NO. 268A12-2 UTILITIES COMMISSION

SUPREME COURT OF NORTH CAROLINA
****

STATE OF NORTH CAROLINA EX REL. UTILITIES COMMISSION; DUKE ENERGY CAROLINAS, LLC, Applicant; PUBLIC STAFF – NORTH CAROLINA UTILITIES COMMISSION, Intervenor,	)	
Appellees,	)	From the North Carolina Utilities Commission
v.	)	Docket No. E-7, Sub 989
ATTORNEY GENERAL ROY COOPER, Intervenor; N.C. WASTE AWARENESS AND REDUCTION NETWORK, Intervenor; N.C. JUSTICE CENTER, Intervenor; N.C. HOUSING COALITION, Intervenor,	)	
Appellants.	)	

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BRIEF OF INTERVENOR-APPELLANT ATTORNEY GENERAL ROY COOPER

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ISSUE PRESENTED

I. DOES THE COMMISSION'S ORDER ON REMAND, GRANTING DUKE THE VERY SAME 10.5% RETURN ON EQUITY THE COMMISSION GRANTED IN ITS ORIGINAL ORDER THAT WAS REVERSED AND REMANDED BY THIS COURT, COMPLY WITH THIS COURT'S HOLDING AND CONTAIN SUFFICIENT FINDINGS OF FACT, CONCLUSIONS OF LAW, AND REASONING?

STATEMENT OF THE CASE

On 27 January 2012, the North Carolina Utilities Commission (the "Commission") granted Duke Energy Carolinas, LLC ("Duke") a $309,033,000 rate increase in conjunction with a return on equity ("ROE") of 10.5%. (R pp 3, 180-81) This Court reversed and remanded. *State ex rel. Utilities Comm'n v. Cooper*, 366 N.C. 484, 739 S.E.2d 541 (2013) ("*Cooper*"). The Attorney General now appeals the subsequent determination made by the Commission on remand.

The underlying case began on 1 July 2011 when Duke filed its application for a rate increase (the "Application"). (R p 170) Following this Court's remand of the Commission's order granting Duke a rate increase, the Attorney General moved to stay Duke's requested rate increase until a new determination was made by the Commission. (R p 108) The Attorney General also requested that the Commission reopen the hearing and permit the parties to submit new or additional evidence in light of the remand. (R pp 109-10) Duke filed a written opposition and the Attorney General filed a reply. (R pp 112, 125)

The Commission denied the Attorney General's motion on 20 May 2013, declining to enter a stay, declining to provide the parties with an opportunity to present new evidence, and, instead, inviting the parties to file "recommendations as to how the Commission should proceed on remand." (R pp 134, 138) The North Carolina Waste Awareness and Reduction Network ("NC WARN") filed its brief containing recommendations on 6 June 2013, and the Attorney General, Duke, and the Public Staff – North Carolina Utilities Commission (the "Public Staff") submitted their briefs with recommendations the following day. (R pp 139, 142-43, 155, 163)

On 23 October 2013, the Commission issued an Order without hearing additional evidence. (R p 170) The Order reaffirms in its entirety the order that was reversed and remanded by this Court in *Cooper* and grants Duke the very same rate increase and 10.5% ROE the Commission previously granted. (R p 212) The Attorney General filed its Notice of Appeal on 21 November 2013. (R p 213) The Record on Appeal was settled on 28 January 2014. (R pp 223-26)

STATEMENT OF THE GROUNDS FOR APPELLATE REVIEW

The Commission's 23 October 2013 order (the "Order") constitutes a final order of the Commission in a general rate case. Appeal to the North Carolina Supreme Court is proper pursuant to N.C. Gen. Stat. §§ 7A-29(b) and 62-90 and N.C. R. App. P. 18.

STATEMENT OF THE FACTS

Much of the relevant factual background to this appeal is recited in the *Cooper* decision. 366 N.C. at 486-89, 739 S.E.2d at 542-44. Therefore, the Attorney General here includes only a brief summary of those facts as well as the additional facts relevant to the Court's current determination on remand.

The underlying case began when Duke filed its Application for a rate increase on 1 July 2011. (R p 170) The Application asked the Commission to set Duke's rates using an ROE of 11.5%. (R p 177) Prior to the evidentiary hearing on the Application, two of the parties, Duke and the Public Staff, filed an Agreement and Stipulation of Settlement (the "Stipulation") that provided for an ROE of 10.5%. (R pp 180-81).

At the evidentiary hearing, five witnesses testified regarding the proper ROE for Duke, including Duke's expert witness Robert B. Hevert ("Hevert"), President of Concentric Energy Advisors, Inc.; the Public Staff's expert witness, Ben Johnson ("Johnson"), Consulting Economist and President, Ben Johnson Associates, Inc.; the Carolina Utility Customers Association, Inc.'s ("CUCA") expert witness Kevin O'Donnell ("O'Donnell"), President of Nova Energy Consultants, Inc.; and the Commercial Group's witnesses Steve Chriss ("Chriss"), Senior Manager for Energy Regulatory Analysis for Wal-Mart Stores, Inc., and Wayne Rosa ("Rosa"), Energy and Maintenance Manager for Food Lion, LLC.

These witnesses testified to a variety of possible ROEs, ranging from 8.5% to 11.5%, although none of the recommendations provided by these witnesses took into account consumer interests or impact of changing economic conditions on consumers. (R pp 177-80) *See also Cooper*, 366 N.C. at 487, 366 S.E.2d at 543-44.

In its initial 27 January 2012 Order, the Commission granted Duke a rate increase and a 10.5% ROE, precisely the ROE contained in the Stipulation between Duke and the Public Staff. (R pp 3, 180-81) This Court reversed and remanded following an appeal by the Attorney General, concluding among other things that the Commission had failed to make the necessary findings of fact to support its ROE determination. *Cooper*, 366 N.C. at 493, 739 S.E.2d at 547. This Court held that the Commission's ROE determination was not independent and, "as guidance on remand" found that the Commission failed to make findings of fact regarding the impact of changing economic conditions on customers. *Id.* at 494, 739 S.E.2d at 547. The Court stated that "it is clear that the Commission must take customer interests into account when making an ROE determination" and "customer interests cannot be measured only indirectly or treated as mere afterthoughts and . . . Chapter 62's ROE provisions cannot be read in isolation as only protecting public utilities and their shareholders." *Id.* at 495, 739 S.E.2d at 548.

Following the remand back to the Commission, the Attorney General moved to stay Duke's requested rate increase until a new determination was made by the Commission. (R p 108) The Attorney General also asked the Commission to reopen the hearing and permit the parties to submit new or additional evidence to satisfy this Court's decision in *Cooper*. (R pp 109-10) Duke filed a written opposition advocating, in essence, that the Commission could merely rewrite its prior Order to comply with *Cooper,* and the Attorney General filed a reply. (R pp 112, 125)

The Commission denied the Attorney General's motion in its entirety on 20 May 2013. (R p 134) According to the Commission, this Court in *Cooper* had not "conclude[d] that the rates established by the Commission were not just and reasonable or that the ROE determined by the Commission was not supported by the evidence." (R p 137) Instead, the Commission ruled that this Court had "remanded the case to the Commission simply because it could not say that the Commission made its own independent conclusion that the proposed ROE was just and reasonable to all parties in light of all the evidence presented." (R p 137) The Commission therefore declined to stay the ordered rate increases and allowed the parties to file "recommendations as to how the Commission should proceed on remand." (R p 138)

In response to this order, NC WARN filed its recommendation on 6 June 2013. (R p 139) NC WARN agreed with the Attorney General that, in light of this Court's opinion in *Cooper*, the Commission should provide the parties with the opportunity to submit new evidence. (R p 139) The Attorney General filed its recommendations the following day, urging the Commission to either "(1) deny the rate increase requested by Duke and provide full refunds to consumers because Duke failed to meet its burden of proof; or (2) provide Duke and other parties with an opportunity to submit new evidence so that there is a more complete record for the Commission to make an informed, legal decision as to a fair and reasonable [ROE] for Duke." (R p 142) The Attorney General noted that the Commission should not "merely change the language in its prior order and come to the same conclusion it reached before." (R pp 142-43)

Duke also filed its recommendations on 7 June 2013. (R p 155) Duke argued that the existing record contained "ample evidence from which the Commission can make the findings and conclusions necessary to satisfy the Supreme Court's instructions and guidance" and, therefore, "no new evidentiary hearings are necessary for the Commission's disposition of this case on remand." (R p 156)

Finally, the Public Staff submitted its recommendations on 7 June 2013. (R p 163) Like Duke, the Public Staff concluded that no new hearing was necessary.

The Public Staff stated that the "Commission should simply respond to the *Cooper* decision by issuing a new order with a discussion of its independent analysis and conclusions regarding ROE and more detailed findings with regard to the impact of changing economic conditions on consumers when determining the proper ROE." (R p 166)

On 8 August 2013, the Commission issued an order that determined among other things that the "Supreme Court's remand of the Rate Order [in *Cooper*] is based on the Supreme Court's concern that it could not discern from the January 27, 2012 Order: (1) whether the Commission's ROE decision was made independently from the ROE agreed upon in the Stipulation, and (2) whether the Commission considered the effects of changing economic conditions on DEC's [Duke's] ratepayers." (R p 168) The order also declined to schedule an additional evidentiary hearing in light of the *Cooper* decision, and instead requested the parties to submit briefs and proposed orders "on the existing record." (R p 169)

After taking briefs, the Commission issued its *Order on Remand* on 23 October 2013 (the "Order"). (R p 170) The Order rejected the Attorney General's argument that further evidence was necessary to satisfy *Cooper*, and concluded that the Commission's new Order could correct the deficiencies addressed in the *Cooper* decision based solely on the "record of evidence compiled in this docket to

date." (R p 186) It is from this Order that the Attorney General now appeals. (R p 213)

Among other things, the remand Order summarizes and recites at greater length than in the initial Order many of the comments the Commission received during six public hearings regarding the proposed rate increase. (R pp 171-77) This testimony included comments from 236 public witnesses, "many of whom testified that the rate increase was not affordable to many customers, including the elderly, persons on fixed incomes, persons with disabilities, the unemployed and underemployed, and the poor." (R p 171) The Order also summarizes the testimonies of experts Hevert, Johnson, O'Donnell and witnesses Chriss and Rosa, none of whom testified regarding the impact of changing economic conditions on consumers and none of whom specifically recommended the ROE of 10.5% that was initially adopted by the Commission and adopted again on remand. (R pp 177-80) The Order also discusses the partial Stipulation, which was likewise previously adopted by the Commission and adopted again on remand. (R pp 180-81) After considerable discussion of what the Commission believes to be the law in this State, the Order ultimately concludes that "the Commission reaffirms its decision of January 27, 2012." (R p 212)

STANDARD OF REVIEW

The standard of review for a decision of the Commission is set forth in N.C. Gen. Stat. § 62-94(b), which provides that this Court:

> may affirm or reverse the decision of the Commission, declare the same null and void, or remand the case for further proceedings; or it may reverse or modify the decision if the substantial rights of the appellants have been prejudiced because the Commission's findings, inferences, conclusions or decisions are:
>
> (1) In violation of constitutional provisions, or
>
> (2) In excess of statutory authority or jurisdiction of the Commission, or
>
> (3) Made upon unlawful proceedings, or
>
> (4) Affected by other errors of law, or
>
> (5) Unsupported by competent, material and substantial evidence in view of the entire record as submitted, or
>
> (6) Arbitrary or capricious.

See also Duke Power Co. v. Pub. Staff, 322 N.C. 689, 698, 370 S.E.2d 567, 573 (1988) ("*Duke Power II*").

Additionally, in order to facilitate appellate review, the Commission's order must:

> be sufficient in detail to enable the court on appeal to determine the controverted questions presented in the proceedings and shall include: (1) Findings and conclusions and the reasons or bases therefor upon all the

> material issues of fact, law, or discretion presented in the record.

N.C. Gen. Stat. § 62-79(a).

The test on appeal is whether the Commission's findings of fact are supported by "competent, material and substantial evidence in view of the entire record." *State ex rel. Utils. Comm'n v. Carolina Util. Customers Ass'n*, 348 N.C. 452, 460, 500 S.E.2d 693, 699 (1998) ("*CUCA I*"). "Substantial evidence" means "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Id.* at 460, 500 S.E.2d at 700 (quoting *Consolidated Edison Co. v. N.L.R.B.*, 305 U.S. 197, 229, 59 S. Ct. 206, 217, 83 L. Ed. 126, 140 (1938)).

Findings of fact are not supported by competent, material, and substantial evidence if the Commission's order does not include all necessary findings of fact. "Failure to include all necessary findings of fact is an error of law and a basis for remand under section 62-94(b)(4) because it frustrates appellate review." *Id.* "What constitutes a fair rate of return on common equity is a conclusion of law which must, in turn, be predicated on adequate factual findings." *Duke Power II*, 322 N.C. at 693, 370 S.E.2d at 570`.

In addition, findings of fact are not supported by competent, material, and substantial evidence if the Commission's ultimate reasoning does not appear in the order or is not supported by the Commission's chain of reasoning. "'Evidence must support findings; findings must support conclusions; conclusions must

support the judgment. Each step of the progression must be taken . . . in logical sequence; each link in the chain of reasoning must appear in the order itself.'" *State ex rel. Utils. Comm'n v. Eddleman*, 320 N.C. 344, 352, 358 S.E.2d 339, 346 (1987) (quoting *Coble v. Coble*, 300 N.C. 708, 714, 268 S.E. 2d 185, 190 (1980)).

On remand, a lower tribunal must comply with the appellate court's decision. *See, e.g., Heath v. Heath*, 132 N.C. App. 36, 38, 509 S.E.2d 804, 805 (1999) (noting that on remand the lower tribunal may receive such further evidence and arguments from the parties as necessary and appropriate to comply with the court's opinion). A lower tribunal is incapable of making appropriate findings of fact when the pertinent facts themselves are not in the record. *See, e.g., State ex rel. Utils. Comm'n v. North Carolina Textile Mfrs. Ass'n, Inc.*, 313 N.C. 215, 328 S.E.2d 264 (1985) (holding that the Commission's conclusion and finding of fact was legally insufficient because there were insufficient facts in the record regarding the issue at hand).

ARGUMENT

Due to the nature of the appeal and the *Cooper* decision, ROE was the only issue for the Commission to examine on remand and is the only issue on appeal before this Court. (R p 143) The Commission's response to this Court's reversal of its prior order and the Court's specific guidance on remand was to simply rewrite its prior order and reach exactly the same conclusion as it did before. This

result-oriented approach is legally insufficient and does not comply with *Cooper* and other governing case law.

The Commission's Order on remand does not attempt to follow this Court's mandate and guidance in *Cooper* but instead tries to "reconcile" *Cooper* with the Commission's own view of what the law should be. (R p 196) Not surprisingly, the Order on remand does not comply with *Cooper* and does not contain sufficient findings of fact, conclusions of law, or reasoning regarding the impact of changing economic conditions on consumers.

Duke is a monopoly utility providing an essential service to captive consumers who have no choice but to purchase electricity from Duke. Unlike typical companies, Duke does not have its prices constrained by competition or market forces. Instead, the Commission regulates Duke's prices and provides the only protection that North Carolina consumers have against unreasonable rates and abuses of monopoly power. Because it fails to follow the legal requirements in Chapter 62 that protect consumers and govern establishment of ROE, the Commission's Order on remand should again be reversed and remanded by this Court so as to ensure that the Commission properly follows these requirements the next time around.

I. THE COMMISSION'S ORDER ON REMAND, GRANTING DUKE THE VERY SAME 10.5% RETURN ON EQUITY THAT THE COMMISSION GRANTED IN ITS INITIAL ORDER, DOES NOT COMPLY WITH THIS COURT'S HOLDING IN *COOPER* AND DOES NOT CONTAIN SUFFICIENT FINDINGS OF FACT, CONCLUSIONS, AND REASONING.

A. The Commission's Order on Remand Refuses to Follow *Cooper*.

It is striking that, on remand, the Commission's Order does not follow the mandate and guidance provided by this Court in *Cooper* but instead tries to get around – or "reconcile" – that mandate and guidance, stating implicitly that it believes this Court was incorrect.

1. This Court's Decision in *Cooper*

This Court's decision in *Cooper* reached several notable conclusions with respect to the record before it and the Commission's prior order. Specifically, the Court noted that although the 10.5% ROE contained in the non-unanimous Stipulation fell within the range of ROEs recommended by the witnesses at the evidentiary hearing, none of the witnesses specifically recommended an ROE of 10.5% based upon their calculations. *Cooper*, 366 N.C. at 493, 739 S.E.2d at 547. The Court concluded that in lieu of weighing the various testimonies presented and addressing why one witness's testimony was more credible than another's or which methodology was afforded the greatest weight, the Commission had "merely recited the witnesses' testimony before reaching an ROE conclusion in its order." *Id.* The Court held that "[w]ithout sufficient findings of fact as to these issues, we

cannot say that the Commission 'ma[de] "its own independent conclusion"…that the propos[ed] [ROE] [wa]s just and reasonable to all parties in light of all the evidence presented." *Id.* (citing *CUCA I*, 348 N.C. at 466, 500 S.E.2d at 703).

Additionally, the Court was clear that the lack of analysis and factual findings extended beyond the Commission's treatment of the experts' testimony. The Court went on to address the Attorney General's argument that N.C. Gen. Stat. § 62-133(b)(4), "in conjunction with Chapter 62 as a whole, mandates that the Commission consider the impact of changing economic conditions on customers when determining ROE." *Id.* at 494, 739 S.E.2d at 547.

Section 62-133(b)(4) provides that the Commission must:

> Fix such rate of return on the cost of the property [used by the utility in providing the service rendered to the public within the State] as will enable the public utility by sound management to produce a fair return for its shareholders, ***considering changing economic conditions and other factors***, including, but not limited to, the inclusion of construction work in progress in the utility's property . . . as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds ***on terms that are reasonable and that are fair to its customers*** and to its existing investors.

N.C. Gen. Stat. § 62-133(b)(4) (emphases added). The Court agreed with the Attorney General that this statute requires substantial analysis and findings by the

Commission regarding the fairness to customers of utility rates in light of changing economic conditions, holding that:

> It is undisputed that section 62–133 dictates that the Commission consider "changing economic conditions" when making an ROE determination. Although subdivision 62–133(b)(4) does not specifically reference "impact on customers," subsection 62–133(a) does emphasize that fairness to customers is a critical consideration in rate cases by including a directive that "the Commission shall fix such rates as shall be fair both to the public utilities ***and to the consumer***." This is consistent with this Court's recognition of the customer-driven focus of Chapter 62 as a whole. . . . . Given the legislature's goal of balancing customer and investor interests, the customer-focused purpose of Chapter 62, and this Court's recognition that the Commission must consider ***all*** evidence presented by interested parties, which necessarily includes customers, ***it is apparent that customer interests cannot be measured only indirectly or treated as mere afterthoughts and that Chapter 62's ROE provisions cannot be read in isolation as only protecting public utilities and their shareholders. Instead, it is clear that the Commission must take customer interests into account when making an ROE determination.*** Therefore, we hold that in retail electric service rate cases the Commission must make findings of fact regarding the impact of changing economic conditions on customers when determining the proper ROE for a public utility.

Cooper, 366 N.C. at 495, 739 S.E.2d at 548 (internal citations omitted; second and third emphases added).

The Court therefore remanded the matter to the Commission with "instructions to make an independent determination regarding the proper ROE

based upon appropriate findings of fact that weigh all the available evidence" (*Id.* at 496, 739 S.E.2d at 548), including "mak[ing] findings of fact regarding the impact of changing economic conditions on customers" (*Id*. at 494, 739 S.E.2d at 547).

On remand, the Attorney General asked the Commission to reopen the hearing and permit the parties to submit new or additional evidence to satisfy this Court's decision. (R pp 108-10) The Attorney General contended, among other things, that:

> In light of the Supreme Court's opinion, it does not appear that the Commission can simply go back and add additional language to its prior order to justify the return on equity and rate increase that the Supreme Court has just reversed. For one thing, the expert testimony previously presented in this matter did not apply the analysis that the Supreme Court said is necessary when determining [ROE]. Neither Mr. Hevert, Duke's expert witness, nor Dr. Johnson, Public Staff's expert witness, accounted for the impact of changing economic conditions on customers when calculating ROE or making ROE recommendations to the Commission. The ROE analysis conducted by these expert witnesses was based on a misunderstanding of what is required under North Carolina law for establishing ROE. In short, there is insufficient evidence in the record that would allow the Commission to adequately perform the analysis that the Supreme Court held is required.

(R pp 109-10) The Commission denied the Attorney General's motion and issued its new Order without hearing any new evidence. (R pp 134, 170)

2. The Commission's Order on Remand

The Commission acknowledges that the "remand is based upon the Court's concern that it could not discern from the Rate Order (1) whether the Commission's rate of return on equity decision was made independently of the [ROE] agreement between the Stipulating Parties expressed in the Stipulation, and (2) whether the Commission adequately considered the effects of changing economic conditions upon [Duke's] customers." (R p 181; *see also* R p 186)

While the Commission goes to some length in its attempt to remedy the first problem – by straining, retroactively, to analyze and interpret the evidence in the record in just such a manner as to justify a 10.5% ROE (even though, again, no expert witness specifically recommended the 10.5% ROE that the Commission once again adopts) (R pp 177-80, 204-09) – it makes no real effort at all to remedy the second problem with its prior order. In fact, outside of conclusory statements acknowledging broad economic trends,[1] the Commission does not make any findings regarding the impact of changing economic conditions on customers. Instead, the Order offers extended analysis implying (without expressly saying) that *Cooper* was wrongly decided. (R pp 187-204)

The Commission starts by contending that the "[s]eminal and controlling jurisprudence" is not *Cooper* or any other North Carolina case decided by this

[1] *See, e.g.*, R pp 183 (economic conditions have caused high unemployment), 202 n.24 (Commission is "fully aware" of recession).

Court but is instead two federal cases – *Fed. Power Comm'n v. Hope Natural Gas Co*., 320 U.S. 591, 64 S. Ct. 281 (1944) ("*Hope*"), and *Bluefield Waterworks & Imp. Co. v. Pub. Serv. Comm'n of W. Va*., 262 U.S. 679, 43 S. Ct. 675 (1923) ("*Bluefield*"). According to the Commission, neither of these federal cases "impose[] a requirement that commissions, in establishing the [ROE] component of the cost of service, augment or discount the cost of that component based on the ability of customers to pay." (R p 187) Rather, the Commission argues, *Hope* requires only an "end result" test and *Bluefield* holds that ROE is to be determined based only on the financial condition of the utility. (R pp 188-89) The Commission concludes that the law in this State is that there is no requirement "to consider consumers' ability to pay" in determining ROE. (R p 190)

From there, the Commission goes on to (1) offer a definition of ROE that it contends is "more complete" than the one the Court provided in *Cooper* (R p 191); (2) contend that because ROE operates like a "cost" to the utility, the Commission cannot change it when factoring in the impact of changing economic conditions on customers (R p 191); (3) contend that the Commission has never been required to assess "the ability of the ratepayer to pay" (R p 192); and (4) contend that no expert has suggested to the Commission that the "cost of equity required by investors . . . should be adjusted . . . to reflect the ability of consumers to pay the rates to be established" (R p 194).

The Commission then claims that instead of just following this Court's mandate in *Cooper*, it "must reconcile" *Cooper*'s requirements with its own view of the law "to the best of its abilities." (R p 196) It does so by effectively rewriting *Cooper*, asserting that "all that the *Cooper* decision" really requires is that the Commission "make [ROE] findings." (R pp 197, 211) The Commission then argues that its prior order (and thus the current, reaffirmed Order) already factored in consumer hardship through "concessions" that favored consumers, such as the stockholder return of $11 million for the benefit of low income customers.[2] (R pp 197-98) According to the Commission, to ascertain the effects of changing economic conditions on consumers, the Commission need only listen to the testimony of public witnesses, which it did. (R pp 202, 204)

Finally, the Commission relies on its contention that it is the Public Staff's duty to "represent[] the using and consuming public, including those having difficulty paying their bills." (R p 200) Because the Public Staff is the entity charged with watching out for consumer interests and the Stipulation, according to the Commission, was a "product of the give and take of the negotiation process," the Commission is of the opinion that the Stipulation itself "addressed all of the costs of service." (R pp 200, 204)

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[2] Of course, the "annual revenue" approved by the Order is in excess of $4.7 billion. (R p 190) Thus, this $11 million dollar "concession" amounts to just a touch over two-tenths of a percentage point of the approved annual revenue. Further, there is no discussion of specifically how this benefits consumers.

The Commission's legal analysis here is deeply flawed, beginning, as a general matter, with the Commission's misguided notion that it, the lower tribunal, need not follow the prior decision of this Court but instead merely has to "reconcile" this Court's decision with its own notions of what the law should be.

Moreover, the starting point of the Commission's legal analysis, with its heavy reliance on two federal cases (*Hope* and *Bluefield*) is off-base, especially given that neither of those federal cases involved state law, specifically North Carolina's statutory provisions regarding ROE contained in Chapter 62. In addition, this statement regarding *Hope* and *Bluefield* in the Commission's Order is simply incorrect: "While the Attorney General has declined to address the requirements of *Hope* and *Bluefield* and its many progeny in his arguments, and consequently the North Carolina Supreme Court does not cite these cases in its reversal and remand opinion, these cases from the highest court in the land bear directly on the issues in this case and must be addressed." (R pp 187-88) The Commission, for some reason, incorrectly assumes that *Hope* and *Bluefield* were not previously briefed before this Court when, in fact, a quick review of the brief filed by Duke and the Attorney General's reply brief in *Cooper* shows that those cases were previously briefed and argued at some length before this Court. *See Br. of Appellee Duke Energy Carolinas, LLC,* No. 268A12, pp. 25-29 (filed Sept. 21,

2012); *Reply Br. of Intervenor-Appellant Attorney General Roy Cooper*, No. 268A12, pp. 6-7 (filed Oct. 17, 2012).

It is true that these federal cases were not cited in this Court's opinion reversing and remanding the Commission's order, but that is not because the cases were not briefed and addressed by Duke and the Attorney General. Presumably, this Court did not find Duke's arguments regarding those inapposite cases persuasive.

Moreover, the Commission's view that ROE should be treated as nothing more than a "cost" to Duke does not comport with the ROE framework contained in Chapter 62, as interpreted by this Court. ROE is not just a cost. The ROE that the Commission authorizes for Duke stays in place until the next rate case. *See* N.C. Gen. Stat. §§ 62-133 & 134. ROE has an impact on the profits Duke is able to earn. Regardless of how the Commission characterizes ROE, the Commission must abide by the statutory and legal framework that governs how it is required to determine Duke's ROE. Pursuant to that framework, the Commission cannot simply treat ROE as a cost that Duke incurs and view ROE only in terms of prospective capital markets. As this Court has stated: "[I]t is clear that the Commission must take customer interests into account when making an ROE determination." *Cooper*, 366 N.C. at 495, 739 S.E.2d at 548. *See also State ex rel. Utils. Comm'n v. General Tel. Co.*, 285 N.C. 671, 680-81, 208 S.E.2d 681, 687

(1974) (holding that Commission can take into account whether utility is providing adequate service to consumers and factor that into ROE percentage authorized for utility). Treating ROE as nothing more than a cost to the utility is directly contrary to this Court's holding that "ROE provisions cannot be read in isolation as only protecting public utilities and their shareholders." *Cooper*, 366 N.C. at 495, 739 S.E.2d at 548.

Likewise, the Commission is incorrect as a legal matter when it states its view that, in terms of consumer interests, all it needs to do is hear what consumers say at public hearings and summarize those views in its Order. "*Cooper* only requires that the Commission *articulate* that it adequately considered changing economic conditions on consumers." (R p 197 n. 17 (emphasis added)) Again, the Commission misreads its important obligations and equates mere form or verbiage with substance. Simply saying, in conclusory fashion, that consumers were considered is not sufficient to comply with the substantive requirement contained in *Cooper* that the Commission actually "take into account" customer interests when it establishes ROE and include sufficient findings of fact and conclusions that show and explain how it did so.

In short, the Commission's contention is simply that *Cooper* is wrong and that the Commission knows better than this Court how to consider the impact of changing economic conditions on customers and how that impact should be

considered in the determination of the proper ROE. According to the Commission, no further evidence was needed and no real findings of fact regarding the impact of changing economic conditions were required when determining the proper ROE for Duke. This position plainly violates this Court's holding in *Cooper*, and, as a result, the Order should be reversed.

B. The Commission's Order Is Not Supported by Competent, Material, and Substantial Evidence and Does Not Contain Sufficient Findings, Conclusions and Reasoning.

Given the Commission's flawed approach regarding the legal requirements pertaining to ROE and its refusal to follow this Court's holding in *Cooper*, it is not surprising that its Order on remand fails to contain sufficient findings, conclusions, and reasoning.

1. There Is Insufficient Evidence in the Record for the Commission to Make Appropriate Findings of Fact Regarding the Impact of Changing Economic Conditions on Customers When Determining Duke's ROE.

The test on appeal is whether the Commission's findings of fact are supported by "competent, material and substantial evidence in view of the entire record." *CUCA I*, 348 N.C. at 460, 500 S.E.2d at 699. "Substantial evidence" means "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Id.* at 460, 500 S.E.2d at 700. "Evidence must support findings." *Eddleman*, 320 N.C. at 352, 358 S.E.2d at 346 (internal quotation marks omitted).

As noted by this Court in *Cooper*, none of the experts testified as to the impact of changing economic conditions on customers when determining the proper ROE for a public utility. Specifically, "Hevert verified that when determining a reasonable ROE, he did not specifically consider factors such as the unemployment or poverty rates in Duke's service area, the impact of his recommendation on the company's fixed income customers or on cities and counties as ratepayers, or its effect on job creation in the region." 366 N.C. at 487, 739 S.E.2d at 543. "Johnson explained that his calculations did not consider the economic impact on Duke's customers when he determined ROE, adding that such considerations are 'beyond the scope of [his] work.'" *Id.* Likewise, "O'Donnell's testimony contained no analysis of economic conditions in Duke's service area and their impact on customers." *Id.* at 488, 739 S.E.2d at 544. And finally, witnesses Chriss and Rosa "did not discuss the fairness of the proposed ROE given the impact of changing economic conditions on customers." *Id*. Indeed, the Commission's own summary of the evidence in the Order on remand makes clear that no expert testifying on the issue of ROE addressed anything about the impact on consumers of changing economic conditions (R pp 177-80), and the Commission expressly acknowledges that this 10.5% number is merely an "average" of a selection of some of the midpoints testified to by various experts (R p 206).

In light of the fact that the expert testimony does not address impact on consumers, the Commission's remand Order turns to public witness testimony, noting that it received comments from 236 public witnesses, "many of whom testified that the rate increase was not affordable to many customers, including the elderly, persons on fixed incomes, persons with disabilities, the unemployed and underemployed, and the poor." (R p 171) This is, according to the Commission, all that is required to ascertain the effects of changing economic conditions on consumers. (R pp 202, 204)

As an initial matter, this argument fails because even the Commission admits that the overwhelming majority of public witnesses strongly opposed a rate increase and described the burden that it would impose. (R pp 171-77) The Order accordingly does not sufficiently explain how the lay testimony supports or justifies the 10.5% ROE. *See Cooper*; *Duke Power II*, 322 N.C. at 701, 370 S.E.2d at 574.

But even ignoring this evidentiary failure, the Commission's position is deeply unfair to consumers. The burden is always on the utility to show that a rate increase it proposes is just and reasonable. N.C. Gen. Stat. § 62-75; *see, e.g.*, *State ex rel. Utils. Comm'n v. Central Telephone Co.*, 60 N.C. App. 393, 394, 299 S.E.2d 264, 265 (1983). The utility should not be allowed to reap the benefits of presenting experts with complex economic models to justify Duke's "need" to

recruit capital in the marketplace, while at the same time being allowed to present nothing as to the impact on consumers of changing economic conditions beyond simply tolerating the admission of lay testimony.

The Attorney General requested on remand that the Commission reopen the hearing and permit the parties (in particular Duke, the party with the burden of proof) to submit new or additional evidence, in part on the grounds that the ROE analysis conducted by the expert witnesses was based on a misunderstanding of what is required under North Carolina law for establishing the proper ROE. (R pp 108-10) The Commission denied the Attorney General's motion and issued its new Order without hearing any new evidence. (R pp 134, 170) Without the presentation of evidence regarding the impact on consumers of changing economic conditions, the Order lacks "competent, material and substantial evidence in view of the entire record" and should be reversed. *CUCA I*, 348 N.C. at 460, 500 S.E.2d at 699.

2. The Order Fails to Contain Sufficient Findings of Fact Regarding the Impact of Changing Economic Conditions on Customers.

In addition to the absence of record evidence regarding the impact on consumers of changing economic conditions, the Order contains insufficient findings of fact on this issue.

As stated in *Cooper*, "in retail electric service rate cases the Commission

must make findings of fact regarding the impact of changing economic conditions on customers when determining the proper ROE for a public utility." 366 N.C. at 495, 739 S.E.2d at 548. In so doing, the Order must "be sufficient in detail to enable the court on appeal to determine the controverted questions presented" and shall include "[f]indings and conclusions and the reasons or bases therefor upon all the material issues of fact, law, or discretion presented in the record." N.C. Gen. Stat. § 62-79(a).

Here, the Commission offers little other than statements recognizing "high levels of unemployment and other economic stress" for consumers (R p 183), acknowledging the "difficulty for consumers" in the "current economic environment" (R p 187), stating that its Order is "fair and reasonable" (R p 183), and asserting that the Commission has "appropriately balance[d]" consumer interests (R p 184). To support these contentions, the Commission points to a number of "adjustments" that were made in the Stipulation purportedly "to reduce rates to consumers," but provides no explanation for how these adjustments actually benefit customers. (R p 187)

In short, the Commission's result-oriented approach of simply rewriting its initial order to include new and different rationales to support the exact ROE number it authorized in its initial order (which was reversed and remanded) renders the Order arbitrary and capricious and legally deficient. The specific ROE

contained in the Stipulation between Duke and the Public Staff was not recommended by any of the expert witnesses who presented testimony in this case, and yet the Order strains to analyze the testimony in such a way as to once again reach the exact ROE number contained in the previously approved Stipulation. The Order's approach in this regard – especially given the history and context of this matter – is not in compliance with this Court's prior precedent or instructions on remand. Accordingly, the Order should be reversed.

3. The Order Takes Consumer Interests into Account Only Indirectly or as Afterthoughts.

Our General Assembly has provided that fairness to consumers is critical in utility rate proceedings and has directed that "the Commission shall fix such rates as shall be fair both to the public utilities *and to the consumer*." N.C. Gen. Stat. § 62-133 (emphasis added). The burden is always on the utility to show that a rate increase it proposes is just and reasonable. N.C. Gen. Stat. § 62-75; *see, e.g.*, *State ex rel. Utils. Comm'n v. Central Telephone Co.*, 60 N.C. App. 393, 394, 299 S.E.2d 264, 265 (1983).

Accordingly, when construing this statute and other provisions in Chapter 62 regarding ratemaking, this Court has recognized that, when the Commission sets rates and establishes an ROE, fairness to consumers is as important, if not more important, than fairness to the utility. "The primary purpose of Chapter 62 of the General Statutes is not to guarantee to the stockholders of a public utility constant

growth in the value of and in the dividend yield from their investment, but is to assure the public of adequate service at a reasonable charge." *General Tel. Co.*, 285 N.C. at 680, 208 S.E.2d at 687. In other words, consumer interests cannot be considered only indirectly or as mere afterthoughts, and the rate of return provisions in Chapter 62 should not be read in isolation as only protecting the utility and its shareholders. *Cooper*, 366 N.C. at 495, 739 S.E.2d at 548.

Indeed, this Court has said that the legislative intent of the rate-setting provisions contained in Chapter 62 is that the Commission "fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States, those of the State Constitution, Art. I, § 19, being the same in this respect." *State ex rel. Utils. Comm'n v. Duke Power Co*., 285 N.C. 377, 388, 206 S.E.2d 269, 276 (1974) ("*Duke Power I*").

N.C. Gen. Stat. § 62-133(b)(4) specifically governs how the Commission is to establish the rate of return that a public utility is authorized to earn on its invested property. In making this determination, the Commission is required to consider "***changing economic conditions and other factors***" and the utility's ability "to compete in the market for capital funds on terms that are ***reasonable and that are fair to its customers*** and to its existing investors." N.C. Gen. Stat. § 62-133(b)(4) (emphases added).

It is well settled that Commission decisions are legally flawed when they fail to make sufficient findings and conclusions regarding any of the statutorily required factors. N.C. Gen. Stat. § 62-79(a) provides that all final orders and decisions of the Commission must be "sufficient in detail" and shall include "[f]indings and conclusions and the reasons or bases therefor upon all the material issues of fact, law, or discretion presented in the record." In performing its statutory duty, the Commission must consider "all factors particularized in § 62-133 . . . to determine what are reasonable and just rates." *Cooper*, 366 N.C. at 494, 739 S.E.2d at 547 (*quoting CUCA I*, 348 N.C. at 462, 500 S.E.2d at 701). "The failure to include all the necessary findings of fact is an error of law and a basis for remand . . . because it frustrates appellate review." *Duke Power II*, 322 N.C. at 699, 370 S.E.2d at 573 (*quoting State ex rel. Utils. Comm'n v. The Public Staff*, 317 N.C. 26, 34, 343 S.E.2d 898, 904 (1986)).

The need to include sufficient findings of fact for appellate review is crucial when reviewing the Commission's determination of the ROE authorized in a rate case. Due to the large impact ROE has on rates paid by consumers, the Commission's task of determining a proper ROE is "an extremely important determination." *Id*. at 697, 370 S.E.2d at 572. In fact, "it is the most expensive form of capital accumulation, which expense is ultimately borne by the ratepayer, and it is the most heavily weighted in arriving at the overall return." *Id.* at 697-98,

370 S.E.2d at 572. Therefore, it is "important that a reviewing court be able to determine the factual underpinnings upon which the Commission's conclusion on this rate of return rests." *Id*. at 698, 370 S.E.2d at 572-73.

While appellate courts give a certain amount of deference to the Commission as the agency tasked with expertise on utilities issues and rates, the "Commission's knowledge, however expert, cannot be considered by this Court unless the facts and findings thereof embraced within that knowledge are in the record." *CUCA I*, 348 N.C. at 460, 500 S.E.2d at 700. Thus, this Court has not hesitated to remand an order or decision by the Commission regarding an ROE issue when the Commission's decision was not predicated on adequate factual findings or when the Commission failed to adequately explain its reasoning or how it employed or quantified factors considered in its rate of return analysis. *See, e.g.*, *Cooper*, 366 N.C. at 494-95, 739 S.E.2d at 547-48; *Duke Power II*, 322 N.C. at 695-701, 370 S.E.2d at 571-74 (insufficient findings as to ROE precluded meaningful appellate review because Commission had merely "recited" testimonies, summarily concluded some proposed ROEs were "excessive" while others were too "conservative," and did not state or quantify what adjustments to proposed ROEs it was making).

Here, the Commission offers little to indicate that consumers are being thought of in any way other than "indirect" or "afterthoughts" when setting the

ROE. The Commission listened to the testimony of lay consumers and then, as discussed above, wrote the Order to state simply that the Commission recognizes times are hard but thinks a 10.5% ROE is fair and reasonable. (R pp 183, 187) The Commission points to "adjustments" amounting to a fraction of a percentage point that purportedly provide relief to some consumers but provides no explanation for how these adjustments actually affect Duke's customers as a whole. (R pp 185, 187). And the Commission argues at great length and in various ways that this Court's express requirement in *Cooper* that consumer interests cannot be considered "indirectly" or as "mere afterthoughts" in the ROE process is, simply, incorrect. (*See, e.g.*, R pp 187-90 (no legal requirement to consider consumers in setting ROE); 191 (Commission cannot alter ROE in response to consumer interests))

This approach is legally deficient because it constitutes the very "indirect" and "afterthought" analysis that is prohibited by *Cooper*. Nothing in N.C. Gen. Stat. § 62-133(a) or *Cooper* abrogates the requirement that proper findings of fact be made regarding the impact of changing economic conditions on customers when ROE is determined simply because the Commission disagrees with the Court and would rather not deal with this complicating factor. *See State ex rel. Utils. Comm'n. v. Gen. Tel. Co*., 281 N.C. 318, 358-59, 189 S.E.2d 705, 730-31 (1972)

("*Gen Tel II*") (findings not "immune" to review because Commission "followed no formula").

In this respect, the Commission's approach in its remand Order is almost identical to the approach used in its original order, where it used lay consumer testimony opposing Duke's rate increase as a basis for supporting the rate increase and the 10.5% ROE. Here, the Commission simply recites and summarizes that consumer testimony in more detail.

In terms of consumer interests, it is hard to imagine an approach that is more "indirect" or more of an "afterthought" than this one. Imagine the reverse scenario, where the Commission held public hearings throughout the state and instead of hearing from consumers heard from individual Duke investors who provided testimony supporting a proposed rate increase. If the Commission then used the testimony of the Duke investors supporting a rate increase as the basis for a decision that reached the opposite result – requiring a rate decrease and establishing an ROE at a rate lower than what Duke requested – it is unlikely that Duke would find that type of approach appropriate. Yet, that is the very type of approach that Duke, along with the Commission and the Public Staff, urge this Court to find sufficient from a consumer interest perspective. Plainly, this is in violation of *Cooper*, which expressly prohibits an approach that treats consumer interests as a mere afterthought.

4. The Order Improperly Shifts the Burden of Proof to Parties Other Than Duke and Does Not Render an Independent ROE Decision.

Duke has the burden of proof in this case, and it has failed to provide substantial evidence showing the impact of changing economic conditions on consumers and that the rate of return is reasonable and fair to Duke's customers as well as its investors. N.C. Gen. Stat. § 62-75. *See also, e.g.*, *State ex rel. Utils. Comm'n v. Central Telephone Co.*, 60 N.C. App. 393, 394, 299 S.E.2d 264, 265 (1983) (burden always on utility to show proposed rate increase is just and reasonable).

In its Order, the Commission simply disagrees with – and fails to follow – the well-established legal principle holding that the burden of proof is on the utility in a rate case where a utility seeks a rate increase. (R pp 202-04) According to the Commission, Duke's evidentiary deficiency is not Duke's problem and, in fact, other parties had the burden of satisfying this element of Duke's case. (R p 202) Among other things, the Commission asserts that (1) "[n]o rate of return on equity evidence was presented by the Attorney General" (R p 205); (2) the Attorney General has not produced contradictory decisions to establish that the Commission's Order is in error (R p 193); and (3) the Attorney General "sponsored no expert economic cost of capital witness and . . . makes no effort to quantify any downward adjustment to the 10.5% rate of return on equity approved in this case"

(R p 195). In short, the Commission concludes that if "the Commission must make a decrement to the rate of [ROE] investors require to reduce rates on income-strapped consumers, the Attorney General has the burden to supply evidence to the record supporting that contention." (R p 203)

Nowhere does the Commission explain why, under this Court's holding in *Cooper*, Duke would have been incapable of presenting evidence regarding the impact of changing economic conditions on consumers. Moreover, the Commission's approach is inherently inconsistent in that it both expressly *declined* to hold further evidentiary hearings in this case (denying parties the opportunity to present evidence), while at the same time criticizing parties other than Duke for not presenting evidence. *See State ex rel. Utils. Comm'n v. Lee Tel. Co*., 263 N.C. 702, 709, 140 S.E.2d 319, 325 (1965) ("[T]here is nothing in the statutes that requires the Commission to accept the rate or rates proposed [by the utility].").

The Commission cannot have it both ways by refusing to allow new evidence on remand while also relying on the fact that certain parties who did not have the burden of proof did not present evidence. "[T]he absence of such evidence in the record does not benefit [the utility], for the burden is upon [the utility] to establish the reasonableness of the rate increases it has proposed." *Duke Power I*, 285 N.C. at 389, 206 S.E.2d at 277-78. Accordingly, the Order should be reversed.

5. The Order Improperly Considers ROEs Authorized for Other Utilities by Other Commissions, ROEs Previously Authorized for Duke by this Commission, and the Higher Rates Requested by Duke in this Matter.

Throughout its Order in this case, the Commission routinely cites as support its prior orders, ROEs authorized by other commissions, and the original application submitted by Duke in this case, cherry picking items that it believes supports its decision. (R pp 182, 184 n.5, 185-86, 193-95, 200-01, 206-07) None of these references provide legal support for the Order at issue or substitute as sufficient findings of fact regarding ROE.

For example, the Order cites an order written by an Idaho commission that, the Commission summarily concludes, was during "a time just as challenging" as North Carolina's economic climate. (R p 193) The Order likewise cites the order of a West Virginia commission that concluded "affordability [for consumers] is not an exclusive issue" upon which the commission can deny a utility a constitutionally reasonable rate of return. (R p 194) The Commission even discusses at some length, on its own initiative, the testimony of a witness who did not even testify in this case and whose testimony was not in the record, again cherry picking from another case to support its preconceived notion of what the result should be in this case. (R pp 194-95)

In *State ex rel. Utils. Comm'n v. Public Staff*, 331 N.C. 215, 415 S.E.2d 354 (1992), the Commission examined the ROE it allowed in another case and ROEs

that five other utility commissions had allowed in other states. This Court found that such considerations and the Commission's concern about reducing ROE a large amount, as opposed to a gradual amount, amounted to "an improper consideration in determining rate of return" because such considerations appeared to "arise from the Commission's inappropriate desire 'to protect investors from swings in market prices.'" *Public Staff*, 331 N.C. at 225, 415 S.E.2d at 361 (citation omitted). Accordingly, this Court reversed the Commission's order. *Id*. at 226, 415 S.E.2d at 362.

Here, the Commission's consideration of the higher or similar ROEs that other commissions in other states have granted other utilities and the other ROEs that the Commission has previously granted Duke are similar to the considerations deemed inappropriate in the *Public Staff* case. As such the Commission's reasoning and decision is legally flawed and not supported by substantial evidence. *See also Duke Power II*, 322 N.C. at 698-700, 370 S.E.2d at 573-74 (reversing Commission's ROE decision where Commission stated in conclusory fashion that one proposed ROE was too "excessive" while others were too "conservative" and "stringent").

Similarly, the Order repeatedly refers to Duke's original, higher request of an 11.5% ROE to justify the decision to grant Duke's later, lower, stipulated ROE of 10.5%. (R pp 182, 185, 186, 200-01) The Order also justifies its conclusions in

part because Duke could have requested a different rate design that would have been even more burdensome for consumers. (R p 184) But the mere fact that Duke came down from its original request or could have made a request that would have been worse does not somehow automatically justify the new, lower request or somehow establish that the new, lower request is in fact appropriate or in accordance with statutory requirements. The fact that Duke entered into a Stipulation with a lower proposed rate does not show that the lower request is actually an appropriate one, but, rather, shows only that the originally requested rate was too high. *See Duke Power I*, 285 N.C. at 388, 206 S.E.2d at 276 (Commission to fix rates "as low as may be reasonably consistent with the requirements of the Due Process Clause"). If such an analysis stands, it only encourages a utility to play the game of first requesting an inflated ROE and then acting as if it has done the public a favor by agreeing to a lower one.

This analysis simply does not reflect an appropriately "independent" decision of the Commission. The reality is that the Order once again analyzes and critiques the expert testimony (recommending different ROEs and ROE ranges) in just such a way so as to reach — to the exact *tenth of a percent* — the precise compromise ROE contained in the Stipulation. It is well established that the absence of evidence in the record of a required element of proof cannot benefit the utility. *See Duke Power I*, 285 N.C. at 389, 206 S.E.2d at 277-78 ("the absence of

such evidence in the record does not benefit [the utility], for the burden is upon [the utility] to establish the reasonableness of the rate increases it has proposed"). *See also* N.C. Gen. Stat. §§ 62-75 and 62-134(c).

If the Commission could only speculate as to a legally required element of the ROE determination, the Commission's recourse was to reject Duke's request for a rate increase instead of plowing forward and making a determination based on an insufficient legal framework and insufficient evidence. The Order should be reversed.

CONCLUSION

For the reasons stated above, the Attorney General respectfully requests that the Commission's Order be reversed and remanded.

Respectfully submitted, this the 17th day of April 2014.

ROY COOPER
Attorney General

/s/ Kevin Anderson
Kevin Anderson
Senior Deputy Attorney General
State Bar No. 22635
kander@ncdoj.gov

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

Phillip K. Woods
Special Deputy Attorney General
State Bar No. 18439
pwoods@ncdoj.gov

Michael T. Henry
Assistant Attorney General
State Bar No. 35338
mhenry@ncdoj.gov

N.C. Department of Justice
Post Office Box 629
Raleigh, NC 27602
Tel: 919.716.6900
Fax: 919.716.6763

Counsel for Intervenor-Appellant

CERTIFICATE OF SERVICE

The undersigned does hereby certify that the foregoing **Brief of the Intervenor-Appellant Attorney General Roy Cooper** was served upon all parties to the appeal via electronic mail, addressed to their Attorney of Record as follows:

Heather Shirley Smith
Deputy General Counsel
Duke Energy Corporation
550 South Tryon Street
Charlotte, NC 28202
Heather.Smith@duke-energy.com

Kendrick Fentress
Associate General Counsel
Duke Energy Corporation
3700 Glenwood Avenue, Suite 330
Raleigh, NC 27612
Kendrick.Fentress@duke-energy.com

Robert W. Kaylor
Law Office of Robert W. Kaylor
3700 Glenwood Avenue, Suite 330
Raleigh, NC 27612
Robert.Kaylor@duke-energy.com

Kiran H. Mehta
K&L Gates, LLP
214 North Tryon Street, 47th Floor
Charlotte, NC 28202
Kiran.Mehta@klgates.com

Counsel for Duke Energy Carolinas, LLC

Antoinette R. Wike, Chief Counsel
antoinette.wike@psncuc.nc.gov
David T. Drooz, Staff Attorney
david.drooz@psncuc.nc.gov
William E. Grantmyre, Staff Attorney
william.grantmyre@psncuc.nc.gov
Public Staff – North Carolina Utilities Commission
4326 Mail Service Center
Raleigh, NC 27699

Counsel for the Public Staff – North Carolina Utilities Commission

John D. Runkle
jrunkle@pricecreek.com
P.O. Box 3793
Chapel Hill, NC 27515-3793

Matthew D. Quinn
matt@attybryanbrice.com
Law Offices of F. Bryan Brice, Jr.
127 West Hargett St., Suite 600
Raleigh, NC 27601

Counsel for North Carolina Waste Awareness & Reduction Network (NC WARN)

This the 17th day of April , 2014.

/s/ Kevin Anderson
Kevin Anderson
Senior Deputy Attorney General