

1 **Q. Are there concerns aside from those you have already addressed that warrant the**
2 **imposition of additional conditions?**

3 A. Yes. The Public Staff is concerned that the merger might reduce this Commission's ability to
4 regulate CP&L in ways that protect the interests of North Carolina ratepayers. A very
5 important example is CP&L's and Florida Power's plan to integrate their power supply
6 resources through their proposed FERC-jurisdictional System Integration Agreement
7 (Integration Agreement), which was filed with the FERC merger application. According to the
8 agreement, its purpose is to provide the contractual basis for integrating CP&L's and Florida
9 Power's power supply resources, including the coordinated planning, operation, and
10 maintenance of the combined resources, and the achievement of economies consistent with the
11 provision of reliable electric service and an equitable sharing of the benefits and costs of such
12 coordinated arrangements. It provides for numerous potential amendments and modifications,
13 as well as for the filing of separate agreements and service schedules in the future.

14
15 According to testimony filed at the FERC, CP&L and Florida Power will jointly plan future
16 generating facilities, coordinate the dispatch of their respective power plants and centralize fuel
17 supply and plant maintenance programs, among other things. To accomplish these ends, the
18 Integration Agreement provides for the establishment of an Operating Committee to administer
19 the agreement, oversee the operation of the two utility's power supply resources, review the
20 allocation of costs and benefits, evaluate the need for future capacity additions, and coordinate
21 the activities of a designated Agent or Agents. Together, the Agent(s) and the Operating
22 Committee will determine, among other things, whether generating resources should be added;
23 if they should be added, who should build them and where; and whether the two utilities should
24 buy from one another pursuant to one of the service schedules attached to the Integration
25 Agreement or from others.

26
27 The Agent also will coordinate trading and marketing activities. Both utilities are required to
28 communicate potential trade opportunities to the Agent and assist the Agent in facilitating
29 transactions (subject to code of conduct restrictions). The Agent has numerous duties with

1 respect to the allocations of costs (between and among wholesale transactions and the two
2 utilities' native loads, for example) and the allocations of earnings (from off-system sales, for
3 example).

4
5 I have been advised by Counsel that the Integration Agreement raises three potential
6 preemption problems, two within the context of current regulation and the third at the onset of
7 retail competition. These are as follows:

- 8
- 9 (1) Under current regulation, CP&L's ratepayers could be forced
10 to pay higher costs or receive less revenues (reduced credits to
11 the revenue requirement from wholesale transactions, for
12 example), if the threat of preemption chills state action or if a
13 court were to rule that the NCUC is preempted;
 - 14
15 (2) Also under current regulation, the NCUC's ability to fulfill its
16 obligations with respect to generation expansion, least cost
17 integrated resource planning, and the adequacy of service could
18 be diminished by claims of or findings with respect to
19 preemption; and
 - 20
21 (3) At the outset of retail competition, when retail stranded costs
22 are being determined and decisions are being made about
23 functional or actual divestiture, utility assertions of and findings
24 with respect to preemption could negatively influence and affect
25 decision-making
- 26

27 Accordingly, the Public Staff has developed a series of conditions which will protect the
28 NCUC's traditional regulatory jurisdiction over CP&L from claims and findings of preemption
29 by FERC:

30
31 The proposed merger of CP&L Energy, Inc., and Florida Progress
32 Corporation and the resulting participation of Carolina Power & Light
33 Company (CP&L) in the proposed System Integration Agreement filed
34 with the Federal Energy Regulatory Commission (FERC) as part of the

1 FERC merger application may adversely affect the NCUC's traditional
2 regulatory authority over CP&L because of the potentially preemptive
3 relationship between the Federal Power Act (FPA) and state law. The
4 following requirements and procedures are intended to protect the
5 NCUC's jurisdiction in that event:
6

- 7 (a) CP&L and/or CP&L Energy shall amend the proposed
8 System Integration Agreement Between Carolina
9 Power & Light Company and Florida Power
10 Corporation (Integration Agreement) filed with the
11 FERC merger application of CP&L Holdings, Inc.
12 (now CP&L Energy), and Florida Progress
13 Corporation on behalf of their public utility subsidiaries,
14 to provide the following:
15
- 16 (i) CP&L's participation in this agreement is voluntary, and CP&L
17 is not obligated to make any purchases or sales pursuant to this
18 agreement; and
 - 19 (ii) CP&L may not make or incur a charge under this agreement
20 except in accordance with North Carolina law and the rules,
21 regulations and orders of the NCUC promulgated thereunder.
22
- 23

24 *If the Integration Agreement has been approved (or accepted for filing) by the*
25 *FERC prior to CP&L having an opportunity to amend it as provided above, then*
26 *CP&L and/or CP&L Energy shall promptly make a filing with the FERC seeking*
27 *an order approving or accepting the Integration Agreement amended as set forth*
28 *above.*
29

- 30 (b) All future FERC-jurisdictional agreements, service schedules
31 and similar arrangements entered into pursuant to the
32 Integration Agreement (or comparable agreements) and filed
33 with the FERC, (a) to which CP&L is a party or (b) which can
34 affect CP&L's costs and revenues, either directly or indirectly
35 through allocation, shall contain the language set forth in
36 subsection (a)(I) and (ii) above.
37
- 38 (c) CP&L and CP&L Energy shall request that the following
39 language be included in any order issued by the FERC
40 approving or accepting a FERC-jurisdictional agreement and/or
41 service schedule entered into pursuant to the Integration

1 Agreement (or comparable agreement) to which CP&L or any
2 Affiliate thereof is a party:

3
4 Approval or acceptance of this agreement and/or service schedule in no
5 way precludes the North Carolina Utilities Commission from
6 scrutinizing and disallowing charges incurred or made or allowing or
7 imputing a different level of such charges when setting retail rates for
8 services rendered to customers of affiliated public utilities in North
9 Carolina.

- 10
11 (d) CP&L shall certify to the NCUC that neither CP&L, CP&L
12 Energy, nor any Affiliate thereof has made any filing with the
13 FERC inconsistent with the foregoing. The first such
14 certification shall be made no later than #_____ and shall be
15 repeated annually thereafter on the anniversary of the first
16 certification.

17
18 With respect to any transfer by a Utility of the control of, operational
19 responsibilities for, or ownership of any asset or portion thereof used
20 for the generation, transmission, distribution or other provision of
21 regulated electric, natural gas, and/or telecommunications service to
22 retail customers in North Carolina:

- 23
24 (a) No Utility shall commit to or carry out such a transfer except in
25 accordance with these conditions, all applicable law, and the
26 rules, regulations and orders of the NCUC promulgated
27 thereunder; and
28
29 (b) No Utility may reflect in rates the value of any such transfer
30 except as allowed by the NCUC.

31
32 CP&L, NCNG, CP&L Energy, and their Affiliates shall include in any application to
33 the FERC for approval of any transfer described in the immediately preceding condition
34 the commitment set forth in that condition. CP&L will not transfer the control of,
35 operational responsibilities for, or ownership of any transmission asset to an Affiliate or
36 non-Affiliate without first obtaining NCUC approval.

37
38 Any filing with the FERC in connection with any asset transfers involving CP&L shall
39 request that the FERC include the following language in its approval order(s):
40

1 Approval of this application in no way precludes the North Carolina Utilities
2 Commission from scrutinizing and establishing the value of the asset transfer for
3 purposes of determining the retail rates for services rendered to CP&L's
4 customers. It is the FERC's intention that the North Carolina Utilities
5 Commission retain the right to review and determine the value of such asset
6 transfer for purposes of determining retail rates.

7
8 Neither CP&L, CP&L Energy, nor any Affiliate thereof shall assert or
9 support the assertion in any forum, with respect to any asset transfer
10 transaction as described in **## Condition No. X** to which CP&L is
11 involved and which is subject to the FPA, that the FPA in any way
12 preempts the NCUC from exercising such authority as it may have
13 under all applicable law to (a) review the reasonableness of any
14 commitment entered into by CP&L and mandate, approve or otherwise
15 regulate a transfer of assets by or to CP&L; and/or (b) disallow costs
16 or impute revenues, related to such commitment, to CP&L and
17 scrutinize and establish the value of the asset transfers for purposes of
18 determining the rates for services rendered to CP&L's retail customers.
19 Should any other entity so assert, CP&L, CP&L Energy and/or other
20 Affiliates shall advise and consult with the NCUC and the Public Staff
21 regarding such assertion.

22
23 CP&L, NCNG, CP&L Energy, and all Affiliates shall take all such
24 actions as may be reasonably necessary and appropriate to hold North
25 Carolina retail ratepayers harmless from rate increases, foregone
26 opportunities for rate decreases, and/or other effects of merger.

27
28 A copy of all applications, reports, contracts, rate schedules, or other
29 documents (including attachments, exhibits, and similar items) filed with
30 the FERC by CP&L Energy, any Service Company, the Utilities, other
31 Affiliates, and/or a Nonpublic Utility Operation shall be filed
32 contemporaneously by CP&L with the NCUC and a copy shall be
33 provided to the Public Staff at the time of the filing. CP&L and NCNG
34 also shall file with the NCUC all orders issued by the FERC that
35 directly or indirectly affect CP&L's and/or NCNG's accounting
36 practices, North Carolina-regulated rates, operations, and/or transfer
37 prices or allocations.

38
39 CP&L may not purchase electricity (and/or related goods and services)
40 from an Affiliate under circumstances where the costs incurred for
41 comparable service (whether directly or through allocation) exceed fair

1 market value, nor may it sell electricity (and/or related goods and
2 services) to an Affiliate for less than fair market value except for
3 emergency interchange transactions.
4
5

6 **Q. Does the proposed Integration Agreement warrant the imposition of other conditions?**

7 A. Yes. In addition to the general conditions set out above, specific conditions should be imposed
8 to ensure that CP&L's current generation is operated for the benefit of its retail native load
9 customers and that the NCUC can continue to exercise some control over CP&L's granting of
10 native load priority to new wholesale customers, which can have profound effects on reliability.
11 These protections should apply to all of CP&L's existing generating units, including those that
12 are not yet operational, if they have already been awarded a certificate.
13

14 While there are some provisions in the Integration Agreement that seek to preserve pre-merger
15 generation for the benefit of native load, the FERC could reject these provisions at the outset or
16 could change them as the Integration Agreement is modified in the future. In addition, new
17 agreements could be filed in the future that do not contain these provisions. Therefore, the
18 Public Staff has developed a series of conditions which will protect North Carolina ratepayers
19 from potential adverse impacts of the proposed Integration Agreement with FPC:
20

21 CP&L and its retail customers will continue to bear the cost
22 responsibility for CP&L's pre-merger power supply resources and
23 receive the revenues from those resources. CP&L shall ensure that its
24 retail native load customers receive the benefits associated with
25 CP&L's existing generation assets, including those for which a
26 certificate has been granted as of the closing date of the merger. *To*
27 *the extent CP&L and/or any of its Affiliates plan to file with the*
28 *FERC proposed amendments, modifications, or supplements to the*
29 *Integration Agreement (or comparable agreement) that change or*
30 *affect that cost responsibility and/or receipt of revenues and/or*
31 *could potentially have a negative effect on CP&L's North*
32 *Carolina retail native load customers, CP&L must obtain*
33 *approval from the NCUC in advance of filing with the FERC.*
34

1 The joint planning and coordinated dispatch of generation contemplated
2 by the Integration Agreement (and/or future comparable agreements)
3 shall ensure retail native load priority and shall ensure that CP&L's
4 retail native load customers receive the benefits of CP&L owned or
5 controlled generation resources. CP&L shall continue to serve its retail
6 native load customers in North Carolina with the lowest-cost power it
7 can reasonably generate or purchase from other sources before making
8 power available for off-system sales. To the extent CP&L owned or
9 controlled system generation is made available for off-system sales,
10 *such sales shall be made and accounted for in a manner that*
11 *maximizes their contribution to the reduction of CP&L's retail*
12 *cost of service. (CP&L's alternative?: "...off-system sales, the*
13 *revenues realized by CP&L from such sales shall continue to be*
14 *used to reduce CP&L's retail cost of service.)*

15
16 CP&L shall not enter into contracts for the sale of energy and/or
17 capacity at native load priority and/or under such terms and conditions
18 as to cause the purchasing entity to fall within the definition of "native
19 load" in the Integration Agreement *without making a showing to the*
20 *NCUC that it has adequate reserve margins to adequately serve*
21 *its retail native load customers and obtaining the NCUC's*
22 *approval.*

23
24 The costs of any resource additions that are allocated or assigned
25 directly or indirectly to CP&L, must be treated for ratemaking
26 purposes in accordance with all applicable laws and all NCUC orders,
27 rules and regulations.

28
29 Changes will be made, if and when necessary, to required affiliated
30 transactions reports and cost allocation manuals.

31
32
33 **Q. These conditions primarily deal with FERC jurisdictional issues. Are additional**
34 **conditions necessary with respect to CP&L Energy's change in status to a registered**
35 **holding under PUHCA as a result of this merger?**

36 A. Yes. The Commission, in its order allowing the formation of CP&L Energy and approving the
37 transfer to it of CP&L, NCNG, and Interpath, imposed a number of conditions relating to the
38 potential preemption of the NCUC's jurisdiction by the Securities and Exchange Commission

1 (SEC). I have been advised by Counsel that several additional conditions, most of which relate
2 to CP&L and NCNG taking service from CP&L Energy's newly-formed service company, are
3 needed. These are set out below.

- 4
- 5 (1) A copy of all applications, reports, or other documents filed
6 with the SEC under PUHCA by CP&L Energy, any Service
7 Company, the Utilities, other Affiliates, and/or any Nonpublic
8 Utility Operation shall be contemporaneously filed with the
9 NCUC and provided to the Public Staff. CP&L and NCNG
10 also shall file with the NCUC promptly upon receipt all orders
11 issued by the SEC that directly or indirectly affect any of the
12 Utilities' accounting practices, financings, operations, and/or
13 transfer prices or allocations.
- 14
- 15 (2) CP&L and NCNG shall not take services from nor provide
16 services to Affiliates other than CP&L Services if comparable
17 services can be provided more economically and efficiently by
18 CP&L Services.
- 19
- 20 (3) CP&L and NCNG shall file with the NCUC in this docket
21 annually *one week before the effective date of the annual*
22 *contract* the list of services each intends to provide to CP&L
23 Services and/or other Affiliates. Any modifications by CP&L
24 and/or NCNG to this list of services shall be filed with the
25 NCUC at the time CP&L and/or NCNG receive written notice
26 of the modifications.
- 27
- 28 (4) CP&L and NCNG shall file with the NCUC in this docket
29 annually *one week before the effective date of the annual*
30 *contract* the list of services each elects to take from CP&L
31 Services. Any modifications by CP&L and/or NCNG to the
32 selection of services shall be filed with the NCUC at the time
33 CP&L and/or NCNG gives written notice to CP&L Services.
- 34
- 35 (5) Any and all proposed changes to CP&L Services' contracts
36 and service contracts between CP&L and/or NCNG and any
37 of their Affiliates must be filed for approval by the NCUC
38 contemporaneously with their being filed with the SEC.
- 39

1
2 **Q. Are there any other conditions, in addition to those you have already discussed, which**
3 **you recommend being imposed upon approval of the merger?**

4 A. Yes. The Public Staff has developed some additional conditions, which cannot easily be
5 grouped into categories. They relate to a future investigation of affiliate transactions in the
6 power and natural gas marketing area; the protection of CP&L's and NCNG's customers from
7 all current and prospective liabilities of FPC, including the litigation involving Mid-Continent Life
8 Insurance Company; service quality; and other areas of concern. For the most part, these
9 conditions are reasonably self-explanatory.

- 10
11
12 (1) CP&L and NCNG shall cooperate fully in any future
13 investigation of power and natural gas marketing activities,
14 including but not limited to, how those activities are structured,
15 how prices and costs are determined and whether these
16 activities are being conducted in compliance with the relevant
17 codes of conduct.
- 18
19 (2) CP&L's North Carolina retail customers and NCNG's
20 customers shall be held harmless from all current and
21 prospective liabilities of Florida Progress and its subsidiaries,
22 including but not limited to, the litigation involving Mid-
23 Continent Life Insurance Company, pensions and other
24 employee benefits, decommissioning costs, and taxes.
- 25
26 (3) CP&L shall provide to the Public Staff immediately upon
27 execution and/or finalization the Tax Allocation Agreement,
28 plans to consolidate employee benefits plans, and other similar
29 agreements and plans.
- 30
31 (4) CP&L and NCNG will continue to take steps to implement
32 and further their commitment to providing superior public utility
33 service following CP&L Energy's acquisition of Florida
34 Progress. To the extent Florida Power Corporation's quality
35 of service practices are found to be superior to CP&L's,
36 CP&L shall incorporate those practices into its own practices
37 to the extent practicable. CP&L and NCNG will work with

1 the Public Staff to ensure the service quality indices are
2 appropriate and to revise them if and when such revisions are
3 necessary.
4

5 (5) Unless expressly superseded by the conditions contained
6 herein, the conditions agreed to by CP&L and NCNG, and
7 ordered by the NCUC, in Docket Nos. E-2, Sub 740, and
8 G-21, Sub 377, and the conditions agreed to by CP&L,
9 NCNG, Interpath, and CP&L Holdings, Inc., (subsequently
10 CP&L Energy), and ordered by the NCUC in Docket Nos. E-
11 2, Sub 753, G-21, Sub 387, and P-708, Sub 5, remain in full
12 force and effect.
13

14 (6) CP&L Energy shall maintain all Utility financial books and
15 records in Raleigh, North Carolina.
16

17 (7) Subject to subsequent revisions relating to this docket, CP&L,
18 all of its Affiliates, and its Nonpublic Utility Operations shall
19 remain bound by the Code of Conduct approved in Docket
20 Nos. E-2, Sub 753, G-21, Sub 387 and P-708, Sub 5.
21 CP&L shall cooperate in revising the Code as necessary to
22 incorporate the Florida Progress merger.
23
24