

166 FERC ¶ 61,026  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Neil Chatterjee, Chairman;  
Cheryl A. LaFleur and Richard Glick.

North Carolina Electric Membership Corporation

v.

Docket No. EL18-168-000

Duke Energy Progress, LLC

ORDER DENYING FORMAL CHALLENGE AND COMPLAINT

(Issued January 17, 2019)

1. On May 31, 2018, pursuant to sections 206, 306, and 309 of the Federal Power Act (FPA),<sup>1</sup> Rule 206 of the Commission's Rules of Practice and Procedure,<sup>2</sup> and Duke Energy Progress, LLC's (DEP) Formula Rate Implementation Protocol (Protocols), North Carolina Electric Membership Corporation (NCEMC) filed a Formal Challenge and Complaint against DEP. NCEMC alleges that DEP has violated and continues to violate its transmission formula rate and Joint Open Access Transmission Tariff (OATT)<sup>3</sup> by failing to reflect in its wholesale transmission rates: (1) the reduction in the federal corporate income tax rate that went into effect on January 1, 2018; (2) the return of excess Accumulated Deferred Income Taxes (ADIT) that relate to the reduction in the federal corporate income tax rate; and (3) the reductions in the North Carolina state corporate income tax rate that went into effect on January 1, 2014, and thereafter. In this order, we deny the Formal Challenge and Complaint.

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<sup>1</sup> 16 U.S.C. §§ 824e, 825e, 825h (2012).

<sup>2</sup> 18 C.F.R. § 385.206 (2018).

<sup>3</sup> DEP's transmission formula rate is part of the Joint OATT accepted by the Commission upon the merger of Duke Energy Corporation and Progress Energy, Inc. in 2012. NCEMC Complaint at 4; Duke Energy Carolinas, LLC, Tariffs, Rate Schedules and Service Agreements (Joint OATT), Attachments H.1 (Formula Rate) (12.0.0), H.2 (Formula Rate Implementation Protocols) (0.0.0), H.3 (Formula Rate Notes) (0.0.0).

## I. Background

2. On December 22, 2017, the President signed into law the Tax Cuts and Jobs Act of 2017 (Tax Cuts and Jobs Act), which, among other things, reduced the federal corporate income tax rate from 35 percent to 21 percent, effective January 1, 2018.<sup>4</sup> This means that, beginning January 1, 2018, companies subject to the Commission's jurisdiction will compute income taxes owed to the Internal Revenue Service (IRS) based on a 21 percent tax rate. The tax rate reduction will result in less corporate income tax expense going forward.<sup>5</sup> The tax rate reduction will also result in a reduction in ADIT liabilities and ADIT assets on the books of rate-regulated companies.<sup>6</sup>

3. On March 15, 2018, pursuant to section 206 of the FPA, the Commission issued two orders to show cause, directing public utilities that use stated transmission rates or transmission formula rates with a fixed line item of 35 percent for the federal corporate income tax rate under an OATT or transmission owner tariff to propose revisions to their stated transmission rates or transmission formula rates to reflect the reduced federal

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<sup>4</sup> Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017).

<sup>5</sup> *See id.* § 13001, 131 Stat. at 2096.

<sup>6</sup> ADIT balances are accumulated on the regulated books and records of public utilities based on the requirements of the Uniform System of Accounts. ADIT arises from timing differences between the method of computing taxable income for reporting to the IRS and the method of computing income for regulatory accounting and ratemaking purposes. *See* 18 C.F.R. § 35.24(d)(2) (2018). As a result of the reduction in the federal corporate income tax rate, a portion of an ADIT liability that was collected from customers will no longer be due from public utilities to the IRS and is considered excess ADIT, which must be returned to customers in a cost-of-service ratemaking context. Additionally, for public utilities that have an ADIT asset, the Tax Cuts and Jobs Act will result in a reduction to that ADIT asset, and public utilities may seek to reflect in rates a portion of such reductions. Public utilities are required to adjust their ADIT assets and ADIT liabilities for the effect of a change in tax rates in the period that the change is enacted. *Public Utility Transmission Rate Changes to Address Accumulated Deferred Income Taxes*, 165 FERC ¶ 61,117, at PP 7-8 (2018) (ADIT NOPR) (citing 18 C.F.R. §§ 35.24, 154.305 (2018); *Regulations Implementing Tax Normalization for Certain Items Reflecting Timing Differences in the Recognition of Expenses or Revenues for Ratemaking and Income Tax Purposes*, Order No. 144, FERC Stats. & Regs. ¶ 30,254 (1981) (cross-referenced at 15 FERC ¶ 61,133), *order on reh'g*, Order No. 144-A, FERC Stats. & Regs. ¶ 30,340 (1982)).

corporate income tax rate or show cause why they should not be required to do so.<sup>7</sup> DEP was not the subject of either of these orders.

4. Also on March 15, 2018, the Commission issued a Notice of Inquiry (Tax NOI) seeking comments on, among other things, whether, and if so, how, the Commission should address the effects of the Tax Cuts and Jobs Act on ADIT.<sup>8</sup> On November 15, 2018, the Commission issued a Notice of Proposed Rulemaking (ADIT NOPR) proposing to require all public utility transmission providers with transmission formula rates under an OATT, a transmission owner tariff, or a rate schedule to revise those rates to: include a mechanism to deduct any excess ADIT from or add any deficient ADIT to their rate bases; include a mechanism that decreases or increases their income tax allowances by any amortized excess or deficient ADIT, respectively; and incorporate a new permanent worksheet that will annually track information related to excess or deficient ADIT.<sup>9</sup>

5. North Carolina also reduced its state corporate income tax rate on multiple occasions in recent years. In 2013, the North Carolina General Assembly passed legislation reducing the state corporate income tax rate from 6.9 percent to six percent, effective January 1, 2014, and further reducing the rate from six percent to five percent, effective January 1, 2015.<sup>10</sup> The legislation provided that upon satisfaction of certain financial thresholds, which were met, the state corporate income tax rate would decrease annually thereafter by one percent through 2017.<sup>11</sup> In 2017, North Carolina further

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<sup>7</sup> See *AEP Appalachian Transmission Co., Inc.*, 162 FERC ¶ 61,225 (2018) (Formula Rates Show Cause Order); *Alcoa Power Generating Inc. – Long Sault Division*, 162 FERC ¶ 61,224 (2018) (Stated Rates Show Cause Order).

<sup>8</sup> See *Inquiry Regarding the Effect of the Tax Cuts and Jobs Act on Commission-Jurisdictional Rates*, 162 FERC ¶ 61,223 (2018) (Tax NOI).

<sup>9</sup> See ADIT NOPR, 165 FERC ¶ 61,117 at PP 1-5.

<sup>10</sup> NCEMC Complaint at 10 (citing 2013 N.C. Sess. Laws 2013-316, §§ 2.1(c), 2.2(a), 2.2(b), <https://www.ncleg.net/enactedlegislation/sessionlaws/pdf/2013-2014/sl2013-316.pdf>).

<sup>11</sup> *Id.*

reduced its state corporate income tax rate from three percent to 2.5 percent, effective January 1, 2019.<sup>12</sup>

6. DEP's cost-based transmission formula rate is the product of a settlement agreement with DEP's transmission customers, including NCEMC, first established in 2008.<sup>13</sup> Pursuant to a 2016 settlement (2016 Settlement Agreement), DEP's transmission formula rate employs a historical test year methodology without a true-up mechanism and is based on actual costs (rather than projected costs).<sup>14</sup> This historical test year methodology is not subject to change during the period January 1, 2016, through December 31, 2019 (DEP Rate Moratorium).<sup>15</sup> Pursuant to DEP's Protocols, DEP must submit an Annual Update of its transmission formula rate by May 15 of each year containing wholesale transmission rates for the period of June 1 of that year through May 31 of the following year, generally based on historical costs incurred in the prior calendar year.<sup>16</sup> The Protocols provide processes for transmission customers to submit information requests and for preliminary and formal challenges to Annual Updates each year.<sup>17</sup> The line item in DEP's transmission formula rate for federal corporate income tax rate shows a placeholder of 0.00 percent,<sup>18</sup> as does the line item for the composite North

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<sup>12</sup> *Id.* (citing 2017 N.C. Sess. Laws 2017-57, § 38.5(a), <https://www.ncleg.net/enactedlegislation/sessionlaws/pdf/2017-2018/sl2017-57.pdf>).

<sup>13</sup> *Id.* at 4; *Carolina Power & Light Co.*, Docket Nos. ER08-889-000, *et al.* (June 27, 2008) (delegated order).

<sup>14</sup> *N.C. Elec. Membership Corp. v. Duke Energy Progress, LLC*, Docket Nos. EL16-29-000, *et al.* (Nov. 21, 2016) (delegated order).

<sup>15</sup> The DEP Rate Moratorium further provides that neither DEP nor any transmission customer may submit an FPA section 205 or 206 filing to change the historical test year methodology effective prior to January 1, 2020. Joint OATT, Attachment H.3 (0.0.0), § 1.21.

<sup>16</sup> Joint OATT, Attachment H.2 (0.0.0), §§ 1.a, 1.b.

<sup>17</sup> *Id.* §§ 2.c, 2.e.

<sup>18</sup> Joint OATT, Attachment H.1 (12.0.0), Ex. DEP-2 at 3, line 25.

and South Carolina state corporate income tax rate.<sup>19</sup> DEP's transmission formula rate also provides for adjustments to rate base for ADIT.<sup>20</sup>

7. DEP's 2017 Annual Update, which calculated the wholesale transmission rates for the period June 1, 2017, through May 31, 2018, reflected the 35 percent federal corporate income tax rate. DEP's 2018 Annual Update, which calculated the wholesale transmission rates for the period June 1, 2018, through May 31, 2019, also reflected the 35 percent federal corporate income tax rate.<sup>21</sup> In a separate proceeding, to hold its customers harmless from a rate base increase, DEP requested, and the Commission granted, waiver of the Joint OATT to allow DEP to adjust its 2018 Annual Update to eliminate the impact of the deferred tax accounting changes made in response to the Tax Cuts and Jobs Act.<sup>22</sup>

## **II. Formal Challenge and Complaint**

8. NCEMC alleges that DEP violated and continues to violate its transmission formula rate and Joint OATT by failing to reflect in its wholesale transmission rates: (1) the reduction in the federal corporate income tax rate that went into effect on January 1, 2018; (2) the return of excess ADIT that relates to the reduction in the federal corporate income tax rate; and (3) the reductions in the North Carolina state corporate income tax rate that went into effect on January 1, 2014, and thereafter.<sup>23</sup> NCEMC contends that DEP's failure to reflect the lower federal corporate income tax and state corporate income tax rates, excluding interest, will result in approximately \$10.18 million of excessive wholesale transmission service charges, approximately \$4.79 million of

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<sup>19</sup> A note in DEP's transmission formula rate provides that the composite state corporate income tax rate is "[d]etermined by annual apportionment provided by Tax Department." *Id.* at 3 line 24, 5 Note G.

<sup>20</sup> Joint OATT, Attachment H.1 (12.0.0), Ex. DEP-2 at 2, lines 19-21.

<sup>21</sup> Duke Energy Progress, LLC, Informational Filing with 2017 Annual Update for the OATT Formula Transmission Rate, Docket No. ER09-1165-000, Ex. DEP-2 at 3, line 25 (filed May 15, 2017); Duke Energy Progress, LLC, Informational Filing with 2018 Annual Update for the OATT Formula Transmission Rate, Docket No. ER09-1165-000, Ex. DEP-2 at 3, line 25 (filed May 15, 2018).

<sup>22</sup> *See Duke Energy Carolinas, LLC*, 163 FERC ¶ 61,240 (2018).

<sup>23</sup> NCEMC Complaint at 1-2.

which NCEMC will bear.<sup>24</sup> NCEMC asserts that DEP's actions will result in its shareholders permanently keeping the savings generated by the lower corporate income tax rates during the relevant period.<sup>25</sup>

9. NCEMC argues that DEP's transmission formula rate is a cost-based rate designed to reflect DEP's actual cost to provide service to its wholesale transmission customers. NCEMC asserts that, although DEP's transmission formula rate is generally based on historical costs from the prior calendar year, the calculation of the federal and state corporate income tax allowance is an exception, such that DEP should use the federal and state corporate income tax rates in effect during the rate period to calculate its annual transmission revenue requirement in any given year. NCEMC explains that the Protocols require that the Annual Update be "based upon the data properly recordable and recorded in FERC Form No. 1<sup>26</sup> for the most recent calendar year (to the extent the Formula Rate specifies Form 1 data as the input source), and, to the extent specified in the Formula Rate, be based upon" DEP's books and records.<sup>27</sup> Because the transmission formula rate does not specify FERC Form No. 1 data or DEP's books and records as the input source for the federal corporate income tax rate, NCEMC argues that DEP must use the federal

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<sup>24</sup> *Id.* at 2. NCEMC asserts that the revenue effect of the change in the federal corporate income tax rate would be a reduction in DEP's annual transmission revenue requirement from June 1, 2018, to May 31, 2019, of approximately \$6.243 million at the wholesale transmission level, approximately \$2.92 million of which would be allocated to NCEMC. In addition, for the rate period January 1, 2018, to May 31, 2018, NCEMC estimates DEP's wholesale transmission customers paid transmission rates that were excessive by more than \$2.6 million (without interest), \$1.217 million of which were paid by NCEMC. *Id.* at 20-21. And NCEMC contends that the revenue effect of the reductions in the North Carolina state corporate income tax rate would be a reduction in DEP's annual transmission revenue requirement for 2013-2018 of \$1.339 million, approximately \$647,000 of which would be NCEMC's share. *Id.* at 27-28.

<sup>25</sup> *Id.* at 7-8.

<sup>26</sup> FERC Form No. 1 "is a comprehensive financial and operating report submitted annually for electric rate regulation, market oversight analysis, and financial audits by Major electric utilities, licensees and others," as defined by the Commission's regulations. FERC.gov, Forms, Form No. 1 – Annual Report of Major Electric Utility, Summary, <https://www.ferc.gov/docs-filing/forms.asp#1> (last visited Jan. 2, 2019); *see also* 18 C.F.R. § 141.1 (2018).

<sup>27</sup> NCEMC Complaint at 12-13 (quoting Joint OATT, Attachment H.2 (0.0.0), § 1.g.i).

corporate income tax rate in effect during the rate period.<sup>28</sup> NCEMC notes that there is nothing in the transmission formula rate template or FERC Form No. 1 that requires that the federal corporate income tax rate placeholder be calculated using the prior year's tax rate.<sup>29</sup> NCEMC argues that the Commission's Formula Rates Show Cause Order demonstrates the Commission's policy of requiring public utilities to pass through to wholesale transmission customers the cost savings from the reduced federal corporate income tax rate.<sup>30</sup> NCEMC argues that the Commission has authority pursuant to section 309 of the FPA to remedy DEP's overstated wholesale transmission rate effective January 1, 2018.<sup>31</sup>

10. NCEMC believes that its position is not contrary to the DEP Rate Moratorium in the 2016 Settlement Agreement because NCEMC is not seeking to change the transmission formula rate.<sup>32</sup> NCEMC contends that nothing in the 2016 Settlement Agreement prohibits a change to the tax rate factor used to determine federal and state income tax allowance. Nevertheless, to the extent the Commission finds that the 35 percent federal corporate income tax rate is part of the transmission formula rate, NCEMC argues that the rate is unjust and unreasonable pursuant to section 206 of the FPA.<sup>33</sup>

11. NCEMC also asserts that DEP violated and continues to violate its transmission formula rate and Joint OATT by failing to reflect reductions in the North Carolina state

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<sup>28</sup> *Id.* at 13, 15. NCEMC notes that DEP does not use actual tax expense paid in the prior year to populate its transmission formula rate; rather, NCEMC continues, DEP calculates its tax allowance by multiplying its return on rate base by the tax revenue requirement factor calculated using federal and state corporate income tax rates. *Id.* at 12.

<sup>29</sup> *Id.* at 14-15.

<sup>30</sup> *Id.* at 17, 21-22.

<sup>31</sup> *Id.* at 22-23.

<sup>32</sup> *Id.* at 17-18.

<sup>33</sup> *Id.* at 18-19. In other words, NCEMC views its challenge to the use of the 35 percent federal corporate income tax rate as a formal challenge under the Protocols and not an FPA section 206 complaint, but to the extent the Commission finds that NCEMC's relief would require a change to the transmission formula rate itself, NCEMC contends that it has met the FPA section 206 burden. *Id.* at 19-20. NCEMC argues the same regarding the state corporate income tax rate. *Id.* at 28.

corporate income tax rate that went into effect on January 1, 2014, and thereafter. NCEMC explains that, at the time it submitted its preliminary challenges to DEP's 2013-2017 Annual Updates, NCEMC was not aware of the potential defect in DEP's calculation of the state corporate income tax allowance in its wholesale transmission rates, and thus did not challenge those calculations (despite challenging a state excess ADIT issue).<sup>34</sup> However, given DEP's treatment of the federal corporate income tax rate reduction, NCEMC states that it is concerned that DEP has not been timely reflecting state corporate income tax rate reductions in its wholesale transmission rates.<sup>35</sup> Like the federal corporate income tax rate, NCEMC contends that the state corporate income tax rate is not a fixed line item nor is it based on the prior year's FERC Form No. 1 cost or data. Therefore, for the same reasons as discussed above, NCEMC contends that the state corporate income tax rate must be calculated using the tax rate in effect during the rate period.<sup>36</sup>

12. NCEMC further argues that DEP should be required to return the excess ADIT associated with the reduced federal corporate income tax rate to its wholesale transmission customers. NCEMC states that DEP's transmission formula rate reflects the Commission's requirement that rate base be reduced by the ADIT in Account 282, Accumulated Deferred Income Taxes – Other Property.<sup>37</sup> Consistent with Commission regulations, NCEMC understands that DEP remeasured its ADIT reserves, and that DEP's 2018 Annual Update continues to reflect the excess ADIT as an offset to rate base to hold customers harmless until the excess ADIT amount is required to be flowed back to customers.<sup>38</sup> NCEMC acknowledges the pendency of the Tax NOI, but claims that its Complaint is not premature because it may be necessary to establish a refund effective date in the event the Commission were to find that a change to DEP's transmission formula rate is needed to flow back the excess ADIT amounts to customers.<sup>39</sup> NCEMC also provides an analysis of how the excess ADIT issue should be resolved for DEP if the Commission decides in the Tax NOI proceeding to address the issue on a case-by-case

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<sup>34</sup> *Id.* at 24.

<sup>35</sup> *Id.* at 10-11, 27.

<sup>36</sup> *Id.* at 26-27.

<sup>37</sup> *Id.* at 29 (citing Joint OATT, Attachment H.1 (12.0.0), Ex. DEP-2 at 2, lines 19-21).

<sup>38</sup> *Id.* at 30-31.

<sup>39</sup> *Id.* at 9, 32.

basis.<sup>40</sup> NCEMC estimates that the total annual amortization for wholesale transmission customers of DEP's excess ADIT balance based on a 40-year period is \$1.435 million, \$672,000 of which is NCEMC's estimated share.<sup>41</sup>

13. NCEMC asks the Commission to: direct DEP to revise the corporate income tax rates used in its 2013-2018 Annual Updates to calculate the tax allowance in the annual transmission revenue requirements using the federal and state corporate income tax rates actually in effect for each period;<sup>42</sup> flow back to wholesale transmission customers the excess ADIT amounts that resulted from the reduction in the federal corporate income tax rate; and recalculate the wholesale transmission charges and provide refunds (with interest) necessary to ensure wholesale transmission customers are receiving the full benefit of the reduced corporate income tax rates.<sup>43</sup> NCEMC asserts that the changes to the calculation of DEP's transmission formula rate that NCEMC requests involve only changes to the factors used to calculate tax allowance and not a change to the transmission formula rate itself. To the extent the Commission finds that a change to the transmission formula rate is necessary, however, NCEMC asks that the Commission establish a refund effective date at the earliest possible date for the relief it seeks.<sup>44</sup>

### **III. Notice of Filing and Responsive Pleadings**

14. Notice of the Formal Challenge and Complaint was published in the *Federal Register*, 83 Fed. Reg. 27,323 (2018), with interventions and protests due on or before June 20, 2018. Fayetteville, North Carolina Public Works Commission (Fayetteville), North Carolina Eastern Municipal Power Agency (NCEMPA), Haywood Electric

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<sup>40</sup> *Id.* at 31-32.

<sup>41</sup> *Id.* at 33.

<sup>42</sup> NCEMC asks that the Commission direct DEP to report on how it reflected the reduced North Carolina state corporate income tax rates in 2013-2018 and, if DEP did not timely incorporate the reductions, to direct DEP to refund the overcharges. *Id.* at 38.

<sup>43</sup> *Id.* at 2.

<sup>44</sup> *Id.* at 2-3, 20, 38. For the federal corporate income tax rate reduction and related federal excess ADIT issue, NCEMC requests that the Commission require DEP to recalculate rates from the date of publication of the Tax NOI in the *Federal Register* on March 21, 2018, which NCEMC argues put all public utilities on notice that the Commission intended to flow through to customers the effects of the reduction in the federal corporate income tax rate at the earliest possible date. For the state corporate income tax rate reduction, NCEMC requests a refund effective date as of the date of the filing of the Formal Challenge and Complaint.

Membership Corporation, and Florida Municipal Power Agency each filed motions to intervene. Fayetteville and NCEMPA (together, Customers) filed joint comments in support of the Formal Challenge and Complaint.

15. DEP filed an answer to the Formal Challenge and Complaint, and NCEMC filed an answer to DEP's answer. DEP filed an answer to Customers' comments and NCEMC's answer, and NCEMC filed an answer to DEP's answer to Customers' comments.

16. On January 7, 2019, NCEMC filed a motion to lodge an order from the North Carolina Utilities Commission, in which the North Carolina Utilities Commission required certain utilities to adjust their retail base rates to reflect the reduction in the federal corporate income tax rate for taxable years beginning after December 31, 2017.

**A. DEP Answer**

17. DEP argues that it properly used the federal and state corporate income tax rates in effect during the historical test year period in all of its Annual Updates, consistent with the historical test year methodology included in its transmission formula rate. DEP states that the reduced federal corporate income tax rate will be reflected in the 2019 Annual Update, just as the reduced state corporate income tax rates were reflected in DEP's annual transmission revenue requirement the year after they went into effect, as dictated by the filed rate.<sup>45</sup>

18. DEP contends that NCEMC's assertion that there is a tax exception to the historical test year methodology is contrary to the filed rate. DEP argues that the header in its transmission formula rate—"Year Ending 12/31/yyyy"—demonstrates that the corporate income tax rates should be filled out as of the end of the relevant year being used to calculate the rate, i.e., the historical test year.<sup>46</sup> DEP also details the instructions to FERC Form No. 1, which require utilities to rely on "the tax return for the year;" DEP interprets this instruction to refer to the tax return for the year covered by the FERC Form No. 1.<sup>47</sup>

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<sup>45</sup> DEP June 28, 2018 Answer at 11-12.

<sup>46</sup> *Id.* at 13-14.

<sup>47</sup> *Id.* at 14-15 (citing FERC Form No. 1: Annual Report of Major Elec. Utilities, Licensees and Others, at 261, <https://www.ferc.gov/docs-filing/forms/form-1/form-1.pdf> (last visited Jan. 2, 2019)).

19. Moreover, DEP asserts that if NCEMC were correct, the parties would have included in the filed rate a tax exception given the clarity of the parties' intent to use a historical test year methodology. DEP points out that the filed rate explicitly includes one exception to the historical test year methodology—Cash Working Capital—meaning that the settling parties knew how to draft an exception.<sup>48</sup> DEP contends that, if the parties wanted to establish an exception, they also would have addressed the existence of two different federal and state corporate income tax rates in effect during each rate period (because the tax rate changes were all effective on January 1st).<sup>49</sup> DEP points to the 2016 Settlement Agreement, which described the historical test year methodology as “[R]ates that change each June 1 based on the immediately preceding year’s cost of service, calculated using end-of-year balances.”<sup>50</sup> DEP asserts that the income tax portion of a utility’s costs is part of the utility’s cost of service. DEP adds that its formula rate includes a 0.00 percent placeholder for the tax rate, but that this figure is simply a placeholder, to be replaced by the tax rate provided for in the filed rate.<sup>51</sup>

20. In addition, according to DEP, to provide appropriate cost recovery, all costs in a test year must be synchronized to reflect costs from the test year, rather than picking and choosing costs that may have increased or decreased after the test year ended.<sup>52</sup> DEP contends that, under formula rates based on a historical test year, the utility’s rates do not recover the utility’s actual costs for the service year, but rather its test year costs, as a proxy for the service year costs.<sup>53</sup>

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<sup>48</sup> *Id.* at 18 (citing Joint OATT, Attachment H.3 (0.0.0), § 1.1).

<sup>49</sup> *Id.* at 18-19.

<sup>50</sup> *Id.* at 20 (quoting 2016 Settlement Agreement, § 1.21) (citing Joint OATT, Schedule 10-B, Ex. C (0.0.0), § 19.0).

<sup>51</sup> *Id.* at 21.

<sup>52</sup> *Id.* at 8-9 (citing *Metropolitan Edison Co.*, 44 FERC ¶ 61,053, at 61,146 (1988); *Delmarva Power & Light Co.*, 38 FERC ¶ 61,098, at 61,257 (1987); *Westar Energy, Inc.*, 122 FERC ¶ 61,268, at P 98 (2008); *Ameren Ill. Co.*, 163 FERC ¶ 61,200 (2018); *Conn. Light & Power Co.*, 19 FERC ¶ 61,150, at 61,268 (1982)); *see also id.* at 17 (citing *Carolina Power & Light Co. v. FERC*, 860 F.2d 1097, 1102 (D.C. Cir. 1988)) (arguing that the only reasonable interpretation of DEP’s transmission formula rate is that the tax rates should be drawn from the time period from which all of the other data are drawn).

<sup>53</sup> *Id.* at 9-10. DEP states that the Commission has only allowed adjustments for known and measurable changes for prospective formula rates that specifically include adjustments as part of the Commission-approved formula, but has rejected adjustments to

21. DEP contends that the parties' course of conduct is consistent with DEP's interpretation of its transmission formula rate. In particular, DEP states that in its 2014-2017 Annual Updates, DEP calculated its annual transmission revenue requirement using composite state corporate income tax rates that reflected the tax rates for the immediately preceding year, as required by the filed rate, and no one challenged this practice despite significant publicity surrounding North Carolina's four-year reduction in its state corporate income tax rate.<sup>54</sup> DEP quotes from its response to an inquiry during the 2015 Annual Update process regarding excess ADIT that stated "[t]he effective state tax rate used in the formula is derived from the North Carolina and South Carolina rates in effect during the calendar year of the FERC Form 1 data."<sup>55</sup> DEP contends that NCEMC has been an active party in DEP's Annual Update review process and never asked whether the tax rate in effect during the calendar year of the FERC Form No. 1 data also was used for tax rate purposes.<sup>56</sup>

22. Even if NCEMC were correct as to the correct corporate income tax rates, DEP argues that the Protocols prohibit refunds beyond the 2016, 2017, and 2018 Annual Updates. According to DEP, the Protocols contain a statute of limitations provision, which provides that errors detected as to a particular year can be remedied only if detected by the first or second subsequent Annual Update.<sup>57</sup> DEP contends that the Commission recognizes and respects statute of limitations provisions in contracts, tariffs, and service agreements, such as the one in DEP's transmission formula rate. While certain exceptions can be made where facts merit, DEP asserts that here DEP would have

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formula inputs where, as here, the formula rate is based on a historical period, and there is nothing in the formula rate allowing adjustments for known and measurable changes. *Id.* at 10 n.16 (citing *Midwest Indep. Transmission Sys. Operator, Inc.*, 131 FERC ¶ 61,173, at PP 6, 7 (2010); *Idaho Power Co.*, 153 FERC ¶ 61,212, at P 33 (2015)).

<sup>54</sup> *Id.* at 23-25. DEP points out that the composite state corporate income tax rates DEP used in 2013 and 2014 are identical even though the North Carolina tax rate dropped on January 1, 2014. To DEP, this means that all customers knew, or were on notice, that DEP used the same North Carolina state corporate income tax rate for the rate period beginning on June 1, 2014, as it did for the one beginning on June 1, 2013. In fact, DEP notes that it would be mathematically impossible for the composite state corporate income tax rate to be above the two individual rates actually in effect as of January 1, 2014, if those tax rates were used. *Id.* at 25-26.

<sup>55</sup> *Id.* at 26 (citing NCEMC Complaint at 25 n.51).

<sup>56</sup> *Id.* at 27 & n.38.

<sup>57</sup> *Id.* at 28-29 (citing Joint OATT, Attachment H.2 (0.0.0), § 3(f)).

provided the composite state corporate income tax rate calculations had anyone asked for them. DEP continues that it answered clearly the question about which corporate income tax rates it was using, and all customers should have been aware of the North Carolina state corporate income tax rate changes.<sup>58</sup> DEP also argues that the statute of limitations provision has been invoked in the past and all parties honored it without challenge.<sup>59</sup>

23. With regard to NCEMC's alternative request that if the Commission finds a change to the filed rate to be necessary, the Commission should find that the filed rate is unjust and unreasonable, DEP asserts that changes to the filed rate pursuant to FPA section 206 are barred by the DEP Rate Moratorium in the 2016 Settlement Agreement. DEP explains that the Joint OATT (i.e., the filed rate) states that "neither DEP nor any Transmission Customer may submit (or lend support to) a filing under Section 205 or 206 of the FPA seeking to change this historical test year methodology" prior to January 1, 2020.<sup>60</sup> DEP believes that use of the prior year's corporate income tax rates is part of the historical test year methodology, such that NCEMC cannot seek to change their use at this time.<sup>61</sup>

24. In any event, DEP argues that NCEMC has failed to demonstrate that the filed rate is unjust and unreasonable because NCEMC merely shows that using the current year corporate income tax rates would produce lower rates for NCEMC in years when tax rates are decreasing. DEP adds that NCEMC provides no evidence that the overall level of DEP's wholesale transmission rates is unjust and unreasonable. On the contrary, DEP contends that its use of a historical test year methodology has lowered its wholesale transmission rates as compared to the use of a current year test year methodology due to DEP's increasing transmission investment. According to DEP, this offsetting of increased and decreased costs is why, generally, the Commission frowns on single-issue ratemaking.<sup>62</sup> DEP further argues that NCEMC was fully aware of DEP's plans to invest

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<sup>58</sup> *Id.* at 30-31 (citing *O'Neil v. Montaup Elec. Co.*, 46 FERC ¶ 61,254 (1989); *Commonwealth Elec. Co. v. Boston Edison Co.*, 47 FERC ¶ 61,118, at 61,350 n.9 (1989); *Exelon Corp. v. PPL Elec. Utils. Corp.*, 111 FERC ¶ 61,065, at P 24 (2005), *order on reh'g*, 114 FERC ¶ 61,298 (2006); *Seminole Elec. Coop., Inc. v. Fla. Power & Light Co.*, 139 FERC ¶ 61,254, at P 43 (2012)).

<sup>59</sup> *Id.* at 31.

<sup>60</sup> *Id.* at 32-33 (quoting Joint OATT, Attachment H.3 (0.0.0), § 1.21).

<sup>61</sup> *Id.* at 33.

<sup>62</sup> *Id.* at 33-35 (citing *Va. Elec. & Power Co.*, 108 FERC ¶ 61,108, at P 11 (2004); *Ne. Utils. Serv. Co.*, 52 FERC ¶ 61,097 (1990), *aff'd sub nom. City of Holyoke Gas &*

in transmission at the time of both the 2008 and 2016 settlements and that the regulatory lag of the historical test year methodology would provide significant benefits to NCEMC. Therefore, DEP avers that it would be inequitable to toss aside the use of the historical test year methodology prior to January 1, 2020.<sup>63</sup> This inequity would be, according to DEP, a violation of the filed rate doctrine and rule against retroactive ratemaking at least with regard to the period from January 1 to May 31, 2018, since NCEMC requested a rate change and refunds on May 31, 2018.<sup>64</sup>

25. Finally, DEP states that NCEMC's Complaint regarding ADIT is premature given the Tax NOI proceeding, which will provide DEP the guidance it needs to appropriately flow back excess ADIT. DEP also asserts that NCEMC's Complaint fails as a matter of law because NCEMC makes no assertion that DEP's treatment of ADIT is inconsistent with the filed rate (or otherwise unjust and unreasonable).<sup>65</sup> DEP states that the full amount of excess ADIT will be flowed back to DEP's wholesale transmission customers regardless of timing, so the "right" to refunds is not related to the refund effective date.<sup>66</sup>

### **B. Customers Comments**

26. Customers agree with NCEMC that DEP has violated and continues to violate the Joint OATT and the principles supporting the Commission's Formula Rates Show Cause Order. Customers reiterate NCEMC's claim that the federal corporate income tax rate is not drawn from FERC Form No. 1 or DEP's books or records, and therefore that the current-year federal corporate income tax rate should be used.<sup>67</sup> Customers contend that DEP cannot carry the burden of proof that the Joint OATT imposes on DEP in

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*Elec. Dep't v. FERC*, 954 F.2d 740 (D.C. Cir. 1992), *order on remand*, 60 FERC ¶ 61,012 (1992)).

<sup>63</sup> *Id.* at 36-40. DEP calculates that over the course of 2009-2019, NCEMC will save about \$12 million as a result of DEP agreeing to the historical test year methodology even with the federal and state corporate income tax rate decreases being put into effect on a lagging basis, just like all other costs. *Id.* at 40.

<sup>64</sup> *Id.* at 40-41 (citing *Old Dominion Elec. Coop. v. FERC*, 892 F.3d 1223 (D.C. Cir. 2018)).

<sup>65</sup> *Id.* at 41 (citing NCEMC Complaint at 8).

<sup>66</sup> *Id.* at 42-43 (citing NCEMC Complaint at 3).

<sup>67</sup> Customers Comments at 4-5 (citing Joint OATT, Attachment H.2 (0.0.0), § 1.g).

responding to a Formal Challenge because using the 35 percent federal corporate income tax rate does not comply with the filed rate.<sup>68</sup>

27. Customers further argue that DEP's interpretation of its transmission formula rate as requiring continued use of the superseded 35 percent federal corporate income tax rate triggers the same policy considerations underlying the Formula Rates Show Cause Order, namely, that use of the prior tax rate will not accurately reflect the utility's cost of service.<sup>69</sup> Customers argue that the distinction between DEP's transmission formula rate and that of Baltimore Gas & Electric Company (BGE), one of the utilities to which the Commission directed the Formula Rates Show Cause Order, is only "superficial." In particular, Customers contend that BGE agreed to use the reduced federal corporate income tax rate based on a notation in its transmission formula rate that stated that the "currently effective income tax rate" is to be used, even though its rate also included the stated value of 35 percent.<sup>70</sup>

28. Customers disagree with DEP that the DEP Rate Moratorium precludes use of the currently effective federal corporate income tax rate. Contrary to DEP's assertions, Customers believe that the reduced federal corporate income tax rate could be reflected in DEP's transmission formula rate without changing the historical test year methodology because the 0.00 percent placeholder confirms that the value is a variable factor.<sup>71</sup> Customers emphasize that the purpose of formula rates is to collect from customers, as accurately as possible, the costs of providing transmission service.<sup>72</sup>

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<sup>68</sup> *Id.* at 5 (citing Joint OATT, Attachment H.2 (0.0.0), § 3.d; *Midcontinent Indep. Sys. Operator, Inc.*, 146 FERC ¶ 61,210, at P 55 (2014)).

<sup>69</sup> *Id.* at 5-6 (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at PP 4, 5).

<sup>70</sup> *Id.* at 6-7 (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at P 5; PJM Interconnection, L.L.C., Intra-PJM Tariffs, OATT, Attachment H-2B (1.1.0), § 2.f; Baltimore Gas & Elec. Co., Response to Show Cause Order, Docket No. EL18-64-000, at 2-3 (filed Mar. 26, 2018)).

<sup>71</sup> *Id.* at 8-10.

<sup>72</sup> *Id.* at 11 (citing *ISO New England Inc.*, 155 FERC ¶ 61,212, at P 24 (2016); *Me. Yankee Atomic Power Co.*, 42 FERC ¶ 61,307, at 61,923 (1988); *PJM Interconnection, L.L.C.*, 110 FERC ¶ 61,053, at 61,255 (2005)).

29. Customers also reiterate NCEMC's arguments regarding DEP's implementation of the reductions in the North Carolina state corporate income tax rate.<sup>73</sup>

**C. Subsequent Answers**

30. NCEMC reasserts that DEP's interpretation of its transmission formula rate is incorrect. NCEMC argues that DEP's position is irreconcilable with the Formula Rates Show Cause Order because DEP is essentially creating a third category of formula rates—one with an input that is adjusted annually, but not until a year and a half after the reduction in the federal corporate income tax rate took effect.<sup>74</sup> NCEMC further claims that the header, "Year Ending 12/31/yyyy," in DEP's transmission formula rate is only a general reference to the requirement that DEP populate its formula based on prior year costs "to the extent the Formula Rate specifies Form 1 data as the input source, and, to the extent specified in the Formula Rate."<sup>75</sup> NCEMC also contends that DEP's argument that if the parties had intended an exception to the historical formula rate methodology, they would have explicitly provided for it, is no more plausible than the argument that if the parties had intended to use the *prior* year tax rate, they would have explicitly provided for it (rather than including a 0.00 percent placeholder).<sup>76</sup>

31. As for DEP's contention that the DEP Rate Moratorium prevents changes to the transmission formula rate, NCEMC responds that it is challenging only how DEP implements one factor in the rate and not the historical nature of the rate.<sup>77</sup> With regard to DEP's argument about the FERC Form No. 1 instructions, NCEMC counters that the fact that those instructions require the utility to calculate tax expense reported on that page using the tax return for the calendar year has no bearing on the allowance for tax expense calculated under the transmission formula rate because the actual prior year tax expense reported in the FERC Form No. 1 does not carry over to the transmission formula rate.<sup>78</sup> NCEMC also notes that the Commission has accepted other utilities' formula rates that combine a historical test year period with a currently effective tax

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<sup>73</sup> *Id.* at 12-13.

<sup>74</sup> NCEMC July 31, 2018 Answer at 3 (quoting Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at P 4).

<sup>75</sup> *Id.* at 4 (quoting Joint OATT, Attachment H.2 (0.0.0), § 1.g.i).

<sup>76</sup> *Id.*

<sup>77</sup> *Id.* at 5.

<sup>78</sup> *Id.* at 6 (citing DEP June 28, 2018 Answer at 15).

rate.<sup>79</sup> As for retroactive ratemaking, NCEMC argues that DEP knew when the Commission issued the Tax NOI and Formula and Stated Rates Show Cause Orders on March 15, 2018, that the Commission was requiring utilities to lower their rates to reflect the reduction in the federal corporate income tax rate.<sup>80</sup> Additionally, NCEMC asserts that its interpretation of DEP's transmission formula rate does not violate Commission policy requiring synchronization because the Commission does not require that all costs in formula rates be synchronized.<sup>81</sup> NCEMC also does not believe that DEP's treatment of state corporate income tax rates established any meaningful course of conduct.<sup>82</sup>

32. NCEMC disagrees with DEP that its alternative section 206 Complaint is barred by the DEP Rate Moratorium because, according to NCEMC, it is not challenging the historical nature of DEP's transmission formula rate, but, rather is challenging the use of the 35 percent federal corporate income tax rate to populate the transmission formula rate. To the extent the Commission finds that a change to the transmission formula rate is needed, NCEMC maintains that it has satisfied its burden because of the significant effect of the reduction in the federal corporate income tax rate on DEP's costs. NCEMC states that the Commission has permitted single-issue ratemaking specifically for changes in the federal corporate income tax rate.<sup>83</sup>

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<sup>79</sup> *Id.* at 7 (citing PJM Interconnection, L.L.C., Intra-PJM Tariffs, OATT, Attachment H-22A (3.0.0), at 5 Note K; *PJM Interconnection, L.L.C.*, 139 FERC ¶ 61,068 (2012), *order rejecting settlement*, 144 FERC ¶ 61,217 (2013)).

<sup>80</sup> *Id.* at 7-8 (citing *Pub. Utils. Comm'n of Ca. v. FERC*, 988 F.2d 154, 164 (D.C. Cir. 1993)).

<sup>81</sup> *Id.* at 8-9 (citing Joint OATT, Sched. 10-B, Attachment B (0.0.0), §§ 2.f, 2.g; Duke Energy Ohio, Inc. & Duke Energy Ky., Inc., Tariff Filing, Docket No. ER18-1274-000, Attachment F, Ex. DOK-1, at 4 (filed Apr. 2, 2018); San Diego Gas & Elec. Co., Response to Show Cause Order, Docket No. EL18-67-000 (filed May 14, 2018)).

<sup>82</sup> *Id.* at 11-12.

<sup>83</sup> *Id.* at 12-15 (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at P 5 n.10; Stated Rates Show Cause Order, 162 FERC ¶ 61,224 at P 4 n.6; *Promoting Transmission Investment through Pricing Reform*, Order No. 679, 116 FERC ¶ 61,057, at P 29 (2006), *order on reh'g*, Order No. 679-A, 117 FERC ¶ 61,345 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007); *Carolina Power & Light Co.*, 149 FERC ¶ 61,266 (2014); Duke Energy Progress, LLC, Tariff Filing, Docket No. ER17-2439-000 (filed Sept. 5, 2017)).

33. NCEMC also disagrees with DEP that NCEMC's challenges to the 2013-2015 Annual Updates are prohibited by the statute of limitations provision in the 2016 Settlement Agreement. NCEMC interprets the statute of limitations provision as preserving the right to pursue a formal challenge so long as any challenge (including a preliminary challenge) has been submitted, noting that NCEMC submitted preliminary challenges to all of the relevant DEP Annual Updates.<sup>84</sup>

34. Finally, with regard to ADIT, NCEMC asserts that its Complaint is not premature. NCEMC notes that Virginia Electric and Power Company (VEPCO) previously sought to amend its transmission formula rate to provide for the flow-back of excess ADIT resulting from the reductions in the North Carolina state corporate income tax rate.<sup>85</sup> NCEMC disagrees that changes to DEP's transmission formula rate are necessary, but to the extent the Commission determines otherwise, NCEMC requests that the Commission require such changes and establish a refund effective date. NCEMC acknowledges the pendency of the Tax NOI proceeding, but asserts that the Commission has the authority to provide a remedy even when an issue is pending elsewhere.<sup>86</sup>

35. In response to Customers, DEP contends that FERC has rejected utilities' attempts to make out-of-test-year adjustments, and the same policy should apply to customers trying to do the same.<sup>87</sup> DEP reiterates that the 0.00 percent placeholder is the equivalent of a blank, and that the corporate income tax rates in effect during the historical test year should be filled using those rates.<sup>88</sup> Additionally, DEP asserts that the corporate income tax rates *are* taken from DEP's books and records, namely, from its tax returns.<sup>89</sup> DEP further argues that the Commission's inaction as to DEP's transmission formula rate is consistent with the Commission's overall approach in the Formula Rates Show Cause

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<sup>84</sup> *Id.* at 17-19 (citing Joint OATT, Attachment H.2 (0.0.0), § 3.f; *Midcontinent Indep. Sys. Operator, Inc.*, 150 FERC ¶ 61,025, at P 49 (2015)).

<sup>85</sup> *Id.* at 19 (citing Va. Elec. & Power Co., Tariff Filing, Docket No. ER16-2116-000, at 3-6 (filed July 1, 2016)).

<sup>86</sup> *Id.* at 20-22 (citing *Indianapolis Power & Light Co. v. Midcontinent Indep. Sys. Operator, Inc.*, 162 FERC ¶ 61,266, at PP 46-48 (2018)).

<sup>87</sup> DEP July 16, 2018 Answer at 2 (citing *Idaho Power Co.*, 153 FERC ¶ 61,212 at P 33).

<sup>88</sup> *Id.* at 3-4 (citing Joint OATT, Attach. H.3 (0.0.0), § 1.21).

<sup>89</sup> *Id.* at 4.

Order because the 35 percent federal corporate income tax rate is not fixed in DEP's transmission formula rate.<sup>90</sup>

36. Moreover, DEP disagrees with Customers that its transmission formula rate is analogous to that of BGE. DEP states that BGE's formula rate specifies that the formula should be populated using "[t]he currently effective income tax rate."<sup>91</sup> In addition, DEP explains that BGE prepares a projection of its future costs based on FERC Form No. 1 data and new transmission additions that have gone or will go into service in the current year, subject to a true-up.<sup>92</sup> Finally, DEP disputes the purpose of formula rates as described by Customers, arguing instead that the purpose of formula rates with historic test years and no true-up mechanism is to collect the cost of service for the historic test year, and not the current rate year.<sup>93</sup>

37. In response to NCEMC's answer, DEP claims that the income taxes included in the 2017 historic test year cost of service used to determine wholesale transmission rates for June 1, 2018, to May 31, 2019, represent DEP's actual income taxes for the 2017 test year; therefore, DEP is not receiving any windfall.<sup>94</sup> With regard to the Formula Rates Show Cause Order, DEP states that the Commission made no statement regarding *when* the reduced federal corporate income tax rate would be reflected in any particular

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<sup>90</sup> *Id.* at 5-6. DEP points to Idaho Power Company as an example of another utility that uses a historical test year methodology with no true-up that was not included in the Formula Rates Show Cause Order and used the 35 percent federal corporate income tax rate in its 2018-2019 rate year informational filing. *Id.* at 6 (citing *Idaho Power Co.*, 153 FERC ¶ 61,212 at P 15). DEP notes that Idaho Power's rate year starts October 1, 2018, so it will be even longer before the reduced federal corporate income tax rate is reflected in Idaho Power's wholesale transmission rates than in DEP's. DEP July 30, 2018 Answer at 3 & n.5.

<sup>91</sup> DEP July 16, 2018 Answer at 6-7 (citing Baltimore Gas & Elec. Co., Response to Show Cause Order, Docket No. EL18-64-000, at 2 (filed Mar. 26, 2018)).

<sup>92</sup> *Id.* at 7-8 (citing Baltimore Gas & Elec. Co., et al., Tariff Filing, Docket No. ER05-515-000, at 2-3 (filed Jan. 31, 2005); *Baltimore Gas & Elec. Co.*, 115 FERC ¶ 61,066 (2006)).

<sup>93</sup> *Id.* at 8-10 (noting that in *Idaho Power Co.*, 153 FERC ¶ 61,212 at P 32, the Commission found important the fact that the utility agreed to a backward-looking rate in settlement proceedings).

<sup>94</sup> DEP July 30, 2018 Answer at 2.

transmission formula rate, but just that it would occur automatically for some rates.<sup>95</sup> DEP notes that while certain of its affiliates began using the 21 percent federal corporate income tax rate at an earlier date, the formula rates of those affiliates either specifically provided for the use of the currently effective federal corporate income tax rate or included a true-up mechanism.<sup>96</sup> Moreover, DEP claims that NCEMC's interpretation of the statute of limitations clause would prevent final resolution of the Annual Update process and encourage parties to keep the Annual Updates open in perpetuity simply by submitting a preliminary challenge on any issue.<sup>97</sup>

38. Responding to DEP's answer to Customers, NCEMPA (one of the Customers) asserts that DEP's "course of conduct" argument is at odds with the Protocols because the Protocols expressly provide that a party's failure to challenge DEP's treatment of an item in any particular Annual Update has no effect on its right to raise that same issue in connection with any later Annual Update.<sup>98</sup>

#### **IV. Commission Determination**

##### **A. Procedural Matters**

39. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,<sup>99</sup> the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

40. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure prohibits an answer to a protest and/or answer unless otherwise ordered by the decisional authority.<sup>100</sup>

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<sup>95</sup> *Id.* at 2-3 (citing Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at PP 4, 6).

<sup>96</sup> *Id.* at 3-4.

<sup>97</sup> *Id.* at 6, 8 (noting that this interpretation would also create the perverse incentive for DEP to never resolve any preliminary challenges informally because doing so would mean the Annual Update is never final).

<sup>98</sup> NCEMPA July 31, 2018 Answer at 3 (citing Joint OATT, Attachment H.2 (0.0.0), § 2.f).

<sup>99</sup> 18 C.F.R. § 385.214 (2018).

<sup>100</sup> *Id.* § 385.213(a)(2).

We will accept NCEMC's, DEP's, and NCEMPA's answers because they have provided information that assisted us in our decision-making process.

41. Rule 508(d) allows the Commission to “take official notice of any matter that may be judicially noticed by the courts of the United States.”<sup>101</sup> We will grant NCEMC's motion to lodge the North Carolina Utilities Commission order.

## **B. Substantive Matters**

42. As discussed below, we deny NCEMC's Formal Challenge and Complaint. We find that DEP correctly applied its historical test year methodology in the 2018 Annual Update. The reduction in the federal corporate income tax rate took effect on January 1, 2018. The 2018 Annual Update was properly based on 2017 costs, including the 35 percent federal corporate income tax rate in effect in 2017. We also deny the Formal Challenge and Complaint as to the period January 1, 2018, to May 31, 2018, for the same reasons. With regard to the reductions in the North Carolina state corporate income tax rate that took effect on January 1, 2014, and thereafter, we find that DEP should have incorporated those reductions in the same manner as the reduction in the federal corporate income tax rate and there is no evidence that DEP did not do so. Finally, we deny the Complaint as to the excess ADIT issue because NCEMC has failed to meet its burden to show that the Joint OATT is unjust and unreasonable in its treatment of ADIT.

43. We deny the Formal Challenge and Complaint with regard to the federal corporate income tax rate used in the 2018 Annual Update (for the period June 1, 2018, through May 31, 2019), as well as to the period January 1, 2018, to May 31, 2018. Consistent with the historical test year methodology contained in DEP's filed transmission formula rate, we find that DEP correctly used the federal corporate income tax rate in effect in 2017 in preparing the 2018 Annual Update, and appropriately did not adjust its January 1, 2018, to May 31, 2018 wholesale transmission rates to reflect the reduction in the federal corporate income tax rate that took effect on January 1, 2018. Neither DEP's transmission formula rate nor the Protocols provide a fixed federal corporate income tax rate. Rather, the line item in the transmission formula rate for the federal corporate income tax rate includes a 0.00 percent placeholder.<sup>102</sup> It is clear, however, that DEP's

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<sup>101</sup> *Id.* § 385.508(d); *see also Elec. Power Supply Ass'n v. AEP Generation Res., Inc.*, 155 FERC ¶ 61,102, at P 54 & n.84 (citing *Nevada Power Co. v. Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶ 61,047, at 61,193, *order on reh'g*, 100 FERC ¶ 61,273 (2002)).

<sup>102</sup> Joint OATT, Attachment H.1 (12.0.0), Ex. DEP-2 at 3, line 25. While NCEMC explains that the spreadsheet DEP uses to populate its transmission formula rate includes an instruction that states, “[l]eave this number [the federal corporate income tax rate] as 35% in order for the calculation of the composite rate in cell F51 [the composite state

transmission formula rate uses a “historical test year without a true-up based on actual costs . . . (i.e., rates that change each June 1 based on the immediately preceding year’s cost of service, calculated using end-of-year balances).”<sup>103</sup>

44. The Commission generally requires that formula rate inputs be calculated on a synchronized basis over the same test period, such that DEP’s use of a historical formula rate methodology generally dictates that DEP use the federal corporate income tax rate in effect during the historical test year period, absent a contrary statement in the filed rate.<sup>104</sup> This synchronization requirement, and the Commission’s related reluctance to permit selective post-test period adjustments,<sup>105</sup> protects both utilities and their customers by preventing either from selectively choosing which inputs should come from which time period to one party’s exclusive benefit.<sup>106</sup> This is particularly important where the

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corporate income tax rate] to work correctly,” this instruction is not part of the filed rate and does not fix the federal corporate income tax rate at 35 percent. NCEMC Complaint at 5-6.

<sup>103</sup> Joint OATT, Attachment H.3 (0.0.0), § 1.21.

<sup>104</sup> See, e.g., *Ameren Ill. Co.*, 163 FERC ¶ 61,200 at P 4 (citations omitted) (noting “the Commission’s requirement that all rate base components and expenses in rates be calculated on a synchronized basis over the same test period”); *Westar Energy, Inc.*, 122 FERC ¶ 61,268 at P 98 (citations omitted) (“Under Commission policy, companies must use a fully-synchronized test period cost-of-service study that uses either an historical test period or a projected test period.”); *Metropolitan Edison Co.*, 44 FERC at 61,146 (“Under Commission ratemaking procedures for developing wholesale cost of service, all test year expenses and revenues, including an allowance for income taxes associated with such revenues, are synchronized.”).

<sup>105</sup> E.g., *Alamito Co.*, 39 FERC ¶ 61,231, at 61,812 (refusing to require utility to reflect lowered federal corporate income tax rate in its formula rate during the rate year and accepting use of blended rate until beginning of the next rate year), *order on reh’g & clarification*, 41 FERC ¶ 61,312 (1987); *Pub. Serv. Co. of N.M.*, Opinion No. 73, 10 FERC ¶ 61,053, at 61,121-23 (1980) (concluding that it is not proper to adjust the test period cost-of-service data in a cost-of-service rate proceeding to reflect post-test year changes in the federal corporate income tax rates).

<sup>106</sup> See *Idaho Power Co.*, 153 FERC ¶ 61,212 at P 33 (“Allowing Idaho Power to continue to use a historic formula rate methodology for recovering all its other expenses, with the certainty and protections that provides to Idaho Power, while allowing it to deviate from the prescribed methodology in this one instance would favor Idaho Power’s interests over that of its customers.”).

formula rate at issue was the product of a negotiated settlement between the utility and its customers, as is the case with DEP's transmission formula rate.<sup>107</sup> In fact, DEP's use of a historical test year without a true-up based on actual costs is the product of multiple settlements between DEP and its customers (including NCEMC), the last of which was entered into in 2016, and provides that the historical test year methodology "shall not be subject to change during the period January 1, 2016 through December 31, 2019" (i.e., the DEP Rate Moratorium).<sup>108</sup>

45. While NCEMC is correct that the Commission has authorized rates that use both historical test year data and current year data, the Commission considers such proposals on a case-by-case basis and those transmission formula rates must clearly state the source for each input that differs from the general formula rate methodology used. For example, NCEMC cites to Duke Energy Carolinas, LLC (DEC), which employs both historical and projected costs.<sup>109</sup> However, DEC's transmission formula rate specifically indicates which costs come from the historical test year and which do not. In addition, unlike DEP's transmission formula rate, DEC's transmission formula rate includes a true-up mechanism.<sup>110</sup> NCEMC also points to Duke Energy Ohio, Inc. and Duke Energy Kentucky, Inc.'s transmission formula rate, which generally employs a historical test year methodology, but which also uses the current year federal corporate income tax rate; however, that transmission formula rate, unlike DEP's, explicitly provides that the utility use the "currently effective income tax rate."<sup>111</sup> Therefore, NCEMC's examples are inapt and only highlight that the Commission has exercised its discretion in accepting formula

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<sup>107</sup> *See id.* ("Idaho Power's Formula Rate, for which it sought and obtained Commission approval, was the product of negotiations among the parties wherein they reached agreement on a comprehensive methodology that would be the sole means by which Idaho Power would recover its costs.").

<sup>108</sup> Joint OATT, Attachment H.3 (0.0.0), § 1.21; *see also* NCEMC, Comments in Support of Settlement Agreement, Docket No. EL16-30-00, at 3 (filed Sept. 8, 2016) ("NCEMC believes that the Settlement Agreement is fair and reasonable and promotes the public interest because it provides substantial benefits to all wholesale transmission customers on the DEC and DEP transmission systems in the form of lower rates and certainty regarding the affected elements of DEC's and DEP's transmission rates for a three-year period.").

<sup>109</sup> NCEMC July 13, 2018 Answer at 8.

<sup>110</sup> Joint OATT, Sched. 10-B, Ex. A (0.0.0), §§ 2.f, 2.g.

<sup>111</sup> PJM Interconnection, L.L.C., Intra-PJM Tariffs, OATT, Attachment H-22A (3.0.0), at 5 Note K.

rates that recognize unique circumstances, while still generally hewing to the synchronization requirement.<sup>112</sup>

46. We are not persuaded by NCEMC's argument that, because DEP's transmission formula rate does not explicitly require the use of the prior year's federal corporate income tax rate and does not specify FERC Form No. 1 data or DEP's books and records as the input source for the federal corporate income tax rate, DEP is obliged to use the federal corporate income tax rate in effect during the rate period.<sup>113</sup> As discussed above, unless the formula rate provides otherwise, the Commission generally requires synchronization of formula rate inputs, meaning that the lack of an explicit requirement in DEP's transmission formula rate one way or the other on the correct federal corporate income tax rate favors use of the prior year rate consistent with the historical test year methodology.

47. As for the Formula Rates Show Cause Order, there, in explaining how adjustments in formula rates usually occur, the Commission noted that "[f]or formula rates with inputs that are adjusted annually, the current 21 percent federal corporate income tax rate will be reflected in a transmission revenue requirement without requiring a revision to the formula rate."<sup>114</sup> The Commission did not speak to the timing for the reduced federal corporate income tax rate to be reflected in transmission formula rates with inputs that are adjusted annually. Consistent with the understanding of annually adjusted formula rates noted in the Formula Rates Show Cause Order, DEP properly states that the lower federal corporate income tax rate will be reflected in the 2019 Annual Update, as dictated by the filed rate.<sup>115</sup>

48. We also deny the Formal Challenge and Complaint with regard to the reductions in the North Carolina state corporate income tax rate that took effect on January 1, 2014, and thereafter. The discussion above concerning appropriate timing for reflecting the

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<sup>112</sup> Note that DEP's transmission formula rate includes an exception to the historical test year methodology, but explicitly provides for that exception in the filed rate: "The Formula Rate shall include the end-of-year balances from DEP's FERC Form No. 1 reports for the rate base items (other than Cash Working Capital) included in the Formula Rate." Joint OATT, Attachment H.3 (0.0.0), § 1.1; DEP June 28, 2018 Answer at 18.

<sup>113</sup> NCEMC Complaint at 12-15 (citing Joint OATT, Attachment H.2 (0.0.0), § 1.g.i).

<sup>114</sup> Formula Rates Show Cause Order, 162 FERC ¶ 61,225 at P 4.

<sup>115</sup> DEP June 28, 2018 Answer at 11-12.

reduction in the federal corporate income tax rate applies with equal force to the reductions in the North Carolina state corporate income tax rate. We find that DEP should have incorporated those reductions in the same manner as the reduction in the federal corporate income tax rate—that is, by reflecting the reduced corporate income tax rates in the historical test year in which they occurred—and there is no evidence that DEP failed to do so. In fact, DEP states that, in its 2014-2017 Annual Updates, DEP calculated its annual transmission revenue requirement using composite state corporate income tax rates that reflected the tax rates for the immediately preceding year, as required by the filed rate.<sup>116</sup>

49. We also deny NCEMC's Complaint as to the excess ADIT issue because NCEMC has failed to meet its burden to show that the Joint OATT is unjust and unreasonable in its treatment of ADIT. NCEMC itself does not believe that changes to DEP's transmission formula rate are necessary to flow back excess ADIT to DEP's wholesale transmission customers,<sup>117</sup> and NCEMC makes no claim that DEP has failed to flow back the excess ADIT that resulted from the reduction in the federal corporate income tax rate. Rather, NCEMC focuses on the potential need for a refund effective date *if* DEP's transmission formula rate does not already provide for the flow back of excess ADIT to its wholesale transmission customers.<sup>118</sup> NCEMC's effort falls short of the burden imposed on complainants pursuant to section 206 of the FPA because NCEMC does not even allege that DEP's transmission formula rate or DEP's practices thereunder are unjust, unreasonable, unduly discriminatory, or preferential.<sup>119</sup> We also note that DEP states that the full amount of excess ADIT will be flowed back to DEP's wholesale transmission customers regardless of timing,<sup>120</sup> which would be consistent with the Commission's pending ADIT NOPR.<sup>121</sup>

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<sup>116</sup> *Id.* at 23-25.

<sup>117</sup> NCEMC July 13, 2018 Answer at 19; *see also* NCEMC Complaint at 29 (citing Joint OATT, Attachment H.1 (12.0.0), Ex. DEP-2 at 2, lines 19-21).

<sup>118</sup> *E.g.*, NCEMC Complaint at 9, 32.

<sup>119</sup> *See* 16 U.S.C. § 824e(b) (2012) (“[T]he burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon . . . the complainant.”).

<sup>120</sup> DEP June 28, 2018 Answer at 43.

<sup>121</sup> *See, e.g.*, ADIT NOPR, 165 FERC ¶ 61,117 at P 39 (“[T]he full regulatory liability for excess ADIT should be captured in rates, beginning on the effective date of any proposed tariff provision.”).

The Commission orders:

The Formal Challenge and Complaint are hereby denied, as discussed in the body of this order.

By the Commission. Commissioner McNamee is not participating.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.