprotected EDIT, and on October 24, 2020, filed Public Staff Late-Filed Exhibit 4, which provided an analysis of the effects of an offset of early coal plant retirement accelerated depreciation by federal unprotected EDIT.

### III. Discussion

The Public Staff believes that in this present rate case proceeding, offsetting known and measurable EDIT refunds owed to DEC's customers against regulatory assets or accelerated depreciation for the early retirement of plants presents

potential significant intergenerational issues and constitutes inappropriate ratemaking. Deferred regulatory assets, such as the CCR costs at issue in this case, are the result of accounting adjustments approved or adopted by the Commission, the purpose of which typically is to spread the recovery of incurred costs over a specified period (the amortization period). The amortization period for each regulatory asset is approved by the Commission based upon its determination of what is fair and reasonable for the ratepayers with regard to the costs associated with that specific regulatory asset, or other specific factors taken into consideration by the Commission at the time of that approval. The accelerated depreciation relating to the early retirement of a plant is likewise determined by specific factors taken into consideration by the Commission at the time of the approval. Finally, the amortization period and method of amortization chosen for unprotected EDIT is itself dependent on factors specific to EDIT and the overall revenue requirement. Choosing simply to offset the unamortized portion of any regulatory asset or the impact of accelerated depreciation with federal unprotected EDIT and/or State EDIT regulatory liability potentially would, effectively, override the Commission's potential decisions as to the appropriate amortization period, depreciation rate, or other ratemaking considerations for each specific item standing alone, by equalizing the remaining amortization period, depreciable life, and the amortization period for the EDIT regulatory liabilities. For example, if standing alone the Commission would adopt a five-year amortization period for the EDIT liability and a 25-year amortization for CCR costs, offsetting the deferred CCR costs up front with the EDIT regulatory liability would effectively convert the

applicable EDIT refund period from five to 25 years, in terms of the resulting revenue requirement. The Public Staff thus believes that the amortization periods for each of these items should be determined separately, based on the specific characteristics of each cost or benefit. Departing from this transparent process in the course of a general rate case simply to offset flowing through the benefit of reductions in an entirely separate category of costs (income taxes) is neither fair nor reasonable.

A. Commission Precedent

Duke, in its Docket No. E-7, Sub 1146 rate case application, proposed to offset nearly all of the \$216 million revenue reduction resulting from the implementation of federal tax reform with a corresponding revenue increase of \$200 million. The Commission rejected the Company's request and required DEC to maintain all EDIT resulting from the Tax Act in a regulatory liability account pending flowback with interest, reflected at the overall weighted cost of capital approved in that case of 7.35% in three years or in DEC's next general rate case proceeding, whichever occurred sooner. Furthermore, the Commission concluded that offsetting known and measurable reductions in taxes to be paid going forward against the recovery of unknown ongoing coal ash basin closure costs, as ultimately proposed by DEC in its Post-Hearing Brief and Proposed Order in the docket, in order to delay reflecting the current Federal corporate income tax rate in base rates constitutes inappropriate ratemaking.

The Commission also addressed the issue of the appropriateness of offsetting federal unprotected EDIT against other regulatory assets in the rate

increase application of Carolina Water Service, Inc. of North Carolina (CWSNC) in Docket No. W-354, Sub 360 (Sub 360). In the Sub 360 docket, CWSNC proposed to offset its unprotected EDIT regulatory liability with the remaining unamortized portion of other regulatory assets approved by the Commission in other proceedings. Public Staff witness Michelle Boswell testified in the Sub 360 docket that amortization periods for regulatory assets and the unprotected federal EDIT and State EDIT regulatory liability should be determined separately, based on the specific characteristics of each cost or benefit, and departing from this transparent process in the course of a general rate case simply to offset flowing through the benefit of reductions in an entirely separate category of costs (income taxes) is neither fair nor reasonable. (Tr. vol. 2, 95-96) Witness Boswell further stated that the question before the Commission was how, and over what length of time, the flowback of EDIT should be implemented. In the Public Staff's opinion, the Commission's primary concern regarding the effects of the Tax Act should be to ensure that ratepayers receive the full benefit of the reduction in the federal corporate income tax rate.

In the Sub 360 docket, the Commission found that CWSNC's federal unprotected EDIT should be returned to ratepayers through a levelized rider. The Commission stated that this treatment appropriately balanced the interests of ratepayers and the Company. In arriving at its conclusion, the Commission gave substantial weight to the testimony of Public Staff witness Boswell, who is also a Public Staff witness in the present case. The Commission agreed with witness Boswell that offsetting known and measurable reductions in taxes to be paid going

forward against either unknown future regulatory assets, or regulatory assets previously approved by the Commission for recovery over a specified period, presents significant intergenerational issues and constitutes inappropriate ratemaking. The Commission further agreed with witness Boswell that the amortization period for each regulatory asset is approved by the Commission based upon its determination of what is fair and reasonable for the ratepayers with regard to the costs associated with that specific regulatory asset, or other specific factors taken into consideration by the Commission at the time of that approval. The Commission's Order stated in pertinent part:

The Commission finds that choosing to simply offset the new unprotected EDIT regulatory liability with the remaining unamortized portion of any regulatory asset would effectively override the Commission's prior decision as to the appropriate amortization period for the regulatory asset, by equalizing the remaining amortization period and the amortization period for the new EDIT regulatory liability. And as CWSNC witness DeStefano testified, he is not aware of a situation wherein the Commission has approved such offsetting treatment.

The Commission further agrees with witness Boswell that the amortization periods for existing regulatory assets and the federal unprotected EDIT should be determined separately, based on the specific characteristics of each cost or benefit. The Commission agrees with witness Boswell that departing from this transparent process in the course of a general rate case simply to offset flowing through the benefit of reductions in an entirely separate category of costs (income taxes) is neither fair nor reasonable. Further, the Commission notes that for customers, a rider will be separately identified on their bills so they can see in dollars and cents the impact of the federal unprotected

EDIT flow through. This transparency would not occur with the offsetting proposed by the Company.

Through the years the Commission has set rates at a level to ensure that the Company would be able to pay its taxes, including deferred taxes, when they became due. These funds were paid by ratepayers to the Company to enable the Company to pay its taxes; now that the funds are no longer needed to pay the Company's taxes, they should be flowed back to ratepayers as quickly as practicable. The fact that the Company has made use of these funds as cost-free capital does not change the fact that these funds are ultimately customer money that is no longer needed for tax payments. The only remaining question for the Commission to decide is what is a reasonable period of time to refund these federal unprotected EDIT to ratepayers.

B. Impact on Customers

As depicted in Public Staff Late-Filed Exhibits 3 and 4 filed in this docket, offsetting federal unprotected EDIT against either coal ash costs or accelerated depreciation changes the periods for which ratepayers receive the benefits associated with the reduction of taxes from the Tax Act. In the case of offsetting the proposed early retirement of the coal-fired plants, instead of ratepayers receiving the full benefit of the tax refunds over five years, the ratepayers will not see the full benefit of the tax return for eight years. This creates an intergenerational issue, as ratepayers who funded the taxes are not necessarily those receiving the benefit of the refund, because the period of refund is extended. In the case of coal ash, the impact is actually skewed toward a ratepayer benefit

in the early years, but that would likely change if the Commission were to change the coal ash amortization period to a greater number of years than five.

IV. Conclusion

For the reasons stated above, the Public Staff believes that EDIT should not be offset against any deferral or other expense, because it would be unfair and unjust to customers. The EDIT held by the Company represents money that was previously paid by DEC customers and the money rightfully belongs to those customers and should be returned to them as agreed to in the Public Staff Second Partial Stipulation. The Public Staff, therefore, believes the Commission should approve the Public Staff Second Partial Stipulation, which is fair to customers and balances the interests of customers and the Company.

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

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**CERTIFICATE OF SERVICE**

I certify that I have served a copy of the foregoing Public Staff Post-Hearing Brief, on all parties of record in accordance with Commission Rule R1-39, by United States mail, postage prepaid, first class; by hand delivery; or by means of electronic delivery upon agreement of the receiving party.

This the 4th day of November, 2020.

Electronically submitted  
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