STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. E-2 SUB 1258
DOCKET NO. E-7 SUB 1241

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of Joint Petition of Duke Energy Carolinas, LLC, and Duke Energy Progress, LLC, for Approval of Accounting Order to Defer Incremental Expenses as a Result of COVID-19	)))))	ORDER APPROVING DEFERRAL REQUEST

BY THE COMMISSION: On August 7, 2020, Duke Energy Carolinas, LLC (DEC), and Duke Energy Progress, LLC (DEP; collectively, the Companies), filed a joint petition in the above-captioned docket requesting that the Commission allow DEC and DEP to establish a regulatory asset to account for incremental costs resulting from the COVID-19 pandemic (COVID or pandemic), pending further action by the Commission in the Companies' next general rate cases.

Petitions to intervene were granted for Carolina Industrial Group for Fair Utility Rates II and III (CIGFUR) and Vote Solar on August 20 and 24, 2020.

On September 8, 2020, the Commission issued an Order Joining Parties and Requesting Comments directing that all parties to DEC's and DEP's pending rate cases in Docket Nos. E-7, Sub 1214 and E-2, Sub 1219 be made parties to this proceeding without the necessity of filing a petition to intervene; allowing parties to file initial and reply comments; and posing five questions to the parties related to the application of the Commission's usual deferral test, incorporation of COVID-related costs into the then-pending rate cases, and what return, if any, should be allowed if the costs were deferred.

Initial comments were filed by Carolina Utility Customers Association, Inc. (CUCA), Center for Biological Diversity and Appalachian Voices (CBD/AV), the North Carolina Attorney General's Office (AGO), and the Public Staff. Reply comments were filed by the Companies, CIGFUR, and the AGO.

On August 6, 2021, the Companies filed an updated summary of incremental COVID-related costs as of June 30, 2021.

On November 15, 2021, the Public Staff filed supplemental comments regarding the Companies' incremental cost filing.

SUMMARY OF PETITION

The Companies state in their petition that the pandemic is continuing to significantly impact economic activity throughout the state and country, resulting in unforeseeable reductions in demand for electricity, reducing and continuing to reduce revenue for the Companies, and increasing their unrecovered incremental costs. The Companies state that they have undertaken and are continuing to undertake extraordinary actions to maintain vital utility service and are incurring extra costs that are not being recovered in their current rates. Further, the Companies detailed Governor Cooper's actions in declaring the State of Emergency and the Commission's orders issued in response to the pandemic.

The Companies state that they have had to implement changes to their business operations due to COVID in response to North Carolina's State of Emergency orders and federal guidelines. Among other things, the Companies state that they have been and will continue to provide employees with appropriate personal protective equipment (PPE) so that safe work practices are maintained and vital infrastructure work can continue. Further, Information technology modifications have been required to implement remote work practices designed to facilitate continued operations and to mitigate the risk of COVID spread. The Companies state that they have incurred and will continue to incur materially negative financial impacts from the measures required to cope with COVID over and above the revenue impact from reduced sales. In addition, the Companies state that although they have been adversely impacted by reduced revenues due to loss of demand, they seek deferral authority for only their increased costs, and not for the lost revenues caused by reduced demand. Specifically, the Companies request deferral of: (1) customer fees waived, (2) bad debt charge-offs, (3) employee stipends to cover unplanned expenses associated with COVID, (4) costs related to employee safety, (5) costs related to remote working, and (6) miscellaneous costs, such as employee overtime.

The Companies state that it is unknown how long the COVID impacts will last beyond 2020. They included separate tables for DEC and DEP showing by category the actual costs incurred through June 30, 2020, and the projected costs through December 2020.[1] DEC estimated that its total costs through December 2020 would be $25,630,000, and DEP estimated that its total costs through December 2020 would be $20,146,000. The Companies contend that because this is not a request for a deferral made out-of-period or between rate cases, and because the requested deferrals would benefit customers, not the Companies, the Commission's test required to justify out-of-period deferrals does not apply. In addition, the Companies state that their request is consistent with the case law and policy of the State for allowing unique regulatory treatment of extraordinary costs. Moreover, the Companies state that absent Commission approval of the requested deferrals DEC and DEP will face significant earnings degradation. In conclusion, DEC and DEP request that the Commission: (1) allow the Companies to

[1] The Companies updated their incremental COVID-related costs through June 30, 2021, in their filing made on August 6, 2021. DEC indicate that its incremental COVID-related costs through June 30, 2021, including return on deferred costs, were $53,177,000; DEP's incremental costs were $33,004,000.

establish a regulatory asset for deferral of their incremental pandemic costs from March 1, 2020, plus carrying costs at each Company's approved overall cost of capital, until the Commission addresses the deferrals for ultimate disposition in each Company's next rate case; (2) authorize the Companies to track and adjust the regulatory asset from March 2020 until the Commission addresses the deferred costs for ultimate disposition in the Companies' next general rate cases; and (3) take notice of the filings and evidence in the Companies' then-pending general rate cases.

SUMMARY OF COMMENTS

Initial Comments

In its comments CUCA expresses concerns that a deferral of COVID-related costs would further burden already burdened customers. CUCA states that no one was immune to the impacts of the pandemic and that other companies were also continuing to be in crisis due to the pandemic. CUCA argues that it was insensitive of the Companies to attempt to recover costs from already suffering customers.

CUCA opines that if the Companies' deferral request is granted by the Commission no return on deferred costs should be allowed. According to CUCA, the pandemic has affected everyone, and the Companies should share in the burden. Further, CUCA notes its concern that cross-subsidization would occur if the Commission allowed the deferrals. CUCA states that it believes that the allocation of the costs in future rate cases should be based on the customer classes which caused the expenses. Additionally, CUCA expresses concern that the Companies' application did not contain data related to cost-saving measures implemented by the Companies. CUCA further states that the Companies should be required to provide a comprehensive list of such cost-cutting measures, and that should a deferral be allowed it should be no more than the net difference between the pandemic-related costs incurred and the cost savings achieved by the Companies.

In their comments CBD/AV oppose the Companies' deferral request, stating that it would inappropriately shift costs to North Carolina ratepayers. CBD/AV state that the Commission should expand the deferral test to include other factors. CBD/AV state that the Companies' deferral request should be denied based on four grounds: (1) the impacts of the pandemic have been felt economy-wide, and the Companies should not be immune; (2) North Carolina ratepayers should not be penalized for the pandemic; (3) the Companies should absorb the requested cost recovery in light of its strong financial assets reflected in increasing shareholder dividends throughout the pandemic, company income, and executive compensation; and (4) the Companies' request fails the deferral test.

CBD/AV state that should the Commission grant a deferral, CBD/AV opposes including a return on the deferred costs and supports a reduction of the deferral amount to reflect the Companies' cost savings. Finally, CBD/AV encourage the Commission to initiate a rulemaking to set standards for future emergency situations that will protect ratepayers and serve the public interest.

In its comments the AGO urges the Commission to conduct an evidentiary hearing to consider the evidence before deciding the question of deferral, providing a list of questions the Commission should ask the Companies at the hearing. Further, the AGO seeks to have the Companies identify additional measures that are appropriate for the benefit of customers.

In its comments the Public Staff contends that deferral should not be allowed because it would be unfair and inappropriate for the Companies to further burden already overburdened customers by even partially insulating themselves from financial losses caused by the pandemic. According to the Public Staff, based on the growing unemployment rate, the uncertainty of the impact of another wave of the coronavirus and possible shutdowns, and each Company's ability to recoup revenues in their rate case applications, it is simply not reasonable or fair to impose any level of additional increase in rates on the Companies' North Carolina ratepayers.

The Public Staff additionally expresses concerns regarding the eligibility for deferral of some of the costs proposed for deferral by DEC and DEP, as well as issues regarding accurate and reasonable quantification of some of the costs. The Public Staff notes that certain costs were difficult to quantify. The Public Staff also states that the Companies had not incorporated cost savings and offsets into their request. The Public Staff specifically discusses issues related to stipends, bad debts and charge-offs, customer fees waived, federal tax credits, and reductions in the Companies' operating and maintenance (O&M) expenses. The Public Staff opines that should the Commission allow the Companies to defer costs, it should offset costs with COVID-related savings.

The Public Staff also discusses the application of the Commission's deferral test to this request. The Public Staff states that the pandemic was an unusual and extraordinary event, and, thus, the Companies' pandemic-related costs meet the first prong of the deferral test. However, the Public Staff states that the estimated costs proposed for deferral by DEC and DEP are not of a magnitude sufficient to justify deferral and, therefore, do not meet the requirements of the second prong of the deferral test. The Public Staff states that the basis point impacts of the estimated costs set forth by DEP and DEC for deferral are 22 basis points for DEC and 27 basis points for DEP. The Public Staff further notes that once the Companies account for funds received through the federal CARES Act, the basis point impacts decline.

Finally, the Public Staff comments that if the Commission approves deferral of the Companies' COVID-related costs, it would be appropriate for the approval to cover only calendar year 2020, and that should the Companies incur costs in 2021 for which they wish to seek deferral the Companies should be required to file a renewed petition for deferral.

Reply Comments

In its reply comments CIGFUR states that it neither opposes nor supports the Companies' request. However, it maintains that cost causation principles should be strictly followed to avoid the possibility of any cross-subsidization between customer

classes. CIGFUR reiterates that the hardships resulting from the pandemic were not just at the residential ratepayer level and that many industrial and commercial customers have suffered losses.

In its reply comments the AGO states that in making its decision the Commission should weigh the fairness to ratepayers to impose the costs in future rates against the fairness to investors of the financial impacts of a decision not to allow deferral. According to the AGO, the Companies should be allowed to demonstrate that they have taken extra measures to assist customers during the emergency and to show why, in fairness, they should be compensated for some or all of the marginal cost of those efforts. The AGO states that it is not opposed to providing for future cost recovery for the Companies as needed to encourage the Companies to assist customers who are struggling during these extraordinary times.

The Companies assert in their reply comments that the regulatory compact establishes that utilities are required to provide reliable service to all customers at a reasonable cost set by the Commission in exchange for the right as a matter of law to recover all prudently incurred costs plus a return on their investment. In response to the comments of the Public Staff, the Companies state that the Public Staff is opposing the deferral based on equity and fairness, which according to the Companies is not an applicable legal standard. Also, the Companies state that the Public Staff did not appropriately apply the deferral test to the Companies' out-of-period costs and contend that many times the Commission has not applied the second prong when considering a rate case period deferral. Moreover, the Companies state that the Public Staff's concerns regarding certain items of costs and estimates are questions appropriate for the Public Staff to investigate in a future rate case but are not an appropriate basis to oppose or deny the Companies' deferral request. The Companies now are only seeking the right to create a regulatory asset account to record the COVID-related costs which they seek to defer. Further, the Companies state that to the extent the Public Staff feels that it needs to do audits in addition to the audits already conducted, the appropriate time for those audits will be when DEP and DEC seek to increase rates in a future rate case. The Companies also state that DEP and DEC will seek to recover only those COVID-related costs that are deemed to be incremental and agree that to the extent those costs have been reduced or mitigated it is entirely appropriate that any deferrals ultimately placed in rates include only the actual incremental costs.

In response to CUCA, the Companies state that CUCA's arguments related to cross-subsidization are premature at this point, as this is a concern for future rate case proceedings. Regarding CUCA's argument that there should be no return allowed on the deferral, should it be granted, the Companies state that there is a real cost to finance the costs that are being included in the deferral for later collection in rates, and, therefore, a return on the deferral is appropriate.

The Companies disagree with the AGO's position that an expert witness hearing is necessary, noting that the recovery of the deferred costs would be decided in the next general rate case, which would include an expert witness hearing. Regarding the AGO's

suggestion that the Companies provide more information about what they are doing to comply with the Commission's Order Lifting Disconnection Moratorium and Allowing Collection of Arrearages Pursuant to Special Repayment Plans, issued in Docket No. M-100 Sub 158 on July 29, 2020, the Companies state that they already keep the Commission apprised of these efforts.

In response to CBD/AV's comments the Companies state that they are not seeking cost recovery at this time, so CBD/AV's comments that the Companies are shifting costs to other ratepayers is incorrect. The Companies further note that their request for an accounting order to defer incremental COVID-related expenses is an effort to track the costs related to COVID, and that most of CBD/AV's comments are premature and relate to whether specific costs should be recovered in a future rate case. The Companies assert that any arguments over cost recovery should occur in future rate cases when DEC and DEP seek to recover the incremental COVID-related costs for which the Companies seek deferral.

Supplemental Comments

In its supplemental comments the Public Staff reiterates that the Companies have not substantiated a need for a deferral of the enumerated costs and that they seek deferral of items deemed inappropriate or premature by the Public Staff. Specifically, the Public Staff notes that in their August 6, 2021 filing the Companies changed their methodology for calculating the estimated bad debt expense. The Public Staff continues to believe that including an estimated level of uncollectibles in a deferral request, and further allowing the estimate to accrue a return, is short-sighted; the Companies have not yet done enough to determine the expected increase in bad debt, which comprises approximately 40% of the Companies' incremental COVID-related costs. Moreover, the Public Staff states that "the amounts currently included by the Companies as bad debt continue to fluctuate, and should not be included in a deferral calculation until such time as a better estimate can be made." Public Staff Supplemental Comments at 5-6. The Public Staff further reiterates that the Companies did not include savings and reductions in taxes and expenses related to the pandemic as an offset to the incremental costs for which they request deferral. In addition, recent federal legislation has designated additional money for payment of customer past due amounts. Lastly, the Public Staff reiterates that because the total amounts are unknown, if the Commission were to allow deferral "it would only be appropriate for the approval to cover calendar year 2020, [and] the updated costs incurred in 2021 for which the Companies seek deferral should be included in a new petition for deferral of costs incurred during that period." *Id*. at 10.

DISCUSSION AND CONCLUSIONS

By statute, the Commission establishes just and reasonable rates prospectively to allow a utility, upon sound management, to recover its reasonable operating expenses plus a return on its rate base. *See* N.C.G.S. § 62-133. In addition, expenses should be paid out of contemporaneously generated revenues. *See, e.g*., Order Allowing Deferral Accounting, Denying Public Staff's Motion for Reconsideration, Granting Transfer of

CPCNs, and Qualifying the Transferred Facilities as New Renewable Energy Facilities, *Transfer of Certificates of Public Convenience and Necessity and Ownership Interests in Generating Facilities from Duke Energy Carolinas, LLC, to Northbrook Carolina Hydro II, LLC, and Northbrook Tuxedo, LLC*, No. E-7, Sub 1181, at 16 (N.C.U.C. June 5, 2019) ("the general rule of matching current costs with current revenues"); Order Denying Request to Implement Rate Rider and Scheduling Hearing to Consider Request for Creation of Regulatory Asset Account, *Application of Duke Energy Carolinas, LLC, for Approval of Rate Rider to Allow Prompt Recovery of Costs Related to Purchases of Capacity Due to Drought Conditions*, No. E-7, Sub 849, at 19-20 (N.C.U.C. June 2, 2008) ("presumption that such cost increases are recovered through rates being charged by Duke at the time they are incurred"). Deferral of expenses is an exception to this general ratemaking principle of matching costs with revenues and is to be allowed on a case-by-case basis only in exceptional circumstances, such as, for example, to grant the utility relief from an unexpected, unusual, or extraordinary cost that, absent deferral, would materially reduce the utility's earnings. Thus, the Commission has generally considered two factors to determine whether a requested cost deferral is justified: (1) whether the costs in question are unusual or extraordinary in nature, and (2) whether, absent deferral, the costs would have a material impact on the utility's financial condition.

The public health emergency due to COVID erupted in early 2020 while the Companies' most recent electric rate cases were pending. The pandemic caused significant delays in the hearings and decisions in those rate cases. The Companies filed their deferral request while those rate cases were pending and argue that the second prong of the two-prong test, therefore, should not apply in this instance: "[W]hen a deferral of costs is made in the context of a rate case and to limit, reduce or postpone recovery to mitigate the rate impact to customers, the two-prong test is unnecessary and should not apply." DEC/DEP Reply Comments at 10. The Companies state that the two-prong test has primarily arisen in the context of out-of-period requests for cost deferral, or requests made between rate cases; "[t]hus, the costs at issue are incurred out of any general rate case test period." *Id*. at 7. Because the Commission is not then reviewing the utility's overall cost of service, which necessarily fluctuates between rate cases, the costs sought to be deferred between rate cases must be extraordinary and material. Deferral requests made in the context of a general rate case, however, argue the Companies, need only meet the first prong of the test because "the costs associated with the deferral request are not reviewed in isolation." *Id*. at 9. In addition, the Companies assert that "a primary reason for the requested deferral of these [incremental pandemic-related] costs is to postpone recovery for the benefit of customers in light of the challenging economic environment and simply to preserve the opportunity for the Companies to seek to recover the costs in future rates." *Id*. at 4. Alternatively, the Companies argue that the costs are both extraordinary and material, and nevertheless meet both prongs of the test. *Id*. at 4-5.

The Public Staff similarly argues that the Commission should not apply the two-prong test, although for a different reason and with a different result. While acknowledging that the pandemic is an unusual and extraordinary occurrence, the Public

Staff states that the Commission's usual two-prong test should not apply to the Companies' request for deferral

> because it would not be just, reasonable, or equitable to impose additional costs on ratepayers while they continue to experience economic hardship . . . . [I]t is simply not reasonable or fair to impose any level of additional increase in rates on [the Companies'] North Carolina ratepayers. . . . Therefore, in the spirit of equity and fairness, the Public Staff does not believe the [Companies] should be able to defer any of the waived expenses requested in their Joint Petition.

Public Staff Comments at 4-5, 8. The Public Staff states that through the Companies' requested — now recently approved — rate increases and the lifting of the moratorium on disconnections the Companies "will be able to recoup most, at least some, of its lost revenues resulting from the moratorium on disconnections and collection of certain fees." Alternatively, argues the Public Staff, even if the Commission were to apply the two-prong test, the costs proposed to be deferred are not of a magnitude sufficient to justify deferral, and the second prong is not met because the impact is not material.

Other intervenors also variously argue that fairness and equity should be given weight in determining either whether or how to apply the two-prong test and that the costs incurred are not material and fail the second prong of the test. CBD/AV, for example, argue that the Commission should deny the request for deferral, stating:

> [T]he Commission should expand the scope of its inquiry beyond the usual two-prong test . . . and consider critical factors of equity, impacts on ratepayers, and the burden-taking of the Company in deciding whether the requested regulatory asset is warranted. . . . The Commission should consider the merits of the accounting deferral request under a holistic equities analysis, as opposed to the two-prong test alone, which focuses solely on a utility's financial condition. . . . The two-prong test ignores equity considerations that are particularly pertinent in the COVID-19 pandemic.

CBD/AV Comments at 1-3. Alternatively, CBD/AV, like the Public Staff, argue that the costs sought to be deferred are not material and fail the second prong of the two-prong test. *Id*. at 11-12. Although not specifically referencing the two-prong test, in its comments CUCA refers to the impacts to the utilities as minor — "CUCA recommends the Commission deny the Companies' request in this case as its needs to avoid a *minor* degradation in its allowed ROE, which pales in comparison to the needs of its industrial customers to stay in business." CUCA Comments at 4 (emphasis added). Lastly, the AGO argues that the two-prong test should apply, and that the Companies "should not be excepted from the usual standard applied in such matters because the initial filing was made at the time that general rate cases were pending, particularly where [the Companies] failed to request relief in the general rate cases." AGO Comments at 2. The AGO apparently concedes that the costs are extraordinary and likely to be extraordinarily high, thus meeting both prongs of the test, but then generally interposes the issue of

equity, stating, “If granted, the deferral must be based on fairness to ratepayers of imposing the costs on future rates, as weighed against the fairness to investors given the burdensomeness of a decision not to allow deferral.” *Id*. In conclusion, “the AGO recommends that the Commission schedule an evidentiary hearing to consider [the] Joint Petition and whether the relief is fair to customers and investors and what other measures are appropriate for the benefit of customers.” *Id*. at 4.

The Commission agrees with the Companies that deferral requests, by their nature, are unique. The Commission, while generally applying a two-prong test when judging deferral requests, has considered each request individually on a case-by-case basis. The Companies argue that consideration of the second prong is unnecessary and has not been applied by the Commission in the past when the deferral request is made in the context of a general rate case, citing as examples post-in-service plant costs, CCR costs, tax changes, and rate case costs. Duke Comments at 15-17; Duke Reply Comments at 9-14. In this case, however, the Commission agrees with the AGO that the fact that the deferral request was filed during the pendency of the rate cases does not moot the relevance of the second prong of the test, especially as the costs sought to be deferred are ongoing and their totals unknown, and they were not included in the consideration of rates in those cases.

When the two-prong test is applied to the present facts, the Commission is persuaded that the first prong of the test is met because the pandemic — the reason for which the costs were incurred — is an unusual and, indeed, extraordinary event. As the Commission has stated elsewhere, “The coronavirus pandemic presents an *unprecedented* State of Emergency for the Commission, the public utilities it regulates, and the ratepaying public it serves.” Order Lifting Disconnection Moratorium and Allowing Collection of Arrearages Pursuant to Special Repayment Plans, *Investigation of Necessary and Appropriate Responses to the Novel Coronavirus COVID-19*, No. M-100, Sub 158, at 5 (N.C.U.C. July 29, 2020) (emphasis added). The Public Staff generally agrees that incremental COVID-related costs are of an unusual or extraordinary nature, and no other party contests the point.

Regarding the second prong of the cost deferral test — whether the impacts are material — the Companies estimated that the projected costs through December 2020 for the pandemic-related items they sought to defer would be approximately $25.6 million for DEC and approximately $20 million for DEP. Using earnings levels available at the time from the most recent filings in each of the Companies’ rate cases as the baseline for measuring earnings impacts, the Public Staff calculated the basis point impacts of the estimated costs set forth by the Companies for deferral to be 22 basis points for DEC and 27 basis points for DEP. In the Companies’ reply comments they state that the financial return on equity impact to DEC of the incremental costs *and* lost revenues absent a deferral would be approximately 70 basis points and the impact to DEP would be approximately 42 basis points. The Companies state that these impacts would have reduced the adjusted rates of return on common equity to 5.38% and 4.08% for DEC and DEP, respectively, before the establishment of new rates in the then-pending rate cases, at a time when the authorized return was 9.9% for each Company. The Companies are not seeking deferral of

lost revenues, however, so it is not appropriate to consider their impact in deciding whether to grant the requested deferral. In their update filed August 6, 2021, the Companies assert that as of June 30, 2021, the incremental costs for which they seek deferral total approximately $53 million for DEC and $33 million for DEP. The Public Staff in its supplemental comments did not provide an updated calculation of the impact to earnings of this increased cost, which have likely continued to increase, nor have the Companies provided updated information on their current financial condition or whether they are realizing their authorized return since new rates were established.

The Commission notes that it allowed deferral for Dominion North Carolina Power for post-in-service costs associated with the Warren County and Brunswick County combined cycle facilities where the impact to earnings were determined to be 47 and 31 basis points, respectively. The utility's earned rate of return on common equity for the test year in that case was only 5.99%, compared to its authorized return of 10.2%. Order Approving Rate Increase and Cost Deferrals and Revising PJM Regulatory Conditions, *Application by Virginia Elec. & Power Co., d/b/a Dominion N.C. Power, for Adjustment of Rates and Charges Applicable to Elec. Util. Serv. in N.C.*, No. E-22, Sub 532, at 63-67 (N.C.U.C. Dec. 22, 2016). Similarly, the Commission previously approved deferral of costs associated with DEC's Buck and Bridgewater facilities where the aggregate impact of the deferred costs was 29 basis points and the Company's estimated rate of return on common equity was 9.74%, less than the authorized return of 10.5%. Order Approving Deferral Accounting, *Petition of Duke Energy Carolinas, LLC, for an Accounting Order to Defer Certain Capital and Operating Costs Incurred for the Buck Natural Gas Combined Cycle Generating Plant and the Bridgewater Hydro Generating Plant*, No. E-7, Sub 999 (N.C.U.C. June 20, 2012).

The impacts represented by the Companies in this case and the Companies' financial condition at the time the deferral request was made and comments filed are comparable to these previous cases where the Commission has granted deferral. The impact of the initial requested deferral amounts, together with the lost revenues, were 22 and 27 basis points. The total combined amounts sought to be deferred has increased from approximately $45.6 million to $86 million, increasing the impact to the Companies. However, in addition to the Companies' decision not to seek deferral of lost revenues, the Public Staff has challenged the amounts and appropriateness of a number of items sought by the Companies to be deferred. For example, the Public Staff raises questions about the purpose of some of the Companies' COVID-related costs and whether such costs should be borne by ratepayers, such as the stipends paid to the Companies' employees. In addition, the Public Staff maintains that there are possible offsets to the Companies' COVID-related costs that should be considered in formulating a deferred cost amount, such as federal tax credits and reductions in the Companies' O&M expenses. Thus, while it is possible that the impacts in this case would be material for the purpose of considering the second prong of the Commission's deferral test, the Commission cannot reach a conclusion on that point because the actual amounts sought to be deferred have not been determined. However, because of the extraordinary and unprecedented nature of the pandemic and the continuation of the Governor-declared State of Emergency, the Commission will allow the requested deferral in this case in order to

provide the Companies an opportunity to capture the estimated incremental pandemic-related costs and to seek recovery of such costs in the Companies' future rate cases.

Consistent with the Companies' request, the Commission's approval of the Companies' deferral request does not authorize recovery of such costs now or in the next general rate case. As the Companies correctly note, the question currently before the Commission is only whether the Companies may create a regulatory asset to include the estimated incremental costs due to the pandemic, including carrying costs at their weighted average cost of capital, not cost recovery of those costs. DEC/DEP Reply Comments at 7 ("In this docket, the Companies are asking the Commission to issue an accounting order so that the Companies can capture their incremental COVID-19 related costs in a Regulatory Asset account. They are not seeking cost recovery in this docket."). Many of the intervenors' comments, including the need for audit of such costs and a hearing with supporting expert witness testimony, as well as the appropriate cost allocation among customer classes, are appropriate at the time the Companies seek cost recovery in a future rate case. As the Companies note, the costs sought to be deferred will "be subject to full review and consideration by the Commission and intervening parties when addressed in those future cases." DEC/DEP Joint Petition at 3; *see also* DEC/DEP Reply Comments at 3 ("[T]he Companies have simply asked for an accounting order to defer their incremental Pandemic costs such that the Commission and all parties may fully investigate them in a future general rate case."). The parties will have a full opportunity to raise these issues when any such costs are included for cost recovery in a future rate case.[2] There, the burden of proof will be on the Companies to justify recovery of such costs. Although the Commission will allow the Companies to include carrying costs on the deferred amounts for accounting purposes, the rate of that return, if any, and the amount to which that return is applied will be subject to determination in that future rate case.

The Public Staff further contends that a deferral order should state a specific amount of costs deferred, not estimates of present or future deferred costs. To that end, the Public Staff proposes that deferral should be approved only for costs incurred in calendar year 2020 and that the Companies should be required to renew their deferral request for COVID-related costs incurred in 2021 and beyond. The Commission notes that in 2003, in Docket No. E-2, Sub 843, DEP (then Progress Energy Carolinas, Inc., or PEC) filed a petition requesting deferral of storm restoration costs for Hurricane Isabel, among other storms. PEC forecasted that the total expenses associated with Hurricane

[2] *See*, e.*g*., DEC/DEP Reply Comments at 19-20, 31-32, 36 ("The use of a deferral permits the Companies to record what they believe to be prudent Pandemic-related costs, which are subject to audit and review when a proposal is made to include those costs in rates at some point in the future. . . . To the extent the Public Staff feels it needs to do audits in addition to the audits already conducted, the appropriate time for those audits will be when the Companies seek to increase rates."; "Once again, a deferral does not ensure recovery for the Companies; that will be decided at a later evidentiary hearing in a general rate case."; "To reiterate, the Companies are not seeking cost recovery at this time. This proceeding is a determination of whether the Companies can establish a regulatory asset to account for incremental costs resulting from COVID-19. . . . [W]hether such costs can be recovered will be determined at a later date."; "If they are allowed to intervene in future rate cases when DEC and DEP actually seek to recover the incremental COVID-19 costs for which the Companies seek deferral, [intervenors] can make arguments against cost recovery at that time when cost recovery is actually an issue for the Commission to decide.").

Isabel would be approximately $12.6 million on a North Carolina retail basis, subject to adjustment once the actual costs of Hurricane Isabel become known. In addition, PEC requested that the Commission allow PEC to establish a deferred account to which PEC could charge the O&M expenses associated with future named storms and significant ice storms, including an annual carrying charge on the balance of the account. The Commission approved PEC's deferral of the approximately $12.6 million restoration costs for Hurricane Isabel, subject to subsequent true-up to actual costs once the actual costs for Hurricane Isabel became known. However, the Commission denied PEC's request to establish a standing deferral account for future storm costs, stating that it would be inappropriate to "in effect, be approving 'deferral and amortization of costs not yet incurred in amounts not yet known,' all done with virtually, if not absolutely, no knowledge of any factor, let alone all relevant factors, germane to a well-reasoned, informed decision regarding the propriety of such deferrals." Order Granting in Part and Denying in Part Request for Deferral Accounting, *Progress Energy Carolinas, Inc.'s Petition to Create a Deferred Account for Major Expenditures to Restore or Replace Property Damaged by Force Majeure,* No. E-2, Sub 843, at 24-25 (N.C.U.C. Dec. 23, 2003). Although the pandemic is not over and the total amount of the costs sought to be deferred are not yet known, the costs at issue in this case are more akin to the costs for Hurricane Isabel, which were allowed to be deferred in Sub 843, than to the future, unknown storms, for which costs were not allowed to be deferred in that docket. The Commission concludes that it would be inefficient to hold an evidentiary hearing now to quantify costs incurred to date and appropriately deferred or for the Companies to be required to periodically file a new deferral request based on updates to pandemic-related costs. Rather, by deferring the costs until the Companies' next rate cases, they can be fully considered at the hearings in those cases. In the interim, the Companies should continue to file updated cost estimates as they did on August 6, 2021, and report amounts actually recorded in response to this Order.

Many of the parties have urged the Commission to consider fairness and equity in this case. The Commission agrees, and notes that it is not blind to the hardships caused by the pandemic on the residents and businesses in North Carolina, including public utilities. The pandemic is truly extraordinary — "unprecedented" — much more so than unusually severe weather and other events for which costs have been allowed to be deferred in the past. The pandemic resulted in a State of Emergency being declared by the Governor in March 2020 which has not yet been lifted. At first voluntarily, and then by order of the Commission and Executive Order of the Governor, the Companies and other utilities were required to reconnect customers and also prohibited from disconnecting customers for nonpayment, and late payment and other fees were required to be waived. Thus, the Companies have been expected to, and have continued to provide service to all of their customers while many customers have not paid the Companies for such service for over a year and a half. Secondly, deferral of these pandemic-related costs inures to the benefit of customers. Rather than impose additional costs on ratepayers during this time of economic hardship, deferral allows the Companies to recover such costs in a later period when, hopefully, the economy has at least begun to improve. Moreover, any such costs allowed to be recovered may be amortized over an additional period of time in future rate cases to further reduce the burden to customers. Lastly, it would be patently unfair

to penalize the Companies by not allowing them an opportunity to justify recovery of such costs in a future rate case. The actions the Companies have taken during the pandemic were in part due to government mandates intended to ease both the financial and public health impacts of the pandemic on North Carolina and its citizens who might likely have been displaced from their homes.[3]

Lastly, in their reply comments the Companies state, "The Regulatory Compact establishes that utilities are required to provide reliable service to all at a reasonable cost set by the Commission in exchange for the right as a matter of law to recover all prudently-incurred costs plus a return on their investment." DEC/DEP Reply Comments at 15; *see also id*. at 34 ("The fact is that all utilities are lawfully entitled to recover their prudently incurred costs of providing service."). As explained above, utility rates are established prospectively so as to allow a utility through sound management to recover its costs and earn a return on its investment. Expenses associated with the provision of service will inevitably increase, and at times the level of earnings will be reduced below the authorized rate of return. At other times, through load growth and cost savings, the utility's actual earnings may exceed its authorized return. These revenues and expenses are not trued up, and absent deferral, the cost of service, including shareholder return, must be paid out of revenues collected at the time. Thus, under traditional ratemaking, there is no guarantee or entitlement that the utility will earn any return or even fully recover its cost of providing service. If a utility's revenues are not sufficient, it may apply for a rate increase; conversely, if its earnings exceed its authorized return over a sustained period the Commission may initiate a rate case to prospectively reduce the utility's rates.

In conclusion, the Commission will grant the Companies' request that estimated incremental costs of utility service that are proximately caused by the pandemic may be deferred pending a final determination on cost recovery in a future rate case and will require the Companies to file updated cost estimates and report amounts actually recorded in response to this Order. This decision is without prejudice to the right of any party to take issue with the amount, if any, of the deferred costs to be allowed for ratemaking purposes, if such costs are included in future rate filings. Moreover, this decision is based on the unique facts of this case and shall not be cited or relied on as precedent in future proceedings.

IT IS, THEREFORE, ORDERED as follows:

1. That the Companies' request to defer estimated incremental pandemic-related costs be, and the same is hereby, approved without prejudice to the Commission's future determination of the appropriate ratemaking treatment ultimately to be accorded such costs in future rate case proceedings;

[3] In its reply comments the AGO agreed: "The AGO is not opposed to providing for future cost recovery for [the Companies] as needed to encourage [them] to assist customers who are struggling during these extraordinary times. The health and safety of communities are affected by the efforts of all residents to stay home and socially distance to slow the spread of the coronavirus. Accordingly, entire communities benefit from efforts to keep electric service turned on in households that are struggling." AGO Reply Comments at 2.

2. That the Companies shall file in these dockets on a semiannual basis an updated summary of their North Carolina retail incremental COVID-related cost estimates, as was filed on August 6, 2021, and shall report in their filings the actual amount deferred;

3. That the AGO's request for an expert witness hearing at this time on the Companies' petition is denied;

4. That the Commission's decision is based on the unique facts of this case and shall not be cited or relied on as precedent in future proceedings.

ISSUED BY ORDER OF THE COMMISSION.

This the 29th day of December, 2021.

NORTH CAROLINA UTILITIES COMMISSION

Erica N. Green, Deputy Clerk

Commissioner Daniel G. Clodfelter concurs in part, and dissents in part, in a separate opinion.
Commissioner Jeffrey A. Hughes concurs.

DOCKET NO. E-2 SUB 1258
DOCKET NO. E-7 SUB 1241

Separate Opinion of Commissioner Daniel G. Clodfelter:

I do not join in the Commission Order in this matter because I am unable to discern exactly what the Commission has, and what it has not, decided. In my view there are at least two ways to read the Commission's decision. On the first reading, the Commission has granted the Companies' Joint Petition and permitted them to establish regulatory asset accounts for incremental expenditures made in response to the circumstances of the Covid-19 pandemic, although the amount of such expenditures and, even more basically, the components of expense for which regulatory asset treatment may ultimately be approved are not yet delineated or identified. On the second reading, the Commission has simply deferred, in the sense of postponing to another day, a decision on what elements of expense and, if any, what amounts the Companies may be allowed to recover from rates established in future general rate cases.

The Public Staff and all other intervenors, save only the Attorney General, oppose a present decision to permit regulatory asset treatment of the Covid-19 related incremental expenses, for a variety of reasons set out in their comments and canvassed in the Commission's order, although some of their comments indicate an openness to consideration of regulatory asset treatment based on a different record and at some future date.[1] The Attorney General suggests, quite properly, that a present decision on regulatory asset treatment should not be made without a sufficient evidentiary record and likewise signals some willingness to consider in the future possible recovery in rates of certain types and amounts of expenses attributable to the Covid-19 pandemic.

The distinction between these two interpretations is not without meaning. Under the first interpretation the Commission is communicating to interested persons that recovery of the incremental expenses in future rates can be considered likely or probable; under the second interpretation no conclusion can be drawn at this point about whether or not any recovery will ultimately be allowed. Under the first interpretation, the Companies would record a regulatory asset using FERC Account Number 182.3 (Other Regulatory Assets),[2]

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[1] The Public Staff and intervenors also contend that the Commission's traditional test for creation of a regulatory asset account should be supplemented or modified by considerations of fairness relating to the unusual and unanticipated burdens on all parts of the economy, including the Companies' ratepayers, arising from the Covid-19 pandemic. They contend that the Companies should share in these burdens along with their ratepayers and should not be made whole at the expense of ratepayers. The Companies reply that the so-called "regulatory compact" means that they should not be required to bear the obligation of universal service (reinforced during the pandemic by moratoria on disconnections and on the collection of certain fees from customers) at any and all costs and without compensation. I find it unnecessary to enter into this debate because I believe the Joint Petition can be decided under the Commission's traditional formulation and without delving into the unknown waters of "fairness" and or what the "regulatory compact" actually entails.

[2] Pertinent language from the FERC manual of accounts states: "The amounts included in this account are to be established by those charges which would have been included in net income determinations in the current period … but for it being probable that such items will be included in a different period(s) for purposes of developing the rates that the utilities is authorized to charge for its utility services."

because the recovery of the deferred amounts in future rates is considered probable. Under the second interpretation, the Companies would record an entry to FERC Account Number 186 (Miscellaneous Deferred Debits), because recovery of the deferred amounts is at present uncertain.[3]

I consider a decision by the Commission to postpone any decision on recovery of the Covid-19 related expenditures to be appropriate in the present circumstances and in light of the highly unusual triggering event of the Covid-19 pandemic, especially since it does not appear possible at this date to determine whether all those expenditures were appropriate and prudent when they were made, to determine the final amount of such expenditures on a net basis after all offsets and credits are taken into account, or to determine whether that final amount has had any material impact on the Companies' financial condition. On these issues much remains to be settled. Some parties dispute the propriety of certain of the expenditures altogether, such as the special stipends paid to employees or the costs of overtime pay. Other items of expenditures, such as costs of facilities and services to support at-home work by employees or costs of providing protective health and safety equipment, may have been necessary and appropriate but may also turn out to have been offset in whole or in part by cost savings in other operating expenses, such as travel and conference expenses, office supplies, and the operating expenses of offices and other buildings.[4] Yet other items, such as customer fees waived or increased bad debt writeoffs may possibly be appropriate for later recovery in rates, but the final amounts cannot be known until the application of relief funds from government and private assistance programs for customers is resolved.

Were I called upon to decide today whether a regulatory asset should be created for the estimated incremental expenses the Companies contend are attributable to the Covid-19 pandemic, I would have to conclude on the record as it stands that the Commission's requirements for the creation of such a regulatory asset are not satisfied. That "record" consists only of unsworn – and often disputed – statements, contentions, comments, and arguments by the parties to the docket. There has been no opportunity to receive sworn testimony, test that evidence by cross-examination, or permit the Commission to explore the facts through its own questions. The parties themselves acknowledge that many of the facts concerning the Companies' incremental Covid-19 related expenses are still unknown or are uncertain, and there has been no opportunity

[3] The description of this account in the FERC manual as it applies to "major utilities" is "…[T]his account shall include all debits not elsewhere provided for, such as miscellaneous work in progress, and unusual or extraordinary expenses, not included in other accounts, which are in process of amortization and items the proper final disposition of which is uncertain."

[4] Confidential information included in the Public Staff's filings indicate that some of these savings have been substantial. Similarly and to the same point, the Public Staff notes that the Companies have received substantial tax benefits in the form of waivers and deferrals resulting from the federal CARES Act passed by Congress in response to the Covid-19 pandemic. None of these savings or federal support are adequately addressed in the Companies' submissions. The Companies contend that much of the federal relief is in the form of deferrals and temporary suspensions of payment obligations and that the amounts deferred or suspended will ultimately have to be paid. Nonetheless, they represent amounts that have been allowed in setting the level of the Companies' present rates, and the Companies are therefore collecting revenues attributable to such items and are able to earn a return on amounts so collected during the deferral period.

to explore by evidentiary hearing the prudence or wisdom of the Companies' decisions to incur those expenses. The parties likewise acknowledge that the amounts involved are in flux, not only because the working circumstances created by the pandemic are continuing but also because some of the more important elements of these expenses – such as the level of bad debt expense attributable to the pandemic – are subject to credits or offsets due to customers' ability to reduce or eliminate such debts through ongoing relief funds available from government and private aid resources. The Commission acknowledges all this and properly, I believe, therefore declines today to decide exactly what categories of expense, if any, may ultimately be approved for recovery in future rates or in what amounts such items may be recovered.

If required today to decide whether deferral accounting treatment is appropriate for some or all of the Companies' Covid-19 related incremental expenses, there is a second reason I would be unable to do so. The Commission declines to follow the Companies' argument that the Commission should forego application of the second element of its two-part test for approval of accounting deferral treatment requests, and for reasons I have discussed at greater length in my dissents in Docket Nos. E-2, Sub 1219 and E-7, Sub 1214, I agree with the Commission's position on this point. The unprecedented nature of the Covid-19 pandemic notwithstanding, creation of a regulatory asset account for the Companies' expenses in response to that pandemic is not warranted unless there has been or will be a material impact on the Companies' earnings or their ability to achieve their authorized returns on equity.

Approximately sixteen months have now passed since the Companies filed the Joint Petition. The present record does not contain sufficient information from which the Commission could determine that the impact of the Covid-19 incremental expenses has caused, is causing, or will likely in the future cause any significant impairment to the Companies' earnings or their ability to earn the rates of return on equity allowed in their last general rate cases. As the Commission notes in its Order, the Companies contend that the impact on their returns on equity due to the expenditures for which deferral is sought equates to approximately 70 basis points for DEC and approximately 42 basis points for DEP. As has been repeatedly pointed out, however, these calculations do not take into account any offsetting reductions in expenditures or credits for payments made by customers from funds provided by available Covid-19 relief programs. Nor has this contention been tested in the normal manner through investigation and examination by the Public Staff or by cross-examination of witnesses. The Public Staff disputes the Companies' claim on this point, contending instead that the impact to returns on equity was, as of the date of the Public Staff's November, 2020, comments, no more 22 basis points for DEC and 27 basis points for DEP. I take note of the fact that the ES-1 filings made by DEC and DEP on December 1, 2021, in Docket No. M-1, Sub 12, and DEC's and DEP's quarterly surveillance reports for the twelve months ending September 30, 2021, show the following earnings and return levels compared to the current authorized earnings and return levels:

Reported ROE	Authorized ROE	Overall Return	Authorized Overall Return
DEC 10.56%	9.6%	7.46%	7.04%
DEP 11.78%	9.6%	7.83%	6.93%

From these figures I am unable to detect any material impairment to the Companies' returns on equity, which as thus reported are higher than the target levels approved in the Companies' most recent general rate cases. For that reason I would be constrained to conclude that the Companies have not made the showing necessary for creation of a regulatory asset account for the Covid-19 incremental expenses incurred to the present time.[5]

If the Commission's order today is interpreted simply as a decision to defer, meaning to postpone, deciding the Companies' Joint Petition until the time of their next general rate cases, then I would concur in that decision. *Cf.*, Order Denying Request to Implement Rate Rider and Scheduling Hearing to Consider Request for Creation of Regulatory Asset Account, *Application of Duke Energy Carolinas, LLC, for Approval of Rate Rider to Allow Prompt Recovery of Costs Related to Purchases of Capacity Due to Drought Conditions,* No, E-7 sub 849 (N.C.U.C. June 2, 20078). If, on the other hand, the Commission's order is interpreted as a decision to approve today the creation of a regulatory asset for recovery and amortization in future general rate cases, that is, to authorize an accounting deferral now, then I dissent.[6]

\s\ Daniel G. Clodfelter
Commissioner Daniel G. Clodfelter

[5] Although the ordering paragraphs of the Commission's decision do not explicitly say so, elsewhere in the Order the Commission states that it will permit the Companies to accrue carrying costs on the amounts deferred "for accounting purposes," but that it will reserve for the future what level of such carrying costs, if any, may be approved for recovery. Opinion pp. 11-12. My own view is that a number of the categories of expenditures for which deferral is sought are plainly in the nature of operating expenses, while others may, arguably, qualify to earn a return on capital. As I have written in the past, I do not believe deferral accounting treatment should routinely become a way to spin "operating expense straw" into "rate base gold." On this question, the Commission's Order today provides no clear guidance.

[6] I would add that on this latter interpretation I believe the Commission's decision would be erroneous as a matter of law in that it lacks a proper evidentiary foundation, that it fails to find that the two-part test established by the Commission to govern departure from the normal expense-to-revenue matching principle has been satisfied, and that it allows the Companies to accrue a return on capital based on what are predominantly, if not entirely, operating expenses.

DOCKET NO. E-2 SUB 1258
DOCKET NO. E-7 SUB 1241

Commissioner Jeffrey A. Hughes, concurring:

I think the Public Staff identified several financial impacts that could be attributed to the Pandemic that were not included in the deferred cost calculations presented to the Commission. While I am concerned about the completeness and accuracy of the specific deferral amounts to date, I agree with the majority that the deferral accounting mechanism itself is appropriate under the circumstances as long there is an opportunity for more robust cost recovery determination analysis in the next general rate case.

\s\ Jeffrey A. Hughes
Commissioner Jeffrey A. Hughes