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September 20, 2006

**FILED**

**SEP 20 2006**

Clerk's Office  
N.C. Utilities Commission

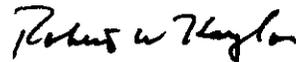
Ms. Renne C. Vance, Chief Clerk  
North Carolina Utilities Commission  
4325 Mail Service Center  
Raleigh, North Carolina 27699-4325

RE: Docket No. E-7, Sub 819

Dear Ms. Vance:

Enclosed for filing are the original and thirty (30) copies of Duke Energy Carolinas' Application for Authority to Recover Nuclear Generation Development Expenses in the above referenced docket.

Sincerely,



Robert W. Kaylor

Enclosures

cc: Robert P. Gruber  
Executive Director  
Public Staff

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BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. E-7, SUB 819

SEP 20 2006

Clerk's Office  
N.C. Utilities Commission

Application of Duke Power Company LLC d/b/a ) Application for Authority to  
Duke Energy Carolinas, LLC, for Authority to ) Recover Nuclear Generation  
Recover Necessary Nuclear Generation ) Development Expenses  
Development Expenses And Request for )  
Expedited Treatment )

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**INTRODUCTION**

Duke Power Company LLC d/b/a Duke Energy Carolinas, LLC (“Duke Energy Carolinas” or “Company”), pursuant to N.C. Gen. Stat. §62-2 and Rule R1-4 of the Rules and Regulations of the North Carolina Utilities Commission (“Commission”), files this Application for authority to recover the North Carolina allocable portion of necessary costs and obligations related to the development of the Company’s proposed William States Lee III Nuclear Station in Cherokee County, South Carolina (“Lee Nuclear Station”) and incurred through December 31, 2007.<sup>1</sup> The Company requests the relief specified in this Application because it is in the public interest to assure that all potential future resource options, including nuclear generation, are fully considered and the most economic resources are available on a timely basis. Additionally, the Company requests such relief because it will benefit customers if the Company can reduce the financial risk that will arise from the development of a new nuclear plant without assurance of cost recovery. Specifically, Duke Energy Carolinas requests that the Commission issue an order:

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<sup>1</sup> Such costs and obligations are generally referred to in this Application as “Development Costs”.

- (1) finding that work performed by Duke Energy Carolinas to ensure the availability of nuclear generation by 2016 for its customers is prudent and consistent with the promotion of adequate, reliable and economical utility service to the citizens of North Carolina and the policies expressed in N.C. Gen. Stat. § 62-2; and
- (2) providing expressly that Duke Energy Carolinas may recover in rates, in a timely fashion, the North Carolina allocable portion of Development Costs prudently incurred for work done in the development of new nuclear generation through December 31, 2007, whether or not a new nuclear facility is constructed.

Such prudently incurred costs are necessary and will be incurred regardless of whether a new nuclear facility is ultimately constructed or not. Further, they are used and useful for the determination of whether the Lee Nuclear Station is the least-cost option to meet future customer needs. A ruling by the Commission is required to ensure that the Company's actions, in keeping nuclear generation available as an option, are consistent with the policies expressed in N.C. Gen. Stat. § 62-2, and that the prudently incurred costs expended in this effort are recoverable in rates in a timely fashion.<sup>2</sup>

In support of this Application, Duke Energy Carolinas respectfully shows the Commission the following:

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<sup>2</sup> The Company will incur other necessary costs and obligations even after December 31, 2007, including licensing fees, costs of design completion, project planning costs, and the purchase of long lead time material and equipment, before construction of the Lee Nuclear Station can begin. Additionally, should the Lee Nuclear Station be determined to be the least-cost option to serve customer needs, the Company will incur construction costs. The Company will seek Commission approval for the timely recovery of the North Carolina allocable portion of all such prudently incurred costs at the appropriate times.

### **Name and Address of Duke Energy Carolinas**

1. The correct name and post office address of the Company are Duke Power Company LLC d/b/a Duke Energy Carolinas, LLC, Post Office Box 1006, Charlotte, North Carolina 28201-1006.

### **Notices and Communications**

2. The names and addresses of the attorneys of Duke Energy Carolinas who are authorized to receive notices and communications with respect to this application are:

Kodwo Ghartey-Tagoe  
Lead Regulatory Counsel  
Lawrence B. Somers  
Assistant General Counsel  
Duke Energy Corporation  
P.O. Box 1006/EC03T  
Charlotte, North Carolina 28201-1006

Robert W. Kaylor  
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Kevin C. Greene  
Brandon F. Marzo  
Troutman Sanders, LLP  
Bank of America Plaza, Suite 5200  
600 Peachtree Street  
Atlanta, GA 30308-2216

### **Description of the Company**

3. The Company is engaged in the generation, transmission, distribution, and sale of electric energy at retail in the central and western portions of North Carolina and the western portion of South Carolina. It also sells electricity at wholesale to many

municipal, cooperative and investor-owned electric utilities. Duke Energy Carolinas is a public utility under the laws of North Carolina and is subject to the jurisdiction of this Commission with respect to its operations in this State. The Company also is authorized to transact business in the State of South Carolina and is a public utility under the laws of that State. Accordingly, its operations in that State are subject to the jurisdiction of the Public Service Commission of South Carolina (“PSCSC”).

### **BACKGROUND**

4. The Commission is well aware that after the Three Mile Island incident in 1979, the US Nuclear Regulatory Commission (“NRC”) appropriately issued significant changes in its regulations as they relate to nuclear power plant safety. Implementation of these new standards in plants already under construction (back fit) resulted in significant schedule delays as well as increases in both direct and financing costs. At this same point in time, escalating oil prices adversely impacted economic growth and led to a reduction in the projected demand for electricity. This resulted in the cancellation of approximately 60 new nuclear generation units that were in various stages of development or construction in the United States. These cancellations led to billions of dollars of utility write-offs, regardless of the prudence of those incurred development costs. Since 1979, no applications for the construction of new nuclear plants have been filed in the United States, partially due to the potential that similar events outside the control of the electric supplier could cause prudently incurred costs not to be recovered.

5. Recently, there has been renewed interest in new nuclear generation in the United States. This renewed interest is attributable to several factors, including (a) a need for new base load generation capacity over the next decade in many areas of the country,

most notably in the Southeast; (b) recognition, both internationally and domestically, in the environmental benefits of nuclear generation as the focus on air emissions heightens, particularly as climate change regulation receives greater consideration; (c) the need for American business and industry, for whom the price of electricity can be a significant component of overall operating costs, to remain competitive in global markets as other countries maintain or even increase their reliance on nuclear generation; (d) rising and often volatile prices associated with the fuels used in fossil generation assets, particularly natural gas but also coal; and (e) increasing concerns about our nation's energy security and energy independence. Because of these factors, the Energy Policy Act of 2005 ("EPAAct") contains various provisions that encourage the development of new nuclear generation.

6. At the same time that these exogenous economic factors have begun to prevail, nuclear generation technology, design, and safety have improved markedly. Perhaps reflecting these developments, the NRC has made improvements to the licensing process for new nuclear plants. Such improvements are intended to remove uncertainty and to enhance the efficiency of the licensing process.

7. Duke Energy Carolinas is a leader in the nuclear generation industry and currently operates seven units at its three nuclear stations (5,020 MW owned, 6,996 MW operated) as part of its diverse generation fleet. The Company's need for new base load generation resources over the next decade, combined with the need for greater fuel diversity, make evaluating new nuclear generation an essential part of future resource planning.

8. Nuclear generation facilities have a very long lead time and require the expenditure of significant dollars during the preliminary siting, design and licensing phases. Duke Energy Carolinas expects to spend as much as \$125 million in Development Costs even before a CPCN is granted. But this work must be done and these funds must be expended in the near future if Duke Energy Carolinas is to ensure that its customers will have nuclear generation available as a resource option by 2016.

**THE COMPANY'S MOST RECENT ANNUAL PLAN IDENTIFIES NEW  
NUCLEAR GENERATION AS A LEAST COST RESOURCE**

9. On September 1, 2006, Duke Energy Carolinas filed its most recent Annual Plan ("Annual Plan"). As the Commission is well aware from the recent public and evidentiary hearings in the 2005 Integrated Resource Planning ("IRP") investigation, Docket No. E-100, Sub 103, the IRP process provides a forum for the Commission, the Public Staff, and interested parties to evaluate the Company's Annual Plan. Consistent with the Company's 2005 Annual Plan recently approved by the Commission in Docket No. E-100, Sub 103, the 2006 Annual Plan identifies the need for significant capacity additions to meet a 17 percent planning reserve margin, including the cumulative need for nearly 4,200 MW of additional capacity by summer 2016. The resource planning analysis has confirmed that base load capacity additions will be required to meet customer needs beginning in 2011 and again in approximately 2016. Duke Energy Carolinas' last coal and nuclear base load plants came on line in 1975 (Belews Creek Steam Station) and 1986 (Catawba Nuclear Station), respectively. Portfolio additions of over 1,700 MW of base load nuclear capacity, 1600 MW of base load coal capacity, 2,207 MW of combustion turbine/combined cycle generation, and the 825 MW Rockingham Power combustion turbine facility, were identified as the least-cost options

to cost-effectively meet customers' generation needs and allow Duke Energy Carolinas to maintain the flexibility needed to ensure system reliability. The 2006 Annual Plan also includes an additional 201 MWs of new demand side management programs ("DSM"), which constitutes 100 MW of additional demand response program capability and 101 MW of additional energy efficiency program capability. The Company will continue to refine and enhance the impact of demand reduction and energy conservation programs in its portfolio as part of the Company's ongoing collaborative efforts with interested stakeholders.

10. Included in the Annual Plan is the Company's near-term action plan, which expressly outlines several steps being taken to ensure that Duke Energy Carolinas customers have the most economic and reliable resource options available. Specifically, the Company informed the Commission that it would be taking the following actions:

- Continue to evaluate new nuclear generation by pursuing the NRC's COL, with the objective of potentially bringing a new plant on line by 2016;
- Actively pursue new coal generation, with the objective of bringing additional capacity on line by 2011 at the existing Cliffside Steam Station;
- Maintain the option to license and permit a new combined-cycle/peaking facility;
- Establish collaborative partnerships to further define, develop, and promote potential demand response and energy efficiency products and services;
- Continue to assess opportunities to benefit from economies of scale in new resource decisions by considering the prospects for joint ownership and/or sales agreements;
- Continue to monitor renewable generation options;
- Continue to monitor energy-related statutory and regulatory activities.

11. Duke Energy Carolinas continues to proceed with the objectives described in its near-term action plan. This includes Duke Energy Carolinas' participation in the

hearings and workshops on DSM programs being conducted in Docket No. E-100, Sub 103, and additional collaborative efforts organized by the Company to develop and implement Duke Energy Carolinas' new DSM approach. In addition, the Company has entered into an agreement to acquire the existing Rockingham County 825 MW combustion turbine peaking facility from Rockingham Power, LLC. On July 25, 2006, the Commission approved the joint request of Rockingham Power, LLC and Duke Energy Carolinas to transfer the facility's Certificate of Public Convenience Necessity ("CPCN") to Duke Energy Carolinas in Docket No. E-7, Sub 816 and EMP-1, Sub 1. The Company has filed its CPCN application for the two 800 MW supercritical pulverized coal additions to its Cliffside Steam Station in Docket No. E-100, Sub 790, and the evidentiary hearing is scheduled to begin September 12, 2006.

12. Duke Energy Carolinas has taken the first steps towards evaluating the possibility of bringing new nuclear generation on line by 2016, also as identified in the recent Annual Plan. But even the preliminary work to evaluate the merits of building the Lee Nuclear Station involves significant costs. Yet, such work is necessary and, indeed, is used in and useful to the process of determining whether new nuclear generation will be available to meet future customer needs. Accordingly, the costs being incurred in connection with such work will be prudently incurred to ensure the availability of facilities necessary to meet future growth.

13. Ultimately, the construction of the Lee Nuclear Station will require the expenditure of significant capital. While not on the same scale, the evaluation and development of the Lee Nuclear Station also requires large sums of money. As noted above, the Development Costs through December 31, 2007 are anticipated to be as much

as \$125 million. The Company is concerned about spending such large sums of money without the assurance of adequate and timely cost recovery.

14. Such cost assurance is appropriate and in the public interest. Duke Energy Carolinas' Annual Plan contemplates large capital investments for base load facilities over an extended period of time to meet future customer service requirements. Future annual capital requirements, along with the related financing costs, are projected to be significantly higher than annual capital expenditures and financing costs typically undertaken by the Company over the past twenty years. The added certainty of Development Cost recovery assurance is likely to strengthen the Company's credit position, as the financial market is more confident in the Company's ability to service the incremental debt and pay dividends to shareholders. This ultimately should result in more financing flexibility and a lower cost of debt than the Company would otherwise experience, thereby benefiting customers through a lower cost of service.

#### **NORTH CAROLINA PUBLIC POLICY**

15. N.C. Gen. Stat. §62-2 declares the public policy of the State of North Carolina regarding the rates, services and operations of public utilities. N.C. Gen. Stat. §62-2(4a) specifically provides as follows,

To assure that facilities necessary to meet future growth can be financed by the utilities operating in this State on terms which are reasonable and fair to both the customers and existing investors of such utilities; and to that end to authorize fixing of rates in such a manner as to result in lower costs over the operating lives of such new facilities by making provisions in the rate-making process for the investment of public utilities in plants under construction.

Thus, the General Assembly has explicitly recognized the importance to the State of utilities' ability to finance generation facilities and the need for provisions to facilitate

utility investment in plants under construction. Part of the process of providing adequate, reliable and economical utility service is ensuring that the most economical supply-side and demand-side options are available when needed by the citizens of North Carolina. Through the annual planning process discussed above, Duke Energy Carolinas has identified nuclear generation as a least cost supply-side alternative to meet North Carolina customers' needs in the 2016 timeframe. The evaluation of nuclear expansion and the incurrence of Development Costs to enable construction is consistent with the policies espoused in N.C. Gen. Stat. § 62-2.

**RECOVERY OF ONGOING, PRUDENTLY INCURRED DEVELOPMENT  
COSTS SHOULD BE AUTHORIZED WHETHER OR NOT A NEW  
NUCLEAR FACILITY IS COMPLETED**

16. Following completion of the environmental investigation of construction and operation of two nuclear generating units in Cherokee County, South Carolina, Duke Energy Carolinas plans to apply to the PSCSC for a CPCN<sup>3</sup>. The South Carolina CPCN process does not provide an absolute assurance of cost recovery in either North Carolina or South Carolina. It also does not adequately account for the cost that is being incurred by Duke Energy Carolinas to evaluate and maintain nuclear generation as an option. If conditions beyond the Company's control result in a new determination that nuclear generation is no longer in the best interest of our customers, then the efforts to preserve the nuclear generation option will still have value to customers in so far as it helps identify the least-cost option. The work being undertaken is reasonably calculated to ensure that the least-cost portfolio, as shown in the Company's 2006 Annual Plan, is

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<sup>3</sup> Under South Carolina law, the CPCN is a "Certificate of Environmental Compatibility and Public Convenience and Necessity."

available to meet customer's needs. This cost is prudently incurred for the benefit of Duke Energy Carolinas' customers and should be recoverable in rates.

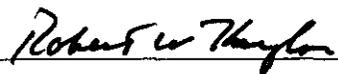
17. Additionally, once a CPCN is granted by the PSCSC, Duke Energy Carolinas still does not have the certainty of recovery that is necessary to pursue a capital intensive project like the development of new nuclear generation.

#### **REQUEST FOR EXPEDITED TREATMENT**

18. To avoid uncertainty and delay, Duke Energy Carolinas respectfully requests that the Commission review and approve this Application in an expeditious manner without the need for a hearing. While the Company submits that the Commission can and should grant the relief as requested in this Application, should the Commission determine that it does not have the statutory authority to grant the relief requested, it is Duke Energy Carolinas' intent to work with the Commission to seek a legislative remedy from the General Assembly. Accordingly, expedited consideration by the Commission would enable the Company to timely take the necessary steps to ensure the viability of the Lee Nuclear Station option.

WHEREFORE, Duke Energy Carolinas respectfully requests that the Commission approve the Company's Application and issue an order that work done to preserve the nuclear option for Duke Energy Carolinas customers is prudent and consistent with N.C. Gen. Stat. §62-2, and that the prudently incurred Development Costs are recoverable in rates.

Respectfully submitted this 20<sup>th</sup> day of September, 2006.



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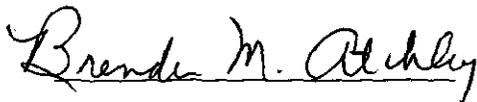
VERIFICATION

STATE OF NORTH CAROLINA       )  
COUNTY OF MECKLENBURG       )

ELLEN T. RUFF, being first duly sworn, deposes and says: That she is President of DUKE POWER COMPANY LLC d/b/a DUKE ENERGY CAROLINAS, LLC, applicant in the above-entitled Application; that she has read the foregoing Application and knows the contents thereof, and that the same is true of her own knowledge.

  
\_\_\_\_\_  
Ellen T. Ruff

Sworn to and subscribed before me  
this 18<sup>th</sup> day of September, 2006.



Notary Public

MY COMMISSION EXPIRES 12-4-09