

**STATE OF NORTH CAROLINA  
UTILITIES COMMISSION  
RALEIGH  
DOCKET NO. M-100, Sub 138**

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	)	
Implementation of House Bill 998 – An Act	)	ATTORNEY GENERAL’S
To Simplify the North Carolina Tax Structure	)	NOTICE OF APPEAL
And to Reduce Individual and Business Tax	)	
Rates	)	

NOW COMES the North Carolina Attorney General (the “Attorney General”), pursuant to N.C. Gen. Stat. § 7A-29(a), § 62-90 et al., and Rule 18 of the North Carolina Rules of Appellate Procedure, and gives Notice of Appeal to the North Carolina Court of Appeals from the 9 October 2014 Order Affirming Dominion North Carolina Power’s and Public Service Company of North Carolina, Inc.’s Exceptions (the “October 9 Order”) issued by the North Carolina Utilities Commission (the “Commission”) in the above-captioned proceeding.

The Commission initiated this rulemaking in order to address the effect on utility costs and utility bills arising from changes to state tax laws made by North Carolina House Session Law 2013-313 – An Act to Simplify the North Carolina Tax Structure and to Reduce Individual and Business Tax Rates (referred to by the Commission as “HB 998”). One issue addressed in this rulemaking was whether utilities should be required to adjust their rates to pass through reductions made by HB 998 to the state corporate income tax for utilities, in the absence of any express mandate in HB 998 that these tax reductions be reflected in rates. The Attorney General contended, among other things, that the Commission should consider the tax changes enacted by the General Assembly

via HB 998 in totality with an eye towards consumers receiving the maximum benefit of any such changes because the Commission has the legal authority to require utilities to pass through reductions in taxes to consumers via rate changes even in the absence of an express mandate in HB 998. On 13 May 2014, after hearing from interested parties, the Commission issued an initial Order Addressing the Impacts of HB 998 on North Carolina Public Utilities (the “May 13 Order”). The May 13 Order states: “[T]he Commission has the authority to reduce utility rates to reflect income tax rate changes in a rulemaking pursuant to the Court’s holding in [*State ex rel. Utilities Com’n v. Nantahala Power & Light Co.*, 326 N.C. 190, 388 S.E.2d 118 (1990) (“*Nantahala*”)]. May 13 Order at p. 23. The May 13 Order concluded, among other things, that HB 998 should be viewed in its totality and the corresponding changes in utility rates should comprehensively reflect the full intent of the changes effectuated by HB 998, including the reductions to the state income tax rate for utilities. *Id.* at pp. 24-25. One Commissioner dissented, opining, among other things, that the Commission did not have the authority in the rulemaking proceeding to order that the reductions to the state income tax be reflected in rates. May 13 Order at dissent pp. 1-11.

On 10 July 2014, two utilities -- Dominion North Carolina Power (DNCP) and Public Service Company of North Carolina Inc. (PSNC) (together, “joint movants”) -- filed a Notice of Appeal, Motion for Reconsideration, and Request to Stay Corporate Income Tax Rate Adjustment Pending Reconsideration and set forth exceptions to the May 13 Order, making arguments regarding the

Commission's authority similar to those described in the May 13 dissent. Among other things, the joint movants contended that the changes to the state corporate income tax effectuated in HB 998 could only be addressed by the Commission in utility-specific rate cases, not in this rulemaking proceeding.

Three months later, without prior notice or further hearing, the Commission, in a 4-3 decision, issued its October 9 Order, "affirming" the exceptions filed by the joint movants and reversing the initial May 13 Order with respect to the rate adjustments required to reflect the changes to the state corporate income tax. Although the Order expressed sympathy for the view that utility rates should be reduced in order to flow through the reduction in utility costs associated with the state corporate income tax reductions, it stated that the Commission lacked the legal authority to do so, contradicting the prior statement made in its May 13 Order regarding its legal authority. Accordingly, rate adjustments were ordered in the rulemaking to effectuate some tax increases but *not* the offsetting effect of the reduction in the state corporate income tax. In other words, utility shareholders were allowed to pocket the cost savings associated with the reduced state corporate income taxes while most customer bills increased from the combined effect of the other tax changes.<sup>1</sup> The October 9 Order contains a Dissent by 3 Commissioners, opining that the Order's decision is legally erroneous, substantively and procedurally, and fails to provide for the fair regulation of public utilities in the interest of the public.

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<sup>1</sup> Note that the Majority decision gave utilities the option to go forward with plans to adjust rates reflecting the state corporate income tax reduction as ordered in the Initial HB 998 Order, and DNCP (the North Carolina subsidiary of a holding company based in Virginia) is the only utility that has indicated it will decline to pass along the state corporate income tax savings to ratepayers.

Pursuant to N.C. Gen. Stat. § 62-90(a), the Attorney General identifies the exceptions and the grounds on which the October 9 Order is considered to be legally erroneous, unlawful, arbitrary and capricious, unconstitutional, unwarranted, and prejudicial.

EXCEPTION NO. 1:

The October 9 Order erroneously declines to adjust rates to reflect the changes in the state corporate income tax based on the arbitrary, capricious, and erroneous conclusion that the Commission lacked the legal authority to do so. See, e.g., *Nantahala*, 326 N.C. 190, 388 S.E.2d 118 (holding Commission has authority to order rate adjustments due to legislative changes regarding corporate taxes); *State ex rel. Utils Com'n v. Edmisten*, 294 N.C. 598, 242 S.E.2d 862 (1978). The Order's conclusion in this regard constitutes reversible error.

When a trial court has failed to exercise its discretion regarding a discretionary matter and has ruled on it under the mistaken impression it is required to rule a particular way as a matter of law, its holding must be reversed and the matter remanded for the trial court to exercise its discretion.

*Lemons v. Old Hickory Council, Boy Scouts, Inc.*, 322 N.C. 271, 277, 367 S.E.2d 655, 658 (1988); see also *State v. Cotton*, 318 N.C. 663, 668, 351 S.E.2d 277, 280 (1987); 1-1 Brandis and Broun on North Carolina Evidence § 20 (2014).

The October 9 Order is also arbitrary, capricious, and legally erroneous by concluding that our Supreme Court's legal reasoning in *Nantahala* was flawed and by failing to follow the holding and reasoning of that case. See October 9 Order at p. 21, note 14. The Commission's decisions must follow appellate

decisions of our Supreme Court, not vice versa. See, e.g., N.C. Gen. Stat. §§ 62-90; 62-94.

The October 9 Order is also arbitrary, capricious, and legally erroneous by erroneously interpreting *Nantahala*, including but not limited to its erroneous interpretation that *Nantahala* requires that the impact of a tax change must meet a threshold amount before it is permissible for the Commission to address a tax change in a rulemaking procedure. Likewise, the October 9 Order is arbitrary, capricious, and legally erroneous in its conclusion that the concern posed by single-issue ratemaking is increased rather than diminished if all of the tax changes in HB 998 -- rather than just some of the tax changes -- are addressed in the rulemaking procedure. Similarly, the October 9 Order is arbitrary, capricious, and legally erroneous when it erroneously distinguishes *Nantahala* from the matter at hand and concludes that it does not apply. In addition, the October 9 Order's interpretation of HB 998 is arbitrary, capricious, and legally erroneous.

The October 9 Order's decision reflects a failure to exercise authority based on an erroneous legal conclusion regarding that authority, as opposed to being a decision that simply reflects a discretionary determination not to exercise the Commission's authority. The October 9 Order makes this clear when it states: "When state corporate income tax rates are reduced and where it is legally permissible to do so, utility rates should be reduced to flow through this reduction in utility costs." October 9 Order at p. 22. For the reasons stated above, the October 9 Order is erroneous, unlawful, arbitrary and capricious,

unjust, unreasonable, unwarranted and prejudicial because, among other things, it fails to adjust utility rates to flow through the reduction in utility costs associated with the state corporate income tax rate reduction based on a legally erroneous interpretation of the Commission's authority.

EXCEPTION NO. 2:

The October 9 Order also violates the legal principle that Commission rules must provide for "fair" regulation of utilities. The decision *not* to flow through the effect of the reduction in state corporate income taxes was unfair to consumers, as that adjustment would have mitigated the increase that most consumers have experienced due to the rate increases associated with other changes in taxes made by HB 998. By failing to exercise its discretion to address *all* effects of HB 998 in the rate adjustments ordered in this rulemaking, the October 9 Order violated the "number one" policy that the Commission is to carry out through the exercise of its rulemaking power, which is "[t]o provide fair regulation of public utilities in the interest of the public." *See, e.g., Nantahala*, 326 N.C. at 196, 388 S.E.2d at 122; N.C. Gen. Stat. § 62-2(1). Thus, the October 9 Order is unjust, unreasonable, unwarranted and prejudicial for failing to adopt a rule that provides for fair regulation.

EXCEPTION NO. 3:

By reversing and rescinding initial decisions made in its May 13 Order, without proper notice and without providing a proper opportunity for hearing, briefing, or opportunity to be heard, the October 9 Order is arbitrary and capricious, unconstitutional, in violation of due process, and in violation of

pertinent statutory procedural requirements contained in N.C. Gen. Stat. § 62-80 and § 62-90 as interpreted by our courts, unfairly prejudicing certain parties.

Likewise, by reversing and rescinding initial decisions made in its May 13 Order, without a proper change of circumstances requiring it for the public interest, the October 9 Order is arbitrary and capricious, unconstitutional, in violation of due process, and in violation of the law. The October 9 Order reaches different conclusions under the exact same legal and factual record and circumstances existent when the May 13 Order was decided. This renders the October 9 Order arbitrary and capricious, unconstitutional, and legally erroneous.

Accordingly, for the reasons stated above, the October 9 Order is legally erroneous, affected by errors of law, made upon unlawful proceedings, in excess of statutory authority, arbitrary, capricious, and unconstitutional.

Respectfully submitted, this the 8<sup>th</sup> day of December, 2014.

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**CERTIFICATE OF SERVICE**

The undersigned certifies that she has served a copy of the foregoing ATTORNEY GENERAL'S NOTICE OF APPEAL upon the parties of record in this proceeding and their attorneys by electronic mail or by U.S. mail.

This the 8th day of December, 2014.

/s/ Margaret A. Force  
Margaret A. Force  
Assistant Attorney General