NOS. 271A18 and 401A18

SUPREME COURT OF NORTH CAROLINA

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STATE OF NORTH CAROLINA ex rel. UTILITIES COMMISSION; DUKE ENERGY PROGRESS, LLC, Applicant;	)	
Appellees,	)	
v.	)	
ATTORNEY GENERAL JOSHUA H. STEIN, Intervenor; SIERRA CLUB, Intervenor;	)	From the North Carolina Utilities Commission
Appellants,	)	
PUBLIC STAFF – NORTH CAROLINA UTILITIES COMMISSION, Intervenor;	)	
Cross-Appellant.	)	

and

NOS. 271A18 and 401A18

SUPREME COURT OF NORTH CAROLINA

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STATE OF NORTH CAROLINA ex rel. UTILITIES COMMISSION; DUKE ENERGY CAROLINAS, LLC, Applicant; Appellees, v. ATTORNEY GENERAL JOSHUA H. STEIN, Intervenor; SIERRA CLUB, Intervenor; NORTH CAROLINA SUSTAINABLE ENERGY ASSOCIATION, Intervenor; NORTH CAROLINA JUSTICE CENTER, NORTH CAROLINA HOUSING COALITION, NATURAL RESOURCES DEFENSE COUNCIL, and SOUTHERN ALLIANCE FOR CLEAN ENERGY, Intervenors; Appellants, PUBLIC STAFF – NORTH CAROLINA UTILITIES COMMISSION, Intervenor; Cross-Appellant.	)	From the North Carolina Utilities Commission

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REPLY BRIEF OF INTERVENOR-CROSS-APPELLANT PUBLIC STAFF - NORTH CAROLINA UTILITIES COMMISSION

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REPLY BRIEF OF INTERVENOR-CROSS-APPELLANT PUBLIC STAFF - NORTH CAROLINA UTILITIES COMMISSION

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Intervenor-Cross Appellant Public Staff of the North Carolina Utilities Commission ("Public Staff") respectfully submits this brief in reply to arguments in the Joint Brief of Appellees Duke Energy Carolinas, LLC and Duke Energy Progress, LLC ("Appellee Brief").

INTRODUCTION

Duke Energy Carolinas, LLC ("DEC"), and Duke Energy Progress, LLC ("DEP"), (collectively, "Duke" or "Appellees") argue on appeal that:

(1) substantial evidence supports the North Carolina Utilities Commission ("Commission") orders allowing costs of coal ash remediation to be recovered in rates, with a return;

(2) the coal ash costs are "property used and useful" under N.C. Gen. Stat. § 62-133(b)(1) and therefore require a return; and

(3) even if a return is not required, the Commission has discretion to allow a return on coal ash costs and properly exercised that discretion.

The Commission has discretion to either allow or deny a return on coal ash costs that have been deferred to a regulatory asset under the Public Staff's reading of the law. However, that discretion is not unbridled – it must be exercised by considering and weighing the material facts of record. The

Commission failed to consider material facts of record, particularly the extensive environmental exceedances resulting from Duke's coal ash impoundments. Moreover, even a discretionary decision may not rest on erroneous legal conclusions and contradictory reasoning. The Commission's orders on "all material issues of fact, law, or discretion" must be supported by "[f]indings and conclusions and the reasons or bases therefor . . . ." N.C. Gen. Stat. § 62-79(a)(1) (emphasis added). The Public Staff disagrees with the Appellee Brief because the Commission's orders fail to meet the requirements of N.C. Gen. Stat. § 62-79(a) due to (1) inconsistent reasoning that leaves the real basis for the orders in doubt, (2) failure to engage in the weighing of material facts of record, and (3) erroneous conclusions of law.

ARGUMENT

I. REPLY TO THE APPELLEES' INTRODUCTION

In the Introduction to the Appellee Brief, Duke argues that its credit rating would decline and its cost of capital would increase, resulting in an ever-worsening "chain reaction," if it were denied recovery of coal ash costs and a return on those costs. Duke claims this would harm customers in the long run. (Appellee Brief pp 2-6)

Duke's concern about capital market reactions in the event of an adverse decision on coal ash cost recovery is not appropriate for an appellate argument. The Court's role is to determine if there is legal error in the Commission's decisions. It is not to evaluate whether an adverse decision on a return for coal ash costs might cause investor confidence in the utility to collapse.

Nor is Duke's argument useful in identifying the point at which an adverse decision on coal ash costs could prompt a credit downgrade, particularly where Duke's creditworthiness is based on its total investment risk and not simply one area of costs.

Duke's view of the threat to its ability to obtain financing has already been shown to be overstated. Duke witnesses testified that investors "required" a 10.75% rate of return on equity as the market-based cost of capital. (DEP R p 541; DEP T 8, pp 30, 146-47; DEC R p 862, DEC T 4, pp 44, 182) The Commission authorized a 9.9% rate of return on equity for both Duke companies. It is not apparent how an 85 basis point reduction from Duke's claim of the "required" 10.75% return to the Commission's approved 9.9% equity return is any less reasonable, in terms of impact on credit-worthiness, than would be an equitable sharing of coal ash costs.

Likewise, Duke fails to address whether a downgrade – if it were to occur and if it were due solely to a decision to allow coal ash cost recovery without a return - would ultimately cost consumers more than the savings of the disallowed return. There is simply no record evidence on that question.

Duke also claims that "[d]eviating from the cost recovery standards mandated by the General Assembly" would result in higher costs of capital. (Appellee Brief p 5) This is misleading because it presumes – incorrectly – that equitable sharing would be a deviation from the statutory framework for ratemaking. Equitable sharing is lawful, rather than a "deviation" from the General Assembly's standards, under N.C. Gen. Stat. § 62-133(d), as this Court has recognized in State ex rel. Utils. Comm'n v. Thornburg, 325 N.C. 463, 385 S.E.2d 451 (1989) ("Thornburg I").

The Appellee Brief repeats in several places the idea that equitable sharing, where implemented through denial of a return on unamortized coal ash costs, is unlawful and even unconstitutional. (Appellee Brief pp 16-17, 60, 70) However, the implementation of equitable sharing under N.C. Gen. Stat. § 62-133(d) is well within the police powers of the State, as noted in part IV C 3 of the Public Staff's initial appellate brief in the instant cases. See also State ex rel. Utils. Comm'n v. Virginia Elec. & Power Co., 285 N.C. 398, 405, 206

S.E.2d 283, 290 (1974) ("VEPCO") (holding that the fixing of rates for utility service is within the police powers of the State). The idea that cost recovery with a return trumps any other consideration of reasonable and just rates has been debunked by the Commission's repeated use of equitable sharing in past cases, and by the decision in Thornburg I. The Court has previously addressed the constitutionality of a regulatory commission's denial of recovery of prudently incurred utility costs:

> The United States Supreme Court has clearly held that a state scheme of utility regulation does not "take" the utility's property in violation of the fifth and fourteenth amendments simply because it disallows recovery of capital investment in cancelled plant not "used and useful in service to the public," even though the expenditures were prudent and reasonable when made. *Duquesne Light Co. v. Barasch*, 488 U.S. 488, 102 L. Ed. 2d 646 (1989).

Thornburg I at 471, 385 S.E.2d at 455-56. Further, this Court has made clear that investor concern for strong earnings, while relevant, is not the polestar for ratemaking:

> The primary purpose of Chapter 62 of the General Statutes is not to guarantee to the stockholders of a public utility constant growth in the value of and in the dividend yield from their investment, but is to assure the public of adequate service at a reasonable charge.

State ex rel. Utils. Comm'n v. Gen. Tel. Co., 285 N.C. 671, 680, 208 S.E.2d 681, 687 (1974).

Duke essentially argues that it knows better than consumer representatives what is in consumers' best long-term interests. (Appellee Brief pp 5-6) The Public Staff could just as well argue that consumers should not have to pay twice for disposal of the same coal ash. These types of arguments may be appropriate to make to the Commission in light of its fact-finding and policy judgment role, but on appeal the arguments should be limited to whether the Commission's orders are affected by legal error.

II. REPLY TO THE APPELLEES' RESTATEMENT OF FACTS

In its Restatement of Facts, Duke asserts that "[n]o party disputes that the facts as actually found by the Commission are supported by 'competent, material and substantial evidence'; accordingly, the facts as actually found are 'conclusive.'" (Appellee Brief p 7) This is not accurate. The Public Staff's initial brief in parts III D and IV A discusses Commission findings of fact that are not supported by evidence.

For example, the Public Staff has argued in the instant appeal that the Commission's orders are not supported by substantial evidence in view of the whole record, where they determine that coal ash costs are "property used and

useful," because the record evidence shows the nature of many of those costs to be "operating expenses." (Public Staff initial brief pp 76-83) In a similar vein, the Public Staff has argued that the Commission erred by deciding that coal ash costs were "property used and useful" without determining from the evidence which coal ash costs were operating expenses and which were property used and useful. (Public Staff initial brief pp 83-85)

The Public Staff also has argued that the Commission's classification of coal ash costs as "working capital" is contrary to the evidence in light of the record as a whole. (Public Staff initial brief pp 92-95) Funds spent in the past to remediate coal ash are not, as a factual matter, cash held to fund the ongoing operations of the utility, which is the definition of cash working capital. This definition of working capital has been recognized by the Court: "the utility's own funds reasonably invested in such materials and supplies and its cash funds reasonably so held for payment of operating expenses, as they become payable . . . ." VEPCO at 414-15, 206 S.E.2d at 295-96. Since the coal ash costs in the Duke rate case applications had already been expended in the past, there is no evidentiary support for the conclusion that they are cash funds (or materials and supplies inventory) under the VEPCO analysis of

working capital funds "held for payment of operating expenses, as they become payable . . . ."

Perhaps the most egregious lack of evidentiary support occurs where the Commission announced that coal ash costs are "working capital," which would make them "property used and useful" under the VEPCO decision and entitle the Company to earn a return on those funds over the period in which the costs are amortized. (DEP R p 674) The Commission expressly relied on the evidence from DEP witness Bateman that coal ash costs had been recorded on the Company's books as "working capital." (DEP R p 673) Yet a closer examination of the evidence from witness Bateman reveals its utter deficiency: she testified that the reason for including coal ash costs in "working capital" was the reason given by Company witness Wright. (DEP T 6, pp 143-44) Company witness Wright, however, testified that coal ash costs were "utility plant." (DEP T 14, p 233; DEP T 20, p 143) As the Commission itself concluded, "working capital" is different from "utility plant." (DEP R p 673) The Commission's reliance on this complete contradiction in Duke's evidence means the "working capital" part of the decision is unsupported by substantial evidence in light of the whole record. The Public Staff initial brief made this argument (pp 86-89). Accordingly, the claim in the Appellee Brief that no

party disputes the evidentiary support for the Commission's orders is not correct.

In addition, part IV A of the Public Staff's initial brief describes three instances where the Commission has mischaracterized the Public Staff's evidence. It is error for the Commission to rely in its findings and conclusions on a false narrative as to what the evidence was.

In short, parts III D and IV A of the Public Staff's initial brief do dispute that certain Commission findings and conclusions are based on competent, material, and substantial evidence. Duke's statement to the contrary in its Restatement of the Facts is not accurate.

III. MISSTATEMENT ON PUBLIC STAFF POSITION AS TO REASONABLENESS OF COSTS

Duke states "[t]he Public Staff does not contest the Commission's findings that the costs at issue were reasonable and prudent." (Appellee Brief p 13; see also pp 15, 19) This too is factually incorrect. As discussed in parts V B, V C, and VI of the Public Staff's initial brief in this appeal, Public Staff witness Lucas recommended a $6.7 million disallowance for DEP, and Public Staff witness Junis recommended a $1.5 million disallowance for DEC, for extraction and treatment costs related to groundwater contamination. These

recommendations for a complete disallowance were based on the unreasonableness (imprudence) of the costs, and fall under N.C. Gen. Stat. § 62-133(b), not an equitable sharing under N.C. Gen. Stat. § 62-133(d).

While the extraction and treatment costs are a small amount of the total dollars spent on coal ash remediation, the Public Staff did contest the Commission's decision on the reasonableness and prudence of those costs, both at the Commission level and as a matter of legal error on appeal. The Public Staff has contested rate recovery of specific groundwater extraction and treatment costs on reasonableness grounds, as discussed again in part IV below, notwithstanding the statement in the Appellee Brief to the contrary.

IV. THE COMMISSION ERRED BY CONCLUDING THAT THE COSTS OF GROUNDWATER EXTRACTION WELLS AND TREATMENT WERE PRUDENT AND REASONABLE

Part I C of the Appellee Brief argues that substantial evidence supports the Commission's findings and conclusions that Duke's coal ash costs were reasonably and prudently incurred. The following discussion focuses on the costs of groundwater extraction wells and treatment, as that is the only part of the Commission's orders that the Public Staff is challenging on appeal with respect to prudence of costs.

A. ERROR IN THE FAILURE TO WEIGH EVIDENCE THAT EXTRACTION WELL AND TREATMENT COSTS WERE UNREASONABLE

Duke argues the Commission is not an environmental regulator, and that the North Carolina Department of Environmental Quality (DEQ) has never obtained an admission from Duke or a finding in litigation against Duke that Duke violated the law with respect to coal ash contamination. (Appellee Brief p 35) Duke is correct that there are no judicial findings of guilt and no Duke admissions of guilt.[1] Duke's position is flawed, however, in presuming that the Commission need not make any further inquiry of reasonableness of the costs once the lack of guilty findings and admissions is determined.

Parts V B and V C of the Public Staff's initial brief discuss why Duke's position is flawed and the Commission's orders commit error of law. To summarize, the Commission has a legal duty to weigh evidence presented to it regarding the reasonableness of costs incurred for environmental compliance deficiencies. The Commission was presented with evidence showing that DEP and DEC incurred specific costs to clean up groundwater

[1] DEC and DEP guilty pleas to misdemeanor violations of the Clean Water Act in federal court are not pertinent because Duke excluded the associated costs from its rate cases.

that was contaminated by their coal ash basins, in violation of State groundwater protection rules, and that those cleanup costs were in addition to the costs resulting from the requirements of the federal Coal Combustion Residuals Rule (CCR Rule) and the North Carolina Coal Ash Management Act (CAMA). The Commission cannot simply ignore that evidence on the grounds that there was no guilty finding or admission. Before Duke can argue that substantial evidence supports the Commission's orders, there is a legal prerequisite that the Commission must have actually weighed all the competent evidence. The Commission cannot lawfully ignore evidence of environmental violations causing offsite contamination, with respect to issues of cost recovery in rates, on the basis that the Commission is not an environmental regulator.

The law on this issue, including N.C. Gen. Stat. § 62-79, is set out in the Public Staff's initial brief. What is notable for purposes of the present Reply Brief is that Duke has not even attempted to refute the Public Staff's argument that the Commission has a duty, separate from environmental regulators, to review evidence of environmental violations as that evidence pertains to utility ratemaking.

B. ERROR IN MISSTATEMENT OF EVIDENCE AND PUBLIC STAFF POSITION

Duke argues that "[t]he evidence of violation presented by the Public Staff was that settlement of the litigation was tantamount to an admission of liability . . . which the Commission found lacking." (Appellee Brief p 36; see also p 33) Duke is correct that the Public Staff offered into evidence the settlement agreement between DEQ and Duke, wherein both DEP and DEC agreed to pay a multi-million dollar penalty to DEQ and to install extraction wells and treat the water from those wells to remediate groundwater contamination caused by its coal ash impoundments. (DEP Doc. Ex. 3100-3112) The Public Staff concedes that the mere existence of a settlement agreement with no admission of guilt, standing alone, should not be evidence of liability. Yet there is a glaring omission in the statement from the Appellee Brief quoted above. Namely, the Public Staff presented substantial additional evidence, apart from the existence of the settlement agreement, showing that the costs of extraction wells and water treatment would not have been incurred to comply with the CCR Rule and CAMA but for Duke's environmental violations.

This evidence is discussed in part V B of the Public Staff's initial brief. In sum, witnesses Lucas and Junis presented the following evidence for groundwater violations causing the need for extraction wells (the bulk of which occurred at DEP's Sutton plant, but also included the Asheville, H.F. Lee, and Belews Creek plants):

- Witnesses Lucas and Junis relied on Duke's own groundwater monitoring reports to DEQ, showing groundwater exceedances at Duke's plants where extraction wells were to be installed. (DEP Doc. Ex. 1123; DEC Doc. Ex. 2043; see Appendix to this Reply Brief)
- Without admitting any wrongdoing, the settlement signed by Duke states that "data show constituents associated with the ash basins at concentrations over the 2L standards . . . have migrated off site"; and "[e]xtraction wells will be used to pump the groundwater to arrest the offsite extent of the migration"; and "[t]his accelerated groundwater remediation is in addition to and shall be performed concurrent with the coal ash impoundment closure obligations set forth in CAMA." (DEP Doc. Ex. 3105)
- Duke witness Wells admitted that the groundwater extraction by DEP would not have been needed absent groundwater

exceedances at DEP's Sutton, H.F. Lee, and Asheville plants. (DEP T 21 pp 175-76)

- Company witness Wright admitted that the groundwater extraction by DEC would not have been needed absent groundwater exceedances at DEC's Belews Creek plant. (DEC T 13 pp 91-92)
- The Public Staff witnesses testified, without contradiction, to the precise costs of the groundwater wells and water treatment. (DEP R p 642; DEC R p 1059)

By arguing that (1) the Public Staff relied only on the existence of a settlement agreement to show Duke caused contamination leading to extraction well and treatment costs, and (2) the Commission properly rejected this evidence of unreasonable costs, the Appellee Brief is misleading by omission. The Public Staff introduced substantial evidence of groundwater contamination at Sutton and other Duke plants, such as the groundwater exceedance data reported by Duke to DEQ, that was independent of the existence of the settlement agreement. Accordingly, Duke's argument that the Public Staff's recommended disallowance was predicated solely on the existence of a settlement, and that the Commission properly rejected the

Public Staff recommendation for that reason, is flawed. The Commission is required to weigh all the material evidence of record, not just the evidence selected by Duke.

C. ERROR IN THE CONCLUSION THAT GROUNDWATER EXCEEDANCES ARE NOT "VIOLATIONS"

Duke also argues that "exceedances are not 'violations" based on the testimony of Duke witness Wells. (Appellee Brief pp 36-37, citing DEP R pp 661-663) This argument is offered in support of the Commission's conclusion that the costs of extraction wells and water treatment were reasonable, for ratemaking purposes, because they resulted from groundwater exceedances but not violations of groundwater standards. (See DEC R pp 1119, 1121-23)

Whether exceedances of groundwater standards in 15A N.C. Admin. Code 02L (the "2L Rule") are violations is a question of law. This is not a question where the testimony of a witness provides substantial evidence and the Commission need only make a finding of fact based on that evidence.

The 2L Rule expressly provides that any exceedance at or beyond the compliance boundary, caused by the person controlling the activity causing the exceedance, is a "violation." That is the plain wording of 15A N.C. Admin. Code 02L .0106. Duke does not dispute that it reported to DEQ many

groundwater exceedances from its coal ash sites, at or beyond the compliance boundaries. No amount of interpretation by a Duke witness can defeat the fact that such exceedances are violations as a matter of law.

The initial Public Staff brief (pp 174, 204) has already addressed the Commission's error in concluding that exceedances at or beyond a compliance boundary are not violations. The Amicus Curiae Brief of DEQ – the state agency charged with enforcement of the 2L Rule – is consistent with the Public Staff's legal conclusion on this issue.

Duke argues that the Commission orders are based on substantial evidence because the orders relied on Duke's witness for an interpretation that exceedances are not violations. (See Appellee Brief p 37) That reliance does not cure the legal error. The Commission relied on the incorrect legal interpretation of a Duke witness to reject the Public Staff's recommendations for disallowance of extraction well and water treatment costs.

D. ERROR IN THE CONCLUSION THAT CAMA REQUIRED GROUNDWATER EXTRACTION EVEN WITHOUT ENVIRONMENTAL VIOLATIONS

The Appellee Brief also identifies testimony from Duke witness Wells as substantial evidence to support the Commission's determination that extraction well and water treatment costs would have been required to comply

with CAMA regardless of any violations, and that such costs are therefore not attributable to groundwater violations. (Appellee Brief p 37) The Commission credited Duke's testimony on this issue as credible:

> Witness Wells further argued, persuasively in the Commission's view, that the groundwater extraction and treatment activity that DEP performed pursuant to the DEQ Settlement Agreement merely accelerated work that would have been required under CAMA in any event.

(DEP R p 662; see also DEC R p 1123 for a similar conclusion) Again, however, this is a question of law, not a question of witness credibility.

The relevant law is discussed at part VI of the Public Staff's initial brief. In summary, CAMA requires groundwater assessment and corrective action planning, but corrective action implementation is only required when needed to "restore" groundwater quality. CAMA provides that "[t]he owner of a coal combustion residuals surface impoundment shall implement corrective action for the restoration of groundwater quality as provided in this subsection." N.C. Gen. Stat. § 130A-309.211(b) (emphasis added). The subsection further provides that "[t]he Groundwater Corrective Action Plan shall provide for the restoration of groundwater in conformance with the requirements of Subchapter L of Chapter 2 of Title 15A of the North Carolina Administrative Code." The 2L Rule requires corrective action for "violations"

of groundwater standards. 15A N.C. Admin. Code 02L .0106. When these statutory and regulatory provisions are read together, as contemplated by CAMA, the law under CAMA provides for "corrective action" to be taken only with respect to "violations" of the 2L Rule.[2]

This is purely a matter of legal interpretation. By casting it as an issue of substantial evidence in support of Commission findings, the Appellee Brief has applied the wrong standard of review (in addition to interpreting the law incorrectly). This reason given by the Commission for declining to disallow extraction well and treatment costs is supported by Duke's evidence, but is still error of law.

V. THE COMMISSION'S ORDERS DO NOT PROVIDE PROPER LEGAL SUPPORT FOR A RETURN ON COAL ASH COSTS

The Commission's orders allow a return on the unamortized balance of

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[2] The DEQ Amicus Brief states the Commission erred by concluding that the Coal Ash Management Act requirements for groundwater assessment and corrective action are triggered by exceedances. (Amicus Brief pp 16-17) A clarification is in order. CAMA does require owners of coal ash basins to conduct groundwater monitoring and assessment, without regard to whether there are any exceedances. N.C. Gen. Stat. § 130A-309.211(a). However, nothing in CAMA requires corrective action in the absence of violations. Without a violation (an exceedance of the standards in the 2L Rule that occurs at or beyond the compliance boundary), there is nothing to correct. The purpose of corrective action in CAMA is to restore groundwater quality to the 2L Rule standards. N.C. Gen. Stat. § 130A-309.211(b).

coal ash costs. Duke argues in support of the Commission that a return is justified because (1) coal ash costs are "property used and useful," and (2) coal ash costs were deferred to a regulatory asset, they were capitalized as "utility plant" under ARO accounting, and the funding was supplied by investors. (Appellee Brief pp 39-40) The Public Staff's reply to those arguments follows.

A. INCONSISTENT REASONING VIOLATES N.C. GEN. STAT. § 62-79

As argued in the Public Staff's initial brief [3], the Commission's orders are rife with inconsistent reasons for support of a return on coal ash costs. For instance, the Commission concluded that all coal ash costs are "property used and useful" within the meaning of N.C. Gen. Stat. § 62-133(b)(1).[4] It also concluded that because of the Commission's "used and useful" classification

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[3] In particular, see part III C of the Brief of Intervenor-Cross-Appellant Public Staff.

[4] For example, "[t]he actual coal ash basin closure costs incurred by DEP, less the $9.5 million, are known and measurable, reasonable and prudent, and used and useful in the provision of service to the Company's customers." (DEP R p 497) Also, "this case does not involve "abandoned plant" or cancellation costs. Rather, it involves 'reasonable and prudent' and 'used and useful' expenditures by the Company . . . ." (DEP R p 670) Further, "[Coal ash costs] are "used and useful" within the meaning of G.S. 62-133(b)(1) in the provision of service. As such, the Company is entitled to earn a return on those funds . . . ." (DEP R p 674)

of coal ash costs, case law "does not support the exercise of discretion as the Public Staff maintains." (DEP R p 670) Similarly,

> The Court [in State ex rel. Utils. Comm'n v. Thornburg, 325 N.C. 484, 385 S.E.2d 463 (1989) ("Thornburg II")] held that the Commission did not possess the discretionary power to effectuate its "equitable sharing" decision. Rather, the facilities were either used and useful," and therefore in rate base, or they were not.

(DEP R p 671) In the DEC rate case order, the Commission noted that it had decided in the earlier DEP case that the coal ash costs were "'used and useful' in the provision of service to customers" and concluded that "[t]he same standard applies in this [DEC] case." (DEC R p 1033; see also pp 1092-93, 1097)

Having concluded that coal ash expenditures qualified as property used and useful, and thus were entitled to a return, the Commission's orders then did an about face and reached a conflicting conclusion. The Commission stated that there is no need to determine if coal ash costs are "used and useful" or whether such costs must be added to rate base as a matter of law, and that its decision on a return on coal ash costs was an "exercise of discretion." (DEP R pp 951-52; DEC R pp 1099-1100) Later, in another inconsistency, the Commission decided that coal ash costs were "used and useful" only "to the extent capital in nature" (apparently recognizing that to the extent coal ash

costs were "operating expenses" in nature, they would not be "property used and useful"). (DEC R p 1135)

These contradictions leave the basis for the Commission's decision unclear. Consequently, the orders fail to provide the logical chain of evidence that supports findings, and findings that support conclusions, "upon all the material issues of fact, law, or discretion" in the rate cases. This is a violation of N.C. Gen. Stat. § 62-79. Moreover, an order based on inconsistent, contradictory reasoning is inherently arbitrary and capricious.

The Public Staff interprets N.C. Gen. Stat. § 62-133(d) and this Court's ruling in Thornburg I as granting the Commission discretion to either allow or deny a return on the unamortized balance of a regulatory asset (including coal ash costs). However, even a discretionary Commission decision must meet the requirements of N.C. Gen. Stat. § 62-79. Even for discretionary issues, Commission orders that rest on inconsistent and contradictory reasoning are inimical to the integrity of the decision-making process.

The Appellee Brief ignores this appeal issue. Duke argues that there is substantial evidence for the Commission's findings (Appellee Brief pp 7, 13, 25, 45, 49, 52-53, etc.); that the Public Staff concedes the award of a return is discretionary (though Duke does not concede it is anything less than

mandatory) (Appellee Brief pp 13, 42); and that coal ash costs are properly in rate base (i.e., allowed a return) because they are "property used and useful" under N.C. Gen. Stat. § 62-133(b)(1) (Appellee Brief pp 10-11, 39-68). These arguments fail to address the first appeal issue raised by the Public Staff's initial brief: that the Commission's orders are deficient under N.C. Gen. Stat. § 62-79 due to inconsistent reasoning. N.C. Gen. Stat. § 62-79 is not even cited in the Appellee Brief.

B. ERROR IN THE CONCLUSION THAT "PROPERTY USED AND USEFUL" INCLUDES ALL FUNDS ADVANCED BY INVESTORS

Duke and the Public Staff agree that "property used and useful" includes both physical assets and working capital as defined in VEPCO. (Appellee Brief pp 40-45; Public Staff initial brief p 51) However, Duke takes a further step and proclaims that any expenditure – including operating expenses not already in rates - qualifies as "property used and useful" if "it serves the public and was paid by debt or equity investors." (Appellee Brief p 41) Duke's argument tracks the Commission's erroneous logic that all investor-supplied funds are "working capital," and all working capital is "property used and useful" as a matter of law. (See DEP R p 674)

As discussed below, a substantial portion of Duke's coal ash costs were incurred for operating expenses, such as excavation and transport of ash to landfills owned by third parties, rather than for construction or acquisition of physical utility plant assets. The question then becomes whether or not such expenditures should be classified as "property" under N.C. Gen. Stat. § 62-133(b)(1) as a form of "working capital."[5]

The Appellee Brief (p 41) quotes an earlier Court ruling on working capital:

> While Chapter 62 of the General Statutes makes no reference to working capital, as such, the utility's own funds reasonably invested in such materials and supplies and its cash funds reasonably so held for payment of operating expenses, as they become payable, fall within the meaning of the term "property used and useful in providing the service," as used in G.S. 62-133(b) (1), and are a proper addition to the rate base on which the utility must be permitted to earn a fair rate of return.

VEPCO at 414-15, 206 S.E.2d at 295-96. To support the outcome of the Commission's award of a return on coal ash costs, Duke interprets this ruling

[5] Duke separately argues that special accounting rules convert "operating expenses" into "property used and useful" by "capitalizing" the expenses for financial reporting purposes. See part V C below.

broadly, to mean that all investor-supplied funds should be included in rate base. This broad interpretation is legal error for two reasons.

First, the VEPCO ruling specifically defines two types of working capital: (1) inventory ("materials and supplies"), and (2) "cash funds . . . held for payment of operating expenses, as they become payable . . . ." No party has taken the position that costs incurred to excavate and transport coal ash, and otherwise clean up the ash basins, is a form of materials and supplies inventory.

Rather, Duke appears to argue the expenditures are a form of cash working capital because they are funds advanced by investors to pay for operating expenses that were not previously included in the ratemaking process. (Appellee Brief p 43) This argument fails because the cash working capital that qualifies for rate base treatment is that which serves the purpose of covering future operating expenses "as they become payable" per the VEPCO ruling. (See Public Staff initial brief p 54, n 17, and pp 92-94) The coal ash costs in the present cases were past expenditures, not cash advanced by investors for the payment of future operating expenses. In other words, the coal ash costs in the present cases do not meet the VEPCO definition of "cash working capital."

Second, investor-supplied funds do not necessarily have a statutory right to recovery in rates, or a return, especially where the funds were used to pay for past operating expenses. Duke's argument that coal ash costs are investor-supplied funds is based on the idea that the coal ash expenditures in 2015 - 2017 were not included in the operating expenses used to establish rates in previous rate cases. Since the expenses were not explicitly included in prior rates, the only other source of funding is from investors. However, N.C. Gen. Stat. § 62-133 does not provide for a return on operating expenses, regardless of whether they were funded by investors. While the Commission may in its discretion under N.C. Gen. Stat. § 62-133(d) allow a return on past operating expenses that have been deferred, that return is not a legal entitlement.

As discussed in the Public Staff's initial brief, there are several cases where the Commission has denied a return on deferred costs; that is, denied a return on investor-supplied funds. In Thornburg I, the costs of abandoned Harris Units 2, 3, and 4 were deferred as operating expenses. Those costs were funds advanced by investors just as much as coal ash costs were, but that did not make them "working capital" that required inclusion in rate base. The Court upheld the denial of a return on those deferred expenditures. Because coal ash costs are deferred costs funded by investors, and include significant

operating expenses, the Commission's decisions in earlier cases that provided for equitable sharing, along with the Thornburg I decision, establish there is no right to a return simply because investors (who incur carrying costs) rather than ratepayers provided the funds.

C. ERROR IN THE CONCLUSION THAT ARO ACCOUNTING CONVERTS COAL ASH COSTS INTO "PROPERTY USED AND USEFUL"

Duke next argues that the Commission properly classified coal ash costs as "property used and useful" because those costs were "capitalized" under ARO accounting. (Appellee Brief pp 48-59) The Public Staff's initial brief, part III D 4, explains why this is incorrect. Some further response to the Appellee Brief is merited.

First, Duke distorts the issue by claiming that the Public Staff's position is that "some of the coal ash basin closure costs incurred by Duke Energy were 'operating expenses' and therefore ineligible for a return." (Appellee Brief p 48) This is incorrect because the Public Staff has throughout this proceeding maintained that the Commission has discretion to award a return – or not - on deferred coal ash costs under N.C. Gen. Stat. § 62-133(d). That is, the coal ash expenditures are "eligible" for but not "entitled" to a return.

Duke's argument that ARO accounting "capitalizes" coal ash costs is similarly misleading. The argument starts on solid footing: coal ash costs that are required under the CCR Rule or CAMA must be recorded on Duke's books as an ARO liability with a corresponding Asset Retirement Cost ("ARC") asset. (Appellee Brief pp 50-51) This accounting convention is required to comply with Generally Accepted Accounting Principles ("GAAP") set by the Financial Accounting Standards Board ("FASB"), and also the Uniform System of Accounts adopted by the Federal Energy Regulatory Commission ("FERC").

Duke and the Commission's orders err in asserting that these requirements established for financial reporting purposes, pursuant to either FASB or FERC rules, also govern accounting for state regulatory accounting and ratemaking actions. (Appellee Brief pp 50-52, citing NCUC Rule R8-27; DEP R p 673; DEC R p 1112) North Carolina Utilities Commission Rule R8-27 provides that orders of the Commission that conflict with the FERC Uniform System of Accounts "shall supersede provisions of the Uniform System of Accounts for North Carolina retail jurisdictional purposes." (See Appendix to this Reply Brief for Rule R8-27) In other words, if the FERC Uniform System of Accounts' provisions for ARO accounting were to conflict with the Commission's use of regulatory assets for North Carolina retail

accounting and ratemaking purposes, then the Commission's approach would supersede the Uniform System of Accounts ARO accounting. The FERC Uniform System of Accounts (including ARO accounting rules) does not govern the outcome of state ratemaking.

In its December 2015 filing with the Commission, Duke stated that the difference between GAAP ARO accounting and state regulatory accounting does not create a conflict, as GAAP recognizes that regulatory assets may be used to account for this difference:

> The FASB recognized that differences may exist between the requirements of ASC 410-20 and the treatment of ARO cost for regulatory purposes, and accordingly, provided that a regulated entity subject to ASC 980, *Regulated Operations,* (formerly SFAS 71, *Accounting for the Effects of Certain Types of Regulation),* could recognize a regulatory asset or liability for any differences between the two approaches, if the facts and circumstances meet the requirements of in ASC 980 for such recognition.

(DEP R p 9) Consistent with that statement, Rule R8-27 recognizes the use of regulatory assets may supersede the effects of ARO accounting "for North Carolina retail jurisdictional purposes." This is not a matter of witness credibility; it is what the Commission's own promulgated rule provides. In other words, where the FERC Uniform System of Accounts requires an estimate of ARO coal ash costs to be booked as a "capitalized asset," that in no

way obligates the Commission to classify deferred past coal ash expenditures as "property used and useful" for state ratemaking purposes.

In addition, Duke's December 2016 deferral petition made abundantly clear that the actual coal ash expenditures were not all capital investment in "property used and useful" that the companies would simply record as rate base. Duke referred to those costs as "[e]xpenses incurred for state and federal compliance . . . ." (DEP R p 15) (emphasis added) Closing ash basins is described as "part of the normal operation of a utility . . . ." (Id.) (emphasis added) Duke further notes that "[c]osts related to the operation of a power plant, including decommissioning costs, are typically paid for by customers." (Id.) (emphasis added) Duke's own filing thus describes at least some of the coal ash costs in terms of operating expenses.

Furthermore, Duke's deferral request in December 2016 was premised on its belief that it would have to write off the coal ash costs; that is, treat them as unrecoverable expenses or losses occurring between rate cases, as opposed to investment in "property used and useful" that remains in rate base.

> Absent the deferral, the Companies may have to write off billions of dollars of costs for accounting purposes, which without question would severely impair the Companies' financial stability and ability to attract capital on reasonable terms.

(DEP R p 27)[6] If the deferral of costs related only to "property used and useful," then Duke's loss without deferral would only be the depreciation and return on those costs until it filed its next rate case – nowhere near a write-off of "billions of dollars."

Duke's deferral request expressly contemplated "non-capital costs [i.e., operating expenses] as well as the depreciation expense and cost of capital . . . for all capital costs" related to coal ash remediation under the CCR Rule and CAMA. (DEP R p 28) This filing defies Duke's argument in the present appeal that coal ash costs are all "property used and useful" on the basis that ARO accounting converted those costs into a capitalized asset.

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[6] Public Staff witness Maness also testified that the deferral of coal ash costs to a regulatory asset served the purposing of avoiding a write-off of those costs:

> [Duke] was at risk of having, I believe, DEP approximately a $291 million write-off [of coal ash expenditures] to expense if they did not receive the deferral accounting treatment that they requested. Coincidentally, the amount that the Company has proposed as a regulatory asset for the 2015/2016 period is $311 million. . . . I think it does serve to illustrate that what we are talking about in this case is, I believe, for the most part, [coal ash] costs that would be written off to expense or as a loss and not costs that would otherwise be recorded as plant [in] service.

(DEP T 19 p 67)

The error of the Commission's conclusion that ARO accounting turns coal ash costs into a "capitalized asset" that belongs in rate base is highlighted by wording in the Commission's own prior order in the very docket that Duke cites in support of its deferral (DEP R pp 4, 6, 8, 18, 22, 32, 35; Appellee Brief pp 8, 55, 56), as noted in Commissioner Clodfelter's dissent:

> [A return on coal ash costs] is also a reversal of the position taken in the Commission's August 8, 2003, Order in Docket No. E-7 sub 723. In that Order the Commission approved the Company's implementation of SFAS 143 accounting treatment for its obligations arising from decommissioning the irradiated portions of its nuclear plants and for environmental clean-up at its Belews Creek Steam Station. The Commission conditioned its approval on a number of specific qualifications and limitations, including "[t]hat no portion of the total ARO asset or liability shall be included in rate base for North Carolina retail accounting or ratemaking purposes."

(DEC R p 1192, n 52) (emphasis added)

Whether specific coal ash expenditures were "property used and useful" or "operating expenses" is a legal conclusion that must be made under N.C. Gen. Stat. § 62-133(b) from findings based on evidence showing the nature of those costs. ARO accounting, which by itself (without a state-approved deferral) could result in a massive write-off of coal ash costs that would preclude any recovery in rates, does not establish the nature of the costs for

North Carolina ratemaking purposes. ARO accounting does not displace or govern the ratemaking provisions of N.C. Gen. Stat. § 62-133.

VI. THE RECORD EVIDENCE DOES NOT SUPPORT DUKE'S STATEMENT THAT "THE VAST MAJORITY" OF COAL ASH COSTS WERE LONG-TERM CAPITAL EXPENSES

Duke argues:

> The vast majority of these [coal ash] costs constitute improvements to real property and are therefore capital assets. Thus, not only are these expenses properly treated as "utility plant" under the required accounting procedures for public utilities, these expenditures give rise to long-term assets that benefit the utility's customers.

(Appellee Brief p 67) This is an incorrect assertion for two reasons.

First, the statement that the "vast majority" of coal ash costs are long-term utility plant assets contradicts the portion of Duke's brief that states coal ash costs are properly classified as working capital. As the Commission itself has observed, investor funds can qualify for rate base treatment as either utility plant or working capital. (DEC R p 1115) Those categories are distinct from each other; an expenditure cannot be both utility plant and working capital. Like the Commission's orders, the Appellee Brief supports rate base treatment for coal ash costs under mutually exclusive theories. This is not the

logical chain of reasoning required by N.C. Gen. Stat. § 62-79, where evidence supports findings that in turn support conclusions.

Second, there is no evidence in the record that quantifies which coal ash costs are "operating expenses" and which are "capital" invested in long-term utility plant. Duke cites no such evidence in its brief. The Commission's orders cite no such evidence. It simply does not exist in these cases. Duke did identify broad categories of expenditures (DEC Doc. Ex. 3641-85). A few of those categories appear to be for capital assets ("Site infrastructure") and a few appear to be for operating expenses ("CCP Inspections and Maintenance"), but for the most part there is insufficient detail to determine which costs fall under N.C. Gen. Stat. § 62-133(b)(1) versus (b)(3). Duke's factual statement in its brief about the "vast majority" of costs has no quantitative basis in the record.

Duke cites to the Commission's order in the DEC case (DEC R p 1101) as support for Duke's claim that "the majority of the coal ash closure costs are improvements to real property . . . ." (Appellee Brief p 66) But this is not accurate. The DEC order actually states

> a <u>significant portion</u> of the costs compiled in the asset retirement obligation has been or will be spent on creation of lined landfills with synthetic liners or impermeable caps

> over existing impoundments. These structures are examples of long-lived assets and are capital in nature- not expenses. Another significant portion, had they not been accounted for in an ARO and deferred, would have been operating or other expenses.

(DEC R p 1101) (emphasis added) Thus, the Commission does not find that a "vast majority" or a "majority" of the coal ash costs were capital expenditures for long-lived assets (i.e., utility plant). The Commission applies the word "significant portion" to operating expenses as well as to expenditures for utility plant. The Commission's actual wording belies the statement in the Appellee Brief.

In short, Duke's claim that the Commission found that the vast majority or a majority of coal ash costs were spent on long-term utility plant is neither supported by the record, nor is what the Commission actually stated.

VII. THE COMMISSION'S REASONS FOR REJECTING EQUITABLE SHARING ARE LEGAL ERROR

A. EQUITABLE SHARING IS NOT UNLAWFUL

The Public Staff has advocated throughout these rate cases that equitable sharing of coal ash costs is a discretionary decision for the Commission pursuant to N.C. Gen. Stat. § 62-133(d). Public Staff witnesses Lucas, Junis, and Maness testified that equitable sharing was appropriate due

to (1) the extensive environmental contamination caused by Duke's coal ash basins, in violation of state environmental laws and regulations, and (2) the extraordinary magnitude of the costs that do not result in any new generation of electricity for customers. (See DEP T 18 p 309; DEC T 22 pp 71-72)

Among the reasons given by the Commission for rejecting an equitable sharing of coal ash costs was the concern that equitable sharing would not be lawful. In particular, the DEP Order indicated that equitable sharing had "legal impediments" (DEP R p 668); that "the Public Staff's view of the Commission's discretion [to order equitable sharing] is overly broad . . . and not supported with the cited Supreme Court precedent" (DEP R p 669); and that equitable sharing was "of questionable legal sustainability" (DEP R p 684). The DEC Order refers to the conclusions on equitable sharing in the DEP Order and states that "[t]he same standard applies in this case." (DEC R p 1033) The DEC Order likewise states, "[t]he Commission chose not to accept the 'equitable sharing' concept in the 2018 DEP Case, and does so again, on the same basis." (DEC R p 1097)

As argued in the Public Staff's initial brief, the Commission is wrong on the law: equitable sharing is lawful, as recognized in prior Commission

decisions and the Thornburg I case. Yet the Appellee Brief (pp 68-78) persists in arguing equitable sharing would not be lawful for coal ash costs.

1. THE COMMISSION'S DISCRETIONARY AUTHORITY IS PROPERLY GUIDED AND LIMITED BY THE REQUIREMENT IN N.C. GEN. STAT. § 62-133(d) TO FIND OTHER MATERIAL FACTS

Duke argues that equitable sharing is not lawful because N.C. Gen. Stat. § 62-133(d) does not give the Commission "unbridled discretion" to adjust rates to achieve an equitable sharing of costs, especially where N.C. Gen. Stat. § 62-133(b) provides for a return on "property used and useful." (Appellee Brief pp 69-70)

The Public Staff agrees that N.C. Gen. Stat. § 62-133(d) does not give the Commission unbridled discretion. The statutory discretion is limited and guided by the requirement that the Commission must make findings with regard to "other material facts of record" that are relevant to the statutory question of "what are reasonable and just rates." Such findings would have to be grounded in evidence per N.C. Gen. Stat. § 62-79; the Commission must justify its exercise of discretion on the basis of record evidence rather than just announce an unsupported outcome.

Furthermore, use of N.C. Gen. Stat. § 62-133(d) to order an equitable sharing of coal ash costs, via denial of a return on the unamortized balance of such costs, does not conflict with the rest of N.C. Gen. Stat. § 62-133. To the extent coal ash costs are "operating expenses" under N.C. Gen. Stat. § 62-133(b)(3), they are not legally entitled to any return. The Court has recognized the Commission's discretion on whether to allow or deny a return on deferred operating expenses, and expressly used the words "equitable sharing" in affirming the Commission's choice of amortization without a return. Thornburg I at 480, 385 S.E.2d at 460.

The Court has made clear that the Commission's discretion under N.C. Gen. Stat. § 62-133(d) operates in addition to the specific ratemaking formula in the rest of N.C. Gen. Stat. § 62-133:

> N.C.G.S. § 62-133(d) has been interpreted by this Court as allowing the Commission to consider "all other material facts of record" beyond those specifically set forth in the statute. *See Utilities Commission v. Duke Power Co.*, 305 N.C. at 18, 287 S.E.2d at 796. Therefore, even assuming arguendo that the Attorney General's interpretation of N.C.G.S. § 62-133(c) is correct, the Commission would not be bound by a strict interpretation of the operating expense component.

Thornburg I at 478, 385 S.E.2d at 459 (emphasis added).

The same reasoning applies to coal ash costs in the present cases, regardless of whether those costs are "operating expenses" or "property used and useful." Just as N.C.G.S. § 62-133(d) gives the Commission discretion to allow a return on deferred operating expenses, despite the fact that N.C.G.S. § 62-133 would otherwise prevent such a return, so too does N.C.G.S. § 62-133(d) allow the Commission discretion to deny a return on "property used and useful." Consistent with Thornburg I, N.C.G.S. § 62-133(d) overlays the provisions of N.C.G.S. § 62-133(b) and lawfully provides the Commission with discretion to adjust rates apart from the cost recovery provisions in N.C.G.S. § 62-133(b), where supported by "other material facts of record."

The Commission's mismanagement penalties for coal ash in the present cases demonstrate that the discretion provided in N.C.G.S. § 62-133(d) overlays other provisions of Chapter 62. The Commission's authority to penalize a utility is set forth in N.C.G.S. § 62-310. That statute contemplates penalties of up to $1,000 per violation. The penalty imposed by the Commission in the present cases is completely different from the penalty framework contemplated in N.C.G.S. § 62-310; it takes the form of a $70 million reduction in amortization of coal ash costs for DEC (DEC R p 1146) and a $30 million reduction for DEP (DEP R p 685). This type of mismanagement

penalty can only be lawful – and it is lawful – due to the discretion authorized by N.C.G.S. § 62-133(d) that overlays other more specific statutory provisions.

In sum, N.C.G.S. § 62-133(d) provides the Commission with discretionary authority to implement equitable sharing, constrained by the requirement that "material facts of record" must justify an adjustment to achieve reasonable and fair rates. That constraint was legally sufficient to uphold equitable sharing under N.C.G.S. § 62-133(d) in Thornburg I. The Court in Thornburg I did not find the Commission's exercise of discretion under N.C.G.S. § 62-133(d) to be "unbridled" or a violation of separation of powers, and the law has not changed since then.

2. THE COMMISSION FAILED TO CONSIDER EVIDENCE OF OTHER MATERIAL FACTS IN THESE CASES

The next question is whether the Commission engaged in weighing of "material facts of record" that relate to the equitable sharing issue. Duke claims that "[t]he Public Staff does not argue that the Commission excluded material facts of record." (Appellee Brief p 69) Similarly, Duke states, "the Public Staff is unable to cite to a single element of the Public Utilities Act that was not properly considered by the Commission." (Appellee Brief p 70) Duke is simply wrong in these assertions. The Public Staff has maintained in its

testimony, in its proposed orders, and in the Public Staff initial brief on appeal that Duke's environmental violations, in addition to the extraordinary amount of coal ash costs that do not result in any additional electricity for customers, are material facts of record that justify equitable sharing. (See, e.g., DEP T 18 pp 274, 282, 309, 339-40; DEC T 22 p 71; DEC T 26 pp 727, 738-42)

The Commission in effect excluded the evidence of environmental violations by ruling that it would only consider a judicial finding of guilt or an admission by Duke as sufficient to show violations, and that environmental matters were outside the Commission's responsibility. For instance:

> The Commission's duty is not to determine liability to and assess damages for torts committed by management for injury to the environment or to receptors of contaminants. Environmental regulators and courts of general jurisdiction are the appropriate arbitrators of those disputes.

(DEC R p 1085) Also,

> Based upon the evidence presented in this case, with the exception of the federal criminal case to which DEP pled guilty, DEP has not been found liable for violations of the law. As stated above, the Commission will not use settlement agreements to find liability.

(DEP R p 663) In both rate cases the Public Staff presented voluminous evidence of environmental violations apart from the existence of settlement agreements. That evidence included Duke's own groundwater exceedance

reports to DEQ, Duke's admission of engineered seeps that channeled coal ash-tainted water from ash basins to surface waters of the State without NPDES permit authorization, and groundwater exceedances noted by the independent federal Court Appointed Monitor as part of the federal criminal plea. (See pp 171-180 of the Public Staff's initial brief)

The Commission's erroneous rejection of evidence of environmental contamination caused by Duke's coal ash, other than Company admissions or judicial findings of guilt, is discussed in the Public Staff's initial brief at parts IV A 1, V A, and V C. That discussion refutes the assertion in the Appellee Brief that the Public Staff does not claim material facts of record were excluded by the Commission. The material facts of record concerning Duke's environmental violations were not ruled inadmissible, but neither were they weighed or considered by the Commission. Instead, the Commission rejected out of hand any consideration or weighing of that evidence on the grounds that the Commission was not an environmental regulator.

As argued at pp 191-97 of the Public Staff's initial brief, the Commission had a legal duty to weigh that evidence as it pertains to the reasonableness of cost recovery in the rate cases. This is not an issue of whether substantial evidence supports the Commission's decision. Rather, the issue on appeal is

whether the Commission failed to engage in the process of weighing material facts of record.

3. THE EQUITABLE SHARING RECOMMENDATION IS NOT STANDARD-LESS AND ARBITRARY

Duke argues that a 50%-50% or 51%-49% sharing of coal ash costs between investors and ratepayers, as recommended by the Public Staff, has no standard and would be unlawfully arbitrary. (Appellee Brief pp 71-72) Duke's argument is incorporated into the Commission's orders (see DEC R pp 1096-98), and is briefly addressed in the Public Staff's initial brief (pp 150-51).

The Public Staff did choose percentages of sharing between investors and ratepayers that it deemed reasonable and just. It then "backed into" an amortization period that would achieve that sharing at a given rate of return. Public Staff witness Maness explained in response to Commission questions that the sharing percentage was ultimately a judgment within the Commission's discretion. (DEP T pp 67-69) A reasonable and just sharing percentage is a qualitative judgment, not an unlawfully arbitrary determination, and has ample precedent in Commission decisions and case law.

Indeed, the Commission in the present DEC rate case authorized a 12-year amortization of cancellation costs for the Lee nuclear plant, with no return on the unamortized balance, on the reasoning that this was a "fair allocation" of the losses between ratepayers and investors. (DEC R pp 981-87) This denial of a return was a purely qualitative decision, one that the Commission described as a matter within its "discretionary" judgment. The Commission justifies its equitable sharing of the Lee nuclear cancellation costs by reference to past decisions on nuclear cancellation costs. (DEC R pp 984-86; see also Thornburg I at 466, 385 S.E.2d at 452) The Commission did not state any standard or quantification method for the percentage of costs to be borne by shareholders and the percentage to be borne by ratepayers. Commission decisions on equitable sharing have typically involved different amortization periods and different rates of return (e.g., a 10.45% overall rate of return and a ten-year amortization for Harris costs as noted in Thornburg I, versus the 7.35% overall rate of return and 12-year amortization for Lee nuclear costs in the present DEC rate case, as noted at DEC R p 838), meaning that the sharing percentages borne by investors versus ratepayers differs among the cases. It is inconsistent for the Commission to conclude that the Public Staff recommendation for a 50%-50% equitable sharing of coal ash

costs is "arbitrary" or "standard-less" when the Commission's long-standing approach to equitable sharing percentages for other costs – and the Court's affirmance of such equitable sharing - has no more basis in quantitative analysis than the Public Staff's equitable sharing recommendations in the present case.

Likewise, the Commission justifies its mismanagement penalties in the present cases as "appropriate" (DEP R p 685; DEC R p 1146). There is no "guiding principle" or quantitative standard stated for the mismanagement penalties – they result from a purely qualitative judgment. Equitable sharing is no less standard-less or arbitrary than the mismanagement penalties approved by the Commission.

B. THE PUBLIC STAFF'S EQUITABLE SHARING RECOMMENDATION IS NOT A "DRAMATIC DEPARTURE" FROM ITS POSITION IN OTHER CASES

Duke next argues that the Public Staff's equitable sharing recommendation in the instant cases is a "dramatic departure" from other cases. (Appellee Brief pp 73-74) It is not apparent how this argument relates to the legal errors the Public Staff has raised on appeal (i.e., inconsistent and legally incorrect Commission conclusions; failure to weigh competent evidence). Moreover, Duke cites only one other case – the Dominion Energy

North Carolina ("Dominion") rate case decided on 22 December 2016 in Docket No. E-22, Sub 532. Duke's argument is flawed because:

1. The Commission expressly stated that its decision in the Dominion case was not to have any precedential effect: "the Commission's approval of DNCP's CCR cost deferral [including amortization with a return] is based on the particular facts and circumstances presented in this docket and, therefore, is not precedent for the treatment of CCR costs in any future proceedings." (Docket No. E-22, Sub 532, Order Approving Rate Increase, p 63, posted at https://starw1.ncuc.net/NCUC/ViewFile.aspx?Id=97d7286c-a5e3-4542-96b3-1cff01e34bf9)

In that regard, the Commission's order in the Dominion rate case accords with case law. While prior Commission decisions may have binding effect for adjudicative facts and findings on specific past costs to be recovered in rates, they do not bind the Commission on recovery of future costs, as each case has new facts and the policy choices in rate cases are more legislative than judicial in character:

> this Court has stated that ratemaking activities of the Commission are a legislative function. *Utilities Comm. v. Edmisten, Attorney General*, 294 N.C. 598, 603, 242 S.E.2d 862, 866 (1978); *Utilities Commission v. General Telephone Company*, 281 N.C. 318, 336, 189 S.E.2d 705, 717 (1972). It

> follows that since the exercise of the Commission's ratemaking power is a legislative rather than a judicial function, such orders are not governed by the principles of res judicata and are reviewable by this Court in later appeals of closely related matters. *See Utilities Comm. v. Edmisten, Attorney General*, 294 N.C. at 603, 242 S.E.2d at 866 (Commission's exercise of rule-making power is legislative and therefore not governed by res judicata).

Thornburg I at 468-69, 385 S.E.2d at 454.

2. When DEP argued that the Commission should follow its decision in the Dominion rate case, the Commission disagreed and disavowed any precedential effect of the coal ash resolution in the Dominion rate case:

> While the Commission's Order here is consistent with the logic of its DNCP Order, it disagrees with DEP that it is bound to follow it. The Commission expressly stated that its CCR determinations in the DNCP Order were non-precedential. Moreover, this is a ratemaking decision in which the Commission exercises its legislative authority. Its past decisions are neither binding, res judicata nor stare decisis.

(DEP R p 672)[7]

[7] Strangely, the Commission took an inconsistent path in its DEC rate case order, where it decided that in its "discretion" it would follow the "precedent" of its Dominion and DEP rate case orders on coal ash costs. (DEC R pp 1099-1100) Perhaps the Commission was trying to say it was choosing a consistent approach across all three cases, but its use of the word "precedent" – which it had expressly disavowed in its Dominion and DEP rate case orders – suggests the Commission felt some legal compulsion or obligation to decide the DEC rate case the same way as prior cases. At the least, this wording in the Commission's order is unclear – the basis for decision is ambiguous.

3. The Public Staff provided ample evidence as to why its support for a five-year amortization with return for Dominion's initial coal ash costs was in no way comparable to Duke's situation. As noted previously, the "other material facts of record" the Public Staff relied upon for its equitable sharing recommendation were the extent of Duke's environmental violations and the magnitude of its coal ash costs. In contrast, the Public Staff investigation of Dominion in Docket No. E-22, Sub 532, produced no evidence of coal ash environmental violations after 1993 (DEC T 26 pp 747-49), whereas there were extensive groundwater exceedances at every one of Duke's coal-fired plants in North Carolina, plus the federal criminal violations of Duke. Additionally, the magnitude of costs for Dominion were a small fraction (12%) of those for Duke. (DEC T 22 pp 84-85)

What Duke sees as a "dramatic departure" by the Public Staff is just one case (Dominion's 2016 rate case). The Public Staff pointed out significant factual differences with that case, rather than recommend a departure from its prior reasoning. And the Commission recognized in its Dominion order that its decision on coal ash costs would not be precedential and each case would stand on its own facts and circumstances. The "dramatic departure"

argument does not relate to, much less rebut, the Public Staff arguments on legal error in the DEP and DEC rate case orders.

C. THE LAW DOES NOT REQUIRE A RETURN ON THE UNAMORTIZED BALANCE OF A REGULATORY ASSET

Duke argues that Thornburg I only affirmed the denial of a return on the unamortized nuclear cancellation costs because those costs were not "used and useful." The Company further argues that Thornburg II requires a return on expenditures for "property used and useful." (Appellee Brief pp 75-78)

As discussed earlier, this argument fails to support the Commission's rate case orders that are the subject of the present appeal because many of the coal ash costs were operating expenses rather than property used and useful. It also errs because rate adjustments may be made, where justified by "other material facts of record," under N.C. Gen. Stat. § 62-133(d) regardless of whether the underlying expenditures were operating expenses or property used and useful. (See Public Staff's initial brief, parts IV C 1 and 2) Additionally, Duke's interpretation of Thornburg I and Thornburg II is incorrect.

In Thornburg I the Attorney General argued that nuclear construction cancellation costs were neither "property used and useful" nor operating expenses, and that therefore no recovery was allowed under N.C. Gen. Stat. §

62-133(b). Thornburg I at 471, 385 S.E.2d at 455. In rejecting this argument, the Court upheld the Commission's "liberal interpretation" of "operating expense" to include the construction costs of nuclear units that would never be operational. Id. at 476, 385 S.E.2d at 458. For statutory support of this "liberal interpretation," the Court cited N.C. Gen. Stat. § 62-133(d). Id. Because past operating expenses normally cannot be recovered in rates without running afoul of the legal prohibition against retroactive ratemaking, the only way for CP&L to preserve its abandoned plant costs for rate recovery was through deferral to a regulatory asset.

If coal ash expenditures were made for "property used and useful," they could simply be added to rate base under N.C. Gen. Stat. § 62-133(b)(1) and (4), thereby allowing the costs to be recovered in rates through depreciation expense over the useful life of the property, with a fair rate of return. However, deferral to a regulatory asset is handled differently. This is underscored by the testimony of the Public Staff's lead accountant on this issue:

> The Company — and the reason I say it doesn't make any difference in this case, is the Company, itself, has chosen not to propose to include these type of costs, at least the ones that have been incurred so far, to my knowledge, as utility plant [in] service. They have said that these costs should be treated as regulatory assets, which puts them in another category entirely.

(DEP T 19 pp 66-67) (emphasis added) Deferral allows expenditures to be recovered at a later date rather than be written off to expense or as a loss – this is the very reason Duke petitioned for deferral of its coal ash costs. This is not a circumstance that would apply to the cost of "used and useful" utility plant, which can simply be added to rate base and recovered in rates in any future rate case. Deferred costs are amortized, and the amortization period is typically shorter than the life of physical assets (e.g., a ten-year amortization for abandoned nuclear plant in Thornburg I and twelve years for the Lee nuclear plant cancellation costs in the instant DEC rate case). In short, the regulatory act of deferring expenditures makes their recovery in rates more a function of N.C. Gen. Stat. § 62-133(d) than N.C. Gen. Stat. § 62-133(b).

Duke is correct in observing that the nuclear abandonment costs in Thornburg I did not qualify as "property used and useful" and therefore were not entitled to earn a return. But Duke is incorrect in stating that this means all "used and useful" costs must earn a return. Even if all the coal ash costs were for "property used and useful" – which is not the case – the deferral of those costs to a regulatory asset leaves the Commission with a discretionary decision on whether or not to allow a return. Nothing in Thornburg I says otherwise. Thornburg I only addressed costs that did not result in "used and

useful" property; the Commission and the Court had no reason to address regulatory assets that hypothetically might involve deferral to a regulatory asset of expenditures for "property used and useful."[8]

Ultimately, Thornburg I decided that costs deferred to a regulatory asset may be denied a return, and that this resulted in an "equitable sharing" that was lawful under N.C. Gen. Stat. § 62-133(d). The Public Staff's position in the present cases is consistent with that outcome: coal ash costs have been deferred to a regulatory asset and therefore may be amortized without a return in the Commission's discretion.

Duke also presents an incorrect interpretation of Thornburg II, arguing that "[t]his Court's decision in Thornburg II similarly does not permit the Commission to refuse to allow a fair rate of return on property that is used and useful." (Appellee Brief p 76) There was no appeal issue in Thornburg II regarding rate base treatment for "used and useful" plant. The Court summarily rejected an imprudence argument from the Attorney General, but

[8] Nor is it surprising that the hypothetical situation of a deferral for "property used and useful" has not come before the Court. As discussed above, investment in "property used and useful" is normally recorded as rate base and recovered in rates set in the next rate case. Those types of costs are not written off to expense or as a loss when incurred, so no deferral is needed.

that was not an issue of "used and useful." [9] The main issue, and basis for reversal of the Commission, was whether costs of excess plant, not used and useful for operation of Harris Unit 1, were properly included in rate base. The Court held:

> Since the excess common facilities are not "used and useful," they cannot be included in the rate base. N.C.G.S. § 62-133(b)(1). The Commission committed an error of law in including $ 389,442,000 in the rate base because this amount was part of the $ 570,000,000 used to construct the excess common facilities to serve abandoned Harris Units 2, 3, and 4.

Thornburg II at 495, 385 S.E.2d at 469.

Consequently, the Court ordered that all the excess common facilities costs must be subject to equitable sharing: "We remand this case to the Commission with instructions to remove the approximately $389,000,000 from the rate base and include it with the approximately $181,000,000 to be treated as cancellation costs." Id. at 498, 385 S.E.2d at 471. This holding flatly contradicts the Commission's conclusion that "[The Court] held that the Commission did not have the discretionary power to effectuate its 'equitable

[9] "The Attorney General contends that the Commission erred in concluding that CP&L's choice of a cluster design in 1971 was prudent. We find no error in this portion of the Commission's order." Thornburg II at 489, 385 S.E.2d at 466.

sharing' decision." (DEC R p 1106) What the Court held was that nuclear cancellation costs could be equitably shared, and that including them in rate base for a return was not equitable sharing.

D. THE COMMISSION DID NOT LAWFULLY EXERCISE DISCRETION WHEN ALLOWING A RETURN ON COAL ASH COSTS

Duke's last argument against the Public Staff's appeal is that the Commission properly exercised its discretion to allow a downward adjustment in Duke's cost recovery for coal ash, and that the decision not to allow a different (and larger) adjustment advocated by the Public Staff was supported by record evidence. Duke characterizes the Public Staff position as arguing abuse of discretion or as seeking an advisory opinion on the legality of "equitable sharing." (Appellee Brief pp 78-81)

There are several reasons why these arguments fail to justify the lawfulness of the Commission's decisions. First, having argued that the coal ash costs were legally entitled to a return as "property used and useful," Duke now takes the inconsistent position that an amortization with return, along with a mismanagement penalty, was a lawful exercise of Commission discretion. Either there is discretion to deny some level of cost recovery (which the Public Staff maintains is supported by N.C. Gen. Stat. § 62-133(d)), or there

is no such discretion. It is legal error for Duke – and the Commission's orders – to rely on mutually exclusive theories for authorization of a return on coal ash costs.

Second, the "downward adjustment" (denial of full cost recovery) that the Commission ordered as a "management penalty" of $30 million for DEP (DEP R p 685) and $70 million for DEC (DEC R p 1146) is not, contrary to Duke's argument, simply a different size adjustment from that recommended by the Public Staff. The management penalty was based on Duke's federal criminal violations of the Clean Water Act. "[H]aving pled guilty to management criminal negligence, DEP cannot go without sanction in the form of cost of service disallowances." (DEP R p 683: see also DEC R p 1145) All the costs associated with those violations had already been excluded by Duke from its rate request. ("[T]he Company has borne responsibility for Dan River remediation costs without ratepayer support." (DEP R p 683: see also DEC R p 1145)) In contrast, the Public Staff sought equitable sharing with respect to costs that were included in the rate requests, and based its rationale on state law violations and the nature and magnitude of the costs – not on the federal violations. Duke is in error when it argues that the management penalty is simply a difference in the size of "adjustment" against Duke. Rather, it serves

a completely different purpose from the Public Staff's equitable sharing recommendation. The Commission's "adjustment" for coal ash costs is a difference of kind, not simply degree.

Third, and most importantly, the Commission's purported exercise of discretion to award a return on coal ash costs is in error because (a) it contradicts other Commission determinations that would make a return mandatory rather than discretionary, and contradictory reasoning in a Commission order violates N.C. Gen. Stat. § 62-79 by leaving the Court without a clear basis for the Commission's decision (see part V A above); and (b) when making a discretionary decision, the Commission must still engage in weighing of all the competent, material evidence, which it failed to do when it rejected evidence of environmental violations on the grounds that the Commission was not an environmental regulator (see parts IV A and VII A 2 above).

CONCLUSION

The Public Staff respectfully requests that the Court reverse the Commission's Order with regard to the errors discussed in the Brief of Intervenor-Cross-Appellant Public Staff in these dockets, and remand the case

with instructions for the Commission to (a) disallow as unreasonable the extraction and treatment costs related to environmental violations at the Sutton and Belews Creek plants, as recommended by witnesses Lucas and Junis, and (b) review and decide whether evidence of Duke's coal ash-related environmental violations and other factors are "other material facts" that justify equitable sharing between ratepayers and investors for the coal ash costs not otherwise disallowed.

This the 12th day of November, 2019.

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N.C. R. App. p 33(b) Certification: I certify that all of the attorneys listed below have authorized me to list their names on this document as if they had personally signed it.

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CERTIFICATE OF SERVICE

I certify that I have served a copy of the foregoing Public Staff Reply Brief on all parties to the appeal by e-mail in accordance with Rule 26 of the North Carolina Rules of Appellate Procedure.

This the 12th day of November, 2019.

Electronically submitted
s/ David Drooz

CONTENTS OF APPENDIX

Rule R8-27. UNIFORM SYSTEM OF ACCOUNTS.

(a) For utilities with annual accounting and reporting periods based on the calendar year, effective January 1, 2002, and for utilities with fiscal year accounting and reporting periods, effective with fiscal years beginning in 2002, the Uniform System of Accounts Prescribed for Public Utilities and Licensees Subject to the Provisions of the Federal Power Act, as currently embodied in the United States Code of Federal Regulations, Title 18, Part 101, and as revised periodically, is hereby adopted by this Commission as its accounting rules for electric utilities and is prescribed for the use of all electric utilities under the jurisdiction of the North Carolina Utilities Commission, subject to the following exceptions and conditions unless otherwise ordered by the Commission:

(1) All orders and practices of the Commission in effect as of the effective date of this Rule with any accounting impacts that conflict with provisions of the Uniform System of Accounts shall remain in effect, and future such orders and practices with such impacts shall supersede the provisions of the Uniform System of Accounts for North Carolina retail jurisdictional purposes.

(2) The electric utilities under the jurisdiction of the Commission must apply to the Commission for any North Carolina retail jurisdictional use of the following accounts:

a. Account 182.1 - Extraordinary Property Losses.

b. Account 182.2 - Unrecovered Plant and Regulatory Study Costs.

c. Account 182.3 - Other Regulatory Assets.

d. Account 254 - Other Regulatory Liabilities.

e. Account 407 - Amortization of Property Losses, Unrecovered Plant and Regulatory Study Costs.

f. Account 407.3 - Regulatory Debits.

g. Account 407.4 - Regulatory Credits.

(b) Each electric utility subject to this Rule shall file the following with the Commission:

(1) In the case of utility filings and other correspondence with the FERC or its staff, on and after the effective date of this Rule, regarding the utility's accounting practices or the Uniform System of Accounts, including but not limited to requests for accounting guidance and or approval of accounting entries, the portion of the initial filing or correspondence by the utility relating to said accounting practices or the Uniform System of Accounts, and the final disposition of the matter.

(2) In the case of other changes in the utility's accounting practices prompted by FERC orders, directives, or correspondence, a written explanation of the change in practice, along with relevant supporting documentation.

(3) In the case of the regular periodic or any special compliance audits performed on and after the effective date of this Rule by the FERC or its staff, notification of the commencement of the audit and a copy of the final audit report.

(c) The accounting treatment to be used for contributions in aid of construction is as follows:

(1) Contributions in aid of construction received before the effective date of this Rule are to be accounted for in the manner prescribed by the Commission in Docket No. E-100, Sub 18.

(2) Contributions in aid of construction received on and after the effective date of this Rule are to be accounted for in the manner prescribed by the Uniform System of Accounts adopted herein.

(d) The following classification system is hereby adopted:

Class A: Electric utilities having annual electric operating revenues of $2,500,000 or more.

Class B: Electric utilities having annual electric operating revenues of $1,000,000 or more but less than $2,500,000.

Class C: Electric utilities having annual electric operating revenues of $150,000 or more but less than $1,000,000.

Class D: Electric utilities having annual electric operating revenues of $25,000 or more but less than $150,000.

(e) Electric utilities with annual gross operating revenues of less than $25,000 shall be exempt from the provisions of this Rule until the average of their annual gross revenues, for a period of three consecutive years, shall exceed $25,000. Electric utilities exceeding the $25,000 threshold but falling below the minimum threshold of 10,000 megawatthours of annual sales included in the FERC Uniform System of Accounts shall nevertheless utilize the FERC Uniform System of Accounts as specified for Nonmajor utilities.

(Source: Administrative Order issued in Docket E-100, February 22, 1960; NCUC Docket No. E-100, Sub 18, 5/24/74; NCUC Docket No. E-100, Sub 91, 9/6/01.)

I/A

Supplemental
Revised Lucas Exhibit No. 6

No. of 2L and IMAC Standards Exceedances At or Beyond the Compliance Boundary by Constituent

Parameters	Generating Station							Violations Subtotal	TBD Subtotal
	Asheville	Cape Fear	Lee	Mayo	Roxboro	Sutton	Weatherspoon		
Antimony	-	2	-	18	4	4	1	23	6
Arsenic	1	-	18	-	1	13	-	15	18
Barium	-	-	1	2	-	-	-	3	-
Beryllium	1	8	-	-	-	-	3	1	11
Boron	78	51	26	11	20	161	-	301	46
Cadmium	6	1	-	1	-	1	2	8	3
Chloride	11	-	-	-	4	15	-	30	-
Chromium	5	1	1	19	16	1	4	45	2
Chromium (VI)	1	-	-	7	-	-	-	8	-
Cobalt	60	8	15	12	19	68	5	182	5
Copper	-	-	-	-	-	-	-	-	-
Iron	148	21	32	16	10	55	8	290	-
Lead	-	-	-	2	1	1	-	3	1
Manganese	210	104	66	90	34	137	19	660	-
Nickel	-	1	-	-	-	-	3	1	3
pH	17	121	104	39	127	108	7	523	-
Selenium	9	15	4	-	8	27	-	36	27
Sulfate	40	64	-	-	54	3	2	163	-
Thallium	10	9	2	5	7	54	4	69	22
Total Dissolved Solids	67	34	-	37	76	39	2	255	-
Total Radium	9	-	7	6	4	1	6	26	7
Vanadium	51	7	32	17	49	35	23	214	-
Zinc	1	-	-	-	-	-	-	1	-
Violations Subtotal	725	411	250	282	394	723	72	2,857	
TBD Subtotal	-	36	58	-	40	-	17		151

Violations Subtotal + TBD Subtotal = 3,008

Notes:

*Highlighted fields are subject to change due to the provisional background threshold value not being estblashed by DEP.

*Data compiled from DEP responses to Public Staff Data Request 20-3, dated October 10, 2017.

*Per DEP, 2L Exceedance counts exclude results where turbidity of sample > 10 NTU.

I/A

Public Staff
Junis Exhibit No. 20
Page 1 of 1

No. of 2L and IMAC Standards Exceedances At or Beyond the Compliance Boundary by Constituent

		Generating Station							Violations	
	Parameters	Allen	Belews Creek	Buck	Cliffside	Dan River	Marshall	Riverbend	Subtotal	TBD Subtotal
IMAC	Antimony	6	45	1	7	13	4	19	95	-
	Arsenic	-	13	-	1	-	-	-	14	-
	Barium	-	5	-	-	-	11	-	16	-
IMAC	Beryllium	-	36	-	1	-	-	-	37	-
	Boron	-	104		-	21	69	-	194	-
	Cadmium	-	33	-	1	-	-	-	34	-
	Chloride	-	9	-	-	-	-	-	9	-
	Chromium	1	95	4	11	1	12	8	120	12
	Chromium (VI)	-	-	-	-	-	1	-	-	1
IMAC	Cobalt	1	132	2	24	6	30	25	220	-
	Copper	-	-	-	-	-	-	-	-	-
	Iron	2	367	20	61	49	36	31	517	49
	Lead	-	7	-	-	-	-	-	7	-
	Manganese	4	398	26	83	70	54	50	685	-
	Mercury	-	5	-	1	-	-	-	6	-
	Nickel	-	3	-	1	-	-	-	4	-
	pH	22	235	-	14	-	59	6	336	-
	Selenium	-	94	-	2	-	7	-	103	-
	Sulfate	5	77	5	46	-	25	-	158	-
IMAC	Thallium	1	50	-	3	2	2	-	58	-
	Total Dissolved Solids	3	95	3	47	-	30	-	178	-
Federal MCL	Total Radium	-	9	-	4	-	9	-	22	-
IMAC	Vanadium	8	114	12	55	42	21	26	278	-
	Zinc	-	-	-	-	-	-	-	-	-
	Violations Subtotal	53	1,926	73	362	155	357	165	3,091	
	TBD Subtotal	-	-	-	-	49	13	-		62

Violations Subtotal + TBD Subtotal = 3,153

Notes:

*Highlighted fields are subject to change due to the provisional background threshold value not being established by DEC and/or accepted NCDEQ.

*Data compiled from DEC supplemental responses to Public Staff Data Request 18A-1, dated December 8, 2017.

*Per DEC, 2L Exceedance counts exclude results where the sample results for turbidity > 10 NTU or pH > 8.5.

*Provisional Background Threshold Values reflect the values represented in the NCDEQ letters dated September 1, 2017 and October 11, 2017.