Jack E. Jirak
Associate General Counsel

Mailing Address:
NCRH 20 / P.O. Box 1551
Raleigh, NC 27602

o: 919.546.3257
f: 919.546.2694

jack.jirak@duke-energy.com

September 9, 2019

VIA ELECTRONIC FILING

Ms. Kimberly A. Campbell, Chief Clerk
North Carolina Utilities Commission
4325 Mail Service Center
Raleigh, North Carolina 27699-4300

RE: Duke Energy Progress, LLC's Initial Pre-Hearing Reply Brief
Application of Friesian Holdings, LLC for a Certificate of Public Convenience and Necessity
Docket No. EMP-105, Sub 0

Dear Ms. Campbell:

Enclosed for filing with the North Carolina Utilities Commission is Duke Energy Progress, LLC's Pre-Hearing Reply Brief in the above-referenced proceeding.

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

Sincerely,

Jack E. Jirak

Enclosure

cc: Parties of Record

CERTIFICATE OF SERVICE

I certify that a copy of Duke Energy Progress, LLC's Initial Pre-Hearing Reply Brief, in Docket No. EMP-105, Sub 0, has been served by electronic mail, hand delivery or by depositing a copy in the United States mail, postage prepaid to parties of record.

This the 9th day of September, 2019.

Jack E. Jirak
Associate General Counsel
Duke Energy Corporation
P.O. Box 1551/NCRH 20
Raleigh, North Carolina 27602
(919) 546-3257
Jack.jirak@duke-energy.com

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. EMP-105, SUB 0

In the Matter of the Application of Friesian Holdings, LLC for a Certificate of Public Convenience and Necessity	))))	**DUKE ENERGY PROGRESS, LLC PRE-HEARING REPLY BRIEF**

NOW COMES Duke Energy Progress, LLC ("DEP" or the "Company"), and respectfully files this pre-hearing reply brief in response to the Commission's *Order Scheduling Hearings, Requiring Filing of Testimony, Establishing Procedural Guidelines, and Requiring Public Notice* ("Scheduling Order").

I. PROCEDURAL BACKGROUND

1. On May 15, 2019, Friesian Holdings, LLC ("Friesian") filed an application for a certificate of public convenience and necessity ("CPCN") for a 70-MW AC solar photovoltaic facility in Scotland County, North Carolina ("Friesian Facility").

2. On June 13, 2019, the North Carolina Utilities Commission ("Commission") issued the *Scheduling Order* in which the Commission ordered that any person having an interest in this proceeding may file a petition to intervene on or before August 5, 2019.

3. On July 23, 2019, Duke DEP filed a Petition to Intervene and on August 2, 2019, the Commission granted DEP's intervention.

4. On August 5, 2019, the Commission issued its *Order Suspending Procedural Deadlines and Allowing Filing of Pre-Hearing Briefs* ("Order"), in which the

Commission suspended certain procedural deadlines and allowed for the filing of pre-hearing briefs.

5. On August 26, 2019, DEP, along with Public Staff, North Carolina Clean Energy Business Alliance ("NCCEBA") and Friesian, filed initial pre-hearing briefs.

II. SUMMARY

In exercising its uncontested jurisdiction over generating siting decision in the state of North Carolina, the Commission is not preempted under federal law from considering the cost of Network Upgrades that will—but have not yet actually been incurred—under a Federal Energy Regulatory Commission ("FERC") interconnection agreement. If the Commission grants the CPCN and the project is constructed, the Commission may not deny retail rate recovery of the retail-allocated portion of the cost of the Network Upgrades, as such an action would impermissibly "trap" costs actually incurred and allocated under a FERC interconnection agreement and tariff, thereby resulting in an illegal "taking" under federal law.

III. ANALYSIS

a. Federal Law Does Not Preempt the Commission's Authority To Consider Future Network Upgrade Costs in Determining Whether To Grant a CPCN.

i. Supreme Court Preemption Precedent Does Not Indicate that a State May Not Consider a FERC Cost Allocation When the State's Action Would Not Affect FERC's Jurisdiction Over Such Allocation

Both Friesian and NCCEBA claim that FERC's exclusive right to allocate costs relating to the interconnection of the Friesian Facility preempts the exclusive right of the State of North Carolina, acting through this Commission, to site the Friesian Facility under the state's CPCN statute. To the contrary, FERC's cost allocation jurisdiction does not preempt state facility siting laws and a FERC-mandated cost allocation regime can be taken into account, and has been taken into account, in the context of state siting proceedings prior to the point when such costs are actually incurred and allocated. In other words, a state commission is not preempted under federal law from undertaking its generating facility siting authority delegated under state law to prevent there being a need to allocate costs in a manner mandated by FERC.

Friesian argues that examining the FERC cost allocation regime in this CPCN proceeding would give the Commission "jurisdiction over the allocation of FERC-jurisdictional Network Upgrade costs" (Friesian Brief at 21) and would be an impermissible intrusion on FERC's jurisdiction. *Id*. at 22. NCCEBA argues that "[t]he allocation of the interconnection costs of FERC-jurisdictional projects is under the exclusive jurisdiction of the FERC, and federal law preempts any decision by this Commission that would 'affect' that allocation." NCCEBA Brief at 9. To the contrary, FERC's exclusive jurisdiction over transmission[1] and/or the orders instituting its cost allocation policies are not at issue here.[2] The only issue presented is whether such jurisdiction preempts state jurisdiction over the siting of the Friesian Facility.

Friesian attempts to make a case for preemption at pages 23-29 of its Brief, relying on the two Supreme Court cases. Although those two cases are among the most important FERC preemption cases, they are not applicable to the preemption issue presented here. The cases cited by Friesian involved a FERC-approved allocation of costs of power that a

[1] *See* Friesian Brief at 20-22; NCCEBA Brief at 9-10.

[2] *See* NCCEBA Brief at 10-14.

state undermined by: 1) not allowing recovery of the costs of non-entitlement power purchased from TVA allocated by FERC (*Nantahala*[3]) or 2) by revisiting the prudence of the power purchase allocation from the Grand Gulf nuclear plant dictated by FERC (*Mississippi Power & Light*[4]). In these cases, the state action had a direct impact on a FERC-determined allocation that was within FERC's exclusive jurisdiction and, importantly, had already occurred.

Here, the facts are quite different. FERC has approved a prospective allocation of costs under a FERC-jurisdictional tariff (the Duke Open Access Transmission Tariff ("OATT"), but there will be no costs to allocate if the state uses its lawful jurisdiction to prohibit the generator from being built. To understand the distinction, it is helpful to consider what an analogous situation would have looked like in the *Nantahala* or *Mississippi Power & Light* cases.

The *Nantahala* case would be analogous if, for example, North Carolina had prohibited Nantahala, before it contracted with TVA, from buying non-entitlement power from TVA on the grounds that such power was sourced from coal. In that case, there would have been no allocation of entitlement and non-entitlement power at all by FERC, as Nantahala could have purchased only entitlement power from TVA's hydroelectric resources in the first place. Similarly, *Mississippi Power & Light* would have been analogous if FERC had approved a FERC-jurisdictional agreement that allocated the costs of a yet-to-be-built Grand Gulf nuclear plant, but then the state refused to site the nuclear plant at all due to concerns of potential prospective cost overruns. Simply stated, if the

[3] *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986) (*Nantahala*).

[4] *Mississippi Power & Light Co. v. Mississippi ex rel. Moore,* 487 U.S. 354 (1988) ("*Mississippi Power & Light*").

relevant state had prevented or mooted the transaction that resulted in the need for a FERC-jurisdictional allocation, there would not have been a preemption issue.

It is instructive to consider other theoretical bases for denial of siting authorization. For instance, if the Friesian Facility was proposed to be sited atop a protected wetland or sacred Native American burial site. In this hypothetical, assuming the CPCN request was denied as a result, such action would arguably similarly "interfere" with prospective FERC-approved cost allocation scheme for the Network Upgrades under the LGIA and OATT. However, there would be no basis for a preemption claim.

The fact that, in this case, the Commission could choose to deny the CPCN based on the results of the FERC-mandated cost allocation regime itself is a distinction without a difference. No matter the basis, so long as the state has lawful authority to approve or deny siting authorization for the facility, the Commission is free to undertake its delegated authority from the General Assembly under the Public Utilities Act to determine whether "public convenience and necessity requires, or will require, such construction" of such facility irrespective of the fact that the Commission's decision may eliminate the need for a potential future allocation of costs under a FERC-jurisdictional agreement and tariff.

ii. FERC Has Acknowledged that It Cannot Prevent a State from Considering Its Cost Allocation Mandates in Siting Decisions

When Congress enacted the Federal Power Act ("FPA") in 1935, it specifically left the issue of siting of generation and transmission to the states. Section 201(a) of the FPA stated that the federal regulation of wholesale power sales and interstate transmission was "to extend only to those matters which *are not subject to regulation by the States*." (Emphasis added.) In 1935, the states generally regulated the siting of both generation and transmission, as FERC has acknowledged. In Order No. 888, FERC held that "Congress left to the States authority to regulate generation and transmission siting."[5] In Order No. 1000 FERC stated "that there is longstanding state authority over certain matters that are relevant to transmission planning and expansion, such as matters relevant to siting, permitting, and construction."[6] In light of the general and expansive nature of the acknowledged state jurisdiction over transmission and generation siting, it would be counterintuitive to suggest that states are forbidden to consider the economics of such projects, even where such economics would ultimately be played out, in part, through a FERC-approved agreement and tariff.

Order No. 1000—FERC's order addressing transmission planning process and cost allocation—proves that a state can preempt a FERC-approved cost allocation by denying a CPCN based on that allocation. The cost allocation of any Order No. 1000 transmission project would be dictated by FERC.[7] But, that does not mean that a state, in considering whether to site the Order No. 1000 transmission project, could not take into account the FERC-mandated cost allocation scheme and refuse to site the project because the cost allocation harmed the state's retail (and/or wholesale) transmission customers.

Order No. 1000 requires the creation of a transmission plan, but it "does not require that such facilities be built, give any entity permission to build a facility, or relieve a

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[5] *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. ¶ 31,036 at 31,782 & n. 543 (1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 12,274 (March 14, 1997), *order on reh'g,* Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd sub nom. Transmission Access Study Group v. FERC*, 225 F. 3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002).

[6] *Transmission Planning & Cost Allocation by Transmission Owning & Operating Pub. Utilities* , Order No. 1000, 136 FERC ¶ 61,051 at P 107 (2011); *order on reh'g and clarification*, Order No. 1000-A, 139 FERC ¶ 61,132, *order on reh'g and clarification*, Order No. 1000-B, 141 FERC ¶ 61,044 (2012), *aff'd per curiam*, *S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41 (D.C. Cir. 2014).

[7] "Order No. 1000 meant to impose binding cost allocation, which Order No. 1000 clearly signaled and the D.C. Circuit has already recognized." *El Paso Elec. Co. v. FERC*, 832 F.3d 495, 509 (5th Cir. 2016).

developer from obtaining any necessary state regulatory approvals."[8] As the D.C. Circuit explained, "the challenged orders take great pains to avoid intrusion on the traditional role of the States," and:

> "nothing in th[e] Final Rule is intended to limit, preempt, or otherwise affect state or local laws or regulations with respect to construction of transmission facilities, including but not limited to authority over siting or permitting of transmission facilities." Order No. 1000 ¶ 227, 76 Fed. Reg. at 49,880. Thus, States retain control over the siting and approval of transmission facilities.[9]

In sum, Order No. 1000 does not prohibit in any manner a state from considering the binding FERC-approved cost allocation regime for an Order No. 1000 project in deciding whether to approve or deny a request to site a particular project. For instance, the Louisiana Public Service Commission issued a rule to this effect, finding:

> by asserting regulatory control over transmission, the Louisiana Commission will be in a position to exercise jurisdiction over the certification, siting and construction process should areas in Louisiana be designated as national interest electric corridors, should transmission be required or recommended by MISO or ITC, or should transmission be recommended due to the FERC Order No. 1000 planning processes. *This assertion of authority also will give the Commission the opportunity to consider the level of costs for any new transmission construction that ultimately may be reflected in retail rates.*[10]

Much like Order No. 1000, ISO/RTO regions have binding cost allocation schemes for certain types of transmission projects, such as MISO's multi-value projects ("MVP")

[8] Order No. 1000-A, 139 FERC ¶ 61,132 at P 191.

[9] *S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41, 76 (D.C. Cir. 2014).

[10] *Louisiana Pub. Serv. Comm'n Ex Parte*, No. R-26018, 2013 WL 5673898, at *6 (Oct. 10, 2013) (emphasis added).

(the costs of which are basically allocated across all of MISO).[11] For example, in 2011, MISO approved the Cardinal-Hickey Creek transmission line, which traversed several states, as an MVP in 2011. Just as is the case in DEP's OATT, the cost allocation regime for transmission projects is specified in the FERC-filed and approved MISO OATT. But, in at least one state siting proceeding still open involving the Cardinal-Hickey Creek line (Wisconsin Public Service Commission Case 5-CE-1476), the state commission is taking the cost impacts on retail customers into account. The Wisconsin PSC Staff, among many others, filed testimony highlighting the costs versus the benefits to Wisconsin transmission customers that would ultimately be recognized in retail rates. Indeed, whether the project is cost-beneficial to Wisconsin, given the MISO cost allocation scheme, is a primary issue in the proceeding.[12] There are also a number of other instances in which state commissions have clearly considered the cost impact of transmission under a FERC-approved tariff.[13]

In sum, there is ample precedent that the cost of the new transmission facilities to retail customers may be considered in any sort of decision of a state commission that is within the state commission's jurisdiction.

[11] When Entergy joined MISO, there were some changes in cost allocation for MVPs that are not relevant here.

[12] The Attorney Generals of Illinois and Michigan even filed an amicus brief with the Wisconsin PSC arguing that the costs to *their* customers outweighed the benefits and that the line should not be sited.

[13] In a recent Virginia State Corporation Commission ("VSCC") CPCN proceeding for the siting of a power plant, the VSCC found that the "Joint Applicants" obligation under the PJM Tariff "to pay for 100 percent of the costs of the minimum amount of Local Upgrades and Network Upgrades necessary to accommodate its New Service Request" relevant. The VSCC conditioned "the CPCNs granted in this proceeding on the Joint Applicants paying for all network upgrade costs PJM assigns to the Joint Applicants, or their designated representative at PJM." *Application of Pleinmont Solar, LLC*, No. PUR-2017-00162, 2018 WL 3830894, at *10 (Aug. 8, 2018). Note that most RTOs have chosen to adopt participant funding for new generator interconnections, i.e., the generator pays for any Network Upgrades. PJM is no exception. FERC remains free to allow or order PJM to change its cost allocation, such that the Joint Applicants would not have to pay the Network Upgrade costs (and they would be spread to all transmission customers), but in that case, the VSCC could revoke its CPCN.

iii. The Position Advocated By NCCEBA and Friesian Is Not Consistent With the Commission's Practice and Is Not Consistent With Sound Policy-Making.

Taking the Friesian and NCCEBA position to its logical extreme, Network Upgrade costs assigned under FERC LGIA could *never* be considered by a state commission in any setting, if the result would be that the state might moot an executed LGIA. For instance, a CPCN application for a DEP generating facility under R8-61 requires submission of "[a]n estimate of the construction costs for the generating facility, including the costs for new substation(s) and transmission line(s), and upgrades to existing substations(s) and transmission lines(s)." Under NCCEBA's and Friesian's view, however, the Commission would be precluded from considering the cost of the transmission lines and upgrades even in the context of a DEP generating facility, since such lines and upgrades will be constructed and the cost allocated under the terms of the OATT.

As a general matter, regulated procurements take into account the total delivered cost of the energy being procured. For instance, as discussed above, DEP-owned generating assets are certainly evaluated to assess the combined cost impact of both the generation facility and transmission costs on customers. Similarly, the ongoing Competitive Procurement of Renewable Energy ("CPRE") process takes into account the cost of any necessary upgrades in determining which resources are in the best interest of customers. This case presents a relatively unique fact pattern in which there is no need to assess the cost of the facility (since output is being sold under a wholesale agreement to an electric cooperative whose retail rates are not regulated by the Commission) and yet, absent the Commission's review of the transmission costs, there would be no regulatory body assessing the prudence of the transmission cost impacts. And neither the party selling output nor the party purchasing the output will, in the end, directly bear a substantial portion of the cost of the Network Upgrades to the DEP transmission system necessary to deliver the energy. Instead, DEP's retail customers in North Carolina would pay for the majority of these costs. Under NCCEBA's argument, this very substantial resource decision (*i.e.*, constructing hundreds of millions of dollars of Network Upgrades) would essentially be made without any Commission pre-approval or oversight.

iv. FERC Cannot Use Its Jurisdiction to Preempt a State's Clear Jurisdiction.

Where a state has clear jurisdiction over an issue (in this case, the siting of generation and transmission lines), it would be inappropriate for FERC's jurisdiction to substantially nullify such jurisdiction. An illustration of this principal can be found in *S. Cal. Edison Co. v. FERC*, 603 F.3d 996 (D.C. Cir. 2010) ("*SCE v. FERC*"). There, FERC had claimed that its jurisdiction over unbundled retail *transmission* allowed it to preempt a state netting law used to measure retail *energy* consumption. The court rejected FERC's reliance on preemption cases where the impact on state jurisdiction was indirect and incidental.

If FERC's jurisdiction to allocate the costs of interstate transmission facilities were to trump a state's siting laws, such an outcome would "not just side-swipe state jurisdiction; it [would] attack it frontally."[14] Ultimately, the *SCE v. FERC* court held that a state commission's finding that a retail sale of power occurred under state law did not impact FERC's separate and independent determination under the Federal Power Act that a retail transmission of power did not occur under the same set of facts. Here, denial or approval

[14] *SCE v. FERC* at 1001.

of the CPCN by this Commission (having considered the cost impact on North Carolina retail customers of the approximate $224 million of Network Upgrades for the Friesian Facility) has no impact on FERC's separate and independent authority to later determine the manner in which the costs will be allocated *if* Friesian does build its generator.

On appeal of the remand order after *SCE v. FERC*, the petitioners tried to rely on *Nantahala*, but the court explained:

> While the facts of *Nantahala* are intricate, the key distinction is that the state order in that case effected an actual conflict with FERC jurisdictional wholesale regulations – the state used different figures for the same calculation, effectively concluding that "the FERC approved wholesale rates [were] unreasonable." … Though the state was ultimately setting retail rates, those rates were based on an allocation of power (for wholesale) directly at odds with FERC's order.[15]

Accordingly, the court concluded "[w]hile the regulation of transmission charges is undoubtedly within FERC's jurisdiction, retail charges are not."[16] FERC's authority to allocate transmission costs does not preempt a state's authority to determine whether a facility may be sited and whether there should be any costs to allocate at all. Contrary to the argument of Friesian,[17] the Commission would *not* be *changing the allocation* of Network Upgrade costs to transmission customers under the LGIA from $224 million to $0 by denying a CPCN; instead, it would simply be ruling there are no prospective costs to be allocated at all. This is a distinction with a difference under the law of preemption.

v. The CPCN Law and Rule Cited by Friesian and NCCEBA Are Not as Narrow as Portrayed.

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[15] *Calpine Corp. v. FERC*, 702 F.3d 41, 48 n.4 (D.C. Cir. 2012) (citation omitted)

[16] *Id*. at 50.

[17] *See* Friesian Brief at 23.

Friesian and the NCCEBA argue that state laws and regulations legally preclude the Commission from considering the Network Upgrades in determining the "public convenience and necessity" of the Friesian Facility. Friesian Brief at 16, 29; *see* NCCEBA Brief at 6-7. For example, Friesian notes that N.C. Gen Stat. Section 61-110.1 (the "Generator CPCN Statute") requires the applicant to file an estimate *only* of the costs of generating facility. Friesian Brief at 16. Friesian also states that Chapter 62 confers no authority for the Commission to consider any costs other than the costs of the generation facility, in a CPCN proceeding. *Id.*[18] Friesian and NCCEBA also rely in part on Commission Rule R8-63, which states that an application must include:

> The nature of the proposed generating facility, including its type, fuel, expected service life, and the gross, net, and nameplate generating capacity of each generating unit and the entire facility, as well as the *facility's* total projected dependable capacity, in megawatts (alternating current); the anticipated beginning date for construction; the expected commercial operation date; and estimated *construction costs*.[19]

The Friesian and NCCEBA Briefs, omit important portions of the Generator CPCN Statute. N.C. Gen Stat. Section 62-110.1(c) states in relevant part:

> The Commission shall develop, publicize, and keep current an analysis of the long-range needs for expansion of facilities for the generation of electricity in North Carolina, including its estimate of the probable future growth of the use of electricity, the probable needed generating reserves, the extent, size, mix and general location of generating plants and arrangements for pooling power to the extent not regulated by the Federal Energy Regulatory Commission and other arrangements with other utilities and energy suppliers *to achieve maximum efficiencies for the benefit of the people of North Carolina*, and shall consider such analysis in acting upon any petition by any utility

[18] While Rule 8-63(b)(2)(iv) mentions transmission facilities, it does so only in the context of a natural gas plant.

[19] Friesian Brief at 17; NCCEBA Brief at 7 (both quoting Rule 8-63(b)(2)(i)) (emphasis added).

> for construction. Emphasis added. Clearly, the statute expects the Commission consider efficiencies in issuing CPCN.

Subsection (e) of the Generator CPCN Statute provides that as "a condition for receiving a certificate, the applicant shall file an estimate of construction costs in such detail *as the Commission may require*." Nothing prevents the Commission from asking for an estimate of Network Upgrade costs.[20] That Subsection also states that "[t]he Commission shall hold a public hearing on each application and no certificate shall be granted unless the Commission has approved the estimated construction costs and made a finding that construction will be consistent with the Commission's plan for expansion of electric generating capacity." This provision places no restrictions on the factors that the Commission may consider. In sum, the mere fact that the Generator CPCN Statute and Commission Rules do not mention estimates of Network Upgrade costs does not exclude them from consideration when the overall breadth of the law is considered. This is consistent with established precedent that holds that "[t]he standard of public convenience and necessity is relative or elastic, rather than abstract or absolute, and the facts of each case must be considered."[21]

DEP would agree that state commissions do not *typically* focus on Network Upgrade costs in analyzing whether to issue a generator a CPCN. There is a very good reason for that – generators that trigger substantial Network Upgrade costs often withdrawn from the interconnection process before they even petition the Commission to obtain a CPCN (or other state or local form of siting permission) if the Interconnection Facility or

[20] Similarly, the fact that R8-63 does not seek an estimate of Network Upgrade costs does not mean that the Commission cannot access such an estimate by examining a public Large Generator Interconnection Agreement.

[21] *State ex rel. Utils. Comm'n v. Casey*, 245 N.C. 297, 302, 96 S.E.2d 8, 13 (1957).

Network Upgrade costs render the entire project over-priced with regard to delivering "least-cost" power (if utility owned) or at or below the utility's avoided costs (where a QF selling under PURPA). Put another way, the economics of siting a generator in a particular location are usually taken into account by any one of a variety of means *before* the generator obtains sufficient financing to even start a CPCN proceeding. This is true of generators when selling to a Commission-regulated utility.[22]

b. If the Commission Does Grant the CPCN and Network Upgrades Are Constructed in Accordance with Requirements of the FERC-Approved Tariff, the Commission May Not Alter a Cost Allocation Set by FERC and Thereby Trap Costs.[23]

Whereas a state commission is permitted to consider the future potential Network Upgrade costs that would arise as a consequence of a siting decision, if the state commission approves the siting and the generating or transmission facility is constructed, the state commission may not deny cost recovery of the portion of costs allocated through retail rates.

Indeed, no party to this proceeding appears to dispute that FERC alone has jurisdiction to allocate the costs of the Network Upgrades incurred under the FERC interconnection agreement and OATT that the Friesian Facility would cause if approved

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[22] In a recent decision involving the Competitive Procurement of Renewable Energy Program, the Commission's attention was focused on the potential that network upgrade costs exceed the estimates developed within the proposal evaluation process and used to evaluate cost-effectiveness. The Commission noted the importance that all network upgrade costs be appropriately assigned to a proposal for evaluating cost-effectiveness pursuant to N.C.G.S. § 62-110.8(b)(2). *In the Matter of Joint Petition of Duke Energy Carolinas, LLC, & Duke Energy Progress, LLC, for Approval of Competitive Procurement of Renewable Energy Progra*m, No. E-2, 2019 WL 2905987, at *18 (July 2, 2019).

[23] In making this argument, DEP has considered Regulatory Condition No. 3.9(a). DEP does not believe that the issues related to the construction of transmission upgrades as required under FERC OATT/LGIA involve the Commission's authority to determine the reasonableness or prudence of DEP's decisions with respect to "supply side resources, demand-side management, or any aspect of resource adequacy." Therefore, Regulatory Condition No. 3.9 is not applicable with respect to the Company's retail rate recovery of the cost of the Network Upgrades in this case.

and that the Commission may not change such allocation. In *Nantahala*, the Supreme Court reviewed orders from this Commission in which the Commission undertook an independent review of the proper allocation of an entitlement to purchased power among two utilities, despite that allocation having been established in a FERC wholesale ratemaking proceeding. The North Carolina Supreme Court, affirming the Commission's decision, determined that the Commission's review of cost recovery of wholesale purchased power expenses under FERC-approved rates was "well within the field of exclusive state rate making authority. . . ."[24] The United States Supreme Court disagreed, holding that once "FERC sets such a rate, a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable."[25] While the Supreme Court affirmed the states' "undoubted jurisdiction over retail sales," that jurisdiction may not be exercised "to prevent the wholesaler-as-seller from recovering the costs of paying the FERC-approved rate."[26]

The Supreme Court affirmed and clarified the scope of this preemption authority in *Mississippi Power & Light*, holding, as noted above, that a state commission must treat FERC-mandated payments for a certain quantity of purchased power from the Grand Gulf nuclear plant as reasonably incurred operating expenses in setting retail rates for the purchasing utility.[27] A state commission review of whether those mandated costs were prudently incurred and an attempt to establish retail rates based on the assumption that the utility's mandated costs for purchasing a particular share of power from Grand Gulf was

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[24]*State ex rel. Util. Comm'n v. Nantahala Power and Light Co.*, 332 SE 2d 397 (N.C. 1985).

[25] *Nantahala*, 476 U.S. at 966.

[26] *Id*. at 970.

[27] 487 U.S. at 373-374.

less than as ordered by FERC was therefore preempted by federal law.[28]

This precedent directly controls the scope of state authority to consider the proper rate treatment of any Network Upgrade costs, once they are actually incurred under the LGIA and OATT. DEP is required under federal law to evaluate generation interconnection requests, offer an option for interconnection, require the interconnection customer fund the construction of Network Upgrades, and then must refund such Network Upgrade costs to the customer. Thereafter, the OATT determines the share of the transmission costs DEP must incur under the LGIA that will be allocated to wholesale transmission customers. The remainder of the costs are then recovered from retail ratepayers.

Because DEP is required under federal law to incur the cost of such Network Upgrades, DEP is entitled to recover all such costs, or unconstitutional "takings" would occur. If and when DEP refunds the amounts paid by Friesian for the Network Upgrades, these costs will represent costs associated with transmission service that DEP is mandated by FERC to pay, and therefore when DEP seeks to include the appropriate allocation of such costs in retail rates, such costs must be treated as reasonably incurred. Any other result would violate the Supremacy Clause and controlling Supreme Court precedent by "trapping" the costs that DEP is mandated to refund Friesian under the OATT.[29] The Supreme Court explained in *Nantahala* that:

> a State may not exercise its undoubted jurisdiction over retail sales to prevent the wholesaler-as-seller from recovering the costs of paying the FERC-approved rate. … Such a "trapping" of costs is prohibited. Here, Nantahala cannot

[28] *Id*. at 374.

[29] *Nantahala.* at 970.

> fully recover its costs of purchasing at the FERC-approved rate if NCUC's order is allowed to stand.[30]

The Supreme Court went on to rule that any action by a state commission that places a utility in the position where it "cannot fully recover its costs of purchasing at the FERC-approved rate" is preempted.[31]

In this case, DEP is not purchasing power, but rather incurring transmission costs that it is mandated to incur as a FERC-regulated public utility and then allocating a FERC-dictated share of such costs to wholesale customers. DEP will seek the remainder of its costs from retail ratepayers. The state has to allow DEP to recover the costs incurred through retail rates or the costs will be trapped. It is this FERC mandate to build the Network Upgrades (and refund the costs paid by Friesian), and then allocate its costs per the DEP OATT that is all important.[32] As the Supreme Court explained: "it might well be unreasonable for a utility to purchase unnecessary quantities of high-cost power, even at FERC-approved rates, *if it had the legal right to refuse to buy that power*."[33] Here, DEP lacks the legal right to refuse to build the Network Upgrades required to interconnection the Friesian Facility and therefore should be authorized to recover the costs incurred to construct the Network Upgrades as a matter of law.

In the end, the distinction is one of timing. As discussed above, the Commission is free to exercise its siting authority and, may take into account the FERC-mandated cost allocations in exercising that authority prior to the point in time at which the costs are

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[30] *Id.*

[31] *Id.*

[32] *See In Re Statewide Elec. Util. Restructuring Plan*, 82 N.H.P.U.C. 122 (Feb. 28, 1997) (explaining that "cost-trapping occurs not when the state declines to reflect in retail rates a FERC-approved rate, but when the state declines to reflect in retail rates the cost of a buying utility's action ordered by FERC.").

[33] *Mississippi Power & Light* at 374 (emphasis added).

actually incurred and allocated. If this Commission does not want DEP's retail customers to incur the Network Upgrade costs, it should act in this proceeding. However, if the Commission determines that countervailing benefits of the Network Upgrades outweigh the costs, then it should grant the CPCN (assuming that all other CPCN conditions have been satisfied). The outcome of that decision will be that DEP will be required to refund approximately $224 million in Network Upgrade costs to Friesian and thereafter will seek recovery of those costs under its OATT from wholesale customers and in retail ratemaking proceedings from retail customers. At that point, the Commission could not take any action that would "trap" such costs.

c. General Timing Issues Can Be Otherwise Addressed and Should Not Impact the Decision Here

NCCEBA also discusses timing issues related to the CPCN process and its relationship to other legal requirements and the "development cycle" for IPPs interconnecting under the OATT and under the NCIP. NCCEBA states "[m]ost projects, whether proceeding under Rule R8-63 or R8-64, file their CPCN applications much earlier in the project development cycle. For R8-64 projects, this is in part because having a CPCN is required to establish a Legally Enforceable Obligation ("LEO") under PURPA."[34] What is important to note is that projects seeking a CPCN under R8-64, which are the vast majority of generation CPCNs obtained in North Carolina, are QFs selling all output to DEP or DEC. As such, their interconnection is state jurisdictional and such projects are therefore directly responsible for bearing the costs of any necessary Network Upgrades. However, merchant generating facilities' interconnections are FERC-jurisdictional and therefore receive a refund of their Network Upgrade costs. Since a LEO is not necessary

[34] NCCEBA Initial Pre-Hearing Brief, at 14.

in the case of a merchant plant, the need to file a CPCN prior to receipt of System Impact Study is substantially lessened. More importantly, timing concerns related to the CPCN process can likely be resolved and should not serve as a basis for the Commission choosing to abdicate its authority.

Respectfully submitted, this the 9th day of September, 2019.

Jack E. Jirak
Associate General Counsel
Duke Energy Corporation
P. O. Box 1551 / NCRH 20
Raleigh, NC 27602
Telephone: 919.546.3257
Email: Jack.Jirak@duke-energy.com

ATTORNEY FOR DUKE ENERGY PROGRESS, LLC