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VIA ELECTRONIC FILING

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

RE: Duke Energy Carolinas, LLC's and Duke Energy Progress, LLC's Response to Public Staff Late-Filed Exhibit No. 1 (Culpability)
Docket No. E-7, Sub 1214
Docket No. E-2, Sub 1219

Dear Ms. Campbell:

On behalf of Duke Energy Carolinas, LLC and Duke Energy Project, LLC (collectively, the "Companies"), please find enclosed for electronic filing the Companies' *Response to Public Staff Late-Filed Exhibit 1 (Culpability).*

Please do not hesitate to contact me should have you have any questions. Thank you for your assistance in this matter.

Sincerely,

/s/ Kiran H. Mehta

Kiran H. Mehta

Enclosure

cc: Parties of Record

DEC Late-Filed Exhibit No. 14	DEP Late-Filed Exhibit No. 14
Duke Energy Carolinas, LLC	Duke Energy Progress, LLC
Docket No. E-7, Sub 1214	Docket No. E-2, Sub 1219

Request: DEC and DEP response to Public Staff Late-Filed Exhibit No. 1 (culpability)

Background

Duke Energy Carolinas, LLC (DEC) seeks in its rate case a total of $378 million in coal ash basin closure costs, consisting of (a) actual costs of closure activities performed during the period from January 1, 2018 through January 31, 2020, all of which have been deferred by order of the Commission, and (b) financing costs incurred during the deferral period through July 2020. Duke Energy Progress, LLC (DEP[1]) seeks in its rate case a total of $440 million in coal ash basin closure costs, consisting of (a) actual costs of closure activities performed during the period from September 1, 2017 through February 29, 2020, all of which have been deferred by order of the Commission, and (b) financing costs incurred during the deferral period through August 2020.[2]

The Companies' closure activities, for which the costs were incurred, are required in order to comply with changes in the law – specifically, in connection with changes in the manner in which the Companies must now manage coal ash, and close and remediate their coal ash basins. The changes in law came about as a result of the promulgation of the Federal CCR Rule in 2015, as well as the passage by the North Carolina General Assembly of the Coal Ash Management Act (CAMA) in 2014 and amendments to CAMA in 2016.

[1] Each of DEC or DEP may also be referred to herein as a "Company" and together as the "Companies".
[2] All costs are on a North Carolina retail basis. The Public Staff concedes that recovery by the Companies of financing costs at their weighted average cost of capital during the deferral period is appropriate. (DEC Tr. vol. 20, p. 494, lines 18-21; DEP Tr. Vol. 15, p. 1557, lines 18-22).

The Public Staff advocates "imprudence" disallowances of a portion of these costs through the testimony of witnesses Garrett and Moore, as well as further discrete allowances through the testimony of witness Junis (in the DEC Docket) and Lucas (in the DEP Docket). Those disallowances are unfounded and without any merit. However, they are not the focus of Public Staff Late-Filed Exhibit No. 1 (PS LFE No. 1).

Rather, PS LFE No. 1 relates to the balance of the Companies' coal ash basin closure costs, with "imprudence" and other discrete disallowances netted out. Net of taxes, the Public Staff advocates that 50% of that balance be disallowed – a disallowance of approximately $100 million in the case of DEC, and approximately $112 million in the case of DEP. The Public Staff creates these punitive disallowances by dribbling the cost recovery out over a quarter-century, without any return on the unamortized balance, despite the fact that 100% of the costs have been fronted by the Companies' debt and equity investors. This lengthy amortization period without any return produces what witness Sean Riley refers to as an "implicit" disallowance. (DEC Tr. vol. 24, p. 37, lines 2-4 (implicit disallowance when Company is not awarded a return on expended amounts)).

These $100 million (DEC) and $112 million (DEP) disallowances are expressly ***not*** predicated on any alleged imprudence by the Company.[3] Instead, the Public Staff premises its argument on a theory created out of whole cloth approximately three years

[3] Witness Junis acknowledged in his pre-filed testimony that the disallowance was not based upon the prudence framework. (See, e.g., (DEC Tr. vol. 20, p. 9, lines 9-10) ("I do not believe the traditional imprudence approach is feasible for most of DEC's coal ash costs."); p. 13, lines 3-5 ("equitable sharing" recommendation is not based on the "imprudence standard"); p. 65, lines 2-7 (Public Staff views "culpability" differently from "prudence" and "did not conduct a prudence review" of the construction and operation of the ash basins due the impossibility of doing so). Witness Lucas's pre-filed testimony is a carbon copy. (See, e.g., (DEP Tr. vol. 15, p. 1444, lines 14-15); p. 1449, lines 5-7; p. 1506, lines 9-13.

ago[4] expressly for the purpose of disallowing a portion of coal ash basin closure costs – a theory the Public Staff calls "equitable sharing," based supposedly on the Company's "culpability" for these costs.[5]

Accordingly, the Public Staff's theory is premised upon taking expenditures made by the Companies, *none* of which have been found by the Public Staff to be imprudently incurred, *none* of which are in the Companies' current rates, *all* of which have been incurred in order to comply with changes in law that came about in 2014 or later, and *all* of which are financed by the Companies' debt and equity investors – and disallowing half of those expenditures based upon the Companies' alleged "culpability" for undefined action(s) that allegedly occurred at some undefined point(s) of time in the past.

The Commission emphatically rejected the Public Staff's theory in the Companies' prior rate cases. In its DEC Order issued June 22, 2018,[6] which also referenced the February 23, 2018 DEP,[7] the Commission held:

> First, the concept is standard-less, and, therefore, from the Commission's view arbitrary for purposes of disallowing identifiable costs – there is no rationale that supports a substantially large 51% disallowance. The Public Staff chose a desirable equitable sharing ratio, then backed into the mechanism to achieve that level of disallowance, leaving the allocation subject to an arbitrary and capricious attack, particularly as it provides no explanation as to why the "equitable" split for DEP in the 2018 DEP Case was in its view 50-50, while the "equitable" split in this case is 51-49. As the

[4] The Public Staff formally introduced its "equitable sharing" concept in its testimony filed in DEP's prior rate case, Docket No. E-2, Sub 1142. That testimony was filed on October 20, 2017.

[5] The last sentence of PS LFE No. 1 goes so far as to assert that "even in the absence of culpability, some level of sharing of CCR costs would be appropriate and reasonable in this proceeding." PS LFE No. 1, at p. 3. The Public Staff therefore has taken the position that even the absence of "imprudence" *and* the absence of "culpability" are not enough to allow the Companies to recover fully its coal ash basin closure costs. This position has no legal basis whatsoever.

[6] Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, Docket No. E-7, Sub 1146 (the "2018 DEC Rate Order").

[7] Order Accepting Stipulation, Deciding Contested Issues and Granting Partial Rate Increase, Docket No. E-2, Sub 1142 (Feb. 23, 2018) (the "2018 DEP Rate Order").

> Commission held in the 2018 DEP Case, the "Public Staff provides insufficient justification for the 50/50 [split] as opposed to 60/40 or 80/20 ...." 2018 DEP Rate Order, p. 189.

2018 DEC Rate Order at 273.

It is against this backdrop that Commissioner McKissick sought, during his examination of the Junis-Maness panel in the DEC Docket, to "understand … what the standards would be for culpability." (DEC Tr. vol. 22, p. 39, lines 7-8.) Noting that the Commission "know[s] what the standards are for imprudence" and that the Commission "understand[s] why in this case there would not be grounds for finding imprudence" (id., lines 8-10), Commissioner McKissick indicated that what he was looking for "in terms of culpability … [was] what could be articulated as a standard that applies not simply to the facts of this case, but to other cases that the Commission might consider if they're going down the path of equitable sharing." (Id., lines 11-15.) He elaborated further:

> So, I mean, I understand what it looks like here in terms of what you're arguing, but when you start using a term like "culpability," which is broad and rather expansive, I'd like to know that it's more than just a subjective feeling that could be arbitrary based upon the way you see and feel it.
>
> So help me try to put my arms around what that term – what are the standards, A, B, C, and D? I mean, we know what they are for imprudence; we've got A, B, C, and D. What are they for culpability?

(Id. at 41, lines 6-15.)

Although the Public Staff has for the past three years (at least) used the "culpability" theory as its basis for disallowing hundreds of millions of dollars of coal ash costs that the Public Staff admits may not be disallowed for imprudence, neither witness Junis nor witness Maness was able to articulate from the witness stand a "standard" for culpability. At that point witness Junis offered to provide a late-filed exhibit to explain the

concept "more succinctly." (Id. at 43, line 23; 44, line 3.) Commissioner McKissick accepted the offer and requested a late-filed exhibit that might provide "as much clarity and specificity as possible … [so as to establish] a bright line [test] not just for the facts of this case." (Id. at 44, lines 20-23.)[8]

Discussion

Commissioner McKissick asked the Public Staff to articulate criteria by which the Commission could *objectively*, not *subjectively*, judge a utility's conduct, and, on the basis of that objective review, determine whether the utility's conduct merited a finding that some costs sought to be recovered should instead be disallowed. PS LFE No. 1 utterly fails to achieve its supposed purpose. The Public Staff expressly states that "culpability" is "not amenable to a bright-line test." (PS LFE No. 1, p. 1). The exhibit does not articulate *any* rules, much less rules that can be objectively and generally applied to conduct beyond the facts and circumstances of this case. Rather, PS LFE No. 1 conclusively proves that the Commission's insight and holding from the 2018 DEC and 2018 DEP Rate Orders was exactly correct – "culpability" and "equitable sharing" are standard-less concepts without any consistent and objectively understandable rationale. To the contrary, they are merely expressions of the Public Staff's "judgment" as to how and in what ratio coal ash costs should be shared between the Company and its customers – an arbitrary judgment of the Public Staff alone.[9] Were the Commission to agree and adopt that

[8] In the DEP-specific hearing, the Public Staff requested and Presiding Commissioner Clodfelter permitted the filing of PS LFE No. 1 in the DEP Docket, and permitted DEP to file a response. (DEP Tr. Vol. 16, p. 17, line 12-p. 18, line 21).

[9] Witness Maness' own testimony evidences the arbitrariness of the Public Staff's "standard." First, in his initial testimony he recommended a 26-year amortization period that produced a customer sharing ratio of 50.4%, which the Public Staff considered "sufficiently close" to 50%. (DEC Tr. vol. 20, p. 544-45.) Then, in his second supplemental testimony, he changed his recommendation to a 27-year amortization period that results in a customer sharing ratio of 49.7%, which the Public Staff considers "closer to 50% than [the alternative]." (Id.) And, of course, in the 2020 Dominion case, the Public Staff's ratio is 60/40.

judgment, it would be acting no less arbitrarily. And for an administrative and adjudicatory body to act arbitrarily is, of course, contrary to law.

North Carolina law regarding cost recovery is clear. First, the operating principle underlying rate regulation is that the utility's reasonable and prudently incurred costs are recoverable in rates. Second, under the evidentiary presumptions governing cost recovery the entirety of the utility's costs is deemed to be reasonable and prudent, unless challenged by an intervenor. Third, if costs are challenged, the challenge must be directed to their reasonableness and prudence – there is simply no other basis in law upon which a challenge may be mounted. The Commission is, after all, an economic regulator – it is not the Companies' environmental regulator, nor is it a court of general jurisdiction. It is body constituted by the General Assembly, which delegated to it the General Assembly's power to regulate public utilities and their rates. That delegation of power is not unbridled, however. Rather, it is governed and constrained by the Public Utilities Act, as well as decisions of the courts and the of Commission itself. Under this framework, the standards for cost disallowance are embedded in the 100-year old prudence doctrine – costs prudently incurred are recoverable; costs imprudently incurred are not recoverable.

In North Carolina, for at least the last 30+ years, the prudence framework has been applied as articulated by this Commission in its Order entered in Docket No. E-2, Sub 537 (the 1988 DEP Rate Case), in which the Commission approved, with some exceptions, costs Duke Energy Progress incurred in connection with the construction of Unit 1 of the Shearon Harris nuclear plant. See Order Granting Partial Increase in Rates and Charges,

Docket No. E-2, Sub 537 (Aug. 5, 1988) (the "1988 DEP Rate Order"). There, the Commission set out the following principles governing the question of prudence:

First, the standard for judging prudence is "whether management decisions were made in a reasonable manner and at an appropriate time on the basis of what was reasonably known or reasonably should have been known at that time. … [T]his standard … must be based on a contemporaneous view of the action or decision under question. Perfection is not required. Hindsight analysis – the judging of events based on subsequent developments — is not permitted." 1988 DEP Rate Order at 14.

Second, challenging prudence requires a detailed and fact intensive analysis, and the challenger is required to (1) identify specific and discrete instances of imprudence; (2) demonstrate the existence of prudent alternatives; and (3) quantify the effects by calculating imprudently incurred costs. Specifically,

- A decision cannot be imprudent if it represents the only feasible way to accomplish a necessary goal.
- The Commission can only disallow imprudent ***expenditures*** – that is, actions (even if imprudent) with no economic impact upon customers are of no consequence. Thus, identification of an imprudent action or inaction is not by itself sufficient; rather, there must be a demonstration of the economic impact.
- The proper amount chargeable to customers is what the expenditure would have been absent the imprudent acts or decisions of management – in other words, the disallowance must be calculated as the difference between the (presumably) higher cost imprudent action and the (presumably) lower cost prudent action.

Id. at 15. The prudence framework was most recently re-articulated and followed in the Commission's February 24, 2020 Order in Docket No. E-22, Sub 562 ("2020 Dominion Rate Order"), at 116.

Further, an integral part of the prudence framework is an examination of the degree to which the utility has or has not acted consistent with industry standards; if it has, then it may not fairly be deemed imprudent. In its prior rate case, after full trial on the merits, the Commission found that the Company ***had*** acted consistent with industry standards:

> Coal-fired power plants have played a predominant role in electricity generation by DEC throughout its history, and the Company is dependent upon coal-fired generation today. With coal-fired generation comes a by-product – coal ash, also known as coal combustion residuals, or CCRs. At least since the 1950s, standard industry practice, particularly in the Southeastern United States, has been reliance on coal ash basins. Such basins were constructed and used at all of the Company's coal-fired generating units.

2018 DEC Rate Order at 208.

The standard-less concept of "culpability" may not be used to undercut the proper application of the prudence framework so as to disallow costs that have not been shown to have been imprudently incurred. That is what the Public Staff wants, but to get there, it simply makes up an entirely new "standard" that is inherently, and by the Public Staff's own admission, arbitrary.

CERTIFICATE OF SERVICE

DOCKET NO. E-7, SUB 1214
DOCKET NO. E-2, SUB 1219

I hereby certify that a copy of the foregoing **DUKE ENERGY CAROLINAS, LLC'S AND DUKE ENERGY PROGRESS, LLC'S RESPONSE TO PUBLIC STAFF LATE-FILED EXHIBIT 1 (CULPABILITY)** was served electronically or by depositing a copy in United States Mail, first class postage prepaid, properly addressed to the parties of record.

This the 20th day of October 2020.

/s/ Kiran H. Mehta
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