

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY	:	
	:	Docket No. 05-0159
Proposal to implement a competitive	:	
procurement process by establishing Rider CPP,	:	
Rider PPO-MVM, Rider TS-CPP and revising	:	
Rider PPO-MI	:	

REPLY BRIEF
OF COMMONWEALTH EDISON COMPANY

October 27, 2005

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Commonwealth Edison Company (“ComEd”), by and through its attorneys, and pursuant to the Illinois Commerce Commission’s (the “Commission’s” or the “ICC’s”) Rules of Practice and the direction of the Administrative Law Judge (the “ALJ”) , submits this Reply Brief.

I. EXECUTIVE SUMMARY

As we near the end of this proceeding, it is abundantly clear that there is overwhelming support for the Illinois Auction Proposal as the best means to procure supply customers require in the post-2006 period. The initial briefs of the parties explored the issues in detail, and described the benefits of the many refinements that have been incorporated at the suggestion of a wide range of participants. ComEd welcomes the debate that has taken place and believes that constructive dialogue on the issues has provided assurance that the procurement process will produce the lowest possible prices for customers. In an environment in which ComEd must acquire supply in the wholesale markets, this proceeding and the Commission’s Post-2006 Initiative which preceded it have identified the most effective way of making those purchases.

The breadth of the consensus is apparent by any measure. Of the many parties who have participated in this case, only three oppose the use of a procurement auction. Their views fall far outside the mainstream of thought on the issues that appropriately determine the outcome of this proceeding. They distrust the competitive forces that underlie the 1997 Restructuring Law and that have charted the course for the electric industry in Illinois for nearly a decade. They view with favor the failed regulatory approaches of the past, which imposed enormous risks and costs on customers, suggesting that a return to those methods will somehow produce better results the second time around. They seek to block implementation of the very best procurement process that many experts over years of study have devised, while offering no alternative that has any

prospect of success; indeed, they offer no alternative proposals at all. In the end, all of their arguments amount to nothing more than the familiar spoiler's refrain: "Just say no."

While the Attorney General (the "AG"), the Citizens Utility Board ("CUB") and the Cook County State's Attorney's Office ("CCSAO") are unwavering in their objection to the Illinois Auction Proposal, it is surprising how little they have to say about the process itself and its widely acknowledged ability to extract the best prices for supply from the wholesale markets. Although they seek an entirely new proceeding to consider alternative procurement processes, their conduct in this case shows that they have no interest in examining the merits of any process. If they had constructive ideas about practical alternatives that could be implemented, this was the place to discuss them. There were no limitations whatsoever on the creativity of solutions that parties could promote and, although some of the suggested approaches were shown to be ill-advised and far inferior to the Illinois Auction Proposal, this proceeding provided the opportunity to propose any procurement method and to have that method considered by the Commission.

Most of the opposition by these three parties focused not on the procurement process that should be used, but on two legal arguments about the Commission's authority. One argument – that the Commission lacks authority to act on ComEd's tariffs – seeks to narrowly confine the Commission with limitations that appear nowhere in the Public Utilities Act (the "Act" or the "PUA"). The other argument – that the Commission must engage in a post-auction prudence review of the resulting wholesale prices – is disingenuous, because any factors that could be examined in a legitimate prudence review of the method of ComEd's procurement of wholesale power will already be known before the auction is held. Thus, what these parties seek is not really a prudence review at all. In a very real sense, these positions have it backwards, understating the Commission's power to accomplish what it should be doing on the front end in

approving retail rates based on a sound auction design and vastly exceeding what it is permitted to do after the wholesale contracts have been accepted.

Section III will explore the deficiencies in these legal arguments on which the Attorney General, CUB and CCSAO rely so heavily. As that discussion demonstrates, the Commission has broad authority under Article IX of the Act and under Sections 16-112, 16-111(i), and 16-109A of the Restructuring Law to approve ComEd's tariffs. In doing so, the Commission must observe the division of responsibility between state and federal authorities, which places exclusive jurisdiction over wholesale power transactions with the Federal Energy Regulatory Commission ("FERC"), but permits state regulators to consider the prudence of utility decisions under standards outlined in the *Pike County* decision.

Under both *Pike County* and well-established Illinois law governing the scope of prudence review, there is no question that the Commission's review is confined to the reasonableness of decisions made by a utility based on the facts that were available when the decision had to be made. Because we are adopting a method to procure supply for customers, the time to conduct a prudence review is now – when the decision is being made and when all of the facts on which the choice should turn are available. The contention that the prudence of the process must be considered after the fact so that the results of the auction can be reviewed in hindsight is flatly contrary to Illinois authority on which there is no basis for disagreement or debate.

In addition to their flawed legal arguments, the opponents of the Illinois Auction Proposal rely on their view that the wholesale markets are not ready to support the process. The evidence was just to the contrary, showing that the broad PJM markets provide an ideal platform for the conduct of the auction, making available all of the products bidders will need to participate and

offering the protection of a sophisticated monitoring unit to check the functioning of the market and spot any irregularities that may occur. There is simply no indication that any deficiency in the wholesale market exists that would preclude the implementation of a successful auction process in Illinois.

After many years of study and planning for post-2006 electric supply arrangements that will bring the benefits of competition to all customers, we are on the verge of a successful conclusion with the implementation of the Illinois Auction. The vast majority of the parties who have participated throughout the process agree that the time has come to proceed with the very best plan that could be identified. It is significant that the Commission's Staff, which has explored the issues in exhaustive detail both internally and with the assistance of a retained expert, Dr. Salant, has concluded that the Illinois Auction Proposal should be approved and incorporates all of the features and protections necessary to be implemented effectively.

While there are a few naysayers, there is no basis for their objections. They do not address the merits of the proposal in an effort to incorporate features that would improve the process. Instead, their goal is to prevent the Commission from approving any process, hoping that their obstructionism will force ComEd to make discretionary procurement decisions, without any guidance, that they can later seek to second guess after the results are known. Their strategy runs counter to all of the Commission's efforts in the Post-2006 Initiative, which began with Staff's White Paper acknowledging that "[t]he Commission should provide guidance and direction to utilities regarding how they should conduct their supply acquisition activities." (Staff's White Paper, 2/19/2004 at 4) The Commission should not permit the gamesmanship of a few critics to stymie the enormous strides that the Commission has made on behalf of customers over the past year and a half.

The Commission's foresight and direction have resulted in a procurement proposal that will achieve the lowest available costs. It emerged from a collaborative process that could not have taken place without the Commission's leadership. The Commission should reject the arguments of those who would undercut the work of this extraordinary initiative and should accept the judgment of the many diverse parties who have strived so hard to develop the Illinois Auction Proposal. It is the best course for customers, and it will complete the task on which the General Assembly embarked with the passage of the 1997 Restructuring Law.

II. NEED FOR COMMISSION ACTION

The Commission has before it everything that is necessary to conclude that the Illinois Auction Proposal is just and reasonable and that ComEd acted prudently in proposing it as a means of acquiring the electricity necessary to serve its retail customers. In the interests of customers and all parties, ComEd urges the Commission to approve ComEd's tariffs so that plans for securing reliable supply at reasonable and stable prices in the post transition-period can proceed in accordance with the Act.

A number of other parties also use Section II of their initial briefs to support Commission action. Staff states its belief that it is appropriate for the Commission to act in this docket. (Staff Init. Br. at 7) Similarly, having articulated various legal and policy arguments that are discussed elsewhere, the Coalition of Energy Suppliers ("CES") concludes that Commission action at this time is both necessary and appropriate. (CES Init. Br. at 6-8) In addition, Constellation Energy Commodities Group, Inc. ("CCG") states that the Commission needs to act to make sure that there is a policy and procedure in place for ComEd to purchase power and energy to meet its obligations. (CCG Init. Br. at 2-4) Direct Energy Services, LLC ("DES") and U.S. Energy Savings Corp. ("USCESC") also support Commission action, indicating that an appropriate

auction in the wholesale market would establish a competitive retail market that would benefit customers. (DES-USESC Br. at 4-5)

As one of only three opponents of the Illinois Auction Proposal, CCSAO asserts that the Commission should act by rejecting ComEd's proposed tariffs, as otherwise such tariffs will go into effect after the Commission's suspension period expires. (CCSAO Init. Br., at 4-5) Likewise, the AG, suggests that the Commission act to suspend the tariffs permanently. (AG Init. Br. at 3) As discussed in other sections of this reply brief, these parties' arguments have no merit. Rather, as the record makes clear, and as almost all other participants have urged, the Commission should act now to approve the Illinois Action Proposal.

III. LEGAL ISSUES

A. **Background: the Illinois Electric Service Customer Choice and Rate Relief Law of 1997.**

The Attorney General urges the Commission to reject ComEd's proposal and to "effectuate an extension of the transition period." (AG Initial Brief ("Init. Br.") at 1) The Commission is *not* at liberty to rewrite the 1997 Act, however, or to ignore the fundamental changes in the electric services industry in Illinois it brought about. The Attorney General urges the Commission to revert to a prior regulatory model and once again to base rates on the cost of generating electricity. *See* Section III.C., *infra*. But whether or not the Commission permissibly can "effectuate an extension of the transition period," the Commission *cannot* turn back the clock, undo divestiture transactions it explicitly approved, or base rates on the costs of generating plants ComEd no longer owns. The 1997 Act explicitly guarantees that, once the Commission approves a sale or transfer of generation assets, as it did for ComEd's generating plants, "[t]he Commission shall not in any subsequent proceeding or otherwise, review such a reorganization or other transaction authorized by this Section," 220 ILCS 5/16-111(g) (emphasis added), and

that “[s]ubsequent to the mandatory transition period, the Commission, in any proceeding to establish rates and charges for tariffed services offered by an electric utility, shall consider *only . . . the then current or projected revenues, costs, investments and cost of capital directly or indirectly associated with the provision of such tariffed services. . . .*” *Id.* at 16-111(i) (emphasis added).

The Commission cannot ignore reality and live in the fantasy world invited by the Attorney General, where rates remain tied to the costs of generation facilities that are no longer owned, operated or controlled by the public utilities regulated by the Commission. ComEd now must *procure* electricity from others and is required to pay such entities a fair market price, as required under FERC and PJM guidelines. And ComEd must be able – and obviously is legally entitled – to recover the *costs* of those purchases, which the company proposes to do here with no markup or profit. The Commission either can help fashion the method by which ComEd will make those purchases, or it can accept the Attorney General’s invitation to place its head in the sand, emerging only when it is too late – after these multi-billion dollar purchases are made, when the Commission would be forced either to accept them without any meaningful input into the process or effectively force ComEd into insolvency.

Following the recommendations that emerged from the Commission’s Post-2006 working group process, ComEd responsibly set forth a detailed procurement proposal in a public tariff filing. The record shows that, with the adjustments ComEd already has made as a result of this proceeding, there is no better way than an open, fair, competitive auction – at which *all* wholesale suppliers may participate – to ensure that ComEd procures electricity at the lowest available price. ComEd’s proposal directly follows from the industry-wide restructuring authorized and contemplated by the 1997 Act, and it should be adopted by the Commission.

B. ICC authority under Article IX and Article XVI to approve the filed tariffs.

1. Section 16-103(c) of the PUA does not deprive the Commission of authority to approve ComEd's tariff.

The Attorney General, CUB and CCSAO repeat their arguments that the Commission lacks authority to approve ComEd's tariff proposal because of Sections 16-103(c) and 16-113 of the PUA. (*See* AG Init. Br. at 8-13; CUB Init. Br. at 5-12; CCSAO Init. Br. at 7-11) These arguments are based on a plain misreading of the statute, which the Commission already has considered and rejected. The Attorney General, CUB and CCSAO offer nothing new that should lead the Commission to change its mind.

The Attorney General's argument merely underscores the obvious fallacy in its position. It argues that "the General Assembly allowed the 'self-generating regulatory force' of the market to set rates only where there is sufficient competition." (AG Init. Br. at 8) But ComEd is not proposing to charge retail rates based upon the "self-generating regulatory force" of retail markets. For ComEd to do that, it would have to propose to charge retail customers whatever price it thought the competitive retail market would bear – in other words, the highest price that ComEd could charge without losing business to competing retail suppliers of electricity. *That* is what would be impermissible under the PUA prior to the time that competition exists in the retail market. But that is entirely different from what ComEd is proposing. The Attorney General's argument is classic smoke and mirrors, failing to differentiate between the competitive *wholesale* market, where ComEd necessarily must purchase wholesale electricity at market-based rates, *see* Section III.C., *infra*, and the as yet non-competitive residential *retail* market, in which ComEd proposes to charge customers only its actual *costs*, without a penny of profit, for its wholesale purchases of electricity.

2. The Commission has authority to approve the formula rates proposed by ComEd in its tariff.

The Attorney General, CUB and CCSAO all contend that ComEd’s proposal is unlawful because it does not include an “actual rate.” (*See* AG Init. Br. at 13 (Commission cannot approve a “blank rate”); CUB Init. Br. at 8 (Commission cannot approve “tariffs that contain no actual rates or charges”); CCSAO Init. Br. at 14 (Commission must review “the actual rate in the tariff before it takes effect”). As framed by CUB, the issue is whether the Commission has “jurisdiction” to “pre approve” ComEd’s “procurement proposals,” or whether the PUA requires an “after-the-fact ICC prudence review or determination of the reasonableness and justness of the actual rates resulting from the auction”). (CUB Init. Br. at 7)

The Commission already has rejected this argument. *See* ALJ Decision in Docket 05-0159, at 7 (noting that “the Commission’s approval of a pass-through rider as the preferred mechanism for recovery of coal-tar cleanup costs is within the Commission’s authority”). Moreover, the claim of the Attorney General, CUB and CCSAO that the PUA requires a tariff to contain an “actual rate” has been squarely and explicitly rejected by the Illinois Supreme Court. In 1958, the Court upheld the Commission’s authority to permit a utility to automatically increase its rates to recover the costs of wholesale power purchases pursuant to an approved “mathematical formula.” *City of Chicago v. Illinois Commerce Comm’n*, 13 Ill. 2d 607, 611-13 (1958).¹ In upholding this ratesetting method, the Court explicitly held that “*it is clear that the statutory authority to approve rate schedules embraces more than the authority to approve rates fixed in terms of dollars and cents,*” as is done in a general ratemaking case. *Id.* at 611 (emphasis added). The Court found it sufficient that the Commission retained its power to initiate a

¹ The Supreme Court upheld the automatic rate adjustment mechanism independent of any specific statutory authorization, under the Commission’s general Article IX authority. *See City of Chicago*, 13 Ill. 2d at 611-13. The General Assembly subsequently enacted specific provisions governing fuel adjustment clauses.

proceeding to investigate the reasonableness of the utility's rates – a statutory power that also remains intact under ComEd's Rider CPP. *Id.* at 617; *see* 220 ILCS 5/9-250. Quoting its earlier decision in *Antioch Milling Co. v. Public Serv. Co. of N. Ill.*, 4 Ill. 2d 200, 210 (1954), the Court emphasized that “[t]he act provides that rates shall be reasonable; but it entrusts the enforcement of that obligation in the first instance to the commission.” *City of Chicago*, 13 Ill. 2d at 618 (internal quotation marks omitted).²

The PUA requires the Commission to ensure that rates are just and reasonable. 220 ILCS 5/9-101. The statute does not dictate *how* the Commission should make this determination, however, and the Supreme Court in *City of Chicago* emphasized that the Commission has wide latitude in establishing “preferable techniques in utility regulation.” 13 Ill. 2d at 618. More recently, the Supreme Court agreed with the Commission that, in the case of “unexpected, volatile or fluctuating expenses,” an adjustment mechanism provides a more “accurate and efficient” means than a general rate case for tracking costs and matching them with rates. *Citizens Util. Bd. v. Illinois Commerce Comm’n*, 166 Ill. 2d 111, 138 (1995). Such mechanisms simply – and fairly – provide for cost recovery and do not affect the utility's fair rate of return. *See City of Chicago v. Illinois Commerce Comm’n*, 281 Ill. App. 3d 617, 628 (1st Dist. 1996). What is critical is that the measure of costs, and the utility's rates, must be outside of the utility's unilateral control. *See Citizens Util. Bd. v. Illinois Commerce Comm’n*, 275 Ill. App. 3d 329,

² Only CUB cites and even attempts to distinguish the Supreme Court's decision in *City of Chicago*. (*See* CUB Init. Br. at 10-11) Its attempt to do so is wholly unavailing, however, and actually proves the precise applicability of the case here. CUB argues that *City of Chicago* was different because it involved wholesale gas purchases, for which it claims “The Natural Gas Act of 1938 . . . vested the power to fix rates for natural gas transported and sold to distributing companies in interstate commerce exclusively in the FPC [Federal Power Commission] and preempted any right which might have existed in the States to regulate such rates. Thus, Illinois had to charge and Peoples [Gas Company] had to pay the FPC determined rate, and the Commission had no power over such rate.” (CUB Init. Br. at 10) The identical points apply with regard to ComEd's wholesale purchases of electricity at issue in Rider CPP. *See* Section III.C, *infra*.

340 (1st Dist. 1995) (“the Commission may not approve a tariff which permits a utility to set its own rates”).³

Such “formula rate” mechanisms have not been limited to fuel purchases. *See Citizens Util. Bd.*, 166 Ill. 2d at 133 (upholding recovery of “coal-tar cleanup expenditures” through a flexible “rider” mechanism, which the Supreme Court described as a mechanism that could “increase a rate, allowing the utility to recover the cost as it is incurred, alleviating the delay of waiting until the utility files a general rate case to recover expenses”); *City of Chicago*, 281 Ill. App. 3d at 627-28 (upholding rider recovery of utility municipal franchise fees); *In re Ill. Power Co.*, No. 04-0294, 2004 WL 2208508, at *47 (Ill. Commerce Comm’n, Sept. 22, 2004) (approving automatic adjustment clause for 90% of asbestos litigation costs). Indeed, each of the following ComEd rates – many of which have been in existence for years – employs formulae or specifies procedures for calculating rates in lieu of actual, stated charges:

- Rate RHEP (Ill. C.C. No. 4, Orig. Sheet No. 55.40 *et seq.*) – calculates monthly access charge and real time energy prices based upon formulae using historical quantities and market energy prices as inputs.
- Rate HEP (Ill. C.C. No. 4, 6th Rev. Sheet No. 55.70 *et seq.*) – structured with unbundled prices for distribution, transmission, and supply components;

³ The Attorney General, CUB and CCSAO all rely heavily upon this *CUB v. ICC* case, 275 Ill. App. 3d 329. *See* AG Init. Br. at 13; CUB Init. Br. at 8; CCSAO at 14. The facts in that case were materially different, however, from what is at issue in Rider CPP. *CUB v. ICC* involved a proposed tariff in which ComEd would have had the ability to negotiate exceptions with up to 25 large customers from ComEd’s published tariff rate, upon evidence that those customers had received a competitive proposal from another supplier of electricity and therefore could “bypass” ComEd. 275 Ill. App. 3d at 332-33. In finding the proposed tariff to be impermissible, the court emphasized that “Edison retained sole discretion in determining whether a customer would have engaged in a bypass absent the negotiated rate. The determination of which [25] customers [out of a universe of 1,700 eligible customers] would be awarded contracts under the proposed tariff likewise rested exclusively with Edison.” *Id.* The court also found “most important” that the exceptions granted “would not be published or open to public inspection.” *Id.* at 333; *see also id.* at 342 (“what is at stake here is Edison’s compliance with the filing and publication requirements of the Act”). ComEd’s Rider CPP suffers from none of these defects. Under the auction, ComEd retains no discretion to select the winning bidder, and the retail rates resulting from the auction will be published and open to public inspection. *See* Rider CPP Orig. Sheet 268. Significantly, the court in *CUB v. ICC* itself distinguished the very type of situation here (and in *City of Chicago*), as involving “a mathematical formula under which rates would fluctuate with the wholesale cost of natural gas.” 275 Ill. App. 3d at 339-40. Obviously, the fact that the instant case involves the wholesale cost of electricity, rather than natural gas, is of no moment.

calculates real time energy prices based upon formulae using historical quantities and PJM market energy prices as inputs.

- Rate IPP (Ill. C.C. No. 4, 1st Rev. Sheet No. 55.77 *et seq.*) – structured with unbundled prices for distribution, transmission, and supply components; calculates energy charges based on market energy prices; calculates transmission charges based on FERC transmission rate.
- Rate PR (Ill. C.C. No. 4, 1st Rev. Sheet No. 140 *et seq.*) – provides for partial requirements service at rate calculated to account for modified load shape of partial load supplied by ComEd.
- Rate CTC (Ill. C.C. No. 4, 3rd rev. Sheet No. 134 *et seq.*) and Rider CTC-MY (Ill. C.C. No. 4, Orig. Sheet No. 235 *et seq.*) – determine transition charges based on MVI formula.
- Rider VLR (Ill. C.C. No. 4, 1st rev. Sheet No. 61.61 *et seq.*) – provides for load reduction payments calculated either based on (a) individual assessment of load response benefits, or (b) formula based on market Locational Marginal Prices (“LMPs”).
- Rider 2 (Ill. C.C. No. 4, 10th Rev. Sheet No. 62 *et seq.*) – determines applicability and amount of deposit requirement for line extensions based on individually-applied engineering criteria and criteria in Rider and ICC rules.
- Rider 3 (Ill. C.C. No. 4, 8th Rev. Sheet No. 62.10 *et seq.*) – calculates equivalent retail rate paid to Qualified Solid Waste Energy Facilities based on mathematical procedure specified in tariff.
- Rider 6 (Ill. C.C. No. 4, 7th rev. Sheet No. 67 *et seq.*) – provides for individually calculated charges for non-standard facilities based on ComEd’s costs or estimated costs.
- Rider 28 (Ill. C.C. No. 4, 4th Rev. Sheet No. 95.05 *et seq.*) – determines charges for residents of municipalities imposing special requirements based on calculated incremental costs to ComEd. Rider 28 was upheld on appeal. *A. Finkl & Sons Co. v. Illinois Commerce Comm’n*, 756 N.E.2d 933 (Ill. App. Ct. 2001).
- Rider PPO (Ill. C.C. No. 4, 5th Rev. Sheet No. 151.1 *et seq.*) – determines charges for PPO service via MVI formula.
- Rider ISS (Ill. C.C. No. 4, 3rd Rev. Sheet No. 152 *et seq.*) – determines charges for energy consumed by customers taking interim supply service based on formula tied to the MVI.

- Rider TS (Ill. C.C. No. 4, 2nd Rev. Sheet No. 217 *et seq.*) – determines transmission charges for unbundled and price unbundled services through use of pass-through formulae and FERC transmission tariff rates.
- Rider ZSS (Ill. C.C. No. 4, Orig. Sheet No. 221 *et seq.*) – determines distribution facility charges for certain high-voltage customers based on engineering assessment of costs using procedure specified in tariff.
- Rider CLR (Ill. C.C. No. 4, Orig. Sheet No. 242 *et seq.*) – calculates payments for avoided capacity based on value determined under PJM tariff.

As evidenced by this list and the cases cited above, formula rates long have been approved in a wide variety of contexts, often without challenge. If pass-through formula rates were unlawful, there would be no way to have functional real time pricing rates, no effective load response rates, and no effective way for ComEd to charge for non-standard facilities demanded by customers.

Thus, the Attorney General, CUB and CCSAO simply are wrong in contending that Rider CPP is defective because it lacks an “actual rate.” Nor is there any “jurisdictional” bar (CUB Init. Br. at 7) that prevents the Commission from “pre approving” a specific process and formula for determining tariff rates. ComEd’s proposal clearly falls within the authority established by *City of Chicago* and other cases. What is critical is that ComEd’s proposal does *not*, as CUB contends, “grant a utility a prospective right to set rates into the future.” (CUB Init. Br. at 9) Under Rider CPP, ComEd has no ability “to set its own rates.” *Citizens Util. Bd.*, 275 Ill. App. 3d at 340. The auction is administered by an independent auction manager, and ComEd has no discretion to select the winning bidders. Nor does ComEd have control over the wholesale market or the prices that will be bid at the auction. Indeed, the auction process involves less discretion and potential for abuse by ComEd than virtually any other process, and it is specifically designed to identify the lowest price for wholesale electricity that is available to ComEd.

3. The auction review process proposed by ComEd is permissible and fully preserves all the consumer protections of the Act.

Judge Wallace previously observed that “[w]hether an auction process, assuming one is approved in some form, should be conditioned on the imposition of a more formal or more comprehensive review process than the one proposed by ComEd involves mixed questions of fact and law that can be addressed by the parties during the course of the proceeding[.]” ALJ Decision, Docket No. 05-0159, at 8. The Attorney General, CUB and CCSAO all argue that ComEd’s proposal is impermissible because it “eliminate[s] any after-the-fact ICC prudence review” (CUB Init. Br. at 7), and fails to afford “consumer protections” required by the Act (AG Init. Br. at 10-12). Significantly, as CUB concedes, “everyone seems to be in agreement” (CUB Init. Br. at 7) that the traditional ratemaking standard applies here – that is, “[u]nder applicable law, if all the cost of acquiring the power is prudently incurred, then those costs can be passed on to customers through rates.” (*Id.*) Thus, the issue before the Commission is not whether ComEd’s wholesale electricity costs may increase, but simply whether those costs are prudently incurred, and whether ComEd’s Rider CPP allows the Commission sufficient opportunity to review whether those costs are prudently incurred. In that regard, it is significant that the prudence of a utility’s actions must be determined with reference to “only those facts available at the time judgment was exercised.” *Illinois Power Co. v. Illinois Commerce Comm’n*, 339 Ill. App. 3d 425, 428 (5th Dist. 2003).

The Commission’s review of the prudence of ComEd’s proposed wholesale acquisitions occurs in two forms, which together allow the Commission ample opportunity to review the prudence of ComEd’s incurrence of these costs. First, through its tariff filing and in connection with this very proceeding, ComEd has provided an unprecedented opportunity to the Commission – and to all interested parties – to review the method by which ComEd will make its

wholesale acquisitions. ComEd has allowed input into the process *before* the fact, rather than restricting the Commission and interested parties to the necessarily limited review that can occur once costs already have been incurred. *See Business & Prof. People for the Pub. Interest v. Illinois Commerce Comm'n*, 279 Ill. App. 3d 824 (1st Dist. 1996) (rejecting claim that costs of unplanned generation plant shutdowns caused by employee errors were not prudently incurred). Consistent with the Commission's Post-2006 working group process, ComEd has proposed for review and approval the very mechanism by which it will make these wholesale acquisitions. Many of the precise issues of "discretionary conduct" raised by CUB – such as how the qualifications of bidders will be established, how much of ComEd's retail power requirements will be offered for bid, how much of ComEd's requirements can be captured by one bidder (*see* CUB Init. Br. at 11-12) – all are available for review and approval by the Commission in this very proceeding.

In addition, ComEd's proposal provides for extensive review of the auction itself by the Commission. Within one business day of the auction's completion date, both the Auction Manager and the Auction Advisor must submit confidential reports to the Commission. Rider CPP, Orig. Sheet 267. The Auction Manager's report will provide "a factual summary of the activities and events that occurred during the course of the CPP Auction and the CPP-H Auction" and an "assessment of whether the auctions were conducted fairly and appropriately in accordance with the CPP rules and procedures." *Id.*, Orig. Sheet 257. The Auction Advisor's report "provides an independent assessment . . . as to whether or not the CPP Auction and the CPP-H Auction were conducted fairly and appropriately and all necessary actions to ensure the competitiveness and integrity of such auctions were followed." *Id.* The Commission can reject the auction results by initiating a "formal investigation or other formal proceeding" by the end of

the third business day following the auction's completion date. *Id.*, Orig. Sheet 268. Also, the tariff does not "in any way limit the Commission's ability to review all the information it has available to it." McNeil, Tr. 504 (cited in ComEd Init. Br. at 112).

These procedures are appropriate and adequate to fulfill the Commission's review function. Because of the unique nature and size of these transactions, further review is neither necessary nor prudent. The Commission has limited oversight over wholesale electricity transactions such as these, and the auction itself is designed to ensure that ComEd prudently purchases wholesale electricity at the lowest available price – the precise issue of oversight retained by the Commission. *See* Section III.C, *infra*. Evidence also shows that to create uncertainty in whether ComEd will recover the costs of, and therefore can pay for, these purchases would increase the auction prices, thereby raising rates unnecessarily for consumers. *See* Schnitzer Dir., ComEd Ex. 6.0, 28:654-29.661. Thus, it is in the interests of consumers for the Commission's review to occur contemporaneously with the auction, not months or longer after the auction has occurred. The Attorney General, CUB and CCSAO fail to identify any purpose that would be served by a further "after-the-fact ICC prudence review." (CUB Init. Br. at 7) There is no inherent value in adding "an element of chance or sport" when a utility is incurring billions of dollars of cost, deferring until the money is spent whether those costs will be approved and may be recovered. This, effectively, is what the Attorney General, CUB and CCSAO seek. If they have a *better* method by which ComEd should make these wholesale acquisitions, this is the proceeding in which they should make those arguments. No credible alternative has been offered, however. *See* Section III.C.3, *infra*.

There is no existing or previous model that dictates how the Commission should review wholesale acquisitions of this magnitude. And the 1997 Act emphasizes that "[l]ong-standing

regulatory relationships need to be altered to accommodate the competition that could fundamentally alter the structure of the electric services market.” 220 ILCS 5/16-101A(b). As specifically authorized by the 1997 Act, ComEd has divested its generation facilities and now must acquire all the electricity needed by its customers. Rider CPP provides a standard for Commission review of the auction *process* and *results* that is *broader* than that typically available in a traditional “prudence” review. In this Docket, the ICC has the opportunity to review the process before any acquisitions are made. And Rider CPP allows the Commission to reject the auction results even if it believes ComEd acted prudently. The tariff simply requires that sufficient cause exist to *open* an investigation. CPP Rider, Orig. Sheet 268.

If an objective process beyond the control of the utility is approved and followed, the utility adds no markup or profit to the resulting costs, and the Commission contemporaneously reviews and accepts the auction results, there necessarily is no basis for a detailed review of the acquisition after the fact. ComEd has yielded the traditional discretion it exercises in the procurement process in favor of a carefully controlled, objective mechanism, in which only those wholesale suppliers who offer the lowest costs for Illinois consumers will be selected. Given these facts, and the Commission’s limited jurisdiction over wholesale electricity transactions, *see* Section III.C., *infra*, the Commission’s review function is entirely consistent with the requirements of the Act.⁴

⁴ As Judge Wallace noted, in the generic coal tar proceeding, Docket Nos. 91-0080 through 91-0095 (Cons.), the Commission approved use of a rider mechanism, but also found that such riders should be subject to an annual reconciliation with a prudence review. *See* Investigation Concerning Issues Related to Coal Tar Clean-up Expenditures, 1992 Ill. PUC LEXIS 379 (Ill. Commerce Comm’n Sept. 30, 1992). The rider mechanism was necessary there, however, because of “the wide variations in and the difficulties in making forecasts of the scope, costs and timing of coal tar investigation and remediation activities.” *Id.* at *135. And the Commission found a reconciliation and prudence review was required to ensure “that the utility’s cleanup activities and costs were necessary [and] cost effective.” *Id.* at *166. The annual prudence review was the only mechanism by which the Commission could review the prudence of the utility’s cleanup activities and costs, which could vary widely in scope, amount and timing. In contrast, with regard to Rider CPP, the “requirements” nature of the auction forecloses any claim that ComEd’s purchases are not “necessary,” and the auction process itself, which is designed

Nor does the review process proposed by ComEd deny any of the vital “consumer protections” advocated by the Attorney General. (AG Init. Br. at 10-12) Every one of the consumer protections identified by the Attorney General is preserved, and indeed advanced, by ComEd’s tariff proposal. The Attorney General’s argument in fact strongly *supports* the appropriateness of the proposal now before the Commission.

The Attorney General first contends that rates must be “based on a review of the prudence of management decisions.” (AG Init. Br. at 10) Yet the instant 11-month tariff review proceeding is designed precisely to allow all parties to review and comment on the prudence of ComEd’s proposed competitive procurement mechanism, and it provides stakeholders far *greater* input into ComEd’s purchasing decisions than they ordinarily would have. Second, the Attorney General claims (without supporting law) that rates must be “based on a direct review of profits.” *Id.* at 11. Here, however, ComEd proposes *no* profits, and it is hard to imagine what “review” by the Commission could be lost. Third, the Attorney General contends that rates must be “determined through public proceedings with procedural safeguards.” *Id.* Yet that is precisely the type of proceeding now pending before the Commission. Fourth, the Attorney General contends that rates must be determined “through a deliberative decision-making process based on the evidence in the record and applicable law.” *Id.* Again, however, that is precisely the type of record now being developed at the Commission. Finally, the Attorney General argues that rates must be “determined by an independent Commission whose ratemaking decisions are subject to scrutiny by the Court and can be reversed or voided for violations of the PUA and ethics laws.” *Id.* at 12 (footnotes omitted). Yet every decision of the Commission,

to identify the lowest cost provider, establishes that the wholesale purchases are “cost effective.” The much more standardized nature of the wholesale electricity product, as compared to environmental cleanup and remediation, allows use of a standardized procurement process that appropriately changes the nature and timing of the Commission’s “prudence review” function.

both in this proceeding and in connection with its review of each auction procurement, remains subject to these standards.

In sum, all the consumer protections invoked by the Attorney General are vibrantly preserved in ComEd's tariff proposal. Indeed, it is the Attorney General, not ComEd, who seeks to deprive consumers of a meaningful opportunity to be heard regarding the manner in which ComEd should make these necessary wholesale electricity purchases, advocating instead for a type of "procurement roulette" in which ComEd would make these procurements on its own, leaving the Commission the highly limited choice of either accepting the purchases "as is" long after the fact or, if it were to reject them, making ComEd operatively insolvent.

Finally, CCSAO contends that in connection with ComEd's "[s]ale and divestiture of . . . generation assets," the Commission "should conclude that ComEd failed to act prudently on behalf of residential ratepayers." (CCSAO Init. Br. at 11, 12) This argument is explicitly foreclosed by the 1997 Act, which provides that following the Commission's approval of a utility's sale or transfer of generation assets (as occurred here), "[t]he Commission shall not in any subsequent proceeding or otherwise, review such a reorganization or other transaction authorized by this Section." 220 ILCS 5/16-111(g). If it were relevant (and it is not), ComEd readily could show that its generation asset transactions were prudent at the time they were made, and still today, particularly given the provisions of the 1997 Act.

C. Relationship of Illinois and federal law and jurisdiction.

The Attorney General, echoed by CUB and CCSAO, challenge ComEd's competitive auction procurement proposal on grounds that are flatly inconsistent with controlling federal law. In particular, and as developed further in this section of ComEd's reply brief:

(1) The Attorney General argues that “the wholesale electricity market is not sufficiently developed” and urges the Commission to scrutinize the costs of ComEd’s wholesale *suppliers* as a basis for setting ComEd’s rates – even though ComEd cannot buy from those suppliers at cost, and even though the Commission cannot regulate the rates at which those suppliers sell to ComEd. The Attorney General’s attacks on the wholesale market must be addressed to FERC, not the Commission. FERC has exclusive jurisdiction over wholesale electricity markets, and state regulators cannot prevent utilities from recovering the costs of wholesale purchases made at FERC-approved rates.

(2) Relying on *Pike County Light & Power Co. v. Pennsylvania PUC*, 465 A.2d 735 (Pa. Commw. Ct. 1983), the Attorney General counters that federal law does not preempt the Commission’s detailed review of wholesale electricity transactions and disallowance of utility costs incurred in such transactions. But *Pike County* stands only for the proposition that a utility is required to make prudent choices among available wholesale alternatives, and provides no support whatsoever for the Attorney General’s attack here on the wholesale market itself. Indeed, *Pike County* strongly supports use of the competitive auction process proposed by ComEd.

(3) The Attorney General contends that “ComEd has failed to . . . use . . . its substantial buying power to negotiate with its generation affiliate to purchase low-cost electricity from Exelon’s Northern Illinois generating plants, which ComEd customers paid to build and maintain.” (AG Init. Br. at 2) But as a matter of federal law, the State of Illinois cannot force Exelon Generation, a FERC-jurisdictional wholesale supplier, to sell to ComEd at below-market rates, thereby subsidizing the delivery of electricity to ComEd’s customers. Nor may the State attempt to appropriate the output of Exelon Generation’s “Northern Illinois generating plants.”

In sum, the Commission cannot regulate rates in the wholesale market, consider the costs of wholesale suppliers, or trap the costs of ComEd's wholesale purchases by preventing ComEd from recovering them. Because that is what the Attorney General, CUB and CCSAO are asking it to do here, the Commission must reject their arguments. ComEd's competitive auction process is designed precisely to ensure that ComEd's wholesale purchases are made at the lowest available price and in a manner consistent with federal regulatory requirements.

1. The Attorney General fundamentally mischaracterizes the nature of federal and state regulatory jurisdiction over wholesale electricity markets.

The Attorney General is critical of the wholesale electricity market, calls for greater regulatory oversight of that market, and argues that the ICC should base ComEd's retail rates on the generation costs of its wholesale suppliers. (AG Init. Br. at 1-2, 14-20) These arguments are not properly directed at this Commission, which lacks jurisdiction over wholesale electricity markets. The Attorney General argues, for example (contrary to the evidence in this case, *see* Section IV, *infra*), that "the wholesale electricity market is not sufficiently developed" and that for this reason "most states have opted to continue cost-of-service regulation." (AG Init. Br. at 2) The fact is, however, that in 1997 the Illinois legislature made the decision to rely more on the competitive forces existing in the electric industry, and what other state legislatures may have done can have no relevance to this Commission. The Attorney General goes so far as to argue that this Commission has authority to examine the costs of wholesale sellers of electricity selling under FERC-approved wholesale rates, second-guessing FERC as to what wholesale rates are

just and reasonable. (AG Init. Br. at 19-20) These arguments invite clear legal error by the Commission.⁵

The Supreme Court has made clear that federal regulation of wholesale electricity transactions is supreme and exclusive, *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 964 (1986), and that States lack authority to engage in the kind of review and analysis of the costs underlying wholesale transactions proposed by the Attorney General here. Congress enacted the Federal Power Act (FPA) in 1935 “to provide effective federal regulation of the expanding business of transmitting and selling electric power in interstate commerce.” *New York v. FERC*, 535 U.S. 1, 6 (2002) (quoting *Gulf States Util. Co. v. FPC*, 411 U.S. 747, 758 (1973)). The statute explicitly provides that “Federal regulation” shall govern “the sale of electric energy at wholesale in interstate commerce.” 16 U.S.C. § 824(a), (b).⁶ The Supreme Court has declared that “Congress has drawn a bright line between state and federal authority in the setting of wholesale rates and in the regulation of agreements that affect wholesale rates.” *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 374 (1988). As a result, “[t]he reasonableness of rates and agreements regulated by FERC may not be collaterally attacked in state or federal courts. The only appropriate forum for such a challenge is before [FERC] or a court reviewing the Commission’s order.” *Id.* at 375. When the Attorney General argues that

⁵ The Attorney General makes numerous references to the costs of wholesaler suppliers in its brief, argues that the Commission has authority to obtain records from wholesale suppliers, (AG Init. Br. at 19), and ultimately contends that “[t]he Commission has extensive powers under state and federal law to obtain information regarding generation costs and other data needed to determine whether costs are reasonable and prudent.” (AG Init. Br. at 20 (emphasis added) However, the Attorney General later concedes that ComEd must be allowed to purchase wholesale electricity at “market price.” (AG Init. Br. at 78). This pivotal concession validates ComEd’s tariff proposal, because there is in fact no better way to ascertain the “market price” of wholesale electricity than through an open and fair competitive auction at which all wholesale suppliers may participate. See Section VI, *infra*. To the extent the Attorney General continues to suggest, as it does earlier in its brief, that the Commission may consider generation costs in determining whether ComEd’s rates are just and reasonable, (AG Init. Br. at 20), those arguments are inconsistent with federal law.

⁶ The statute provides that “[t]he term ‘sale of electric energy at wholesale’ . . . means a sale of electric energy to any person for resale.” 16 U.S.C. § 824(d).

the rates that will result from the proposed auction will be too high because the prices ComEd will pay in the open wholesale market are too high, (AG Init. Br. at 2), it is making an argument that is squarely foreclosed by the Federal Power Act.

This exclusive federal jurisdiction over wholesale electricity transactions stems from their uniquely interstate character. The Supreme Court has explained that “unlike the local power networks of the past, electricity is now delivered over three major networks, or grids. . . . [A]ny electricity that enters the grid immediately becomes a part of a vast pool of energy that is constantly moving in interstate commerce.” *New York v. FERC*, 535 U.S. at 7; *see also id.* at 7 n.5 (“[E]nergy flowing onto a power network or grid *energizes the entire grid*, and consumers then draw undifferentiated energy from that grid.’ As a result . . . any activity on the interstate grid affects the rest of the grid.”) (emphasis in original) (internal citation omitted).

FERC actively regulates the precise issues raised by the Attorney General in its brief: whether a wholesale market is competitive, and whether a wholesale supplier may charge rates based on market prices, rather than costs. *See, e.g., AEP Power Mktg., Inc.*, 107 FERC ¶ 61,018 (2004), *on reconsideration*, 108 FERC ¶ 61,026 (2004) (defining new FERC standards for market-based rate authority).⁷ In a 1994 order, FERC distinguished the market-based approach from a cost-based one: “In the case of a market-based formula rate . . . neither the rate (which is the formula itself) nor any of its individual components has to be justified on a cost basis. Rather, if the Commission is satisfied that the rate results from competitive market forces or that the seller does not have market power over the buyer, *we do not examine the underlying cost structure of the seller.*” *Ocean State Power II*, 69 FERC ¶ 61,146 at 61,546 (1994) (emphasis

⁷ A wholesale supplier may request initial market-based rate authority by filing a blanket rate schedule with FERC to sell at negotiated rates pursuant to section 35.13 of the Commission’s regulations. *See* 18 C.F.R. § 35.13. Exelon Generation has market-based rate authority. *See Exelon Generation Co.*, 112 FERC ¶ 61,027 (2005).

added). The Attorney General in fact concedes that FERC “has increasingly allowed electricity wholesalers to charge market-based rates”; that FERC only may do so where there is a competitive market; and that FERC recently revoked Duke Power’s market-based rate authority. (AG Init. Br. at 15-16) Given that these matters indisputably are regulated by FERC, they “may not be collaterally attacked” in state proceedings. *Mississippi Power*, 487 U.S. at 375.

The Supreme Court also has made clear that FERC jurisdiction over wholesale electricity rates and agreements preempts state regulation even if FERC has not yet acted. Thus, in *Nantahala*, the Court observed that it earlier had overturned a state court decision that had assumed the Federal Power Commission (the “FPC”) would approve certain rates as reasonable, although the rates in fact were never filed with the FPC.⁸ The Court had explained that “the [FPC] alone is empowered to make that judgment [of reasonableness].... The court below ... has consequently usurped a function that Congress has assigned to a federal regulatory body.” 476 U.S. at 964 (quoting *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 581-82 (1981); brackets in original). Similarly, in *Mississippi Power*, the Court held that “[t]he Mississippi Supreme Court erred in adopting the view that the pre-emptive effect of FERC jurisdiction turned on whether a particular matter was actually determined in the FERC proceedings.” 487 U.S. at 374.

Thus, the Attorney General’s arguments in its brief are misdirected. The ICC has no power to determine, based upon its assessment of the competitiveness of the wholesale market, whether wholesale transactions should be based upon market prices or the costs of particular wholesale suppliers. Those are matters exclusively for FERC to decide. If the Attorney General is dissatisfied with FERC’s regulation of the wholesale market, or with FERC’s grant of market-based rate authority to any particular wholesale supplier, it must raise those objections with

⁸ The FPC was the predecessor of FERC.

FERC, not with this Commission. The Commission should reject the Attorney General's invitation to examine, and presumably base retail rate decisions upon, the costs of wholesale suppliers, because such examination has nothing to do with "the effective discharge of the State commission's regulatory responsibilities." 16 U.S.C. § 824(g).

2. The Attorney General misconstrues the "*Pike County*" exception to federal preemption of state review of wholesale transactions.

The Attorney General relies heavily on the so-called "*Pike County*" exception, *see Pike County Light & Power Co.*, 465 A.2d 735, to federal preemption of state review of a utility's wholesale electricity purchases. (*See* AG Init. Br. at 15 (citing *Pike County*); *id.* at 18 (same); *id.* at 19 (same); *see also* CCSAO Init. Br. at 17-18) On the basis of *Pike County*, the Attorney General contends that "the ICC has authority to determine whether the cost of wholesale electricity purchased at FERC-approved wholesale rates, was prudently and reasonably incurred" (AG Init. Br. at 18), and it cites *Pike County* for the proposition that "[t]he ICC's authority to review costs incurred by electric utilities, to determine whether they are just, reasonable and prudently incurred, *extends to review of the cost of electricity* procured under wholesale rates established by FERC" (AG Init. Br. at 19, *emphasis added*).

But *Pike County* stands for the narrow proposition that when a utility chooses among various wholesale providers, it must choose prudently and may not unreasonably favor its own high-cost affiliate. Nothing in *Pike County* remotely suggests that a state commission has the authority to declare that the lowest cost wholesale provider's rates as determined in an open auction are "too high" and may not be recovered through retail rates.

The facts of the case are instructive. *Pike County*, a utility, appealed a disallowance of cost by the Pennsylvania PUC. *Pike's* power supply was provided by its parent company

(Orange & Rockland, a New York State operating utility), through a power supply agreement filed with FERC. Substantial evidence before the PUC, however, showed that Pike had not even considered other lower-priced sources of power. In particular, Pike had not considered the viability of power purchases from Pennsylvania Power & Light Company (“PPL”), pursuant to *lower* PP&L rates also approved by FERC. *See* 465 A.2d at 738 (“Pike failed to even explore this alternative to the more costly purchases from its parent company”). The fact that Orange & Rockland’s rates may have been reasonable in light of its own costs (at a time when FERC’s regulation was cost-based) did not justify Pike’s purchases from its parent company at higher rates than Pike could have obtained from another, more local supplier.

The *Pike County* court’s affirmance of the PUC’s disallowance of costs clearly does not support the proposition that a state utility commission may review the competitiveness of wholesale markets or whether a wholesale provider’s prices are “too high.” *Pike County* stands for the proposition that a state commission may require a utility to consider competitive alternatives where such alternatives exist, rather than to purchase blindly from a high-cost affiliate. *Pike County* hardly supports rejection of ComEd’s competitive auction proposal here, in which *all* potential suppliers, affiliated and unaffiliated, have an open and fair opportunity to compete to supply electricity to ComEd.

This correct construction of *Pike County* is not open to dispute. In both *Nantahala* and *Mississippi Power*, the Supreme Court considered and *rejected* a broad construction of *Pike County* identical to that proposed by the Attorney General here. In *Nantahala*, a state commission disallowed recovery of wholesale costs just as the Attorney General is arguing the Commission should do here. The Supreme Court reversed, holding that “a state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred as

a result of paying a FERC-determined wholesale price....Once FERC sets such a rate, a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A State must rather give effect to Congress' desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority." 476 U.S. at 965, 966; *see also Mississippi Power*, 487 U.S. at 371-73. Stated differently, "[s]uch a 'trapping' of costs is prohibited." *Nantahala*, 476 U.S. at 970.

In so ruling, the Supreme Court explained that its decision was entirely consistent with the *Pike County* case. The Court in *Nantahala* explained: "Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*." *Id.* at 972 (emphasis in original) (citing *Pike County*); *see also Mississippi Power*, 487 U.S. at 373-74. The key, however, is whether "lower cost power is available elsewhere." *Nantahala*, 476 U.S. at 972. Whereas the utility in *Pike County* made no effort even to consider whether "lower cost power" was available from suppliers other than its parent, here ComEd's competitive procurement auction is expressly designed to identify the "*lowest* cost power" available from *any* wholesale supplier.

3. ComEd has not impermissibly failed to consider purchasing electricity at below-market prices from its affiliate.

The Attorney General's ultimate objection to ComEd's tariff proposal is set forth at the outset of its brief: "ComEd has failed to adequately consider . . . use of its substantial buying power to negotiate with its generation affiliate to purchase low-cost electricity from Exelon's Northern Illinois generating plants, which ComEd customers paid to build and maintain." (AG Init. Br. at 2) Obviously, if Exelon Generation offers the lowest available *market* price at the

auction, it will be selected under ComEd's proposal. Accordingly, "low-cost" in this context can only mean one thing: at *below-market* wholesale prices.

The Attorney General is asking the Commission to ignore controlling federal law: the Commission simply cannot compel such a below-market transaction. Wholesale electricity contracts between affiliated companies are directly controlled by explicit federal standards, and those standards require FERC review of wholesale transactions between a utility and an affiliate at market-based rates, to ensure that such insider transactions do not unduly favor affiliates or harm the competitive wholesale market. *See, e.g., Boston Edison Co.*, 55 FERC ¶ 61,382 (1991) *Edgar*; *Allegheny Energy Supply Co.*, 108 FERC ¶ 61,082 (2004); *Southern California Edison Co.*, 106 FERC ¶ 61,183 (2004); *Ameren Energy Generating Co.*, 108 FERC ¶ 61,081 (2004). As explained in *Edgar*, "Under section 205(a) of the Federal Power Act, all rates for the transmission or sale of electric energy at wholesale in interstate commerce must be 'just and reasonable' and not unduly discriminatory or preferential. Market-based rates for sales involving affiliates will be found to violate section 205(a) of the FPA unless there is a clear showing of lack of potential affiliate abuse." 55 FERC ¶ 61,382 at 62,167 (footnotes omitted).

In *Southern California Edison*, FERC noted the traditional concern (also present in the *Pike County* case, *supra*) that a utility may unduly favor rates offered by its affiliate seller over lower rates offered by other non-affiliated sellers. 106 FERC ¶ 61,183 at 61,145. FERC emphasized, however, this was not its *only* concern: "We are *also* concerned that granting undue preference to affiliates, whether through cost-based or market-based transactions, *could cause long-term harm to the wholesale competitive market.*" *Id.* at 61,145, ¶ 59 (emphasis added); *see also Allegheny Energy*, 108 FERC ¶ 61,082 at 61,419. Requiring a sweetheart deal between affiliates at below-market rates would assuredly invite complaints at FERC from wholesale

competitors who were foreclosed from selling in northern Illinois, and private investment in generation could be discouraged as well.⁹

FERC held in *Edgar* and other cases that for a utility to establish that an affiliate transaction is reasonable, it must show that the rate is comparable to the price of an arms-length transaction between non-affiliates. “[T]he essence of the test is that a franchised utility must make a showing that a sale of power at market-based rates from its own affiliate is reasonably price compared to alternatives in the market.” *Report of the Electric Utility Regulation Committee*, 26 Energy L.J. 217, 244 (2005); *see also Southern California Edison*, 106 FERC ¶ 61,183 at 61,638, ¶ 11. Significantly, as FERC explained in *Edgar*, “[i]n an arm’s-length (unaffiliated) transaction, the buyer has no economic incentive to favor anyone but the least-cost supplier (considering price and nonprice factors).” 55 FERC ¶ 61,382 at 62,168.

In *Edgar*, FERC identified three showings a utility could make to establish the reasonableness of an affiliate transaction – each of which requires proof the sale is comparable to an arms-length transaction between non-affiliates. As the Attorney General is forced to acknowledge, *Edgar* requires (1) “evidence of direct head-to-head competition between the affiliate and competing unaffiliated suppliers in a formal solicitation or informal negotiation process”; (2) “evidence of the prices which non-affiliated buyers were willing to pay for similar services from the affiliate”; or (3) “benchmark evidence that shows the prices, terms and

⁹ ComEd and Exelon Generation have sought approval from FERC of any affiliate transactions that could result from the auction. *See* Application of Commonwealth Edison Co. and Exelon Generation Co. Under Section 205 of the Federal Power Act, FERC Docket No. ER06-43-000 (filed Oct. 17, 2005) (attached hereto as Exhibit A). Such approval is necessary as a result of the FERC decisions cited above. Thus, ComEd is not asking the Commission alone to review and approve the auction process, but also has sought the approval of FERC that any affiliate transactions resulting from the auction will be permissible under governing federal law controlling such wholesale electricity transactions. Of course, under *Nantahala* and *Mississippi Power*, such FERC approval would foreclose the Commission from denying recovery of those wholesale costs, just as with any FERC-approved wholesale transaction. The nature of the auction, if approved contemporaneously by this Commission, would preclude any *Pike County* claim that cheaper wholesale electricity was available elsewhere. *See* Section III.C.2, *supra*.

conditions of sales made by non-affiliated sellers.” (AG Init. Br. at 17, emphasis added) None of those criteria are met in the Attorney General’s proposal. Although FERC has stated that these three options were not intended to be an all-inclusive list, *id.*, FERC has never deviated from the fundamental requirement that wholesale electricity transactions between affiliates must be comparable to arms-length transactions between non-affiliates. *See, e.g., Allegheny Energy*, 108 FERC ¶ 61,082; *Ameren Energy*, 108 FERC ¶ 61,081.

Indeed, FERC recently *expanded* the application of the *Edgar* standard to the precise circumstance advocated by the Attorney General here: a wholesale contract between affiliates at *cost*-based rates. *Southern California Edison*, 106 FERC ¶ 61,183. FERC explained that “we will henceforth require that all affiliate long-term (one year or longer) power purchase agreements, *whether at cost or market*, be subject to the conditions set forth in *Edgar*.” *Id.* at 61,645, ¶ 58 (emphasis added).

In essence, the Attorney General seeks to force Exelon Generation to subsidize the delivery of electricity to Illinois consumers at below-market rates. In addition to the preemptive effect of the FERC decisions cited above, any effort by the State to do so would violate clearly established state and federal law. *See, e.g., Mich. Bell Tel. Co. v. Engler*, 257 F.3d 587, 594 (6th Cir. 2001) (“although the [utilities] have other unregulated income streams, they are not required to subsidize their regulated services with income from rates either deemed to be competitive, or with revenues generated from unregulated services”); *Brooks-Scanlon Co. v. Railroad Comm’n*, 251 U.S. 396, 399 (1920) (Holmes, J.) (same); *New England Power Co. v. New Hampshire*, 455 U.S. 331, 338 (1982) (holding that efforts by a State to reserve for its residents any benefits or

cost advantages of wholesale electricity generated within the State violate the Commerce Clause).¹⁰

4. The Attorney General misconstrues the issues before the Commission.

For all these reasons, the Attorney General fails to address the issues that properly may be decided by the Commission in this proceeding. The Commission is empowered to ensure the auction will result in the prudent procurement of electricity for ComEd's customers. ComEd's proposal is designed precisely to achieve that result. It creates a format in which *all* potential wholesale suppliers may compete fairly, without discrimination or preference, thereby identifying the lowest cost manner for ComEd to meet its supply obligations. The Commission certainly has a role, to the extent not inconsistent with federal standards, *see, e.g., Allegheny Energy*, 108 FERC ¶ 61,082 at 61,417 (identifying criteria for sufficiency of competitive bid process), to ensure that the auction is structured to provide a fair and level playing field for all participants, so that the auction in fact constitutes a prudent procurement method for ComEd to use and produces just and reasonable rates for ComEd's customers. But the Commission may not, as invited by the Attorney General, assess the competitiveness of the wholesale market in Illinois and evaluate the reasonableness of ComEd's rates based on the costs of ComEd's wholesale suppliers.

¹⁰ The suggestion by the Attorney General that ComEd's customers "paid to build and maintain" the generating plants now owned by Exelon Generation is highly misleading. (AG Init. Br. at 2) Those plants, and all the decommissioning and other liabilities associated with those plants, were transferred from ComEd to Exelon Generation, pursuant to the explicit authority of 220 ILCS 5/16-111(g), following a public proceeding in which all parties here participated. *See In re Commonwealth Edison Co.*, Proceeding Pursuant to Section 16-111(g), 2000 Ill. PUC LEXIS 667 (Aug. 17, 2000). The Commission approved the transfer, and the PUA specifically precludes further review of that transaction. 220 ILCS 5/16-111(g).

IV. SUFFICIENCY OF THE COMPETITIVE MARKET

Although the Commission's jurisdiction with regard to wholesale electricity markets and specific wholesale transactions is limited, see Section III(c), *supra*, the record evidence amply demonstrates that the wholesale electricity market is sufficiently developed to allow the Commission to determine that ComEd's auction proposal is a prudent – and, indeed, is the most superior – method by which ComEd may make the wholesale purchases of electricity necessary to serve its customers. The evidence shows that the wholesale electricity market from which ComEd must and will purchase the electricity is functional, efficient, and competitive. That market:

- Is regional, stretching from the Atlantic coast to the western boundary of Illinois and, in many cases, to MISO and other regions beyond. (Naumann Dir., ComEd Ex. 5.0, 5:103-112)
- Is deep and unconcentrated. There are literally hundreds of independent sellers and buyers of energy and dozens of independent parties transacting in capacity, in a market that is nearly ten times as large as the total quantity of power and energy ComEd will need to purchase at peak. (*Id.* at 12:267 – 13:289)
- Operates under transparent rules that provide for efficient economic dispatch of generation, efficient economic resolution of transmission constraints, and that let market participants bid for auction load without requiring physical transmission into ComEd's service territory. (*Id.* at 5:92-98; 24:523 – 26:567)
- Has an effective transmission planning process, designed expressly to address risks of future transmission congestion, and a track record of successful generation entry. (*Id.* at 15:320-338, 19:416-421)
- Is subject to plenary oversight and control by the independent PJM RTO and FERC itself, as well as to constant monitoring by PJM's dedicated Market Monitoring Unit ("MMU"). (*Id.* at 1:9-12, 21:455-468)
- Has no historical record of falling victim to collusion or other market misconduct, and no history of permitting new load pockets to form in which generator access is restricted to geographically-local units.

The evidence equally shows that the PJM market is anything but the "immature," "concentrated," "non-functional," or manipulable caricature that the few objecting intervenors

portray. As will be shown here, parties making such claims do so based on a combination of bare assertions with:

- Reliance on obsolete generation and congestion data, and descriptions of markets and market behavior that predate ComEd's and AEP's full integration into the very regional PJM market that they try to attack;
- A trivial notion of "transmission constraints," calimed to exist wherever nodal prices for generation differ, regardless of the fact that both economic transactions and physical flows continue across the market undisturbed;
- A persistent reliance on a strawman market definition -- a distinct "northern Illinois market" that does not exist; and
- Invocation of the threat that -- despite the newest and best evidence to the contrary -- unspecified problems could occur in the market in the future, without explanation of how any other procurement system could be expected to weather such events any better.

The objecting intervenors' various arguments are made in parts of the outline of Section IV, and in some cases, in more than one. For efficiency and clarity, ComEd will attempt to address them in a combined fashion, referring to specific arguments as they relate to the outline.

A. Markets' Relationship to Auction Process

As shown in ComEd's Initial Brief, the wholesale electricity market in PJM is well established and geographically vast. (Naumann Dir., ComEd Ex. 5.0, 5:103-112) It is unconcentrated, with a huge number of participants and a volume many times greater than ComEd's needs. (*Id.* at 12:267 – 13:289) It possesses tested mechanisms for dealing with both congestion and transmission expansion needs. (*Id.* at 5:92-98; 24:523 – 26:567) The AG, however, asserts that "the wholesale market in and around Illinois is not sufficiently developed, at this time, to ensure a level of competition among suppliers that yields competitive prices." (AG Init. Br. at 20) The evidence of record overwhelmingly refutes this assertion. Indeed the AG is forced almost immediately to concede tacitly that the assertion rests on speculative

scenarios: “*if* there were an insufficient number of suppliers or there is inadequate transmission access to import electricity into the ComEd service territory, *it is possible* that one supplier or a small group of suppliers *would be able* to have *some degree* of control over the wholesale market price.” (AG Init. Br. at 21, emphasis supplied) As shown below, the record in fact shows that there *are* a sufficient number of suppliers, that there *is* adequate transmission capacity into northern Illinois, and that no supplier or small group of suppliers will have any degree of control over the wholesale market price.

The record evidence shows beyond cavil that PJM operates the largest, most experienced, and most sophisticated wholesale electric market in the United States. (Naumann Dir., ComEd Ex. 5.0, 12:267 – 13:289; Hieronymus Reb., ComEd Ex. 15.0, 6:112-126) The PJM region has included more than 130,000 MW of load, 160,000 MW after integration of Dominion, and an even larger volume of generation, compared to less than 20,000 MW of ComEd load. (Naumann Dir., ComEd Ex. 5.0, 12:267 – 13:289) It is centrally dispatched using structure that ensures efficient dispatch of generation, deliverability of energy to load, and efficient use of the transmission system. (*Id.* at 7:145-148; Hieronymus Reb., ComEd Ex. 15.0, 6:112-126) That market structure has been tried and found efficient and effective for years in a huge area of the country and ComEd’s integration into it was approved by FERC. (Hieronymus Reb., ComEd Ex. 15.0, 5:107 – 6:126) As Midwest Gen notes, the competitiveness of the PJM market will allow retail customers in northern Illinois to gain the advantages of efficient wholesale pricing. (Midwest Gen. Init. Br. at 4-6) Midwest Gen also explains that the conditions in northern Illinois compare favorably to those in New Jersey, which already has run several very similar auctions successfully. (Midwest Gen. Init. Br. at 5-6)

The suggestion that there may not be enough suppliers to make the PJM market competitive is absurd.

For example, even AG witness Dr. Rose readily recognized the extensive level of diversity of entities already competing in PJM. Having agreed that one component of a competitive market is having many buyers and sellers, Dr. Rose noted that the number of unaffiliated entities that sold more than 1000 MW of power in PJM last year was “probably in the hundreds.” (Rose Tr., 662:9-663:5) Dr. Rose, moreover, acknowledged that, even in his view, “dozens” of different unaffiliated generator owners or other power marketers submitted bids in the PJM market for delivering resources to northern Illinois specifically, and admitted that he would not be surprised if the number were over a hundred. (Rose, Tr. 663:6-14)

Given the breadth of the PJM market, a very large number of suppliers is available to bid into the proposed auction. As Dr. Hieronymus emphasized, suppliers will have every incentive to sell into the auction as an organized opportunity to enter into long-term contracts, thus avoiding the volatility of the spot market. (Hieronymus, ComEd Ex. 15, 18:367-19:377) As Mr. Naumann noted, ComEd’s expectation that supplier participation will be brisk is strongly supported by the data to date, including the fact that there is already a robust forward market at the northern Illinois trading hub, where over twenty active market participants engage in transactions, including fifteen generation owners and ten purely financial players. (Naumann Dir., ComEd Ex. 5.0, 24:525-530) Furthermore, as discussed in sub-section G below, no transmission constraints¹¹ into northern Illinois currently exist or appear likely to arise in the

¹¹ ComEd will use the term “transmission constraints” to refer a condition on the transmission system that would prevent energy flows to local load from the regional market (*i.e.*, that would create a load pocket) or that would make participation in the auction by financial sellers or sellers with remote generation impossible or impractical at competitive prices. “Congestion” is the meaningful term for the LMP differentials that arise between nodes from the common result of efficiently maximizing the use of finite transmission system elements. (Naumann Sur.,

future. Accordingly, contrary to the AG's suggestion (AG Init. Br. at 21), the record evidence unquestionably shows that there is a robustly competitive wholesale market of which northern Illinois forms an integral part and that market will provide support for an efficient competitive outcome in the Illinois Auction.

The AG also claims that whether retail customers will benefit from the auction depends on the resolution of three purported problems – (1) the alleged concentration of generation ownership, (2) the question whether PJM administrative costs are justified through operating cost efficiencies and (3) the alleged fact that wholesale prices may be set on a part of the supply curve where they rise vertically. (AG Init. Br. at 21-23) All of this is baseless speculation on the AG's part. Moreover, as stated above, the only issue regarding the wholesale market proposed before the Commission is whether the Illinois Auction is a prudent means by which ComEd may procure electricity from the wholesale market.

(1) As discussed in sub-section F below, northern Illinois is not a separate market, but an integral part of the PJM market, in which generation ownership is not highly concentrated. (2) The question the AG attempts to raise about PJM administrative costs appears nowhere in the record and is being raised for the first time on brief.¹² The question is in any case irrelevant to any issue in this docket. (3) The record also demonstrates that the AG's concern that wholesale prices will be set along the vertical segment of the supply curve in many hours of the year is groundless. The vertical part of the curve consists of old, inefficient peaking units that are expensive to run. In PJM, and especially the Midwestern part of PJM, there is so much excess

ComEd Ex. 23.0, 5:92-104) Congestion neither creates a load pocket nor is evidence of market failure. (Naumann Sur., ComEd Ex. 23.0, 5:105-6:119)

¹² The AG says that the three factors are discussed in Dr. Rose's Direct Testimony, AG Ex. 1.0 at 7-21. (AG Init. Br. at 22 n.27) However, the cited passage does not discuss "The increased costs of operating ISO or RTO" nor is the AG's argument supported by the record. Therefore, the AG's arguments under the heading "Transmission Costs" should be ignored.

capacity that such units rarely run in merit and set prices. The units generally run only for testing, to solve local problems, or as a consequence of providing ancillary services. None of these activities affects energy market prices. (Hieronymus Reb. ComEd Ex. 15, 28:566-572)

Despite the full record in this proceeding, the AG urges delay, suggesting the Commission must study alleged structural problems in the wholesale market further. (AG Init. Br. at 23-24) This position is without merit. As explained in detail above, questions about alleged problems in the wholesale market are properly addressed to FERC, not to this Commission. Even if the existing wholesale market is not perfect, the Illinois Auction remains a prudent, and indeed, is the most superior alternative for procuring wholesale electricity after 2006. (Clark Dir., ComEd Ex. 1.0, 12:276-285, 18:409-416; McNeil Dir., ComEd Ex. 3.0, 8:164-14:307) As Staff has noted, opponents of the auction have not shown why the New Jersey model should be rejected, or how an alternative would somehow circumvent a less-than-competitive wholesale market and produce a better result for consumers. (Staff Init. Br. at 18) In fact, Staff explained that the alternatives being suggested by the AG, CUB, and CCSAO, “(i) still rely upon the same wholesale market, (ii) involve actions arguably outside the scope of the Commission’s jurisdiction, (iii) involve actions arguably contrary to Illinois statutes, or (iv) are simply too vague and incomplete.” (Staff Init. Br. at 19)

B. Other Jurisdictions’ Experience with Competitive Electricity Procurement

The AG uses this section of its brief (included in the agreed outline at the AG’s urging) to argue that restructuring of the electric industry to take advantage of competitive forces and market structures -- which the Act established as a goal of the State -- is a poor public policy choice compared with the regulated monopoly structure that predated the 1997 Restructuring Law. (AG Init. Br. at 24-31) Thus, the AG argues that most states have opted to stay with cost

of service regulation and that the trend is away from restructuring. (AG Init. Br. at 24-25) Such arguments are not properly addressed to the Commission but to the Legislature, as the AG presumably understands. Illinois' restructuring has been highly successful to date. Among those benefits are that almost half of ComEd's large customers are taking service from competitive suppliers (O'Connor Dir., CES Ex. 1.0, 34:745-755) of their choosing, and customers of all types have saved billions of dollars. (Clark Dir., ComEd Ex. 1.0, 5:118 – 6:136) The AG makes no attempt to deny this, nor to explain how "trends" – based on states that have never restructured, are not part of RTOs, rely on allocations of federal hydro-power, or (unlike Illinois) are addressing poorly designed programs - would allow the Commission to ignore either the changes brought about by the 1997 Restructuring Law or the demonstrated benefits of the Illinois Auction Proposal to customers in this State.

The most relevant experience in other states is that of New Jersey, whose auction the AG recognizes is the process most similar to the Illinois Auction proposal. (AG Init. Br. at 26) New Jersey is in PJM, has restructured utilities that own substantially no generation, has ended its transition, and has significant retail switching in its commercial and industrial classes. (LaCasse Dir., ComEd Ex. 4.0, 17:371-19:435) The New Jersey auctions, which have been conducted since 2002 to acquire \$5 billion of electric supply, have been a clear success and have been widely applauded, including by the New Jersey consumer advocate. (LaCasse Dir., ComEd Ex. 4.0, 5:105 – 6:134) The New Jersey process maximizes the transparency of the procurement decision, requires bidders to compete on equal footing, and involves prices set by the forces of supply and demand. (Moler Dir., ComEd Ex. 2.0, 9:198-202) In addition, the New Jersey experience demonstrates that a competitive auction process that is approved by a regulatory

authority and run by an independent party, such as the Illinois Auction proposal, ensures that suppliers affiliated with a utility are not being favored.

Furthermore, the New Jersey auctions have demonstrated convincingly that the PJM market works in the context of an auction like the Illinois Auction Proposal. In each hour PJM dispatches the entire system so that all loads are served by the lowest-cost resources available. Separate and apart from this, parties can enter into forward contracts – such as in the auction – in which they fix the price of electricity between them in advance. For this reason, even though areas of New Jersey are constrained as to transmission imports (which the data show is not the case for northern Illinois), the bidders in the New Jersey auctions have not been limited to companies with local generation portfolios. Rather, there also have been many other competing suppliers bidding into those auctions at fixed prices, including owners of peaking generation who use financial products or forward contracts to supplement their own generation, financial players such as Morgan Stanley who do not own any generation in PJM, and other generators outside PJM. (Naumann Dir., ComEd Ex. 5.0, 19:416-20:435); Moler Dir., ComEd Ex. 2.0, 4:87-5:101)

ComEd President Frank Clark noted that New Jersey's success in bringing the benefits of competition to its customers and driving down power and energy prices was a significant factor in developing the Illinois Auction Proposal. He also noted that suppliers' participation in the New Jersey auctions shows their acceptance of the New Jersey model. (Clark Dir., ComEd Ex. 1.0, 16:381-17:388)

The AG points out that in the 2002, 2003 and 2004 New Jersey auctions, prices increased modestly or declined modestly, but that in the 2005 auction they increased more significantly. (AG Init. Br. at 26-27) This increase in wholesale prices, however, was moderated by the mix of different contract lengths in the auction, which increase price stability over time. (McNeil Dir.,

ComEd Ex. 3.0, 24:525-27:580) This stability will be enhanced in the Illinois Auction by ComEd's inclusion of five-year contracts, which are not part of the New Jersey solicitation. (*Id.*) Dr. Hieronymus explained that the 2005 increase was attributable to significant fuel cost increases. (Hieronymus Reb., ComEd. Ex. 15.0, 32:664-666) The AG quarrels with Dr. Hieronymus' coal price increase data (AG Init. Br. at 27), but as Dr. Hieronymus explained on surrebuttal, the AG is not using prices from eastern mines, relevant to the spot price that can set marginal electricity prices. (Hieronymus Sur., ComEd Ex. 24.0, 26:554-565)

The AG goes on to list other jurisdictions that have adopted other competitive procurement mechanisms and in which electric rates have increased. (AG Init. Br. at 27-31) None of this travelogue is relevant to this proceeding. Presumably the AG again wishes to suggest that the Illinois legislature made a bad policy choice when it enacted the Restructuring Act in 1997. That argument, again, is not cognizable here. In addition, this string of examples assumes a causal relationship that does not appear in the record. Commodity price increases have explanations. Mr. McNeil explained, for example, that the price of supply under any procurement process will depend on the cost of the inputs (such as fuel prices), as well as the balance between supply and demand. (McNeil Sur., ComEd Ex. 18.0, 18:383-391) Dr. Hieronymus concurred, noting that other factors, such as fuel price increases, have contributed to the increases. (Hieronymus Reb., ComEd Ex. 15.0, 32:664-33:681) Fuel cost increases increase the price of electricity under either a competitive market model or a regulated monopoly model of the industry. Even CUB-CCSAO witness Dr. Steinhurst suggested that many factors, including increased fuel costs and power market prices, caused price increases. (Hogan Sur., ComEd Ex. 25.0, 15:304-313); Steinhurst Reb., CUB-CCSAO Ex. 4.0, 29:643-650)

C. Retail Market Conditions

The AG uses this section of the brief (included in the agreed outline at its urging) to survey the extent of retail competition in the United States in support of its argument that industry restructuring is a mistake. (AG Init. Br. at 31-33) This is not an argument that may be heard in this forum. The state of competition in the Illinois retail market, let alone in other states, is not an issue in this case, which deals with a proposed competitive procurement methodology for retail customers that continue to take bundled service from ComEd. It is undisputed that as yet no competitive provider has offered to supply electric service to residential customers in Illinois. But the AG, CUB and CCASO refuse to see the reason for this, which is as plain as day. As Ms. Moler testified, competitive providers cannot make a profit from supplying residential customers who are paying rates that are 20% lower than they were in 1997. (Moler Dir., ComEd Ex. 2.0, 4:70-83)

By contrast, the record shows that many commercial and industrial end-use customers in ComEd's service territory have directly taken advantage of offerings by competitive suppliers, and that even smaller commercial and industrial customers in ComEd's territory have switched, although not in the same numbers. CES recognizes these positive developments, noting that the commercial and industrial market has developed well and that benefits are already being delivered to consumers. (CES Init. Br. at 13-17)

Further, as Ms. Moler explained, it is the very lack of development in the retail market for the smallest customers that requires ComEd to act as an aggregator of their load, obtaining power prudently in the wholesale market and passing the wholesale cost of the power, and thus the benefits of wholesale competition, along to customers. (Moler Dir., ComEd Ex. 2.0, 4:70-83) Moreover, the evidence shows while there can be no guarantee that supply costs will not

rise, competitive forces are the best tool to ensure that those costs are held as low as reasonably possible in the future. (Moler Dir., ComEd Ex. 2.0, 2:38-3:51)

D. Relevant Product Market

1. Required Products

Auction bidders must be able to supply electric power and energy and applicable ancillary services as required to serve the retail load represented by the tranches that they win. As a practical matter, the energy supply portfolio must include base load, intermediate, and peaking output -- or the responsibility to bear the financial costs of such supply. No party disputed these facts, or the fact that the record showed that all of the required resources were available from the PJM markets and/or bilaterally within PJM. No other party raised other issues directed to this sub-section.

2. Physical vs. Financial Markets

The record showed that auction suppliers could meet their load obligations through generation that they owned, controlled, or purchased themselves, and that the required capacity was available and deliverable within PJM. (Naumann Dir., ComEd Ex. 5.0, 24:523 – 26:554) The evidence, however, also showed that bidders could compete robustly in the auction without any physical generation, or regardless of a bidder's ability to physically deliver its own generation, through the financial markets made possible by the PJM structure. (Ogur Dir., Staff Ex. 4.0, 20:452-457) The significance of this fact cannot be underestimated: regardless of the physical transmission condition or configuration, parties remain able to bid, and to hedge their bids using physical generation. (Naumann Dir., ComEd Ex. 5.0, 24:523 – 26:567) No party directly commented on these facts or offered other arguments properly directed to this sub-section.

3. PJM Capacity Market

The evidence showed that the PJM capacity market, like the PJM energy market, is huge and unconcentrated, populated by numerous buyers and sellers. (Naumann Dir., ComEd Ex. 5.0, 1:19-2:25) There is no dispute about these facts. They are acknowledged by the same AG and CUB-CCSAO witnesses who purport to provide testimony supporting claims of market concentration. (Rose, Jt. Tr. at 662-665; Fagan, Jt. Tr. at 354-358)

The AG nonetheless claims that the “capacity market” in ComEd’s former control area is highly concentrated, and asserts that suppliers who do not already control generating capacity could find participating in the proposed auction very difficult. (AG Init. Br. at 34) There is, however, no separate capacity market in ComEd’s former control area and thus no reason why auction bidders would have to acquire capacity in that non-existent “market” to begin with. Northern Illinois is an integrated part of the PJM capacity market, as it is of the PJM energy market. (Fagan, Jt. Tr. at 359; Rose Jt. Tr. at 674-676) Moreover, in no event does the approach of pretending northern Illinois is a relevant capacity market suggest that the resources on which auction bidders can draw are concentrated. (Hieronymus Reb., ComEd Ex. 15.0, 20:400-410) Capacity is deliverable throughout PJM and, as noted above, the PJM capacity market is both huge and unconcentrated. (Naumann Dir., ComEd Ex. 5.0, 1:19-2:25) Indeed, by failing to address the ability of bidders to use financial markets, the AG has simply ignored the fact that bidders need not themselves own or control generation anywhere.

It is also worth noting that, to support its claim, the AG cites to portions of the PJM MMU’s 2004 State of the Market Report, which is not only irrelevant but underscores the fact that this argument relies on obsolete data about a market structure that no longer exists. In 2004, the period covered by the report, ComEd -- and AEP between ComEd and the rest of PJM -- were not fully integrated into PJM and PJM, therefore, operated a separate capacity market in

northern Illinois. (Hieronymus Reb., ComEd Ex. 15.0, 20:400-410) That is why the MMU evaluated it separately (and, even then found that local market only moderately concentrated). The answer, however, was to integrate ComEd, as occurred on June 1, 2005, not to pretend that the larger PJM market was inadequate or to falsely assert that a northern Illinois capacity market persists. In fact, the evidence is clear: since that date, suppliers of load in northern Illinois have been able to purchase their capacity literally anywhere in PJM. (Hieronymus Reb., ComEd Ex. 15.0, 20:404-405)

AG's suggestion about a supposed lack of capacity is even more speculative. There is not a shred of evidence suggesting that there is a shortage of deliverable capacity, and the record shows otherwise. PJM has more than enough capacity to be used by potential suppliers who do not own generation or have pre-existing bilateral contracts.

On the same subject, CCSAO's brief makes the equally unpersuasive claim that the PJM wholesale energy and capacity markets in northern Illinois are not fully competitive. (CCSAO Init. Br. at 20) It is unclear what, if any, basis CCSAO has for this claim. There is clearly no disagreement as to the markets' size, the large number of buyers and sellers, and the immense quantity of energy and capacity cleared compared to ComEd's needs.

CCSAO also asserts that the MISO spot energy markets are relatively "immature." (CCSAO Init. Br. at 20) The MISO spot market will have been in operation for several years by the time the auction is held, and there is no reason to expect that the MISO spot market will take years to develop. As the record shows, there is considerable experience with RTOs, and the MISO has had a long period of gestation. In addition, even with a somewhat immature MISO and some remaining seams issues, MISO and the integration of other Midwestern utilities into PJM has already enhanced competitiveness in the market. (Hieronymus Reb., ComEd Ex. 15.0,

29:604-30—30:618) Finally, it is unclear why the relative “immaturity” of the MISO market counsels against an auction, as opposed to some other method of procurement from the market, let alone why it is relevant to ComEd’s auction, which will depend primarily on the PJM market, a very mature market.

Indeed, no party explains why any of the arguments offered in this section is a reason to reject the auction. ComEd must use electric power and energy delivered using the PJM transmission system. It must acquire it using generators in PJM (or delivered through PJM), and must purchase resources in accordance with the PJM tariffs. Whether the electricity is purchased from an affiliate or competitively, whether the risks are managed directly and shouldered by ComEd’s customers or addressed competitively by suppliers, the generators will be dispatched and the transmission system operated by PJM. The resources and markets are much more than adequate to meet those needs; but even if they were not, that would hardly be a reason for Illinois to try to acquire resources from that market in an inferior way.

E. Relevant Geographic Market

1. Significance of Political Boundaries (e.g., Northern Illinois)

PJM operates energy and capacity markets in thirteen states and the District of Columbia. (Naumann Dir., ComEd Ex. 5.0, 12:267-270) The markets are operated on an integrated basis, with a single common dispatch, with unified market structures and rules, and a regional deliverability test applied to all capacity resources. (Naumann Dir., ComEd Ex. 5.0, 6:126-134) Despite repeated references (*see* Naumann Sur., ComEd Ex. 23.0, 8:155-170) in the objecting intervenor testimonies to the “ComEd control area” or “control zone,” those terms have no operational meaning -- a fact that their witnesses do not and cannot dispute this. (*See* Naumann Sur., ComEd Ex. 23.0, 8:155-170) Their witnesses do not and cannot dispute that the entire PJM

region is operated as a single, integrated control area and that, since its integration into PJM, ComEd has operated no distinct control area or function. (Naumann Dir., comEd Ex. 5.0, 6:126-134) There are, in short, no northern Illinois electrons. Their flow is not arrested or impeded at the state line. There is no preference given to using local generation to respond to changes in load. Generation throughout PJM -- as well as imports when net inflows into PJM are positive -- can and do serve load throughout the region. (Naumann Reb., ComEd Ex. 14.0, 10:201-208) And, there is no market structure that requires suppliers to have local supply. The claim, therefore, that there remains insular market structures that prevent either generators elsewhere in PJM beyond, or purely financial participants, from competing for ComEd load is simply no longer credible.

Nonetheless, the AG, CUB, and CCSAO all claim in varying terms that northern Illinois is the appropriate market to be used when analyzing with respect to ComEd's proposal. CUB asserts that potential binding transmission constraints could permit the exercise of market power in the area, while CCSAO claims that such potential constraints make the area proper for analyzing market concentration. (CUB Init. Br. at 14-15; CCSAO Init. Br. at 20-21) And while the AG says it is not claiming that northern Illinois is a relevant geographic market, its brief does not hesitate to talk about concentration and other market conditions in northern Illinois as if it were. (AG Init. Br. at 34-36) These assertions are incorrect on multiple levels.

As noted above, the record leaves no doubt that the relevant market, including for the purpose of measuring market concentration, is the entire PJM regional market. (Hieronymus Sur., ComEd Ex. 24.0, 32:688-706) None of the parties offers any response to either the regional structure established by the PJM tariffs or the operational reality of the regional market. Moreover, contrary to the AG's assertions that the market has not been studied economically, the

record contains two such studies -- both presented by Dr. Hieronymus, a leading expert in the area -- confirming the facts of the PJM market. The first showed that wholesale electric prices in northern Illinois are formed over a broad interstate area, and thus ComEd zonal prices are essentially identical to those in other areas of PJM. (Hieronymus Reb., ComEd Ex. 15.0, 10:203-11:223) The other is based on the U.S. Department of Justice and Federal Trade Commission *Merger Guidelines*, which define a relevant geographical market by whether a monopolist who controlled all the supply in that region could profitably sustain a small but significant price increase. Dr. Hieronymus showed that northern Illinois does not meet that test. (Hieronymus Reb., ComEd Ex. 15.0, 11:226-12:237)

Indeed, when confronted with the evidence that there is no separate ComEd market, both CUB-CCSAO witness Mr. Fagan and AG witness Dr. Rose acknowledged the facts. (Fagan, Jt. Tr. at 359; Rose Jt. Tr. at 674-676) Moreover, both made clear that they were not claiming that northern Illinois is a relevant geographical market for assessing market power. (Rose Reb., AG Ex. 5.0, 17:18–19:4; Fagan Reb., CUB-CCSAO Ex. 3.0, 13:299-301). In fact, each conceded that there is no such market. (*E.g.*, Fagan, Tr. 358:21 - 361:8; Rose, Tr. 646:11 - 647:9, 674:6 - 676:8). Yet, as noted above, the AG, CUB, and CCSAO continue to argue in their briefs as if there were such a market.

The objecting intervenors also claim that the northern Illinois area will somehow become a relevant market because of unspecified -- and, as noted elsewhere, utterly unsubstantiated -- “transmission constraints.” This argument is simply groundless. As discussed in sub-section G below, the record proves that no transmission constraints on imports into northern Illinois of the type that CUB and CCSAO hypothesize either exist now or can be reasonably assumed to exist in the future. Moreover, there is simply no evidence that any transmission constraints will ever

cause northern Illinois to become a load pocket or to be sufficiently isolated from the rest of PJM that bidders could not compete absent local generation -- the condition that would cause a separate local market to exist. Accordingly, there is no basis for the claims of these parties that northern Illinois should be the focus of hypothetical claims about market power and market concentration.

The equally groundless claim in the objecting intervenors' briefs that "market power" in northern Illinois will result in uncompetitive prices flows directly from the fiction that there is a concentrated northern Illinois market. (AG Init. Br. at 21-24, 39-42; CCSAO Init. Br. at 22-25) The fact is, however, that there is no evidence that market power can or will be exercised, locally or anywhere else in PJM, or that it could be exercised profitably. (Fagan, Jt. Tr. at 338) This is not simply because efforts to raise prices would be met inevitably by competing suppliers, as with any competitive market. The exercise of market power is also checked by the PJM market structure and by the market monitoring function. (Hieronymus Reb., ComEd Ex. 15.0, 11:226-12:246; Juracek Dir., ComEd Ex. 2.0, 6:121-131) The Commission should have no doubt on this point. It is not ComEd that is speculating about the ability of competition, a broad market, and market and legal structures to deliver efficient prices. Rather these objecting intervenors are speculating about an invented exercise of market power. Even including the period prior to ComEd's integration into the PJM market -- with its size and structure -- not a single witness on these subjects could identify a single instance of market power being exercised in northern Illinois.

Moreover, this claim again ignores the question before the Commission. Given that ComEd must acquire electricity in the wholesale market, how does the risk of market power argue for use of a less transparent, less competitive option than ComEd proposes? It also ignores

the nature of the auction and of the parties eligible to bid -- which includes purely financial players. Neither CUB nor CCSAO – nor the AG – alleged that the auction itself, which is essentially an auction for financial hedges, could be a market in which market power could be exercised. (Fagan Reb., CUB-CCSAO Ex. 3.0, 31:693-706) This omission is important, because to show market power in the auction, one would have to show that there was market power in the market for financial hedges, not in the physical spot markets mentioned by CUB-CCSAO. (Hogan Reb., ComEd Ex. 16.0, 19:405-419)

The AG also makes assertions about price convergence between northern Illinois and portions of PJM to the east. (AG Init. Br. at 34-36) Any price convergence is a function of the integration of the markets, not of the means ComEd chooses to buy its electricity. What these assertions do show, however, is how little credence even the AG's witnesses give to the claim that northern Illinois is a separate market. Moreover, price convergence is hardly a reason to reject the auction. Illinois is in a regional market and generators here operate under the PJM tariff as well as their own FERC tariffs. Rejecting the auction will simply result in giving up the benefits of competitive procurement in the broader market; it will not somehow keep Illinois separate or hold the prices at which local generators can sell their output below market.

ComEd, moreover, notes the irony in this argument: the AG wants to claim that northern Illinois is a separate market in which market power can be exercised at the same time as it argues that ComEd's integration into the regional market is increasing prices. If prices are converging, that only bolsters Dr. Hieronymus's study showing identical prices in the region, and underscores the conclusion that the entire PJM regional is the relevant market. Such a convergence also undermines CUB's and CCSAO's claim about transmission constraints, as prices in northern Illinois would be higher if there were such meaningful constraints on imports.

(Hieronymus Sur., ComEd Ex. 24.0, 25:578-549) At the same time, nothing in any alleged price increase is tied to integration of the markets.

2. PJM/MISO “Seam” and Joint Operating Agreement.

CCSAO asserts that a “seam” exists between PJM and MISO, the two RTOs operating in Illinois, so as to impose impediments to transactions occurring between the two, and that this would make markets in both RTOs less competitive. (CCSAO Init. Br. at 21) CCSAO errs. For purposes of the competitiveness of the auction, the seam is largely technical and is no impediment. But, even if it were, the PJM market is large enough to support the ComEd auction itself. (Naumann Reb., ComEd Ex. 14.0, 17:345–346) Moreover, the seam is simply no reason to reject the auction in favor of some other procurement process.

CCSAO’s assertion that a seam exists ignores several important facts regarding PJM and MISO. First, the record shows that PJM and MISO is in the process of implementing a joint and common market under which they will essentially operate one market. (Naumann Reb., ComEd Ex. 14.0, 17:363 – 18:373) The record shows that PJM and MISO have already taken essential steps towards the joint and common market and that concluding work is underway. (*Id.*)

Second, CCSAO essentially ignores the fact that, as of December 1, 2004, FERC eliminated the transmission rate “barrier” between the two RTOs, so that a transaction passing between them pays only one transmission rate, not two. Thus, the cost of transmission will be the same, whether the generator is located in MISO or PJM. The result of all of these facts ignored by CCSAO is that even if the auction were held today, bidders could rely on supplies in MISO. (*See* Ogur Dir., Staff Ex. 4.0, 24:537–40; Naumann Reb., ComEd Ex. 14.0, 20:414–421)

Third, while CUB-CCSAO witness Mr. Fagan referred to “day to day operational hurdles the RTOs must overcome to allow efficient transactions between the regions,” he fails to discuss

the significance of those “hurdles” or to discuss the fact that day to day operations are now being handled under the PJM/MISO Joint Operating Agreement (“JOA”). (Fagan Dir., CUB-CCSAO Ex. 1.0, 22:432-435) The JOA has resulted in substantial operational integration between the two RTOs and has moved PJM and MISO much closer to a full joint and common market. (Naumann Reb., ComEd Ex. 14.0, 17:354–18:368; Hieronymus Reb., ComEd Ex. 15.0, 30:611–613) ComEd witness Prof. Hogan testified that the practical effect of the JOA is to substantially blur the electrical boundaries between the two RTOs, so that “the boundary ‘seams’ are disappearing.” (Hogan Sur., ComEd Ex. 25.0, 9:n6) Staff witness Ogur confirms that generators in each RTO can supply load and even qualify as capacity resources in the other by meeting the standard requirements in the applicable transmission tariff. (Ogur Dir., Staff Ex. 4.0, 9:206 – 10:232)

F. Market Characteristics, Including Supplier Concentration

The AG, CUB, and CCSAO claim that supply ownership in northern Illinois is highly concentrated, and that this supposed concentration could lessen the competitiveness of the wholesale markets and could permit the exercise of market power, particularly when binding transmission constraints allegedly arise. (AG Init. Br. at 22, 36, 38; CUB Init. Br. at 14-15; CCSAO Init. Br. at 24-25) These claims are untenable on multiple grounds.

First, they universally depend on the false premise that northern Illinois is a separate market in which to assess concentration or market power. As discussed above in sub-section E, it is not. The wholesale electricity market encompasses the entire PJM region, and the record shows overwhelmingly that there is no northern Illinois market in which supplier concentration could affect the market separately. The record shows, as discussed above in sub-section A, that the PJM market is fully functioning and robust, and competition in that market is thriving.

Moreover, as discussed below in sub-section G, the evidence clearly shows that there are not now, nor are there likely to be, any binding transmission constraints that could impede potential suppliers from participating in ComEd's auction. Further, as discussed below in sub-section H, there are no significant limitations on entry of new generators in the PJM market, including northern Illinois.

Given that northern Illinois is not a separate market, calculating HHI and pivotal supplier index concentration statistics (AG Init. Br. at 39-42) within that political boundary is at best an exercise in irrelevant mathematics and at worst deceptive. Dr. Hieronymus explained that under the *Merger Guidelines*, the HHI market concentration statistics are calculated only for a relevant geographical market. (Hieronymus Sur., ComEd Ex. 24.0, 29:627-642) As noted above, that market is the entire PJM market – a result consistent with FERC's conclusion that the issue of generation market power within PJM should be analyzed on a PJM-wide basis. (Naumann Reb., ComEd Ex. 14.0, 8:156-177)

Moreover, although AG witnesses claim not to be assuming that northern Illinois is the relevant geographical market (Rose Reb., AG Ex. 5.0, 13:11-23), they frequently repeat that inaccurate assumption (*see* Naumann Sur., ComEd Ex. 23.0, 8:158-170) and the AG's entire discussion of concentration statistics and their significance depends on that inaccurate assumption being true. To illustrate, the "market" for soda on a given corner can be statistically "concentrated" in one vending machine, but concluding that its owner is a monopolist or can exercise market power without looking at the actual soda market ignores economic reality, often in the concrete form of the neighborhood "megamart." Similarly, implying that northern Illinois generators can exercise market power ignores the PJM megamart and is equally meaningless and misleading.

In any event, the AG's claims suffer from other flaws. For example, the record shows that even if northern Illinois were a relevant geographic market, a proper calculation of HHIs would demonstrate that this "market" was only moderately concentrated, rather than highly concentrated. (Hieronymus Reb., ComEd Ex. 15.0, 9:Fn2) In fact, Dr. Hieronymus demonstrated that the hypothetical concentration level would be moderate even if assumptions about import capacity were more conservative. (Hieronymus Sur., ComEd Ex. 24.0, 17:372-18:399) Moreover, as noted above, there is no evidence that there has ever been a successful exercise of market power in the area, even before integration into PJM.

The AG also claims that the possibility of collusion, strategic bidding, and other anti-competitive behavior could increase with market concentration and modeling. (AG Init. Br. at 42-45) There is no evidence supporting this claim. The record contains no evidence suggesting that such collusive behavior will or even might occur under ComEd's proposal; indeed, open auctions are a potential answer to limiting the effectiveness of such strategies. (LaCasse Dir., ComEd Ex. 4.0, 59:1394-1396, 63:1492-1496) It is also noteworthy that, the materials that the AG argues suggest this risk (*e.g.*, seminar brochures and "academic papers") have no relation at all to ComEd's proposal (LaCasse, Jt. Tr. 961-965) and, in the main are not improper or collusive. Studying lawful strategies to maximize chances of success in bidding is not collusion, but simply good business. Indeed, the AG offers no explanation of what anti-competitive practices or strategies could or would be used, let alone whether they would be possible under PJM market rules or the anti-trust law. In any event, this entire argument depends on the existence of market concentration, which the record shows is not an issue under ComEd's proposal, preventing competition.

The AG also makes several utterly unsubstantiated assertions regarding the pending Exelon-PSEG merger, claiming that it could lead to greater market concentration absent mitigation. (AG Init. Br. at 40-41) As discussed in sub-section K below, however, the merger presents no issues affecting competition in Illinois. Moreover, the AG ignores both the role of FERC oversight and the mitigation FERC has approved. The PJM MMU concluded that Exelon's and PSEG's proposed mitigation (divestiture of or of control over 6,600 MW of generation) is sufficient to cure any competitive concerns. Likewise, FERC, which has approved the merger, concluded that the proposed mitigation will restore competition to the pre-merger level and thus the merger, as mitigated, will not harm competition. *Exelon Corporation and Public Service Enterprise Group*, 112 FERC ¶ 61,011 at P 131 (2005). There is no reason to find otherwise.

Equally unfounded is CCSAO's assertions that the end of the ComEd's contract with Exelon Generation LLC ("ExGen") in December 2006 will permit the exercise of market power. (CCSAO Init. Br. at 22, 24) Such assertions are purely speculative, not supported by a shred of evidence. Moreover, they are at odds with the nuclear nature of ExGen's generation. As the record shows, nuclear plants cannot be started up and stopped on short notice, and thus are not amenable to the withholding that CCSAO conjures. In fact, the evidence demonstrates that owners of such plants are in fact price-takers, and are thus unable to exercise market power.

Just as meritless is CCSAO's claim that FERC's criteria for determining whether an entity has market power after 2006 are not certain. (CCSAO Init. Br. at 22) This claim is not only inherently speculative, but also appears designed to suggest that somehow FERC will loosen up those criteria, a suggestion for which there is not a hint of evidence or logic. In fact, the record shows recent FERC actions should mitigate concerns about market concentration and

access in northern Illinois. One of those actions was the November 18, 2004 FERC Order that instructed PJM and MISO to eliminate by December 1, 2004 any charges for new through and out transmission service between them, which charges were seen as a potential barrier to free trade between the two regions. In addition, prior FERC orders had required MISO and PJM to coordinate their efforts in the operation of their markets and calculation of Available Transmission Capacity so as to allow for greater inter-RTO commerce. (Naumann Dir., ComEd Ex. 5.0, 22:485-494)

G. Transmission Constraints

The AG claims that transmission constraints into northern Illinois currently exist and cannot be eliminated in the short term. (AG Init. Br. at 49-51) CUB and CCSAO also point to “constraints” as supporting their particular claims of market flaw or failure. These claims are unproven, unfounded, and -- unless they cagily refer to trivial “constraints” that have no significance to the issues before the Commission¹³ -- simply false. As Midwest Gen noted (Midwest Gen. Init. Br. at 3), neither the AG nor CUB-CCSAO can cite any evidence whatsoever that there is even any reasonable likelihood that there will be a single transmission constraint into northern Illinois that will affect the auction in any way, let alone a constraint persistent and significant enough to turn northern Illinois into a “load pocket” in which local generation will enjoy protected market power. (Hieronymus Reb., ComEd Ex. 15.0, 14:286-16:309; Hogan Reb., ComEd Ex. 16.0, 14:288–301) To the contrary, the record contains overwhelming evidence from multiple experts, including qualified professional engineers and system operators, that no transmission constraints currently exist or are likely to exist in the future that would harm the market or prevent generation from outside northern Illinois from

¹³ See footnote 11, above.

effectively competing in the auction. (Naumann Reb., ComEd Ex. 14.0, 13:281-288; Hieronymus Reb., ComEd Ex. 15.0, 14:286-16:309; Hogan Reb., ComEd Ex. 16.0, 14:288–301)

Evidence of actual operating conditions confirm the absence of such constraints. PJM data on limiting transmission elements in the area around northern Illinois show no significant constraint into northern Illinois, and this is confirmed by transmission loading relief data. (Hieronymus Reb., ComEd Ex. 15.0, 14:286-16:309) Additionally, updated data showing that binding transmission constraints that would isolate northern Illinois simply have not happened through August 16, 2005. These data capture the summer season of 2005. (Naumann Sur., ComEd Ex. 23.0, 12:252-255) The data clearly show that there will not be persistent or significant constraints in northern Illinois. Dr. Hieronymus presented a study showing that prices in the ComEd zone are essentially identical to those in a wide interstate region, thereby demonstrating that transmission constraints are not separating northern Illinois from the broader PJM market. (Hieronymus Reb., ComEd Ex. 15.0, 10:194–11:209; ComEd Ex. 15.2) Moreover, the data show that, in most hours when prices are not identical, the northern Illinois load zone, largely because of a lack of transmission constraints, enjoys among the lowest LMPs in PJM, and during some hours, LMPs in northern Illinois are materially lower than LMPs in eastern areas of PJM. (Naumann Dir., ComEd Ex. 5.0, 16:353-358) This would be impossible if transmission constraints were limiting otherwise economic imports into northern Illinois.

Moreover, the record shows that the PJM markets have effective means of dealing with transmission congestion that will not freeze bidders with remote generation out of the auction. First, in the short term, PJM dispatches all generation on an integrated basis consistent with system operation; this is called “security-constrained economic dispatch,” meaning that PJM directs the generators to operate in the very best (*i.e.*, most economic) way possible consistent

with serving all the load. (Naumann Dir., ComEd Ex. 5.0, 6:127-134) As a result, any local transmission limits are internalized by the market, which adjusts the dispatch to make sure that all the load is served while at the same time there is no violation of constraints on the transmission system. (*Id.*) Moreover, it is undisputed that PJM offers or permits the use of a variety of hedges, including but not limited to FTRs and bilateral financial transactions, that can offset any cost of congestion. (Naumann Reb., ComEd Ex. 14.0, 13:273-278)

Furthermore, in the longer term, it is equally undisputed that PJM, as an RTO, has a transmission planning process, the very purpose of which is to anticipate and address any bottlenecks on the regional transmission system. ComEd presented unrefuted evidence that the process, which involves the continual performance of studies to identify where potential constraints can develop on the system, anticipates and responds to developing transmission needs which then become the basis for planning system reinforcements. (Naumann Sur., ComEd Ex. 23.0, 14-16:329) There is no evidence suggesting that this process is, or will be, anything less than effective. Uncontradicted evidence also showed that there is no problem in northern Illinois with physical transmission constraints. (Naumann Reb., ComEd Ex 14.0, 14:298–305)

CCSAO complains that ComEd did not analyze post-2006 constraints during summer peak periods, and did not perform simulation modeling about strategic bidding behavior that supposedly could occur during the period 2007 through 2011. (CCSAO Init. Br. at 25) These claims are flawed in several respects. Initially, they are nothing but speculation. There is simply no evidence suggesting that transmission constraints will arise after 2007; the evidence is that they will not. Moreover, ComEd's analysis is based on the newest and best available data. Dr. Hieronymus observed that both FERC and the antitrust agencies accept and use current and near term forward conditions in assessing the potential for the exercise of market power on a

going-forward basis. (Hieronymus Sur., ComEd Ex. 24.0, 7:148-150) Dr. Hieronymus also explained that structural modeling is relied on by FERC, the Department of Justice and the Federal Trade Commission for analyzing market power, in preference to behavioral modeling such as CCSAO touts, because it is more reliable. Behavioral modeling (strategic bidding, *etc.*) is of necessity based on so many questionable assumptions that its probabitive value is suspect. Moreover, FERC has recognized that structural analysis does in fact provide information about both unilateral and multilateral potential market power, such as one would hope to derive from behavioral modeling. (Hieronymus Sur., ComEd Ex. 24.0, 8:178-184)

Finally, CUB suggests that the possibility that market power might be present during 2007-2011 because of transmission constraints requires some other analysis to be undertaken (CUB Init. Br. at 14) This claim is unfounded. The record contains evidence of the physical condition of the transmission system, its current operation, the process for planning its expansion, the prices that result, and the ability of generators to use it in the auction. ComEd used the best and newest data available. CUB does not and cannot point to what additional “analysis” could or should be done, let alone prove any inadequacy in the huge volume of evidence presented. Not only is there no evidence of transmission constraints, as noted above, but there also is no basis for assuming that the current state of the market, in which northern Illinois is a net exporter, would so radically change in a short time to warrant a presumption that the market will become a load pocket in which local generators could exercise market power. (Hieronymus Sur., ComEd Ex. 24.0, 7:143-146)

H. Limitations on Generator Entry

The AG asserts that generators entering a market face significant market risk and uncertainty in either building generation or transmission facilities. (AG Init. Br. at 50-51) This

broad assertion, however, has little relevance to the PJM market and none to whether or not ComEd's proposal should be approved. Nothing about the auction impedes generator entry, nor is more susceptible to a lack of entry than alternative proposals that are less effective at generating competition among the suppliers that there are.

The record also shows that there are no significant limitations on entry in the PJM market, including northern Illinois. In the short term, it shows that entry is unnecessary given the substantial excess capacity in the PJM market. In the longer term, the record shows that generator entry is largely unimpeded and rapid. Existing transmission system and operating rules permit efficient generator entry, and historically substantial generator entry has occurred in response to demand. (Naumann Reb., ComEd Ex., 14.0, 15:316–318) In northern Illinois alone, more than 8,000 MW of new generation, nearly all owned by independent generators, has been interconnected to ComEd's system since 1999. (Naumann Reb., ComEd Ex. 14.0, 15:320–16:341) Moreover, because the PJM markets have visible locational prices, the increase in prices for energy and capacity as supplies tighten signals the need for new generation even better than in the past. In addition, the standardized interconnection processes and terms in the PJM transmission tariff facilitate entry. (Naumann Reb., ComEd Ex. 14.0, 15:320–16:327) There is no basis for the contention that there are significant limitations on entry in the PJM market.

I. Small Commercial and Residential Customers

CCSAO claims that small commercial and residential customers have not benefited from retail competition, based on the low level of switching of such customers to alternative suppliers. (CCSAO Init. Br. at 25-26) This is hardly a reason to reject the auction, which is designed expressly to bring the benefits of competition to all customers -- even those that continue to take bundled service from utilities. (McNeil Dir., ComEd Ex. 3.0, 2:27-39) Moreover, the benefits to

small customers will only grow with competitive procurement. Under ComEd's proposal, ComEd will in effect aggregate the demands of small customers and offer them to wholesale suppliers through a transparent auction process. The record shows that accessing the market in this way should result in ComEd's incurring the lowest cost available to serve these customers – and in doing so, should bring the benefits of wholesale competitive markets to them.

The record also shows that small customers have benefited in the past. As the drafters of the residential bundled rate reduction and freeze understood, retail switching is far from the only way retail customers benefit from the transition to competition. The non-switching residential customers have enjoyed reductions of twenty percent and nearly a decade of frozen bundled rates. (McNeil Dir., ComEd Ex. 3.0, 7:135-143) This is true even though residential customers have yet to receive direct offers from competitive providers, who have not seen a profit in aggregating small accounts at the low prevailing prices. (Moler Dir., ComEd Ex. 2.0, 3:54-4:76)

The AG claims that if wholesale markets are not fully developed, prices in such markets will likely increase, and small commercial and residential customers will be forced to pay such retail prices in the short run because of the inelasticity of electricity demand. (AG Init. Br. at 51-52) This argument suffers from numerous flaws. First and foremost, the fact that the auction result and the underlying wholesale markets will be competitive has been fully supported; ComEd will not repeat the volume of evidence here. Moreover, by using competitive procurement, ComEd's proposal allows retail customers who do not switch to get the benefit of competitive prices. A non-competitive alternative, not the Illinois Auction Proposal, could leave non-switching customers paying artificially high rates. It is true that the acquisition of new supply by any means after 2006 is unlikely to leave rates at their current artificially low level (Moler Dir., ComEd Ex. 2.0, 3:54-4:83) But, the evidence shows that under the Illinois Auction

Proposal, small commercial and residential customers will enjoy the lowest costs that their aggregated demand can garner in the market. Thus, any rate increases will be minimized and they will directly benefit.

J. Market Rules and Monitoring.

As noted in ComEd's Initial Brief, PJM maintains an independent Market Monitoring Unit ("MMU") to monitor the behavior of all market participants, and PJM's market rules themselves in many respects prevent the exercise of market power by generation owners. Especially when coupled with the anti-trust laws, there is no reason to suspect that anti-competitive illegal or improper behavior will affect the auction clearing price market or the underlying markets. Contrary claims are pure speculation, and ignore the evidence of the both the numerous legal and structural safeguards and of the fundamental check provided by the competitive market itself.

1. PJM Market Rules

ComEd and other parties presented evidence of the PJM market rules and structures that prevent the exercise of market power. These rules: (a) prevent or make impractical and unprofitable the physical or economic withholding of generation, which is the chief strategy for exercising market power; and (b) when transmission constraints exist in a local region, require (with minor exceptions not relevant to ComEd) that bids be at no more than cost plus 10 percent. (*See* ComEd Init. Br. at 60-63)

The AG says that PJM provides insufficient safeguards to prevent generators from exercising market power and causing increased clearing prices in the auctions. (AG. Init. Br. at 46-47) However, it provides no details as to the alleged insufficiencies and flaws in the PJM rules, and cites no evidence of their inadequacy. And, there is none.

Moreover, there is no evidence that such strategies could be used profitably. As ComEd explained in its Initial Brief, increasing prices through the exercise of market power, as the AG, CUB and CCSAO assert is possible, inherently involves withholding supply. (ComEd Init. Br. at 60) In order for such a strategy to reap benefits for a generator, it must secure high prices on the generation that is not withheld such that they more than make up for not being paid for the generation that is withheld. (Hieronymus Reb., ComEd Ex. 15.0, 18:356–359) However, the PJM market rules require that every generator that qualifies as a capacity resource — which includes nearly all generation in northern Illinois — must bid into the PJM day-ahead market every day unless the generation is on an authorized scheduled outage or a legitimate forced outage. (Hieronymus Reb., ComEd Ex. 15.0, 13:283-291) This must-bid rule functions to prevent the exercise of potential market power in the forward market through withholding supply.

Even if transmission constraints were to temporarily isolate northern Illinois from the rest of PJM and leave it with fewer than three pivotal suppliers, which it would not for reasons discussed in sub-section G above and in detail in ComEd’s Initial Brief, then PJM’s market mitigation rules would be triggered automatically. (ComEd Init. Br. at 55) PJM’s market mitigation rules prevent the generators in the constrained area from bidding their generation at market rates, instead limiting their bids to no more than their marginal cost plus 10%, an amount insufficient to allow for an exercise of market power. (Hieronymus Reb., ComEd Ex. 15.0, 13:263–271; Hieronymus Sur., ComEd Ex. 24.0, 3:64–4:81) Despite assertions by the AG, ComEd notes that an allowance above marginal costs is necessary to allow for recovery of fixed costs. (Hieronymus Reb., ComEd Ex. 15.0, 25:516–523) ComEd witness Mr. Naumann stated that, FERC has agreed that “PJM’s current offer capping rules work effectively to mitigate

market power in a manner that is fair to most generating units.” (Naumann Sur., ComEd Ex. 23.0, 23:505–508) CUB-CCSAO has asserted that PJM’s bid mitigation rules would not apply when transmission constraints were binding. (Fagan Reb., CUB-CCSAO Ex. 3.0, 8:172–10:206) However, this argument ignores that fact that the bid mitigation rule would not apply only where the situations posed no risk to the market, *i.e.*, where FERC has determined that no generator could exercise market power. (Naumann Sur., ComEd Ex. 23.0, 12:254–265, 24:524–555) The AG has also argued that PJM’s bid mitigation rule does not adequately protect customers because the generator would receive the higher of the market price or their offer price cap. (Rose Dir., AG Ex. 1.0, 20:6–7) However, this argument misconstrues the function of the offer cap. If the capped unit is the marginal unit, its mitigated bid defines the market price; if another unit is the marginal unit, that unit’s bid defines the market price. The offer cap simply prevents the mitigated unit from exploiting its location in relation to a constraint. (Hogan Reb., ComEd Ex. 16.0, 23:505–24:518)

In addition to the PJM rules themselves, the type of generation present in northern Illinois undermines the AG’s CUB’s and CCSAO’s assumptions regarding the withholding of generation. The largest generation owner in northern Illinois is Exelon Generation and its generation is primarily nuclear. It has been widely recognized, including by FERC, that “the operational characteristics of, and regulatory scrutiny over, nuclear units virtually eliminate the possibility of withholding output to drive up prices.” *Exelon Corporation and Public Service Enterprise Corporation, Inc.*, 112 FERC ¶ 61,011 (2005). *See also USGen New England, Inc.*, 109 FERC ¶ 61,361 (2004); *Commonwealth Edison Co.*, 91 FERC ¶ 61,036 (2000). Thus, the largest northern Illinois generator simply could not engage in either physical or economic

withholding because of the operational characteristics of its generation facilities. (Hieronymus Sur., ComEd Ex. 24.0, 14:272–283)

2. PJM Market Monitoring Unit (“MMU”).

The record shows that the PJM MMU is active and effective. It continually monitors the operation of the market for potential exercises of market power or other attempts at manipulation or gaming, and has tools to prevent physical or economic withholding of generation to drive up prices. (Naumann Dir., ComEd Ex. 5.0, 21:456-461) The MMU detects physical withholding by reviewing forced outages or deratings and detects economic withholding by reviewing bids against cost information. (Naumann Dir., ComEd Ex. 5.0, 21:461–468) If the MMU identifies a problem, it generally discusses the issue informally with the market participants involved, which is itself effective in ending behavior the MMU questions. (Naumann Sur., ComEd Ex. 23.0, 21:451-22:460) If this does not yield results, the MMU issues a Demand Letter requesting the market participant to desist and provides copies to FERC and relevant state regulator(s). FERC also has authority to monitor the PJM markets and has established protocols to work with the MMU to ensure that FERC can exercise its statutory authority to ensure that rates are just and reasonable. (Naumann Sur., ComEd Ex. 23.0, 21:451-22:473) The MMU must report to FERC all instances where it has reason to believe a market violation has occurred. (Naumann Sur., ComEd Ex. 23.0, 21:451–22:473)

In response, the AG simply asserts that the “MMU’s analysis is not sufficiently detailed to determine the extent to which wholesale markets are competitive.” (AG Init. Br. at 52) There is no substance to this claim. The evidence established no fault in the MMU’s analytic methods and no inadequacies in its powers.

3. Proposed Illinois Market Monitor.

CUB-CCSAO proposed that a separate Illinois Market Monitoring Unit be established that would review the effectiveness and competitiveness of the PJM market structure and would have access to confidential market data to detect actual and potential market power and take action to prevent or eliminate abuse. (Steinhurst Dir., CUB-CCSAO Ex. 2.0, 44:1008–1010) This proposal is, in effect, a proposal for an Illinois entity to review whether the PJM MMU is performing its job. (Naumann Reb., ComEd Ex. 14.0, 21:437–438)

The record shows that this proposal suffers from two problems. The first is that there is no authority — and Dr. Steinhurst suggests none — for an Illinois entity to monitor transactions in wholesale power markets in interstate commerce, which transactions are by federal statute subject to the exclusive jurisdiction of FERC. In fact, FERC has addressed this issue, stating that “[w]e disagree, however, that state commissions can serve as co-regulators with regard to wholesale energy markets.” (*Midwest Independent Transmission System Operator*, 111 FERC ¶ 61, 448 at P 41; *see order on rehearing and compliance filing*, 114 FERC ¶ 61.081 (2005). The second problem is that for the reasons explained above, there is no need for this duplicative function, already performed adequately by the PJM MMU and FERC.

K. Other Competitive Market Issues.

The AG asserts that the pending Exelon-PSEG merger, already approved by FERC, would have a “material impact on the development of wholesale markets across the country”. (Rose Reb., AG Ex. 3.0, 2:13–7:11) The AG, however, simply discounts FERC’s approval, and without any supporting evidence claims that FERC did not comprehensively address competition in the very markets that it is exclusively empowered to monitor and regulate. In any event, the AG’s arguments are incorrect. Dr. Hieronymus, who was the Applicant’s principal market

power witness in the FERC proceeding, notes that no party to that proceeding presented evidence that the merger would have competitive implications in Illinois; the focus of the proceeding was on combining generation fleets in New Jersey and Pennsylvania. (Hieronymus Sur., ComEd Ex. 24.0, 23:479–494) There is no evidence that the merger will affect the auction, let alone render it uncompetitive or disadvantaged it relative to any other alternative.

V. AUCTION DESIGN ISSUES

A. General Effectiveness and Suitability

For all of the reasons described in ComEd’s Initial Brief, the Illinois Auction’s descending clock, vertical tranche process is a reasonable approach to procure supply for customers, is suitable for use in Illinois and will be effective in meeting the needs of customers in the post-2006 period.¹⁴

B. Full Requirements Product

The full requirements product frees customers from numerous risks that suppliers will assume, is a significant advantage of the Illinois Auction proposal, and is a central feature of the recommendation in the Staff’s Final Report that large utilities should procure supply through a vertical tranche auction. In its brief, Staff continues to strongly support the full requirements product definition.

The Attorney General questions the use of a full requirements product, arguing that, by putting the risk of volume fluctuations on suppliers, the costs associated with that risk will result in a risk premium, which will be included in bid prices. (AG Init. Br. at 55-56) The Attorney

¹⁴ On October 21, 2005, ComEd served, at the request of the ALJ, a chart comparing the Illinois Auction Proposal, the Ameren Auction Proposal, and the New Jersey BGS Auction Process. Upon review of that chart, we determined that certain corrections and/or clarifications were needed. Attached as Exhibit B to this Reply Brief is a corrected version of the chart as well as a version showing the corrections and/or clarifications.

General also faults ComEd for not providing a study establishing the magnitude of the risk premium that will be imposed by suppliers for assuming the risks of a full requirements product.

CCSAO makes the same argument about the effectiveness of the auction and the full requirements product definition, suggesting that Dr. LaCasse should have been able to predict the prices that would result from it. Because Dr. LaCasse “can’t tell the Commission what rates we can expect,” CCSAO would have the Commission reject the Illinois Auction. (CCSAO Init. Br. at 30-31)

Far from identifying a deficiency in the Illinois Auction proposal, the Attorney General’s and CCSAO’s risk premium arguments highlight one of its principal advantages. Provision of a full requirements product for customers involves risk, and costs will be incurred to manage that risk. Suppliers will provide for these costs when determining their bids in the auction. Specifically, each bidder will make its own judgments about how best to meet the supply obligation and manage the associated risks, and the bidders will compete on the basis of who can do this at the lowest cost. As a result, the auction uses the forces of competition and the participation of numerous bidders, sophisticated in risk management, to obtain services customers need at the lowest possible prices.

No study could foretell how a diverse group of suppliers will manage the risks of providing a full requirements product or their estimates of the associated costs (i.e., the Attorney General’s “risk premium”). However, the extensive evidence underlying the selection of the vertical tranche auction approach establishes that, whatever these costs may ultimately be, they are likely to result in lower costs to customers than a system that foregoes the benefits of a full requirements product, multiple suppliers and a diversity of risk management solutions.

In summary, the test of a prudent procurement process is not whether it enables observers to predict the prices it will produce one year in advance. The Attorney General and CCSAO have not even proposed a process that could be implemented, much less one that satisfied the type of results-predicting standard that they seek to apply. The Illinois Auction process incorporates the key features, discussed in this brief and in ComEd's Initial Brief, that give the Commission confidence that reasonable and prudent prices for customers will be achieved.

C. Multiple Round Descending Clock Format

1. General Effectiveness and Suitability

The multiple round, descending clock format is a transparent process that enables bidders to compare the prices of the various products in the auction and to continuously evaluate their bids with the benefit of information provided during the progress of the auction. It is one of the key strengths of the process, is suitable for use in Illinois and will be effective in securing supply for customers.

2. Load Caps

ComEd's Initial Brief explained that the Illinois Auction design includes a 35% load cap, which is one of a number of competitive safeguards that serve the goal of maximizing the competitiveness of the auction, and of obtaining supply for customers at prices that are competitive and reflective of market conditions. The load cap limits the number of tranches of each product that a single bidder can bid and win in the auction, thus limiting the influence that any one bidder can have on the results and limiting the exposure of ComEd and its customers to default by any particular supplier. As ComEd explained in its Initial Brief, the 35% load cap is supported by the Staff and by Midwest Generation, two of the three parties submitting testimony on this issue. Only IIEC opposes the use of a load cap, and the initial briefs filed by the Staff

and Midwest Generation discuss IIEC's opposition, explaining why it provides no basis for abandoning this important competitive safeguard.

Midwest Generation notes that IIEC witness Brian Collins expressed the view that a load cap could potentially raise costs by limiting participation in the auction by large low cost suppliers. However, Midwest Generation points out that, in support of his belief, Mr. Collins "offers nothing more than a hypothetical example," which he admits is "based on pure assumption." (Midwest Gen. Init. Br. at 14) Staff's Brief reviews the testimony addressing the purpose and benefits of load caps, and concludes that "the weight of the evidence supports the Company's 35% load cap proposal." For that reason, Staff recommends that "the Commission reject the IIEC proposal for the elimination of the load cap, and that the Commission approve the use of a 35% load cap per auction." (Staff Init. Br. at 35)

IIEC's brief acknowledges that its position has garnered no support in this proceeding, but seeks to respond to the many arguments that have been advanced in favor of a 35% load cap. IIEC begins by contending that, in all of the points raised by those who defend the importance of load caps, "the price to consumers is addressed only indirectly, if at all." (IIEC Init. Br. at 18) The evidence does not support this conclusion, showing instead that protecting the competitiveness of the process is directly related to achieving the lowest prices for customers. Dr. LaCasse specifically stressed this relationship when responding to IIEC's proposal to dispense with a load cap entirely, testifying that, doing so "strips the auction of essential protections against bidder strategies that can lead to higher auction prices." (LaCasse Reb., ComEd Ex. 11.0, 28:692-693) The notion that load caps provide no protection against higher prices is inconsistent with the testimony of numerous witnesses testifying for the Staff, Midwest Generation and ComEd.

IIEC seeks to dismiss the many reasons cited by Dr. LaCasse in support of load caps by characterizing them as qualitative factors, rather than proof through quantitative analysis. (IIEC Init. Br. at 22) However, the considerations discussed by Dr. LaCasse provide a sound basis for concluding that load caps have important benefits. They are far more persuasive than the hypothetical example on which Mr. Collins relies in advancing IIEC's position. Moreover, as the Staff notes in its brief, Dr. LaCasse reviewed the arguments made by Mr. Collins against use of a load cap and found them to be limited in focus, failing to consider key factors that support reliance on load caps:

Mr. Collins considers only one of the four factors that are relevant to evaluating the level of the load cap. He rightly points out that a higher load cap – and 100% is as high as a load cap gets – has the potential benefit of providing additional opportunities for some entities to bid in a greater amount of supply. However, this is only one side of the equation. Mr. Collins does not take into account that a 100% load cap has real costs. A 100% load cap would remove the needed discipline on bidders' ability to over-represent their interest in the auction, remove the needed discipline on a single bidder's ability to influence the auction results, and provide no assurance whatsoever of diversification of the supplier pool.

(LaCasse Reb., ComEd Ex. 11.0, 28:684-692)

The case for a 35% load cap is far stronger than whatever case might be made against it. A load cap is and always has been a key component of the successful New Jersey BGS auction process. It is supported by the Staff, which has carefully reviewed the testimony of all parties on this subject. The Commission should follow the advice of its Staff, the experience from four annual auctions in New Jersey and the opinion of experts, such as Dr. LaCasse, and should include this important competitive safeguard as part of the Illinois Auction design.

3. Starting Prices

ComEd explained in its Initial Brief that the starting prices for products in the auction will be established by the Auction Manager in consultation with the ICC Staff and ComEd.

(ComEd Ex. 19.3) The prices will fall within the maximum and minimum starting prices provided to qualified bidders in connection with submission of their Part 2 applications to participate in the auction. The Part 2 applications must include indicative offers from prospective bidders indicating the number of tranches they would be willing to serve at the maximum and minimum prices. The indicative offers are then taken into account in setting the starting prices. (ComEd Ex. 19.3)

The Attorney General faults ComEd for not providing an estimate of starting bids or a specific method for determining the maximum and minimum prices provided to qualified bidders. That criticism is not well founded. ComEd cannot provide an estimate of starting bids because it does not know what maximum and minimum starting prices the Auction Manager will establish; it does not know what indicative offers bidders will submit, and it does not know what conclusions will be reached by the Auction Manager about the appropriate starting prices based on information that will not be available until sometime in the future.

The process for establishing starting prices has been used in the New Jersey BGS auctions through four annual procurement cycles. It has worked well. There has never been a requirement in New Jersey that utilities state far in advance of the auction what the starting prices will be, nor could there be any such requirement. There is no basis for imposing any such requirement here. The Commission should approve the well designed and tested process for establishing starting prices that has been incorporated in the Illinois Auction proposal.

4. Bid Decrements

No parties have raised any issues in their briefs concerning the bid decrement approach outlined by ComEd in its testimony. The Staff notes that Dr. LaCasse has provided “a good

structure for setting bid decrements,” and suggests only that the Auction Manager consult with the Staff to finalize the formulas. (Staff Init. Br. at 41) ComEd supports that suggestion.

To the extent that the pay-as-bid proposal advanced by BOMA relies upon rigid, pre-determined price declines from round to round during the auction, that approach is discussed in Section V.D of this brief.

5. Auction Volume Reductions

ComEd’s Initial Brief discussed the proposal made by Dr. Salant to provide the Auction Manager with discretionary volume adjustment power for the purpose of exerting pressure on suppliers to mitigate potential use of market power. Dr. LaCasse responded to this suggestion in her testimony, disagreeing that volume adjustments should or could be used for this purpose and pointing out the significant risks that such adjustments would pose for customers. Apart from Dr. Salant, no other witness and no other party supported the suggestion that the Auction Manager be given power to reduce volume in the auction under the circumstances described by Dr. Salant.

The Staff’s Brief examines the arguments made by Dr. Salant in support of his broad volume adjustment power and concludes that Dr. LaCasse’s position is more persuasive and should be adopted:

While the proposal by Drs. Salant and Sibley are certainly well-intentioned and theoretically correct, the record unfortunately provides no reliable method for discerning the underlying motivation of suppliers who are withdrawing tranches. Without a practical method of implementing such a proposal, Staff is reluctant to imbue the Auction Manager (or the Staff) with the power to cut back auction volumes, unless it is extremely clear that such reductions will benefit ratepayers. As Dr. LaCasse warns, volume cutbacks are not without risks, since they perforce shift the Company’s demand for energy to some other procurement venue (such as the PJM spot market).

(Staff Init. Br. at 44-45) For these reasons, the Staff recommends that the Commission accept Dr. LaCasse's position with respect to limitation in the use of volume cutbacks.

ComEd agrees with the Staff's position and the record supports it. The Commission should approve the Illinois Auction proposal's volume reduction approach.

6. Portfolio Rebalancing

ComEd's Initial Brief also discussed Dr. Salant's suggestion that the volume reduction power be used to readjust the individual auction product volumes, increasing volume for products with excess supply and decreasing it for products with limited supply offers. Dr. LaCasse opposed this use of the volume adjustment power, explaining that it disregards the dynamic nature of the auction process in which initial interest in particular products does not always reflect the ultimate distribution of bids and would destroy the careful balance between price and stability that the choice of durations was intended to achieve. (LaCasse Reb., ComEd Ex. 11.0, 53:1261–54:1284)

The Staff's Brief discusses the disadvantages identified by Dr. LaCasse with this portfolio rebalancing approach, as well as later misgivings by Dr. Salant about broad use of any such power. Ultimately, the Staff concludes that portfolio rebalancing should only be used when, after consulting with the Staff, there is consensus between the Auction Manager and Staff that it is appropriate and provided the Auction Manager, in consultation with the Staff can devise a protocol deemed appropriate by the Auction Manager for carrying out such portfolio rebalancing. (Staff Init. Br. at 48)

ComEd continues to believe, based on the testimony of Dr. LaCasse, that use of the volume reduction power to rebalance the portfolio is ill advised. While ComEd understands that the Staff's proposal would result in use of such power only if the Auction Manager agreed it was

appropriate and could devise a protocol for carrying it out, the evidence indicates that those conditions cannot be satisfied. Therefore, ComEd recommends that the Commission not complicate the auction design by introducing the possibility of portfolio rebalancing volume reductions that are dependent upon Dr. LaCasse's agreement when Dr. LaCasse has already provided her professional judgment that such adjustments are a bad idea.

7. Association and Confidential Information Rules

The Illinois Auction design includes detailed association and confidential information rules comparable to those that have been used in New Jersey. The rules ensure the independence of bidders, prevent collusion among bidders and prevent any one bidder from gaining an advantage in the auction through better information about its competitors. (LaCasse Dir., ComEd Ex. 4.0, 32:757–760)

In its Initial Brief, ComEd responded to a suggestion by Staff witness Salant that bidders be required to disclose any full requirements agreements with wholesale suppliers that are contingent on the outcome of the auction. (Salant Reb., Staff Ex. 11.0, 31:693–702) ComEd consulted Dr. LaCasse about that proposal and was advised that it conflicts with the approach taken in the successful New Jersey auctions, would require bidders to disclose sensitive business information that they would be reluctant to provide, and could chill participation in the auction. (LaCasse Reb., ComEd Ex. 11.0, 49:1160–52:1238)

Staff's Brief reviews the issues presented by Dr. Salant's proposal and concludes that there are reasonable arguments against requiring the additional disclosures suggested by Dr. Salant and that there is a "real potential for some negative unintended consequences" if they were adopted. (Staff Init. Br. at 52) For those and other reasons, Staff does not recommend that

Dr. Salant's proposed modifications to the association and confidentiality rules be adopted. (Staff Init. Br. at 52-53)

One party, Peoples Energy, recommends that the association and confidentiality rules be revised to prohibit bidders from sharing any information with other unaffiliated but "associated" bidders in the auction. Peoples also expressed concern that the ability under the rules to provide information to advisors to bidders might become a loophole used to supply information to an unaffiliated RES.

Dr. LaCasse responded to these suggestions in her testimony, pointing out that, under the rules, associations with other bidders must be disclosed. Dr. LaCasse also proposed a modification to the definition of "advisor" to provide that it includes only individuals and that an advisor cannot disclose confidential information to anyone but a bidder.

Peoples' Brief indicates that the revision to the advisor definition is responsive in part to its concerns, but proposes further modifications to the definition and continues to seek additional restrictions on bidder disclosures. The modifications sought by Peoples have not been proposed by any other party. Similar concerns are not shared by other participants in this proceeding. The potential problems Peoples speculates might occur have not resulted in changes to the association and confidentiality rules for the New Jersey BGS auction. For these and other reasons discussed in the testimony of Dr. LaCasse, ComEd submits that further modifications to the association and confidentiality rules are not necessary and should not be required.

8. Tranche Size

Staff's Brief recommends that the Commission approve ComEd's proposed tranche size of approximately 50 MW, and no other party has taken a position on this issue. ComEd therefore recommends that the proposed tranche size be approved.

9. “Price Taker” Proposal

ComEd’s Initial Brief discussed Dr. Salant’s “price taker” feature under which a supplier could elect not to participate in the auction directly, but announce its willingness to supply a specified portion of load (which could exceed the load cap applicable to auction bidders) at the auction clearing price. (Salant Dir., Staff Ex. 1.0, 65:1476 – 69:1571) Dr. LaCasse responded to this proposal in her rebuttal testimony, explaining that it would negate the advantages of an open auction, that the resulting auction volume reduction would deter participation by other suppliers (and would increase default risk by the price-taking supplier, who would be committed to providing supply before it knows the price that it will receive), and pointing out that a price taker experiment in Connecticut failed and was abandoned for future auctions. (LaCasse Reb., ComEd Ex. 11.0, 41:989– 47:1125)

Staff’s Brief reviews the testimony of Drs. Salant and LaCasse on this proposal, agreeing with some of Dr. Salant’s reasoning, but noting a significant list of disadvantages identified by Dr. LaCasse that would arise from following the price taker approach. Ultimately, after expressing some ambivalence about the proposal, the Staff Brief recommends against it. Among other things, the Staff observes that the proposal is unnecessary because suppliers can always sell their power by other means, enabling consumers “to gain access to low-cost producers’ power.” (Staff Init. Brief at 58) Midwest Generation also recommends against adoption of the price taker proposal, concluding that it “is not likely to benefit, and may well harm, consumers.” (Midwest Gen Init. Br. at 17)

ComEd believes that, for the reasons identified by Dr. LaCasse and Midwest Generation, and in accordance with the Staff’s recommendation, the Commission should not include the price taker feature as part of the Illinois Auction design.

10. Other Format Concepts and Issues

a. Detailed Auction “Task Plan” Suggestions

The testimony of Staff witness Salant raised several issues that were grouped under the heading of “task plan” suggestions, most of which had to do with providing more specificity on particular details of the auction process. Dr. LaCasse and Mr. McNeil provided additional specificity in later rounds of their testimony, and ComEd believes that there are no remaining “task plan” issues to be addressed by the Commission.

b. Price Cap Proposal

ComEd responded to Prof. Reny’s price cap proposal in its Initial Brief, noting that Dr. Reny admitted that he had no experience with electricity markets or the design of auctions for such markets, and that he had not made a specific proposal that could be implemented. Expert testimony establishes that Prof. Reny’s price cap suggestion incorrectly assumes that bidders can be forced to sell for less than market prices, does not reflect that there are alternatives available to sell outside the auction, depends upon the existence of accurate knowledge of supplier costs, and, even if those obstacles could be overcome, would be short sighted because it would discourage investment in the Illinois electricity sector. (Hogan Sur., ComEd Ex. 25.0, 22:482–493) Nothing in the testimony of Prof. Reny calls for any change in the Illinois Auction design.

D. Clearing Price: Uniform vs. Pay-as-Bid

As discussed in ComEd’s Initial Brief, BOMA’s proposed pay-as-bid modification to the Illinois Auction design would provide for auction rounds in which the price of each product would tick down by uniform amounts and suppliers would submit bids in each round without receiving any information about the total volume of bids in the auction as a whole or for any particular product. The auction would continue until all prices declined to a level at which no

supplier was willing to bid, and the winning bidders would then be selected starting with the lowest prices bid and working upward until the necessary requirements for each product had been procured.

Dr. LaCasse analyzed the pay-as-bid proposal in her testimony and demonstrated that it would eliminate the transparency that drives down supplier bids through multiple auction rounds, would pose a significant risk of gaming to defeat the purpose of the auction and would increase the risk that products in the auction end up undersubscribed. (LaCasse Reb., ComEd Ex. 11.0, 66:1565 – 68:1607 74:1750 – 75:1767; LaCasse Sur., ComEd Ex. 19.0, 30:644 – 37:782) The pay-as-bid approach has never been used in any jurisdiction in this country to procure supply for electric utility customers, and it was considered and twice rejected for use in the New Jersey BGS auctions.

Staff reviews the evidence addressing the pay-as-bid proposal and notes that “Dr. Laffer’s claims for the superiority of his pay-as-bid auction were refuted by several experts on electricity markets, auctions, and economics.” (Staff Init. Br. at 60) For example, Staff cites Dr. Hogan’s testimony concluding that predictions of lower prices resulting from a pay-as-bid auction are not supported by economic theory or actual practice. Similarly, Staff notes that Mr. Parece, an expert on energy economics with experience designing, implementing and monitoring electricity auctions, believes that the pay-as-bid approach would lead to higher electricity costs than would be achieved under the Illinois Auction proposal. (Staff Init. Br. at 61) The Staff also agrees with Dr. LaCasse’s observation that Dr. Laffer’s proposal is vague at best and appeared to shift from one round of testimony to another, introducing in rebuttal, for example, a new concept that bidders would be allowed to drop out and jump back into the auction at will. (Staff’s Init. Brief at 63.) Concluding that Dr. Laffer lacks the necessary expertise to design an auction

proposal, that recognized experts have identified numerous flaws in his pay-as-bid approach, and that the shifting suggestions he makes for modification of the Illinois Auction are either internally inconsistent or ambiguous, Staff recommends that BOMA's "unrealistic" pay-as-bid proposal be rejected. (Staff Init. Br. at 68-69)

Midwest Generation also analyzes BOMA's pay-as-bid proposal, commenting that there is absolutely no empirical evidence to support Dr. Laffer's claim that lower prices will result from his suggestions. (Midwest Gen Init. Br. at 18-19) Midwest also highlights that Dr. Laffer relies on his own common sense notions about the possible effects of his proposal, while ignoring the many adverse impacts that his changes in the auction rules could have on bidder behavior. Significantly, Midwest concludes that there is a "substantial possibility that a pay-as-bid approach would depress supplier participation." (Midwest Gen Init. Br. at 20) As a result, Midwest, like Staff, recommends that the pay-as-bid proposal be rejected.

In its brief, BOMA continues to rely on the simplistic, "common sense" rationale on which Dr. Laffer bases his proposal, offering no response to the evidence demonstrating that the pay-as-bid approach has never been used to acquire electricity in this country, has been rejected in the one jurisdiction – New Jersey – that has studied the issue most closely and is not supported by any expert with knowledge or experience in energy markets. BOMA seeks to answer specific arguments raised in opposition to the proposal, but misstates the issues presented in an effort to side step the severe problems with Dr. Laffer's ill-defined suggestions.

For example, BOMA attempts to respond to the real risk that a pay-as-bid modification will leave individual products in the auction undersubscribed by referring to the broad PJM markets, which ensure sufficiency of supply to meet the needs of customers in Illinois. (BOMA Init. Br. at 9-10) BOMA also cites the testimony of Dr. LaCasse, who believes that, under the

well designed Illinois Auction proposal, there will be suppliers interested in the 1, 3, and 5 year products. What BOMA ignores is that the problem is not the sufficiency of supply in PJM markets or the adequacy of supplier interest in auction products in a well designed auction. The problem is that the pay-as-bid modification to the auction rules eliminates the transparency of the auction process and prevents bidders from making the comparisons between individual products and prices, both of which work together to achieve an efficient result under which all products are subscribed at the lowest possible prices. As Dr. LaCasse explained:

In the ComEd proposed auction, if a product has less interest at the beginning of the auction, its price will not tick down, while the prices of the others products will. This will induce bidders to switch their tranches into the higher price product. For this balancing mechanism to operate, bidders must be provided relative price information—that is, bidders must be able to see that interest in a product, and they see this because a price differential opens between a less popular product and another one.... This balancing mechanism is completely absent from the Laffer pay-as-bid proposal.

(LaCasse Sur., ComEd Ex. 19.0, 35:756 – 36:766)

Similarly, BOMA tries to gloss over Dr. Laffer’s lack of familiarity with basic principles of auction design, such as the “winner’s curse” phenomenon, which supports the use of a transparent process like the Illinois Auction Proposal for procurement of supply. BOMA contends that potential suppliers of electricity are sophisticated and require no “protection from an alleged ‘winner’s curse.’” (BOMA Init. Br. at 13) That response, by itself, displays BOMA’s and Dr. Laffer’s misunderstanding of the issue, which has nothing to do with whether a bidder is sophisticated or has the ability to develop estimates on which to base bids at an auction. As Dr. LaCasse explained:

Sophisticated bidders who understand the winner’s curse will bid cautiously. These bidders will understand that if they bid strictly on the basis of their estimates, they will regret it.... if bidders obtain additional information regarding the value of what they are bidding on, they can sharpen their estimate, they can have more confidence in their evaluation, and they can bid less cautiously and more aggressively.

(LaCasse Sur., ComEd Ex. 19.0, 27:572 – 28:580) Staff’s Brief also stresses the importance of this principle of auction theory, noting Dr. Laffer’s “failure to recognize the influence of the ‘winner’s curse’ on bidding strategies and auction outcomes.” (Staff Init. Br. at 64)

Finally, the suggestion by BOMA and Dr. Laffer that the well designed Illinois Auction Proposal, including its rejection of the flawed pay-as-bid feature, is the product of a conflict of interest and an effort to favor Exelon Generation is simply baseless. The successful New Jersey BGS auctions use the same sound format that is being proposed for the Illinois Auction. That format has been reviewed repeatedly by New Jersey regulators and found to be effective and in the interest of customers. New Jersey authorities have twice rejected the pay-as-bid proposal and have never concluded that any conflict of interest problems were present, despite the fact that New Jersey utilities, like ComEd, have generation company affiliates.

Moreover, the recommendation to use the vertical tranche descending clock format, not a pay-as-bid process, was the key conclusion in the Staff Report at the end of the Commission’s Post 2006 Initiative. (ComEd Ex.1.1) The Staff recommended the Illinois Auction process because it best meets the 18 consensus attributes identified during the lengthy review of proposed procurement approaches. The Staff’s recommendation flatly contradicts BOMA’s suggestion that the auction process is the product of conflicts of interest or efforts to benefit generation affiliates.

In summary, BOMA’s pay-as-bid proposal is ill conceived, eliminates the important benefits that arise from a transparent process, is inconsistent with the consensus attributes of the ideal procurement process identified through the Post 2006 Initiative, will provide no benefits and risks higher costs and undersubscription of auction products, forcing resort to spot markets to fill in necessary supply. The Commission should reject this uninformed proposal made by

only one witness who lacks the necessary experience or credentials to design the process on which Illinois customers will rely for their electric supply.

E. Auction Management

1. Auction Manager

Staff recommends that the Commission approve the proposal to have the Illinois Auction conducted by an independent auction manager, and stresses that, under the proposal, Staff will be able to monitor and provide input on the performance of the auction manager's functions. (Staff Init. Br. at 74) Staff also reports that it has reviewed the qualifications of Dr. LaCasse and has concluded that she is competent to be the auction manager for the Illinois Auction. (Staff Init. Br. at 69)

ComEd recommends that the Commission accept the Staff's recommendations on this important subject and authorize the appointment of Dr. LaCasse as auction manager.

2. Role of ComEd

As ComEd explained in its Initial Brief, ComEd will retain the Auction Manager, but the Auction Manager will conduct the auction independently in accordance with procedures approved by the Commission, and not under the direction of ComEd. CUB contends that ComEd's role is much broader, arguing that the process provides for enormous non-reviewable discretion to be exercised by ComEd on such matters as the amount of supply to be sought in the auction, the size of the load cap, maximum and minimum starting prices, the product design, the customer supply groups, and the durations of supply contracts.

CUB's contention is inconsistent with the evidence in the record. Under the Illinois Auction proposal, ComEd does not have enormous non-reviewable discretion to determine any of these matters. ComEd has made proposals on these subjects, drawing on the results of the

Commission's Post 2006 Initiative and taking into consideration the views of other parties, but the decisions regarding these features of the proposal will not rest with ComEd. The way in which each of these issues will be handled will be determined by the Commission in its order in this proceeding.

3. Role of Staff

Staff will have a major role in all aspects of the auction process, and will submit a formal report to the Commission following each auction. The role of the Staff is entirely appropriate and there is no reason to impose any additional limitations on the Staff's involvement with the process.

4. Representation of Consumer Interests / Separate Consumer Observer

ComEd's Initial Brief described its reasons for concluding that the Staff is well suited to represent the interests of consumers. Staff's significant involvement in the oversight of the Illinois Auction provides the opportunity and access for it to perform that role well, making a separate consumer representative unnecessary. Although Staff takes no position on the proposal by CUB and CCSAO to designate an additional consumer observer, Staff indicates that it "is willing to accept the responsibility for observing and assessing the auction as a neutral party, which Staff believes is in the best interests of consumers." (Staff Init. Br. at 79)

The suggestion that an additional consumer interest representative be appointed is not only unnecessary, but is a veiled attempt to derail the auction process itself. Those parties that recommend the appointment of a consumer advocate -- the Attorney General, CCSAO and CUB -- have not disguised their true objective to stop the auction, at any cost. There is every reason to believe that the touted "consumer advocate" would not be independent but would instead embody the thinking of these nay-sayers, and would do nothing more than interfere with the

auction and put at risk ComEd's ability to procure energy for its customers following the transition period. Appointing a consumer advocate based on the recommendation of the AG, CCSAO and CUB would be the regulatory equivalent of putting the fox in charge of the hen house.

F. Date of Initial Auction

In its Initial Brief, ComEd proposed that the initial auction be conducted in September, 2006 — a date that is sufficiently close to the period in which supply will be provided to avoid potential risk premiums that might arise from a longer lag time between the auction and the flow of energy. (McNeil Dir., ComEd Ex. 3.0, 33:708–715) ComEd also noted that a September date also provides adequate lead time for customers to make decisions about alternative supply options. Ameren supports the September 2006 date for the first auction, making a joint process to acquire supply for all affected utilities possible.

The Coalition and Constellation submitted testimony advocating that the initial auction take place in May, 2006. In their briefs, however, they have indicated a willingness to go along with the September 2006 auction date, although continuing to prefer the May option. For example, Constellation states “[n]otwithstanding its preference, CCG does not object to a simultaneous September auction, but prefers May.” (CCG Init. Br. at 14) The Coalition reviews the reasons why it believes that an earlier date would provide benefits, but concludes that “[g]iven ComEd's other revisions to the other portions of its proposal, it might be reasonable for the Commission to decide that the initial auction should be held in September 2006.” (CES Init. Br. at 22)

ComEd appreciates the flexibility of the Coalition and Constellation in withdrawing or easing their opposition to a September, 2006 auction. Balancing the different viewpoints of the

parties on this question is not easy. However, given the agreement of ComEd and Ameren on a September 2006 auction, and given the Staff's recommendation that the Commission approve the September 2006 date, (Staff Init. Br. at 82) ComEd submits that it is appropriate for the Commission to determine that the date for the initial auction should be in September, 2006.

G. Common Versus Parallel Auction

Staff's Initial Brief notes that the controversies that existed at the beginning of this proceeding about the grouping of products in the auction and switching between products that should be permitted have been resolved. (Staff Init. Br. at 82) ComEd agrees with that assessment, and, in the absence of any opposing viewpoints, will merely report the resolution on each issue in the following sections with a recommendation that the Commission approve that resolution.

1. Among Fixed-Price Products and Hourly Products

ComEd recommends that switching be allowed among all fixed price products included in the auction. ComEd also recommends that switching be allowed among all hourly products included in the auction.

2. Between Fixed-Price and Hourly Products

ComEd recommends that the Illinois Auction not provide for switching between fixed and hourly products.

3. Between ComEd and Ameren Products

ComEd recommends that the Illinois Auction provide for switching between ComEd and Ameren fixed price products and between the hourly products of ComEd and the hourly products of Ameren. ComEd Ex. 11.5 (b) is a diagram showing the fixed and hourly price products of ComEd and Ameren to be included in the Illinois Auction divided between the Fixed Price

Section (within which switching is permitted) and the Hourly Price Section (within which switching is also permitted).

H. Contract Durations for Blended, Fixed Price Product

1. Proposed Blends for Residential and Small Commercial Customer Supply

Staff's Initial Brief summarizes that "the weight of the evidence supports adoption of the Company's proposed mix of 1-year, 3-year, and a conservatively small number of 5-year supply contracts for serving the so-called 'blended segment.'" (Staff Init. Br. at 97) ComEd agrees with this assessment. As Staff observed "there is no evidence of a better way of balancing 'the twin goals of price stability and market sensitive pricing.'" (Staff Init. Br. at 97) ComEd submits that the Commission should approve the proposed blended portfolio to be used to provide supply for residential and small commercial customers.

2. 5-year Agreements

Although a few parties expressed some disagreement with the use of 5-year supply agreements, as discussed in ComEd's Initial Brief, the majority of the participants in this proceeding raise no opposition. Midwest Generation reviews the arguments in favor of a limited percentage of longer term agreements in the blended portfolio, concluding that they benefit customers by smoothing out changes in electricity prices over a longer period of time, thereby decreasing rate volatility. (Midwest Gen Init. Br. at 20) ComEd believes that the evidence supports the inclusion of 5-year agreements in the portfolio and urges the Commission to approve their use.

3. 3-year Agreements

Three year agreements are an important ingredient in the mix of the blended portfolio. They have been used extensively to provide supply in the New Jersey BGS auctions, and it is appropriate that they be included in the Illinois Auction Proposal as well.

4. 1-year Agreements

One year agreements also provide benefits as a part of the blended portfolio, providing a measure of responsiveness to market conditions, and serve as the basis for the fixed price product used to provide supply for larger customers. The role of 1-year agreements under the Illinois Auction proposal is appropriate and should be approved.

5. Percentage of Supply Acquired at Subsequent Auctions

As ComEd explained in its Initial Brief, the blended portfolio of 1-year, 3-year and 5-year supply agreements is designed to stagger procurement following the initial auction so that no more than 40% of the supply to serve ComEd's customers is procured in any one year. The Attorney General does not quarrel with the staggered structure of the portfolio, but highlights the unavoidable fact that, in the initial auction, ComEd must procure 100% of the supply needed to serve its customers. (AG Init. Br. at 55) The Attorney General's contention that this makes the auction process "ill-suited to Illinois" is without merit. The Illinois Auction Proposal is the method recommended in Staff's Final Report from the Post 2006 Initiative, and that recommendation was made with full knowledge that 100% of the supply necessary to serve ComEd's customers would have to be purchased in the first annual auction. The percentage of supply to be acquired in the initial auction and in subsequent auctions under ComEd's proposal is appropriate and should be approved.

I. Fixed Price Auction Product and Tariffed Services for Larger Customers

1. Nature of Auction Product and Tariffed Services for 1–3 MW Customers

ComEd’s initial proposal contemplated that supply for customers with peak demands between 1 MW and 3 MW would be procured through agreements with 1-year terms. The 1-year term of the fixed price product for this customer group has remained unchanged.

BOMA argues that the blended product provided to residential and small commercial customers should also be made available to customers with demands between 1 MW and 3 MW, contending that they would benefit from the additional price stability arising from the use of 1-year, 3-year and 5-year agreements. (BOMA Init. Br. at 17-19) IIEC also recommends that a multi-year product be considered for these customers. (IIEC Init. Br. at 47) Direct Energy and USESC, on the other hand, propose that the 1-3 MW customer group be supplied with an hourly energy product only. (DES Init. Br. at 23)

Staff reviews the positions of the parties on this issue and supports the use of 1-year supply agreements for this customer group. (Staff Init. Br. at 99-101) ComEd believes that 1-year agreements are appropriate supply sources for these customers for all of the reasons explained in Mr. McNeil’s testimony. As Mr. McNeil summarized:

ComEd believes that its proposed one-year fixed-price contracts for CPP-A supply strike the right balance between providing price stability to these customers and sending adequate price signals to promote the development of competition in the retail and wholesale markets. Customers with demands between 1 MW and 3 MW, which ComEd has proposed to be eligible for CPP-A service, have greater switching rates than do smaller customers, and as a result they do not require the price protection that is afforded to smaller customers through CPP-B supply. In fact, providing these customers with such price protection may discourage them from seeking out competitive retail suppliers, thereby retarding the development of the competitive retail markets. Furthermore, if 1-3 MW customers were included in the CPP-B product, it would logistically be more difficult to transition these customers to a different CPP service in the future should these customers be declared competitive at some future date. As a result, I

disagree with BOMA's proposal to allow 1-3 MW customers to be eligible for CPP-B service. At the same time, 1-3 MW customers are distinguished from >3 MW customers in that most >3MW customers have been declared competitive; this indicates that 1-3 MW customers require greater protection against uncertainty in market prices than do >3MW customers, who would be eligible for hourly pricing through CPP-H supply. Furthermore, in its Final Report to the Commission, the ICC Staff stated that, "...if an hourly price plan were to be adopted, Staff would recommend that the Commission consider limiting that plan to only the largest utility customers, perhaps in the 3 MW and above range..." (Staff's Final Report at 26). Therefore, I believe that it is appropriate to offer a one-year fixed-price CPP product rather than an hourly-priced CPP product to 1-3 MW customers. ComEd's proposal regarding the CPP-A supply contract duration balances the concerns of customer groups, such as BOMA, who seek price stability and the concerns of retail suppliers, such as Direct Energy, who prefer that customers be exposed to hourly price signals in order to encourage more customers to participate in the competitive retail market.

(McNeil Reb., ComEd Ex. 10.0, 52:1118-53:1144)

2. Nature of Auction Product and Tariffed Services for 400 kW–1 MW Customers

After initially proposing that 400kW to 1 MW customers be supplied through the blended product, ComEd agreed with suggestions by the Coalition and other parties that these customers be included in the 1-year fixed price auction segment (subject to a resolution of the opt in / opt out issue described in section VII (B)(4)(a)(ii)). (McNeil Sur., ComEd Ex. 18.0, 19:415–21:460) BOMA argues ComEd's original proposal was preferable to the position adopted at the urging of the Coalition. (BOMA Init. Br. at 19) Direct Energy and USESC suggest that customers with demands under 1 MW receive monthly energy if their annual usage is greater than 15,000 kWh and quarterly energy if their usage is less. (DES Init. Br. at 23)

Staff does not support the proposals of BOMA or Direct Energy and, for the reasons described in Mr. McNeil's testimony, ComEd believes that the proposal to include customers with peak demands between 400 kW and 1 MW in the annual auction is appropriate.

3. Treatment of Customers (\geq 3MW) Taking Services Subject to a Competitive Declaration

As discussed in ComEd's Initial brief, BOMA, the Department of Energy, IIEC and Staff advocate inclusion of this customer group in the 1-year fixed price supply auction. ComEd considered these suggestions, but determined that the line between customers whose service is subject to a competitive declaration and those who are not should be respected. The customers in the over 3 MW category have alternative sources of supply if they agree to reasonable commercial terms, and there are already many RESs in Illinois offering service to this customer group. (McNeil, Tr. 581) Mr. McNeil's testimony reviewed the many reasons for concluding that a fixed price product should not be offered to these customers:

First, ComEd has no obligation to provide such service to these customers and does not choose to offer it. Second, these customers have exhibited a willingness and ability to participate in the competitive retail market. This assertion is supported by the fact that bundled electric service for these customers have been declared competitive by operation of law. Furthermore, there are currently nine competitive retail suppliers who have obtained the necessary approvals to serve these customers, and eight of them are currently serving these customers. Offering a fixed-price CPP product to these customers would only discourage these customers from shopping and comparing attractive service offerings in the competitive retail market, thereby retarding competitive retail market development to the detriment of all customers.

Additionally, suppliers would be likely to incorporate very large risk premiums into fixed-price CPP products for >3 MW customers. As I noted previously, Constellation Energy Commodities Group, Inc., a prospective bidder, has cautioned about the price premiums associated with the proposed CPP-A product offered to 1-3 MW customers. The risk premiums associated with a fixed-price CPP product offering for >3 MW customers would be even greater. As Dr. Kahal states, "...there can be huge movements in the POLR loads that [fixed-price >3 MW CPP suppliers] ultimately must serve between the loads specified in Com Ed's RFP and the loads that actually sign up for this service..." (Kahal, p.20) These risk premiums would still be very high even if the CPP product incorporated Mr. Stephens' proposal to require >3 MW customers to "prequalify their load" because this proposal does not require the customers to commit to CPP service prior to the auction (lines 458-476).

It is important to mention that many customers with demands greater than 3 MW in other states are currently only offered hourly-priced service from their utilities.

For example, as Direct Energy witness Steffes explains, "...all New Jersey customers over 1,250 kW (1.25 MW) are offered hourly pass through default pricing. The same is true for all Maryland customers over 600 kW and in Pennsylvania, all Duquesne Light customers over 500 kW." (Steffes, lines 568-571)

Intervenors who support fixed-price CPP service for >3MW customers often use historical data regarding the percentage of >3MW customer load that is supplied by competitive retail suppliers to support their position (*for example, see* Stephens, lines 143-155 and 225-247). They have tried to argue that since a portion of >3MW customers still elect utility service, the competitive retail market is not adequately developed for these customers, so a fixed-price CPP product must be offered (*for example, see* Stephens, lines 143-155). However, these arguments do not consider the possibility that the >3MW customers on utility service may not have elected service from a competitive retail supplier because their utility-offered rate, which was set in many cases over a decade ago, may now be a below-market-price offering. I believe that, after 2006, when the existing utility rate is no longer available, non-utility retail suppliers will compete to serve these customers. My belief is supported by statements made by DOE witness Swan: "For the first six years (through 2004), [the Defense Energy Support Center] cumulatively received just five bids from certified RESs and was unable to make an award to any of them because they could not beat either Rate 6L and/or the PPO rate." (Swan, lines 181-184) Also, "This year is the first time in nine attempts over seven years that one of the Federal Government's competitive solicitations has resulted in awards of fixed-price contracts to alternative suppliers. The success this year is probably due to the fact that the two DOE facilities no longer qualify for ComEd's PPO service because their CTCs were no longer positive." (*Id.*, lines 212-216)

(McNeil Reb., ComEd Ex. 10.0, 57:1239-59:1287)

In summary, these customers are treated differently under the Illinois Auction for good reasons. Their special status is reflected by the existence of the competitive declaration, and, as Dr. O'Connor testified, inclusion of these customers in the annual auction "would have the practical effect of rescinding the competitive declaration..." (O'Connor, Tr. 202) ComEd agrees with Dr. O'Connor that the Commission should reject the recommendation to do so.

IIEC made an additional recommendation, initially with respect to customers with demands in excess of 3 MW, but then extended to address all customers in the over 1 MW

category. The proposal is to isolate a demand charge component to be charged on a per kW basis. As IIEC explains:

IIEC recommends that the energy price resulting from the CPP-A auction be modified to isolate a capacity component, which can then be charged on a per kW basis, with the remainder of the auction price being charged on an energy basis. This capacity charge would not be an adder to the auction price. (Stephens Dir. IIEC Ex. 1 at 23:504-508). ComEd proposes to perform a separate capacity auction for use with the hourly price product (associated with the CPP-H segment), or it will use the PJM capacity market once it is sufficiently developed and approved. Because these capacity values will be readily available, they would provide the most straightforward approach for use in developing the demand charge component in the ultimate customer prices. (Stephens Dir. IIEC Ex. 1 at 23:513-519).

(IIEC Init. Br. at 50-51)

ComEd does not recommend that this proposal be accepted by the Commission. IIEC has not provided a persuasive justification for adding this additional level of complexity to the auction. The proposal has been made only by IIEC and is not supported by the Staff or by any other intervenors, all of whom presumably consider it to be unnecessary or inappropriate. In addition, the suggestion is not sufficiently detailed to enable the Commission to provide for its implementation.

J. Continuation of CPP-H Auction

ComEd provided assurances that it would acquire supply for its largest customers through the hourly CPP-H auction until the PJM Reliability Pricing Model or a functionally equivalent model is in place in PJM. (McNeil Dir., ComEd Ex. 3.0, 27:573-576; Naumann Reb., ComEd Ex. 14.0, 20:423-429) IIEC nonetheless argues that the CPP-H auction should be required until the ICC finds that any PJM centralized capacity market or its equivalent is a reasonable approach for acquiring capacity for hourly pricing customers in Illinois. (IIEC Init. Br. at 51-57) IIEC

argues that the ICC may impose such a requirement, despite FERC’s exclusive jurisdiction and despite the filed rate doctrine, under the *Pike County* prudence exception.

Although Staff expresses support for IIEC’s position, (Staff Brief at 108) for the reasons stated in Mr. Naumann’s testimony, ComEd continues to believe that there is no need for ICC prescriptions on this subject, that ComEd’s assurances address any legitimate concern, and that there is no reason to resolve the questions of federal/state jurisdiction that IIEC’s proposal raises.

K. Contingencies

1. Volume Reduction

The Illinois Auction design provides for replacement power to be acquired in the PJM spot market in the event that volume in the auction has to be reduced to ensure a competitive bidding environment. Staff supports this contingency proposal, but seeks clarification that, if the ICC rejects the auction results, all replacement power (including any portion attributable to volume reductions) will be acquired under the “rejection contingency” provisions. (Staff Init. Br. at 110-111) ComEd has no objection to this clarification.

2. Supplier Default

In the event that a supplier selected through the auction process defaults, the process provides for replacement power to be procured in one of three ways — through the PJM markets, through an RFP-type solicitation process or through another auction, depending on the length of the remaining term of the affected contract and the percentage of ComEd’s total retail load involved. (McNeil Dir., ComEd Ex. 3.0, 53:1163–56:1233) Staff has no objection to these contingency provisions, (Staff Init. Br. at 111-112) and ComEd believes that they are appropriate.

3. ICC Rejection

In the event that the ICC rejects the auction results, acquisition of supply from the prevailing bidders would not proceed and a process involving Staff, the Auction Manager and ComEd would be initiated promptly to determine whether the reasons for the rejection could be remedied by conducting another auction or whether a one-year interim procurement plan should be put in place until the next annual auction. (McNeil Dir., ComEd Ex. 3.0, 56:1234–57:1253) Staff has no objection to this contingency provision, but indicates that it would expect ComEd to be prepared to make a proposal promptly in the event that auction results are rejected. (Staff Init. Br. at 112-113) ComEd understands and shares Staff’s interest in making prompt arrangements in this contingency and will make every effort to submit a proposal as quickly as possible.

4. Subsequent Prudence Reviews of Actions in Response to Contingencies

ComEd and Staff have reached a stipulation addressing the Commission’s oversight of purchases of replacement or additional power due to ComEd’s implementation of a contingency plan, as is discussed further in Section VII.B.9 of this Reply brief. (ComEd Cross Ex. 11; ComEd Init. Br. at 109, 157-159) The stipulation, if adopted by the Commission, resolves all issues that have been raised by the Staff on this subject. (Staff Init. Br. at 115-116) It provides for Commission review when review is appropriate and permissible under the *Pike County* exception to FERC’s exclusive jurisdiction over wholesale power transactions.

The Attorney General objects to confining the scope of review of replacement power purchases to the areas that are permitted under *Pike County*. It argues that the Commission’s responsibility to determine if rates are just and reasonable means that it must review replacement power purchases for “the rates consumers will be required to pay.” (AG Init. Br. at 61) That view is contrary to federal law. The stipulation between ComEd and the Staff concerning review

of replacement power purchases observes the requirements of the law and focuses the Commission's review on the subject over which it has jurisdiction – prudence issues reserved to State authorities under *Pike County*. The Attorney General's effort to have the Commission exceed its jurisdiction and violate federal law should be rejected.

L. Regulatory Oversight and Review

1. Nature of Commission Review Before, During, and After Auction

ComEd's Initial Brief explained that the time for the Commission to determine the prudence of the Illinois Auction process is now. Decisions about the overall approach and the details of its execution should be considered in advance, when changes can be made to reflect the Commission's judgment about how best to proceed. This proceeding offers the ideal opportunity for the Commission to accomplish precisely what prudence review is intended to provide—a review of the decision that Illinois utilities are making about procurement of supply for customers based on the facts that are available at the very time the decision must be made.

The Attorney General and CUB argue that review of the process in this proceeding is somehow inconsistent with the Commission's obligation to consider the prudence of ComEd's procurement decisions that will affect the rates that customers pay. (AG Init. Br. at 62-65; CUB Init. Br. at 19-23) As explained above, that simply is not so. *See* Section III(B), *supra*, The Commission will review ComEd's proposal and consider every important decision that is embodied in it. If the Commission approves ComEd's tariffs, the procurement approach ComEd follows will be a prudent process reflecting the best expert views available. That review and determination satisfies every obligation of the Commission with respect to the prudence of the procurement process.

The contention of the Attorney General and CUB that some additional after-the-fact prudence review is required when the auction has been concluded and the prices for supply become known does not accord with Illinois law. *See* Section III(B), *supra*. As ComEd explained in its Initial Brief, under Illinois law, prudence relates to decisions that are made and judgment that is exercised. (BPI v. Illinois Commerce Commission, 279 Ill. App. 3d 834 (1st Dist 1996)) When the auction takes place, it will proceed in accordance with decisions that have already been made and that are reflected in tariffs approved by the Commission. Those decisions and tariffs are not subject to a second prudence review by the Commission. A utility must comply with the provisions of its approved tariffs and has no discretion to do otherwise. There are no decisions being made and no judgments being exercised.

2. Post Auction Commission Review Of Results

As in New Jersey, the Illinois Auction process does not provide for supply prices to become immediately effective and applicable to customer rates at the conclusion of the auction. If the Commission initiates a formal investigation or other proceeding concerning the auction results, the prices determined through the auction will not take effect.

The Attorney General, CCSAO and CUB argue that the three-day period provided for the Commission to take action following the auction is insufficient, but the evidence establishes that prompt consideration is essential and that, under similar circumstances in New Jersey, a post-auction 2-day period has worked effectively. Providing a longer period would increase the costs of supply because bidders would be required to hold offers open for longer periods of time during which the outcome of the process remained uncertain.

Prospective participants in the process emphasize the need for certainty and expedition. They advocate more specificity in the scope of the Commission's consideration, seeking to

confine it to whether there were anomalies in the bids or the process that would call into question the competitiveness of the auction. (MSCG Init. Br. at 3-4; CCG Init. Br. at 16) While ComEd understands the position of these parties, it has stated in this proceeding and continues to believe that the Commission should not be constrained by a prescriptive standard. ComEd's tariffs provide an appropriate period for action and the scope of the Commission's consideration should be governed by the facts and the law, not by pre-approved language that requires the Commission to anticipate and define how it will proceed.

3. Post-Auction Workshop Process

After each auction, a well-designed post-auction workshop process will take place, enabling parties to assess the need for improvements and any response to address lessons learned from the process. (McNeil Dir., ComEd Ex. 3.0, 61:1327-1332) IIEC argues that a workshop alone might not be adequate and that formal proceedings should be required each year to consider the process. (IIEC Init. Br. at 58-59) ComEd has emphasized that, if the Commission or any other party believes that there is a need for a formal proceeding, they will continue to have their rights under the Public Utilities Act to initiate or to request such a proceeding. Given the ability to commence formal proceedings when they are necessary, ComEd believes that it is not essential to require them each year when they may not be needed. The workshop process is an appropriate way to provide an annual opportunity to consider the process and any improvements to it that might be suggested.

4. Formal Proceeding(s) to Consider Process

Although ComEd does not believe that annual proceedings to consider the auction process are appropriate, it did modify its proposal to provide for a proceeding every three years. The three year interval between formal proceedings provides time to build an experience base for

consideration. Although no issues may arise, the knowledge that a formal opportunity to address the process will be available responds to the concerns of those who advocate a pre-scheduled docket.

5. Other Processes and Proceedings

In ComEd's judgment the Illinois Auction proposal is complete. No other processes or proceedings are required.

6. Summary

The combination of review by the Commission of the prudence of the Illinois Auction Proposal in this proceeding, post-auction consideration of the results, annual workshops to discuss possible improvements and other matters and formal docketed proceedings every three years meets every need for review and oversight. The process is well designed and should be approved.

M. Supplier Forward Contracts

1. Uniformity in General

ComEd proposed the use of a uniform supply contract to eliminate negotiations over non-price terms and to permit supplier offers to be compared directly on the basis of price. (McNeil Dir., ComEd Ex. 3.0, 41:881-892) It also sought to achieve as much uniformity as possible between the ComEd and Ameren agreements. ComEd has proposed that the efforts in that direction continue and that a compliance filing be required within 30 days after the final order in this proceeding for submission of the final agreements.

Dynegy seeks to be involved with any further changes to the agreements that the Commission may permit ComEd to implement and proposes that workshops be conducted to finalize the agreements. Staff suggests that an opportunity for additional supplier input be

provided by delaying the compliance filing until 60 days after the posting of a draft contract on the auction web site, which Staff proposes should occur within 7 days of entry of the final order in this matter. (Staff Init. Br. at 119-120)

ComEd believes that the extensive process that has already taken place to solicit input from suppliers is more than adequate for that purpose and that the remaining tasks do not require workshops or an extended compliance filing period.

2. Credit Requirements

Staff has proposed revisions to Section 6.1 of the SFCs, which permit ComEd to unilaterally reduce its credit requirements in response to industry events or unanticipated conditions in the wholesale marketplace. Staff suggests that a report be provided to Staff within 15 days of any such changes so that the reasonableness of the modification can be considered. Staff also suggests that the agreement be amended to clarify that ComEd may restore the former credit requirements following any reduction in standards made under Section 6.1.

ComEd believes that the Section 6.1 procedures are not necessary and could be eliminated entirely. If circumstances ever arose in which a reduction in credit requirements seemed appropriate, the better course of action would be for discussions to take place with Staff prior to the implementation of any change. For that reason, ComEd suggests that the provision granting ComEd the unilateral right to make changes to credit requirements be eliminated from the agreement.

3. Proposed Clarifications and Modifications Accepted by ComEd

As discussed in ComEd's Initial Brief, ComEd made many changes to the SFCs in response to suggestions from suppliers, both prior to the filing of this proceeding and in the course of it, all of which are reflected in the record.

4. Proposed Clarifications and Modifications Not Accepted by ComEd

Several changes to the SFCs have been proposed that ComEd cannot accept for reasons that are described in Ms. Juracek's testimony (Juracek Reb., ComEd Ex. 9.0, 36:860-45:1064; Juracek Sur., ComEd Ex. 17.0, 33:750, 36:807-40:917) and those changes continue to be advocated in the Initial Briefs filed by Constellation and Direct Energy Services. ComEd relies upon the responses included in Ms. Juracek's testimony and urges that these few remaining suggestions be rejected by the Commission.

N. Other Auction Design Issues

There are no other auction design issues for consideration by the Commission.

VI. PROCUREMENT PROCESSES ALTERNATIVES

The Attorney General, CCSAO and CUB suggest that the need to develop a procurement process for the post-2006 period is a problem of ComEd's own making – one that should never have arisen and that could have been avoided entirely by careful planning. CCSAO argues that ComEd “has known what its responsibilities were with respect to serving residential and small commercial customers,” but nonetheless “voluntarily divested ... its generation assets,” creating a supply acquisition dilemma that the Commission must now solve. (CCSAO Init. Br. at 2)) Arguing that “[c]learly, there were other options available to ComEd,” CCSAO maintains that the ICC should simply reject the Illinois Auction Proposal. (Id. At 5) The Attorney General is even more explicit, faulting ComEd for refusing to address the benefits of continuing to acquire supply from Exelon Generation and flatly stating that, rather than proposing an arms-length, competitive procurement approach of the type envisioned by the Restructuring Act, ComEd should have used “its substantial buying power .. to purchase low-cost nuclear power” from Exelon Generation. (AG Init. Br. at 76)

The suggestion that ComEd failed to plan for post-2006 power procurement, overlooked available options or proceeded in a way that is contrary to the interests of customers and the direction of the Commission is plainly inconsistent with the facts. As ComEd explained in its Initial Brief, long before the expiration of the existing power purchase agreement, ComEd began to consider available alternatives to procure supply in 2007 and subsequent years. In 2003, in connection with a plan to acquire Illinois Power, ComEd proposed to acquire supply for both utilities through a long-term agreement with Exelon Generation. (Clark, Tr. 159; Juracek, Tr. 263) Through no fault of ComEd, that proposal met with opposition, and ultimately had to be abandoned. The experience made it clear that some stakeholders in Illinois did not favor approaches that relied upon a long term power purchase agreement with Exelon Generation, and that unilateral efforts by ComEd to address the post 2006 supply issue were likely to be less successful than a proposal that emerged after a process in which the views of stakeholders could be explored and considered.

As a result, ComEd went “back to the drawing board,” and broadened its consideration of acquisition alternatives to include available methods for acquiring supply through the wholesale markets. (Clark, Tr. 159; Juracek, Tr. 264) The Commission assumed an active leadership role, stressing the need for a coordinated approach to post 2006 supply issues, launching the Post-2006 Initiative to provide a framework for considering available alternatives, and discouraging implementation of unilateral procurement plans in favor of a process that would enable all stakeholders to express their views. ComEd cooperated fully with that effort.

In filing its tariffs in this case, ComEd has followed the guidance and direction provided in the December 2, 2004 Final Staff Report from the Post 2006 Initiative recommending that ComEd procure electricity for customers through a vertical tranche auction process. As ComEd

President Frank Clark emphasized, ComEd has “participate[d] in any and every forum where this debate has been on going for the last year and a half...” (Clark, Tr. 109) It has taken its responsibilities to customers very seriously. The remainder of this section will address the few comments about alternative procurement approaches that have been made in the briefs of other parties. However, as stated at the outset of this Reply Brief, the limited opposition to the Illinois Auction Proposal from a few parties is not based on the availability of a better alternative. It is based, quite frankly, on an irresponsible determination to block any effort by the Commission to approve a procurement approach.

A. Active Portfolio Management

ComEd’s Initial Brief discussed the recommendation of three parties, the Illinois Attorney General, CCSAO and CUB, that ComEd engage in active portfolio management to provide supply for customers. For the reasons described in ComEd’s Initial Brief, the active portfolio management suggestion should be rejected. The proposal is not described in any detail, and therefore presents nothing that could be adopted or implemented. The approach would require ComEd to acquire a portfolio of baseload, intermediate and peaking generation resources, together with any associated hedges (for risks such as customer switching, fuel price, outages and locational price differences), sufficient to provide full requirements supply for customers, and would impose the costs and risks of assembling such a portfolio on ComEd’s customers, rather than on suppliers. It would rely on the judgment of one party — ComEd — to assemble the necessary portfolio instead of relying on multiple suppliers, each of whom might employ different strategies and techniques to meet the variable demands of customers. Reliance on a number of competing sophisticated suppliers to arrive at the best supply approach will not only achieve a better result, but it will eliminate the risk of huge losses that can arise when a utility undertakes unilateral responsibility for supply decisions.

As ComEd explained in its Initial brief, the active portfolio management approach was one of the procurement scenarios considered during the Commission's Post 2006 Initiative. (ComEd Ex. 1.4) Staff's Final Report did not recommend that ComEd pursue this approach, with good reason. (ComEd Ex. 1.2) The significant benefits of the Illinois Auction Proposal would be lost and major new risks would be imposed on customers under an active portfolio management approach.

The Attorney General contends that, if ComEd engaged in active portfolio management, it could "use all the variables that go into purchasing to the advantage of consumers," and that it would be "giving up" those variables and the opportunity to benefit consumers by procuring supply through the Illinois Auction. (AG Init. Br. at 74) The record does not support that contention. Dr. Steinhurst attempted to make the same argument in his testimony, and it was shown to be without basis:

What Dr. Steinhurst appears to be arguing, however, is that the *only* way for ComEd customers to receive these benefits from a risk-diversified mix of market-based arrangements is by forcing ComEd to design the inputs and directly acquire and actively manage each of the individual components of this diverse portfolio. CUB-CCSAO Exh. 4.0 at 18:402 to 19:428; 24:526-532.... It is not the only way, and in my judgment not the best way, since it requires the Commission to examine the entire portfolio and each individual component after the fact, while numerous intervenors selectively second guess, support, oppose or modify those features that do or do not favor their interests. This is a prescription for institutionalizing serious regulatory uncertainty, which will likely raise risks and costs for ComEd, but more importantly, also raise risks and costs for those suppliers with whom ComEd must deal, and ultimately ComEd's customers.

The ComEd auction proposal is a better approach for achieving the desired ends. What Dr. Steinhurst appears not to accept is that the same types of diversified, risk-managed portfolios that he favors could be pursued and brought to ComEd and its customers *by the bidders* themselves. Through the competitive pressures of the auction's design, and the resulting contract obligations to supply for various fixed terms at the auction's market-clearing prices, successful bidders will have strong incentives to manage risks efficiently and minimize costs while reliably meeting their contract obligations. They will then reflect those benefits in the prices they accept in their bids for each auction product. These are the same

incentives that Dr. Steinhurst seeks to foster to benefit consumers. The auction is simply a workable mechanism to induce the market bidders to acquire the desired mix, and the resulting contracts will then transfer to consumers the combined benefits of the market's collective judgment regarding cost-effective risk mitigation strategies.

(Hogan Sur., ComEd Ex. 25.0, 13:256-14:281)

The Attorney General argues that, by procuring supply through the Illinois Auction, ComEd will be losing its “substantial buying power” and economies of scale that it could capture for its customers. (AG Init. Br. at 75) The evidence shows that this is not so. As Dr. LaCasse explained:

The proposed Auction Process does leverage the buying power of both ComEd and Ameren by procuring all load in a single auction process. This creates a competitive environment and will ensure that ComEd can obtain the best price for customers.... [T]he proposed Auction Process itself takes advantage of buying power by pooling all load purchases...There is no reason to believe that ComEd would achieve a better result from an exercise of buying power in a series of procurements of different products than in a central large auction where it is buying all its load.

(LaCasse Sur., ComEd Ex. 19.0, 92:2011-92:2024)

The Attorney General also maintains that the Illinois Auction relies on one product, foregoing the use of a diverse set of “less risky products” that might help to minimize the costs customers pay. (AG Init. Br. at 75) The testimony demonstrated that the one-product argument is without basis as well:

By nature, the product proposed by ComEd for its Auction Process creates strong incentives for suppliers to optimize the use of available products in the wholesale market and to offer customers the lowest price for a fixed-price product for a given term. Under ComEd's proposed Auction Process, suppliers will be accessing the market and acquiring the diverse set of products that minimize costs. By optimizing to offer the lowest fixed price, suppliers are meeting customer needs. The entire range of products ...is available to suppliers for developing a portfolio, and the optimal aggregation of these diverse products will be made by suppliers.

(LaCasse Sur., ComEd Ex. 19.0, 94:2064-94:2075)

B. Request for Proposal

ComEd's Initial Brief and Mr. McNeil's testimony explain the reasons for concluding that the Illinois Auction Proposal is a better procurement approach than a request for proposal process. The Commission's Staff agreed in its Final Report, and the Commission should reach the same conclusion.

C. Affiliate Contract

The Attorney General suggests that ComEd should seek to obtain supply for its customers under a power purchase agreement with Exelon Generation – an approach that the Post 2006 Initiative determined had far more disadvantages than advantages and that the Commission's Staff rejected in the Final Report. The Attorney General's proposal is based entirely on the demonstrably incorrect assumption that ComEd has special bargaining power that would enable it to acquire supply from Exelon Generation at prices that are lower than Exelon Generation (and other suppliers) could obtain in the wholesale marketplace. The record in this proceeding establishes that there is no basis for that assumption.

Seeking to respond to the obvious deficiencies in this affiliate contract proposal, the Attorney General protests that the suggestion is not that below market prices would be obtained, but rather that there are many types of market prices. In other words, there are market prices that are available to all suppliers selling in the PJM markets, and, according to the Attorney General, there is another, lower market price that Exelon Generation should be willing to provide to ComEd. That proposition is untenable. The mere articulation of the rationale for the position shows how baseless it is.

Ordering Exelon Generation to provide supply to ComEd at special below-everyone-else's market prices is not one of the options available for consideration in this proceeding. It

could not be ordered in any forum. It certainly could not be ordered here, given that the price of wholesale power transactions is a subject that falls outside the Commission's jurisdiction and is vested exclusively with the FERC.

D. Other Competitive Procurement Mechanisms

There are no other competitive procurement mechanisms requiring discussion or consideration by the Commission.

E. Other Competitive Processes Alternatives

For all of the reasons described in ComEd's Initial Brief and in this Reply Brief, there are no other competitive processes that warrant further consideration as alternatives to the vertical tranche auction proposal.

VII. TARIFF AND RATE DESIGN ISSUES

A. General Tariff and Rate Design Issues

The evidence establishes that ComEd's proposed tariffs and tariff amendments, including the improvements and clarifications that ComEd has agreed to and proposed in Rider CPP and Rider PPO-MVM - Power Purchase Option (Market Value Methodology) ("Rider PPO-MVM") since the outset of this proceeding, are just and reasonable for customers as well as the utility and its shareholders, and should be approved. (*E.g.*, ComEd Init. Br. at 125-173)

Staff and intervenors generally either support or do not oppose ComEd's proposals on most aspects of tariff and rate design. Their respective positions on a relatively small number of tariff and rate design issues, however, are disparate. The evidence shows that ComEd supports the best approach, or an appropriate, reasonable compromise, on each of those issues.

The provisions of proposed Rider CPP relating to details of the Illinois auction proposal have been discussed, directly and indirectly, in ComEd's Initial Brief and earlier Sections of this Reply Brief. This Section VII addresses the remaining tariff and rate design issues.

B. Matters Concerning Rider CPP

1. Rider CPP-Organization

ComEd and Staff agree that the evidence supports the organizational structure of proposed Rider CPP, as revised and agreed to by ComEd and Staff. (ComEd Init. Br. at 127; Staff Init. Br. at 143-144) No intervenor disagrees. The revised structure should be approved.

2. Rider CPP-Definitions

a. Customer Supply Group Definitions

ComEd's Initial Brief showed that the evidence supports its proposed Customer Supply Group definitions, subject to a one-word conforming change in the definition of the Large Load Customer Supply Group that is needed if the Commission approves moving that Group from the CPP-B auction segment to the CPP-A auction segment. (ComEd Init. Br. at 127-128) No party disagrees. The definitions should be approved, with that change if needed.

b. Peak and Off-Peak Period Definitions

ComEd's Initial Brief showed that the evidence supports its proposed compromise of using existing Peak and Off-Peak period definitions, with the North American Electric Reliability Council ("NERC") holidays, in the "translation" formulae for calculating Supply Charges under Rider CPP and in defining those charges; and that, absent that compromise, the evidence supports ComEd's initial proposal for new definitions. (ComEd Init. Br. at 128-130)

Staff continues to oppose ComEd's original proposal, but Staff apparently accepts ComEd's compromise proposal. (*See* Staff Init. Br. at 145-149) While BOMA and Dynegey, in

testimony, respectively opposed and supported ComEd’s original proposal (ComEd Init. Br. at 129), neither addressed the subject in their Initial Brief. No other intervenor submitted evidence on the subject or addressed it in their Initial Brief. ComEd’s compromise proposal should be approved. (*Id.* at 128-30) Otherwise, its original proposal should be adopted. (*Id.*)

3. Rider CPP–Specification of Competitive Procurement Process

ComEd’s Initial Brief showed that the Commission should approve the Competitive Procurement Process part of Rider CPP, subject to such conforming changes as are needed to effectuate the Commission’s determinations on the issues raised regarding the design and implementation of the proposed CPP auctions. The open questions with regard to this part of the tariff are entirely derivative of those issues, apart from two limited exceptions discussed in Sections VII.B.4.a.i and ii and VII.B.9 of ComEd’s Initial Brief and this Reply Brief. (ComEd Init. Br. at 130-131) No other party included discussion in Section VII.B.3 of their Initial Briefs.

4. Rider CPP–Retail Customer Switching Rules

a. Enrollment Window

The issues addressed in Section VII.B.4.a of the parties’ Initial Briefs relate solely to CPP-A service. The issues here are: (1) whether or which customers eligible for CPP-A service should be placed on the service only if they request it, i.e., the “opt in” approach, or unless they do not request it, i.e., the “opt out” approach; and (2) what should be the duration of the enrollment window, whether it is “opt in” or “opt out”. ComEd’s compromise proposal on those issues should be approved, as explained below.

i. Duration of Window

ComEd originally proposed that CPP-A eligible customers have a 30-day enrollment window within which to “opt-in” to CPP-A service following an auction; otherwise, unless they

elected to take service from a RES, they would “default” to CPP-H service. (ComEd Ex. 7.1, Original Sheet No. 272) ComEd supported the 30-day enrollment window as the most appropriate balancing of concerns regarding the time required by customers to make service decisions, with the effects on suppliers’ bids due to longer enrollment windows. (McNeil Dir., ComEd Ex. 3.0, 38:811-39:839; *see also* McNeil Reb., ComEd Ex. 10.0, 51:1098-1115, 53:1149-54:1163, 54:1173-55:1204) Also, a 75-day window could conflict with the timing of the auctions. (McNeil Reb., ComEd Ex. 10.0, 55:1191-1196)

ComEd, in surrebuttal, presented a revised proposal: (1) eligible customers taking bundled electric service, as of January 1, 2007, under Rate 6 - General Service, Rate 6L - Large General Service, and Rate 24 - Water-Supply and Sewage Pumping Service, would be placed on CPP-A service on an “opt out” basis, with the ability to choose RES supply on a 7 day “DASR” basis at any time during the term of service; and (2) eligible customers taking hourly service or delivery services as of January 1, 2007, would have to “opt in” to during the initial 30-day enrollment window in order to take CPP-A service, and would have to remain for the full term of service. (McNeil Sur., ComEd Ex. 18.0, 26:569-27:591, 28:621-30:674, 31:693-34:766)

ComEd in its Initial Brief (at 132) presented a further revision, a compromise that would alter, as to the “opt in” customers (only), the duration of the enrollment window. ComEd, as to the “opt in” customers, proposed, as a compromise, a 50-day enrollment window in the first auction period and a 45-day window in later auction years. (*Id.* at 132-133)

ComEd noted that those customers who would become subject to a term requirement by opting into CPP-A service would not be limited to that 50-day (and later 45-day) period within which to begin and complete their analysis of the available service options. (ComEd Init. Br. at 133) They can canvass the RES market in advance of the auction, preparing themselves to

evaluate the auction results, and when the results become known, that advance preparation will assist them in making informed service decisions within the enrollment window. (*E.g.*, McNeil Reb., ComEd Ex. 13.0, 53:1155-54:1163; Schlaf JTr., 1345-1346)

Staff, in its direct testimony, agreed with ComEd's proposal for a 30-day window, while recommending further study. (Schlaf Dir., Staff Ex. 5.0, 6:126-142) Staff, in rebuttal testimony, opposed CES' direct testimony proposing a 75-day window. (Schlaf Reb., Staff Ex. 13.0, 2:50-51, 4:95-7:161) Staff estimated that auction bidders can be expected to add an additional 1.8% to their bids to account for the 75-day window instead of a 30-day window. (*Id.* at 5:129-6:155) Staff later indicated that a window of up to no more than 40 to 45 days would be a reasonable compromise. (Staff Init. Br. at 153) (citing Schlaf JTr., 1340, 1346)

As indicated above, CES initially proposed a 75-day window, but CES has modified its position, and now supports use of a 50-day window for the initial auction period and a 45-day window for subsequent auctions. (CES Init. Br. at 29)

The other parties took conflicting positions. Dynegy, IIEC, and the U.S. Department of Energy each advocate a 30-day window. (Dynegy Init. Br. at 20-21; IIEC Init. Br. at 70-73, Init. Br. at 13-14) CCG did not take a position on this subject, but it did express concern about increasing supplier risk premiums. (Smith Dir., CCG Ex. 1.0, 3:83-89) IIEC agreed with ComEd regarding the need for a balance between allowing customers sufficient time to make a decision and keeping bid premiums to a minimum. (Stephens Reb., IIEC Ex. 4.0, 11:244-13:294; Stephens, JTr. 62) BOMA advocated the use of a 75-day window. (Childress/Brookover Dir., BOMA Ex. 2.0, 25:535-26:551) IIEC stressed that CES' and BOMA's citations to existing Rider PPO - Power Purchase Option ("Rider PPO-MI") as support for a 75-day window were inappropriate because the window of time for electing Rider PPO-MI

has no impact on the price of the service and for other reasons. (Stephens Reb., IIEC Ex. 4.0, 12:268-13:294) DES-USESC Energy, in the context of its proposal to significantly alter the nature and timing of the auctions, opposed an enrollment window. (Steffes Dir., DES-USESC Ex. 1.0, 33:699-702) DES-USESC Energy did not present evidence or argument, in the context of the Illinois auction proposal, regarding the appropriate length of the window.

The Commission should approve ComEd's compromise proposal as presented in its Initial Brief. The proposal reasonably balances customer flexibility, avoiding excessive risk premiums in auction bids, and avoiding interference with the auction timeline.

ii. Opt In vs. Opt Out

ComEd's proposal to change its approach from "opt in" to "opt out" as to customers on Rates 6, 6L, and 24 as of the relevant date is supported by Staff. (Staff Init. Br. at 155) The intervenors do not appear to support or oppose this aspect of ComEd's proposal. As indicated above, based on the evidence, ComEd's proposal is reasonable and should be approved.

b. Other Switching Rule Issues

The Commission, with regard to the Retail Customer Switching Rules part of Rider CPP, is presented with five additional issues, three of which relate to CPP-A service and two of which relate to CPP-H service: (1) whether "new accounts" that are eligible for CPP-A service should be allowed to elect to take CPP-A service outside of the enrollment window; (2) whether "successors accounts" to existing customers that were eligible for, but elected not to take, CPP-A service should be allowed to elect to take CPP-A service outside of the enrollment window; (3) whether CPP-A eligible customers that were on Rates 6, 6L, and 24 and that were migrated to CPP-A service should be allowed to switch to delivery services and obtain supply service from a RES with 7 days notice; (4) how much advance notice a CPP-H customer should be required to

give to ComEd before terminating that service; and (5) whether a CPP-H customer should be allowed to request to be switched off of that service on an “off-cycle” basis (i.e., on a date other than the customer’s regularly scheduled meter reading date).

The first, second, and fourth issues now appear to be uncontested. The Commission should approve ComEd’s proposed clarifications of, and compromises on, all five issues.

i. The CPP-A Issues.

As ComEd explained in its Initial Brief, as to the first two issues here, ComEd is willing to agree to Staff’s proposal to permit new accounts that are eligible for CPP-A service to elect to take CPP-A service outside of the enrollment window, provided that the definition of new accounts does not permit “successor accounts” to existing customers that were eligible for, but chose not to take, CPP-A service, to elect to take CPP-A service outside of the window. (ComEd Init. Br. at 134-137) Staff now accepts ComEd’s position. (Staff Init. Br. at 156-157) ComEd’s now-unopposed proposed compromise is supported by the evidence and should be approved.

As to the third issue, Dynegy opposes ComEd’s proposal that CPP-A eligible customers that were on Rates 6, 6L, and 24 that were migrated to CPP-A service should be allowed to switch to delivery services and obtain supply service from a RES with 7 days notice (Dynegy Init. Br. at 20-22), but this feature of ComEd’s compromise proposal should be approved, on balance, because of the flexibility it gives to these customers.

ii. The CPP-H Issues.

As ComEd explained in its Initial Brief, as to the two CPP-H service issues, ComEd is willing to agree to reduce the notice period for terminating such service to the 7 days notice under the existing DASR rules relating to delivery services, provided the termination occurs on a normally scheduled meter reading date, i.e., not off-cycle. (ComEd Init. Br. at 137-139)

Staff's Initial Brief accepts ComEd's position to the extent that it adopts the 7 day DASR rules, but continues to oppose the limitation to on-cycle switching. (Staff Init. Br. at 156) No intervenor presented evidence, or argued in its Initial Brief, in support of off-cycle switching.

Allowing off-cycle switching here would impose substantial unwarranted administrative burdens and costs on ComEd. (ComEd Init. Br. at 138-139) The evidence shows there may be far greater interest on the part of customer agents (General Account Agents) in having customers move on to and off of CPP-H service in the post-transition period, which means that off-cycle switching could be far more burdensome and costly for ComEd than Staff assumes. (*Id.*) Staff's witness admitted, on cross-examination, that, depending on price movements, switching in relation to CPP-H service may increase. (Schlaf, Tr. 1352–1353) Although in theory, as Staff notes (Staff Init. Br. at 156), an off-cycle switching fee could enable ComEd to recover from CPP-H customers that request off-cycle switching the costs of the additional burdens imposed thereby on ComEd (Alongi / Crumrine, Tr. 772–773), no such fee has been proposed in this Docket, and Staff has not shown that the existing fee applicable to delivery services customers would be sufficient here.¹⁵ ComEd's compromise proposal should be approved.

5. Rider CPP–Limitations and Contingencies

The Commission should approve the Limitations and Contingencies part of Rider CPP subject to such conforming changes as are needed to effectuate the Commission's findings on the issues that have been raised regarding contingent scenarios, discussed in Section V.K.1, 2, and 3 of ComEd's Initial Brief and this Reply Brief, and to the Commission's findings regarding

¹⁵ If the Commission were to direct that ComEd permit off-cycle switching in relation to CPP-H service, then ComEd would request that the Order also state or indicate that ComEd may apply an off-cycle switching fee to such switching subject to its being supported and reviewed in ComEd's pending (ICC Docket No. 05-0597) and future rate cases. Setting the fee in a rate case would be the most appropriate procedure.

Staff's and ComEd's joint proposal relating to Commission review in certain contingent scenarios, discussed in Sections V.J.4 and VII.B.9 of ComEd's Initial Brief and this Reply Brief.

In brief, the Limitations and Contingencies part addresses the contingent competitive procurement processes to be used in the event of undersubscription of an auction or default under an SFC. (ComEd Init. Br. at 140) The open questions with regard to this part, in relation to the contingent processes as such, are entirely derivative of the issues regarding those processes. (*Id.*)

6. Rider CPP-Translation to Retail Charges

The evidence supports ComEd's revised proposed "translation" formulae (also referred to as "prisms") for "translating" the results of the CPP auctions into retail Supply Charges, without mark-ups, for each Customer Supply Group, as applicable. (ComEd Init. Br. at 140-145) Staff and every intervenor that has addressed the subject supports or does not oppose the concept of using the prisms to allocate to the applicable Customer Supply Groups the costs that ComEd will incur under the SFCs, although a few specifics remain open issues. The evidence supports ComEd's positions on those items.

There have been only four issues raised in this Docket with regard to the specifics of the prisms: (1) the definitions of Peak and Off-Peak periods, (2) the use of the Migration Risk Factor in the "prism" for calculating CPP-B service Supply Charges, (3) the use of forwards in the prisms, and (4) whether the prisms should be modified for CPP-H service. In accordance with the ALJ's approved briefing outline, the first issue is discussed in Section VII.B.2.b of ComEd's Initial Brief and this Reply Brief, and the fourth issue is discussed in Section VII.B.10 of ComEd's Initial Brief and this Reply Brief. The second and third issues appear to have been resolved, subject to the Commission's approval, as explained in the following two subsections.

a. Customer Supply Group Migration Risk Factor

ComEd's Initial Brief showed, based on the evidence, that the Commission should approve the elimination of the Migration Risk Factor from the CPP-B prism, if and only if, the Commission approves the integrated "package" of rate design changes referenced in earlier subsections of ComEd's Initial Brief; and that, otherwise, the Commission should approve ComEd's original proposal to employ the factor in that prism, without CES' proposed changes in the factor. (ComEd Init. Br. at 142-144)

Staff continues to oppose the Migration Risk Factor. (Staff Init. Br. at 160-163) CES' supports the factor, in particular with CES' proposed adjustments to the factor. (CES Init. Br. at 35-41) No other party's Initial Brief addressed the subject. ComEd's above compromise position should be approved, but, otherwise, its version of the factor should be approved.

b. Market Cost Information–Market Energy Costs

ComEd's Initial Brief showed that the evidence supports its use of forward price information in the translation formulae. (ComEd Init. Br. at 144-145) Staff agrees. (Staff Init. Br. at 64) No other party submitted evidence on this subject or discussed it in its Initial Brief. ComEd's proposed use of forward price data in the formulae should be approved.

7. Rider CPP-Supply Administration Charge

ComEd's proposed Supply Administration Charge is found not in proposed Rider CPP, but rather in proposed Rider PPO-MVM. In accordance with the ALJ's approved briefing outline, the charge, therefore, is addressed in Section VII.C.2 of this Reply Brief.

8. Rider CPP-Accuracy Assurance Mechanisms

As ComEd's Initial Brief stated, the Commission, with regard to the Accuracy Assurance Mechanisms ("AAM") part of Rider CPP, is presented with a large number of issues, some

substantive and some not.¹⁶ ComEd and Staff are the only parties to have submitted evidence on, and are the only parties to have discussed in their Initial Briefs, those issues as such.¹⁷

ComEd's Initial Brief provided the following uncontested background information, which is repeated here to provide context and terminology:

The AAM part of Rider CPP is intended to ensure accurate cost recovery, which benefits customers and the utility alike. The AAM part provides for a monthly charge or credit (depending on the underlying calculations applicable to any given month) called the Accuracy Assurance Factor ("AAF"). (ComEd Ex. 7.1, Original Sheet Nos. 291–294). The AAF in turn is composed of two factors, the Customer Demand and Usage ("CDU") Factor and the Contingency Factor ("CF"). (*Id.*). "The CDU Factor serves to balance the amounts billed to retail customers taking ComEd supply service with payments made to suppliers as a function of the contract terms and prices determined in accordance with Rider CPP, and based on changes in retails' customers usage and demands. The need for this factor stems from the fact that there will be differences between retail customers' actual demands and usage and the historical retail customer demand and usage data used in developing the wholesale to retail translation ratios." (Alongi / Crumrine Dir., ComEd Ex. 7.0, 66:1470–1476). The CF "addresses the Company's net costs in the event of use of the contingent wholesale market competitive procurement processes" provided for in the Limitations and Contingencies part of proposed Rider CPP. (*Id.*, 67:1498–1499; *see also id.*, 67:1500–68:1513). Rider CPP provides for ComEd's submitting to the ICC, on a monthly basis, informational filings regarding the AAF and the underlying data and calculations. (*Id.*, 68:1514–1518).

(ComEd Init. Br. at 145-146)

ComEd's Initial Brief pointed out that Staff raised three kinds of issues relating to the AAM part: (1) verification issues, (2) formulae and calculations issues, and (3) clarification issues. (ComEd Init. Br. at 146, *et seq.*) The evidence shows that ComEd's positions appropriately and fully address all real concerns on each category of issues.

¹⁶ Please note that certain related issues involving the Limitations and Contingencies part and the Competitive Procurement Process part of Rider CPP are discussed in Section VII.B.9 of this Reply Brief.

¹⁷ Please note that Staff addressed, in Section VII.B.9 of its Initial Brief, some of the AAM part issues that ComEd addressed in Section VII.B.8 of its Initial Brief. ComEd is adhering to the location in its Initial Brief.

a. Issues That Have Been Resolved.

As noted above, many issues relating to the AAM part of Rider CPP have been resolved, subject to the Commission's approval. ComEd's Initial Brief listed many of those issues, while noting that a few had related open items.¹⁸ (ComEd Init. Br. at 147-149 and Exhibit 1 thereto)

Staff's Initial Brief also provides lengthy lists of uncontested issues relating to the AAM part. (Staff Init. Br. at 165-170; *see also id.* at 180-181) ComEd agrees with or does not oppose Staff's lists, except that, as to "Factor A" in the AAM part, Staff mistakenly listed conditional agreements on language as unconditional agreements on the underlying substantive issues, as is discussed in Section VII.B.8.b.3 of this Reply Brief.

b. Issues That Remain Open.

There are four remaining open issues, some with more than one aspect, with regard to the AAM part. The Commission should approve ComEd's positions on those issues. ComEd's positions are supported by the evidence in the record and are just and reasonable.¹⁹

i. Monthly Informational Filing Due Date.

The Commission should approve ComEd's proposal to submit its monthly informational filings setting forth the AAFs no later than the third business day before the monthly billing period in which the AAFs will be applicable. ComEd's Initial Brief provided extensive, detailed reasons, supported by compelling evidence, that Staff's proposal, that the monthly informational filings be postmarked by the 20th day of the month preceding the monthly billing period, is

¹⁸ As to one of those ten issues, whether supply-related uncollectibles expenses should be tracked in the AAF calculation, CES' Initial Brief disagrees, in one passing sentence, with Staff and ComEd. (CES Init. Br. at 47) CES' position is without merit, as Staff's Initial Brief shows. (Staff Init. Br. at 186-189)

¹⁹ Please note that Staff briefed these issues in Section VII.B.9 of its Initial Brief.

unwarranted and is contrary to the interests of customers and the utility. (ComEd Init. Br. at 149-152) Staff's Initial Brief disagrees (Staff Init. Br. at 171-174), but errs here.²⁰

Detailed evidence shows, and Staff does not deny, that, if the AAF charge or credit is calculated on ComEd's proposed two month lag basis, which is the earliest possible basis given when the necessary meter data becomes available, then Staff's proposed monthly informational filing due date suffers from serious practical problems, including: (1) the requisite data are not available that early; (2) any changes in the AAFs based on Staff's review of the filing could not be implemented in ComEd's billing system in the next monthly billing period, because of the extensive testing that ComEd needs to and does perform when a new or changed charge or credit is put into the system, in order to ensure that it is charged or credited correctly and does not cause system problems. (See Staff Init. Br. at 172; see also ComEd Init. Br. at 150-151)

Staff, after listing dozens of issues as to the AAM part on which ComEd reached agreement with Staff, appears to criticize ComEd for its unwillingness to compromise on this particular issue. (Staff Init. Br. at 173-174)²¹ ComEd did not compromise here because its proposed due date is in the best interests of customers and the utility.

Staff claims to have proposed a "sensible solution" (Staff Init. Br. at 173) but is mistaken. Staff proposes that ComEd should postpone the AAF process by switching to calculating and implementing AAFs on a three month, instead of two month, lag basis. (*Id.*) Staff's proposal is inappropriate. As ComEd's surrebuttal testimony stated:

Although Mr. Knepler offers this as a compromise, ComEd cannot accept his proposal to extend the lag period to three months. In light of the fact

²⁰ Please note that Staff addressed this subject in Section VII.B.9.1 and 2 of its Initial Brief.

²¹ Staff cites ComEd witness Mr. Alongi's statement that he was not aware of certain alleged facts that Staff included in a cross-examination question as if that statement were evidence that those alleged facts are true. (Staff Init. Br. at 173-174) That is improper. In any event, the alleged facts, which involve whether four gas utilities use a three month lag in their purchased gas adjustment clause filings (Staff Init. Br. at 173-174) are irrelevant here.

that the purpose of the AAF is to balance the several billions of dollars of revenues and expenses that will be incurred annually, ComEd has proposed a process that would minimize the lag to the shortest period practicable (*i.e.*, a two month lag). We believe it is important for both customers and ComEd to reflect the appropriate charge or credit through the AAF in as timely a fashion as possible. Therefore, ComEd believes it would be inappropriate to inject an additional month's delay into the process.

(Alongi / Crumrine Sur., ComEd Ex. 21.0, 31:714–721) As noted earlier, the AAF in any given month can be a credit or charge. To delay the AAF by a month, in any given month, is needlessly going to cause either customers or the utility to lose the time value of money, possibly very substantial amounts in the aggregate, and that would occur every month, one way or the other. Staff ignores that fact. Moreover, delays in implementing CPP-B and CPP-A AAFs could even jeopardize rate stability, as discussed further below. (ComEd Init. Br. at 151)

Staff does not, and cannot, argue that, under ComEd's proposal, an error in an AAF, if such were to occur, will not be corrected. Such an error is highly unlikely, although, if Staff's proposal led to AAF changes being implemented without extensive testing, then they would be more likely. (ComEd Init. Br. at 150-151) In any event, it is undisputed that under ComEd's proposal, any such error will be corrected in the following monthly billing period. (ComEd Init. Br. at 151) ComEd's proposed due date should be approved.

ComEd's Initial Brief also showed that Staff's related proposal, regarding requiring special permission filings if an AAF monthly information filing is late, lacks a valid legal basis and should be rejected for multiple reasons. (ComEd Init. Br. at 151-152)

Staff's Initial Brief disagrees, but its reasoning is circular, *i.e.*, it assumes that the Act requires a special permission filing, but it does not actually show that there is any such requirement. (*See* Staff Init. Br. at 175) Staff's proposal should not be approved.

ii. Staff's Proposal for Litigation and Commission Approval of Which Accounts and Sub-Accounts ComEd Should Use.

ComEd's Initial Brief showed that the Commission should reject Staff's proposal for further contested proceedings regarding ComEd's identification of the Accounts that should be used to record the components of the AAF calculations, and of the specific sub-Accounts that ultimately will be created for use in those calculations. The evidence establishes that Staff's proposal would serve no useful purpose, and would impose needless burdens on Staff, ComEd, any other interested party, if any, and the Commission. (ComEd Init. Br. at 152-154) Staff's Initial Brief disagrees (Staff Init. Br. at 181-185), but Staff's arguments lack merit.²²

The Commission's Post-2006 Initiative's Rates Working Group, in its Final Report, determined that, given a full requirements auction, "utilities should pass through, with no 'mark-ups' or 'return on', the costs of the commodity itself." (Alongi / Crumrine Dir., ComEd Ex. 7.0, 17:369-372) (quoting the report, ComEd Ex. 1.5, at page 16)

ComEd agreed with the principle of passing through those costs with no mark-up, and it structured the specific provisions of Rider CPP to incorporate that principle. (*E.g.*, Alongi / Crumrine Dir., ComEd Ex. 7.0, 17:372-373) Staff itself states that: "ComEd's proposal is designed to charge customers for the power that ComEd acquires at ComEd's costs, without markup." (Staff Init. Br. at 2) Neither Staff nor any intervenor has claimed that Rider CPP is not designed to pass through, without mark-up, ComEd's costs incurred under the SFCs resulting from the CPP auctions (and under the contingent procurement methods).

Thus, it is the language of Rider CPP, not the Accounts or sub-Accounts that ComEd uses to account for costs and revenues, that should and does determine which categories of costs

²² Please note that Staff addressed this subject in Section VII.B.9.f of its Initial Brief.

and revenues properly flow through the AAF calculations. ComEd's witnesses were absolutely clear on that point. (*E.g.*, Alongi / Crumrine Sur., ComEd Ex. 21.0, 21:471-472; Waden Sur., ComEd Ex. 22.0, 6:122-124)

Staff originally proposed that it be given the authority to approve which Accounts in the Uniform System of Accounts (the "USoA") ComEd would use to record the components of the AAF calculations. (Selvaggio Dir., Staff Ex. 8.0, 9:231-10-255) ComEd, in rebuttal testimony, to address Staff's concerns, provided a table showing which Accounts would be used, i.e., ComEd Ex. 13.2 (Revised). (Alongi / Crumrine Reb., ComEd Ex. 13.0, 36:774-787)

ComEd's Initial Brief pointed out that Staff apparently no longer disputes ComEd's identification in ComEd Ex. 13.2 (Revised) of the particular Accounts within the USoA that would be used, citing, *inter alia*, the testimony of Staff's witness on cross-examination. (ComEd Init. Br. at 148) Staff's Initial Brief takes no issue with the accounts listed in ComEd Ex. 13.2 (Revised). The USoA defines which Accounts are to be used to record each category of expense and revenues, and ComEd correctly applied the USoA to Staff's question. (*E.g.*, Waden Sur., ComEd Ex. 22.0, 4:75-80) Staff acknowledged that fact.²³

Staff's Initial Brief states that ComEd "admitted" that ComEd Ex. 13.2 (Revised) does not determine which costs and revenues properly flow through the AAF calculations. (Staff Init. Br. at 183) As noted above, that is because it is the language of Rider CPP, not the list in ComEd Ex. 13.2 (Revised), that is supposed to, and does, determine which costs and revenues properly flow through the AAF calculation.

Staff correctly notes that some of the Accounts in ComEd Ex. 13.2 (Revised) will include other costs and revenues that do not belong in the AAF calculation (Staff Init. Br. at 183), but

²³ Staff previously had expressed concern or confusion about why Account 566 was listed in ComEd Ex. 13.2 (Revised), but Staff has acknowledged that that has been cleared up. (Staff Init. Br. at 169-170)

that is not relevant. Again, it is the tariff that determines which costs and revenues properly flow through the AAF calculation. The fact that the USoA dictates that other costs or revenues might also go in some of the Accounts used to record components of the AAF calculation is a fact that ComEd pointed out when it first answered Staff's question about which Accounts would be used. (Alongi / Crumrine Reb., ComEd Ex. 13.0, 36:779-37:783 and footnote 3) ComEd is simply complying with the USoA. That does not mean that any costs or revenues included in those Accounts, that do not belong in the AAF calculation, by virtue of those Accounts being listed in ComEd Ex. 13.2 (Revised), become "eligible" for inclusion in the calculation. The evidence clearly shows they do not, as noted above. (*See also* Staff Init. Br. at 169-170)

In addition, ComEd and Staff have entered into a stipulation, subject to the Commission's approval, in brief, to include express language in Rider CPP that permits Commission review of calculations of Supply Charges as well as AAFs, including not only arithmetical errors but also whether ComEd has included only those costs authorized to be included by the Commission's Order in this Docket, and that permits appropriate relief, including refunds. (ComEd Init. Br. at 157 and footnote 19; *see also* Section VII.B.9.a of this Reply Brief)

The above leaves only the question of which sub-Accounts ComEd will create and use. The evidence shows not only that sub-Accounts have not been, but also that they should not be, created by ComEd at this time. (ComEd Init. Br. at 152-154) Staff's complaint, that "ComEd's proposal does not provide Staff or the Commission any process by which to contest the future decisions that ComEd makes in determining the appropriate sub-accounts to flow through the AAF mechanism" (Staff Init. Br. at 184), is incorrect and ignores ComEd's express commitment to work with Staff on this subject (ComEd Init. Br. at 153)

Staff's proposal should be rejected. The proposed proceeding would impose unnecessary burdens and costs on ComEd, Staff, any other parties that participated, and the Commission.

iii. Staff's Proposal That All Disputes Must Be Resolved Through a Formal Commission Proceeding.

ComEd's Initial Brief showed that ComEd and Staff are in partial agreement on the addition of a factor to the CDU Factor and CF calculations to reflect adjustments for refunds or additional collections, but that ComEd and Staff differed on both the substance, in two respects, and the name of this factor. (ComEd Init. Br. at 148-149, 154-156)

Staff's Initial Brief has simplified, somewhat, the first substantive issue, which relates to informal dispute resolution, and the issue of the name of the factor.²⁴ Staff agrees that, if the Commission agrees with ComEd's position, that Staff and ComEd should be allowed to attempt to resolve any disputes regarding AAF calculations on an informal basis, then the adjustment factor may then be named "Factor A". (Staff Init. Br. at 185) Staff argues, however, that, if the Commission agrees with Staff's position, that resolution of such disputes should not be allowed on an informal basis, and that they should only be resolved through the automatic annual docketed reconciliation proceedings discussed in Section VII.B.9.c of this Reply Brief, then the adjustment factor should be called "Factor O" for "ordered". (Staff Init. Br. at 185)

It is not clear why Staff has coupled the question of whether Staff and ComEd should be allowed to attempt to resolve any disputes regarding AAF calculations on an informal basis with the question of whether there should be automatic annual docketed reconciliation proceedings. ComEd sees no reason that such disputes cannot or should not be resolved informally when possible, even if, hypothetically, there were to be such proceedings. As ComEd's Initial Brief

²⁴ Please note that Staff addressed this subject in Section VII.B.9.f.2 of its Initial Brief.

showed, the evidence shows that: (1) Factor A should cover both adjustments made based on the utility working with Staff to resolve disputed issues without a formal Commission proceeding and adjustments made pursuant to a Commission Order, if any; (2) to assume, or require, that all such disputed issues be resolved through formal proceedings only would be unnecessary, overly litigious, and administratively burdensome on ComEd, Staff, and the Commission, and potentially other stakeholders; and (3) such a requirement could unnecessarily delay, possibly for extended periods, the correction of errors, which may significantly harm customers and the utility. (ComEd Init. Br. at 154-155; *see also id.* at 159-163)

Staff's Initial Brief did not expressly address the second substantive dispute relating to Factor A, whether Factor A should permit ComEd to amortize adjustments over multiple effective periods with interest (interest is included because Staff proposed it). (ComEd Init. Br. at 155) Staff presumably agrees, however, that Factor A should permit such, if the Commission approves ComEd's position on allowing informal as well as formal dispute resolution.²⁵

iv. Interest.

ComEd's Initial Brief showed that, if the Commission agrees that informal as well as formal resolution of issues relating to possible Factor A adjustments are appropriate, as discussed in the preceding subsection of this Reply Brief, then the Commission also should approve ComEd's position that the interest component of Factor A should run from when the erroneous AAF was applied through when it was corrected. (ComEd Init. Br. at 156) Staff presumably agrees, for the reasons discussed in that subsection.

²⁵ ComEd notes that Staff mistakenly included, in a list of uncontested issues earlier in its Initial Brief, ComEd's alleged agreement to Staff's above positions and to Staff's position related to the next subsection of this Reply Brief. (See Staff Init. Br. at 167) (citing Alongi / Crumrine Sur., ComEd Ex. 21.0, lines 702-709) The testimony cited by Staff expressly stated that ComEd's agreement was limited to that point that, if the Commission were to adopt Staff's positions on those issues, then the language appearing on lines 702-709 of the cited testimony would be appropriate language. (Alongi / Crumrine Sur., ComEd Ex. 21.0, lines 696-709)

c. Accounting reconciliations

Please *see* the following subsection of this Reply Brief.

9. Rider CPP–Subsequent Review / Contingencies

As ComEd’s Initial Brief stated, the Commission is presented with four related issues relating to the review of charges, of the calculation of charges, and of accounting under Rider CPP: (1) general issues regarding the subject of additional (retrospective) “prudence review”; (2) Staff’s and ComEd’s joint proposal relating to review of Supply Charges and AAFs, which involves proposed language for the CPP Timeline section of the Competitive Procurement Process part of Rider CPP; (3) Staff’s and ComEd’s joint proposal relating to review in certain contingent scenarios, which involves proposed language for the Limitations and Contingencies part of Rider CPP; and (4) Staff’s revised (i.e., expanded) proposal for automatic annual docketed reconciliation proceedings under Rider CPP, Rider PPO-MVM, and Rider TS-CPP - Transmission Services (Competitive Procurement Process) (“Rider TS-CPP”). In accordance with the ALJ’s approved briefing outline, the first of those four subjects is addressed (primarily) in Section V.L.1 and 2 of ComEd’s Initial Brief and this Reply Brief. The other three subjects are discussed in Section VII.B.9 of ComEd’s Initial Brief and this Reply Brief.

a. Staff and Commission Review of Supply Charges for Accuracy and for Inclusion of Only Those Costs Authorized to Be Included by the Order in this Docket.

ComEd’s Initial Brief showed that the evidence supports Staff’s and ComEd’s stipulation, subject to Commission approval, that, in brief, would include express language in Rider CPP that permits Staff and Commission review of calculations of Supply Charges as well as AAFs for arithmetical accuracy and for whether ComEd has included only those costs authorized to be included by the Commission’s Order in this Docket, and permits the

Commission to order appropriate relief, including refunds. (ComEd Init. Br. at 157) Staff agrees. (Staff Init. Br. at 170-171) No intervenor addressed the proposal. It should be approved.

b. Reporting to Staff, and Staff and Commission Review of AAFs, in Certain Contingent Scenarios.

ComEd's Initial Brief showed that the evidence supports Staff's and ComEd's final revised agreement, subject to Commission approval, that, in brief, relates to certain contingent procurement scenarios, requires ComEd to provide reports to Staff, and provides for review, informally by Staff and, on the Commission's own motion or upon complaint, formally, of the prudence of actions and omissions of ComEd, if any, that caused it to procure full requirements electric supply under the Limitations and Contingencies part of Rider CPP, when not due to an under subscription or a volume reduction, and that provides for the Commission ordering appropriate relief, including refunds. (ComEd Init. Br. at 109, 157-159) Staff agrees. (Staff Init. Br. at 157-158)²⁶ No intervenor addressed this proposal, apart from the AG's inappropriate argument for more expansive review, discussed in Section V.K.4 of this Reply Brief. The proposal should be approved.

c. Staff's Proposal for Automatic Annual Docketed Reconciliation Proceedings.

ComEd's Initial Brief showed that the evidence does not support Staff's revised (expanded) proposal for automatic annual docketed reconciliation proceedings under Rider CPP, Rider PPO-MVM, and Rider TS-CPP. (ComEd Init. Br. at 159-163) Staff disagrees (Staff Init. Br. at 176-180), but the evidence shows that Staff's revised proposal is unwarranted and is unnecessarily burdensome and costly for ComEd, Staff, the Commission, and interested parties.

²⁶ Please note that Staff discussed this subject in Section VII.B.5 of its Initial Brief.

Staff originally proposed automatic annual docketed proceedings to reconcile full requirements electric supply costs with recoveries under Rider CPP. (Knepler Dir., Staff Ex. 10.0, 2:23-24, 6:127–9:200) The stated purposes were “[r]eviewing the cost mechanism on an annual basis to ensure that the Company’s process is effective” and “[c]orrecting omissions, errors, or misclassifications of cost[.]” (*Id.*, 7:130–132)²⁷ Staff, in rebuttal, adhered to that proposal and, with minimal explanation, proposed to expand it to Riders PPO-MVM and TS-CPP. (Knepler Reb., Staff Ex. 18.0, 2:25–27, 10:206–11:232, 14:290–309, 15:313–321)

As discussed in ComEd’s Initial Brief and earlier Sections of this Reply Brief, ComEd already has proposed or agreed to a host of tariff provisions, processes, reports, and other matters, including Commission review, that will ensure that both the Supply Charges under Rider CPP (and Rider PPO-MVM)²⁸ and the AAF charges/credits under Rider CPP are calculated accurately and that only properly “includable” costs are included within the charges, all of which will be transparent and auditable, including, among other things:

1. specifying in Rider CPP the costs and revenues that properly are included in the Supply Charges and the AAFs (*e.g.*, ComEd Init. Br. at 140-141, 145-146);
2. specifying in Rider CPP the details and the data sources of the “prisms” for calculating Supply Charges, and proposing compromises that implement Staff’s few proposals on the prisms (*e.g.*, *id.* at 140-144);

²⁷ As ComEd’s Initial Brief noted, the Staff witness who presented this proposal in direct testimony incorporated in it, at that time, a third purpose, i.e., review of the prudence of procurement in certain contingent scenarios, but that part of the proposal later was superseded by the separate Staff-ComEd agreement on that subject. (ComEd Init. Br. at 159, footnote 21) That agreement is discussed in the preceding subsection of this Reply Brief.

²⁸ Staff’s extension of its proposal to the Supply Charges under Rider PPO-MVM indisputably is redundant. The only difference between the Supply Charges calculated under Rider CPP and the Supply Charges incorporated from Rider CPP in Rider PPO-MVM is that the latter adds the supply-related uncollectibles adjustment, which Staff made clear should not be reconciled, showing CES’ proposal to track supply-related uncollectibles expenses through the AAF to be without merit. (ComEd Init. Br. at 149, 162 and footnote 22; Staff Init. Br. at 186-189)

3. proposing to take the needed steps, and to have the requisite internal controls in place, to ensure accurate and appropriate calculation of Supply Charges and AAFs, and agreeing to Staff's proposal for an interest component when an AAF is corrected, an added incentive for correct calculations (*e.g., id.* at 149, 151);
4. proposing to provide a monthly informational report to Staff regarding the calculation of the AAFs, and agreeing to work with Staff on the format and content of the report (*e.g., id.* at 147-148);
5. agreeing to file an annual report, verified by a ComEd officer, with Staff that summarizes the operation of the AAM part for the previous year (*e.g., id.* at 147);
6. agreeing to conduct an annual internal audit of costs and recoveries under Rider CPP and to file a copy of the report with Staff (*e.g., id.*);
7. proposing to maintain the records that impact the AAF calculations in sufficient detail that they will be readily auditable by Staff (*e.g., id.* at 152);
8. identifying which Accounts in the USoA will be used to record which components of the AAF calculations (*e.g., id.* at 148, 153);
9. identifying the general approach to the creation of sub-Accounts that ComEd will use in performing the AAF calculations, and agreeing to meet with Staff when the necessary information is available to create the sub-Accounts, in order to facilitate Staff's understanding and review of ComEd's decisions (*e.g., id.* at 152-153);
10. entering into the stipulation with Staff, subject to Commission approval, regarding Staff and Commission review of calculations of Supply Charges and AAFs for arithmetical accuracy and for whether ComEd included only the costs authorized to be included (*e.g., id.* at 157), discussed in Section VII.B.9.a of this Reply Brief;

11. entering into the agreement with Staff, subject to Commission approval, that, in brief, relates to certain contingent procurement scenarios, requires ComEd to provide reports to Staff regarding the reasons for such contingent procurement, and provides for Staff and Commission review (*e.g., id.* at 157-159), discussed in Section VII.B.9.b of this Reply Brief;
12. proposing to work with Staff to resolve any disputes or questions regarding AAF calculations on an efficient, informal basis (*e.g., id.* at 154-156); and
13. proposing that the Commission's final Order in this Docket formally direct Staff to (1) review the information supplied by ComEd annually; and (2) within six months issue a report to the Commission regarding Staff's findings, including a recommendation regarding the need for a formal investigation (*e.g., id.* at 160).

Thus, it could not be more clear that ComEd has proposed and agreed to multiple measures that fully address Staff's underlying concerns, and, as a result, that the only contested issue here, as to Rider CPP and Rider PPO-MVM, is whether, as ComEd proposes, the Commission should initiate reconciliation proceedings when needed, with that need determined, not by ComEd, but by the Commission; or, as Staff proposes, the Commission should automatically initiate annual docketed reconciliation proceedings regardless of need.

The evidence does not support conducting automatic annual docketed reconciliation proceedings. The evidence instead shows that such automatic proceedings are not warranted and would impose unnecessary burdens on customers and other stakeholders, ComEd, Staff, and the Commission. (ComEd Init. Br. at 159-163) None of Staff's eight arguments in its Initial Brief warrant its position.

Staff's first argument, that ComEd somehow has the ability to prevent Staff from requesting a reconciliation proceeding, is incorrect. Staff's assertion is wrong, as a matter of law and not supported by evidence in the record. Staff begins by correctly noting that ComEd's proposal that the Commission's final Order in this Docket formally direct Staff to (1) review the information supplied by ComEd annually; and (2) within six months issue a report to the Commission regarding Staff's findings, including a recommendation regarding the need, or lack thereof, for a formal Commission investigation. (Staff Init. Br. at 176-177) Staff then extrapolates from ComEd's proposal, with no citations, the following argument:

In other words, ComEd proposes to shift the burden to Staff. If the responses to Staff's inquiries provided were inadequate, then Staff would be forced to make additional inquiries and if ComEd could delay the matter for 6 months then the clock would run out and the matter would be closed.

(Staff Init. Br. at 177) The Commission has extensive legal authority to request information from a utility. *E.g.*, 200 ILCS 5/4-401. Moreover, ComEd submitted evidence that it is willing to work with Staff to make sure Staff gets the information it needs. (*E.g.*, ComEd Init. Br. at 147-148) In contrast, Staff cites no law or evidence that ComEd even could, much less would, thwart any Staff request for appropriate information. There is none. Even more importantly, Staff cites no law or evidence for the notion that, if ComEd did so, that Staff could not at any point in that six months file a report with the Commission, document the problem, and on that and/or any other appropriate basis ask the Commission to initiate an investigation. Staff, in rebuttal testimony, had the opportunity, but did not respond to ComEd's proposal for a Staff report. (Alongi / Crumrine Sur., ComEd Ex. 21.0, 23:528-24:537)

Staff's second argument is its assertion that the Procurement Working Group's goal of "transparency" supports Staff's proposal for automatic annual docketed reconciliation proceedings. (Staff Init. Br. at 177) That is incorrect. Staff does not and cannot claim that the

Procurement Working Group's report recommended such proceedings. (ComEd Ex. 1.4) Moreover, Staff overlooks the many items, listed above, that already ensure transparency.

Staff's third argument is to cite Ameren's agreement to automatic annual docketed reconciliation proceedings in ICC Docket No. 05-0160, *et al.* (Staff Init. Br. at 177-178) Staff does not discuss, much less provide evidence, however, regarding, whether Ameren proposed or agreed to all of the other items that ComEd proposed and accepted, listed above. In any event, Staff's citation is not evidence that such proceedings make sense given the facts here. (Alongi / Crumrine Sur., ComEd Ex. 21.0, 24:538-549)

Staff's fourth argument is its assertion that: "ComEd did not provide any studies or documentation to support its belief that its customers would be best served without an annual docketed proceeding to determine whether they were over charged or not." (Staff Init. Br. at 178) On the contrary, ComEd proposed and agreed to a host of measures that ensure the accuracy of the Supply Charges and AAFs, provide for transparency in their determination and Staff review, and also provide for a formal Commission investigation if needed, as shown above. Moreover, ComEd submitted evidence that the proposed automatic annual docketed proceedings would be unnecessary, overly litigious, and administratively burdensome on the Commission, ComEd, and other stakeholders. (Alongi / Crumrine Reb., ComEd Ex. 13.0, 38:821-39:827; Alongi / Crumrine Sur., ComEd Ex. 21.0, 24:544-547)

Staff's fifth argument is to contend that the absence of intervenor objection to ComEd's proposal, and the absence of intervenor support for Staff's proposal, does not mean that Staff's proposal should be rejected. (Staff Init. Br. at 178) The silence speaks for itself (i.e., intervenors have expressed no objection to ComEd's proposal and no support for Staff's proposal).

Staff's sixth argument is the assertion that ComEd's facing automatic annual docketed reconciliation proceedings "could have a positive impact on the accuracy of ComEd's calculations." (Staff Init. Br. at 178) Staff cites no evidence. There is none. ComEd has every intention and reason to accurately calculate the Supply Charges and AAFs, as shown above.

Staff's seventh argument is the proposition that it somehow is efficient to have automatic annual docketed reconciliation proceedings. (Staff Init. Br. at 178-179) With all of the reports and other information that, it is undisputed, will be available to Staff, and with Staff having the ability to obtain the additional appropriate information it needs, it is not reasonable to claim that it is efficient to reject an approach in which an investigation would be initiated only if there actually appears to be a reason to conduct one. Staff's complaint here, that the format and content of the annual reports has not been finalized and that the reports will or might be inadequate (Staff Init. Br. at 179), has no basis. The very evidence cited by Staff shows that ComEd has agreed to work with Staff on the format and content of the annual reports (*Id.* (citing Waden, Tr. 871); *see also* ComEd Init. Br. at 147-148) There is no contrary evidence. Staff does not and cannot cite any evidence that the annual reports inherently will be incomplete or deficient and Staff, again, ignores its ability to obtain more information. ComEd notes that its filing of its annual FERC Form 1 and its annual ICC Form 21, which set forth its costs and revenues, do not prompt automatic FERC or Commission proceedings to review the accuracy of those forms. (Crumrine, Tr. pp. 851-851)

Staff's eighth and final argument is its assertion that ComEd, when it had a fuel adjustment clause, participated in annual reconciliations under 83 Ill. Adm. Code Part 425, "without any apparent harm from this additional regulatory burden." (Staff Init. Br. at 179-180)

That assertion is supported by no evidence, and it overlooks that the 1997 amendments to the Act allowed ComEd to terminate that clause, 220 ILCS 5/9-220, which ComEd did.

The only other issue here is that Staff belatedly and with minimal explanation extended its proposal to Rider TS-CPP. ComEd provided evidence that explained, in detail, why the extension to Rider TS-CPP, which parallels a tariff that has been in effect for over two years and that is not claimed to have led to any problems despite the absence of reconciliations, is unwarranted and inappropriate. (ComEd Init. Br. at 162-163) There is no contrary evidence.

10. Alternative Proposals re Service to Self-Generation Customers

ComEd's Initial Brief showed, in detail, that the evidence does not support, and instead warrants rejection of, IIEC's recommendation that ComEd either: (1) charge self-generating customers on a dollars and cents per kilowatt-day basis (e.g., \$X.XX/kW-Day) or (2) create a new translation process for self-generating customers. (ComEd Init. Br. at 163-164) No other party submitted any evidence or argument in support of IIEC's position.

IIEC's Initial Brief contends or implies that 18 C.F.R. § 295.305(c) requires or supports its position or its alternative position (*see* IIEC Init. Br. at 6, 68), but it never explains or shows how ComEd's proposal, which in relevant part simply reflects PJM's rules (ComEd Init. Br. at 163; *e.g.*, Alongi / Crumrine Sur., ComEd Ex. 21.0, 16:336-358), is inconsistent with the cited legal provision. They appear to be entirely consistent.

IIEC emphasizes the ability of (some) self-generating customers to schedule generation maintenance during off-peak periods and the "low probability" of outages during system peaks or simultaneous with other self-generating customers' outages. (IIEC Init. Br. at 6, 68-70) As IIEC admits, however, under ComEd's proposal, which reflects PJM's rules, such customers' demands are determined based on five different peak days of the previous year, not a single peak.

(IIEC Init. Br. at 70-71; ComEd Init. Br. at 163-164) That is consistent with the costs those customers will cause ComEd to incur from wholesale suppliers. (Alongi / Crumrine Reb., ComEd Ex. 13.0, 28:600-607; Alongi / Crumrine Sur., ComEd Ex. 21.0, 16:339-345, 354-358) That also appears to be consistent with the legal provision IIEC cites.

IIEC claims that ComEd's proposal does not give self-generating customers the benefits of "group diversity". (IIEC Init. Br. at 71) What that means, however, is that IIEC is proposing to socialize the total capacity cost of self-generating customers amongst all self-generating customers, including forcing it on independent power producers, by allocating the aggregate capacity obligation for the group on a pro rata basis to each individual customer. (Alongi / Crumrine Sur., ComEd Ex. 21.0, 15:326–17:371). That is tantamount to a self-insurance scheme, one that such customers could voluntarily enter into, but which should not be imposed on them. (*Id.*) IIEC's proposal and alternative proposal should not be adopted.

11. Alternative Proposals re Interruptible Service (ALM and Non-ALM Demand Response)

In its Initial Brief, IIEC recommends that ComEd provide an active load management ("ALM") credit to the capacity billing units for hourly pricing customers who meet PJM ALM requirements. (IIEC Init. Br. at 71). IIEC proposes to do this by splitting supply procurement for CPP-H load into two segments – ALM and non-ALM supply. (IIEC Init. Br. at 73). As discussed in ComEd's Initial Brief, there is no need to adopt IIEC's proposal. Not only is IIEC's proposal unnecessary, but it would be very difficult to implement.

As William McNeil explained in surrebutal testimony, ComEd Rider CLR compensates customers participating in PJM active load management in full with a curtailable capacity credit, making the modification suggested by IIEC unnecessary. (McNeil, Tr. 594) The only

incremental value created by ALM load is on the capacity component, and ComEd's proposal compensates customers in full for that value (McNeil Sur., ComEd Ex. 18.0, 41:917-42:926)

IIEC's proposal would also be complicated to implement because ComEd would have to perform direct acquisition for individual customers for a portion of their hourly load at the same time it is providing CPP-H service for the other portion of the customers' load. (Alongi/Crumine Surr. ComEd. Ex. 21.0, 17:379-18:384). There is no need to introduce this complexity when Rider CLR already provides the full appropriate credit.

IIEC also argues that all 3 MW and over customers taking bundled service from ComEd should be given the opportunity to participate directly in the PJM emergency load response program and the economic response program. (IIEC Init. Br. at 76). IIEC's argument is moot and not relevant to this Docket because (1) the opportunity to participate in the PJM emergency load program is already provided to all non-residential customers through existing Rider VLR – Voluntary Load Response & System Reliability program (ILL. C.C. No. 4, 1st Revised Sheet No. 61.61 *et seq.*) – regardless of whether or not the customer is over 3 MW or receiving supply from a RES – and (2) over 3 MW customers subject to the competitive declaration are not eligible for a fixed-price full requirements product from ComEd and the IIEC has offered no evidence that RESs are not offering such customers the opportunity to participate in ComEd's PJM's economic response program.

C. Matters Concerning Proposed Rider PPO-MVM

1. Supply Charge

The Commission is presented with two issues relating to the Supply Charges in Rider PPO-MVM, but the positions taken in ComEd's Initial Brief now are uncontested. (ComEd Init. Br. at 163-164; *see also* Staff Init. Br. at 202-203)²⁹

2. Supply Administration Charge

The Commission is presented with two issues (one of which should not be addressed in this Docket) relating to the Supply Administration Charges in Rider PPO-MVM. First, ComEd and Staff have agreed on revised clarifying tariff language, that is supported by the evidence in the record, relating to the Supply Administration Charges in Rider PPO-MVM. (ComEd Init. Br. at 165; *see also* Staff Init. Br. at 190-191) No party disagrees, except to the extent that the second issue, discussed below, would affect that language. That language should be approved.

Second, CES and CUB-CCSAO made various general recommendations regarding how the Supply Administration Charges should be calculated and assessed, and CES has pursued this subject in its Initial Brief, although CUB-CCSAO has not done so. (ComEd Init. Br. at 165-166; CES Init. Br. at 41-45) ComEd has shown, however, and Staff agrees, that CES' (and CUB-CCSAO's) recommendations relating to the Supply Administration Charges are premature, and should not be approved, because the language regarding these charges in Rider PPO-MVM is placeholder language, the actual charges are to be determined in ComEd's rate case, which now is pending as ICC Docket No. 05-0597, and, thus, the issues sought to be raised by CES (and

²⁹ There are two other issues related to this subsection. CES' cursory proposal that supply-related uncollectibles expenses, which are an adjustment to the Supply Charges, should be tracked through the AAM part (CES Init. Br. at 47) is addressed in Section VII.B.8.a of this Reply Brief. CES' rather vague proposal that the Commission order ComEd to implement "an appropriate methodology for the proper allocation of uncollectible expenses" (CES Init. Br. at 47) is inappropriate in this Docket. The determination of that component of the Supply Charges should be

CUB-CCSAO) are appropriately dealt with in that Docket, not here. (ComEd Init. Br. at 166; Staff Init. Br. at 189)³⁰ CES admits that the Supply Administration Charge should be set in ICC Docket No. 05-0597, but CES argues, citing very cursory testimony, that the Commission nonetheless should determine the types of costs that should be included in the charge, and the allocation method, and the manner in which the charge will be set, in the instant Docket. (CES Init. Br. at 44-45) CES' superficial argument simply is unconvincing. There is no good reason to set the charges here or to make the determinations that CES seeks. There is not anything close to a sufficient evidentiary record to do so, and, in any event, the appropriate Docket for those issues is ICC Docket No. 05-0597. CES' request should not be approved.

3. Retention of a Market Index Tariff Such as Those Currently Effective or a Neutral Fact Finder Tariff, in Addition to the Auction-Based Determination of Market Value

ComEd's Initial Brief showed, in detail, that BOMA's proposal, that Rider PPO-MI should not be replaced by Rider PPO-MVM, and that ComEd should be required to continue to offer Rider PPO-MI or an equivalent rider based on the "neutral fact finder" ("NFF") methodology, is not supported by, but rather is contrary to, the evidence in the record. (ComEd Init. Br. at 166-167)³¹ BOMA's witnesses were uncertain on key aspects of the proposal and alternative and admitted lacking knowledge of the specifics of why the Commission rejected the NFF methodology in favor of the market index approach. (Childress / Brookover, Tr. 894-895)

addressed in ICC Docket No. 05-0597, ComEd's pending rate case, where the adjustment will be determined. (E.g., Alongi / Crumrine Reb., ComEd Ex. 13.0, lines 1332-1324)

³⁰ Please see also Section VII.D.7 of this Reply Brief.

³¹ ComEd, in Section VII.C.3 of its Initial Brief, focused on the factual aspects of BOMA's proposal. ComEd addressed the relevant statutory provisions in a number of Sections of its Initial Brief, primarily Section III.B.3. Similarly, ComEd is addressing the relevant statutory provisions in a number of Sections of its Reply Brief, primarily Section III.B.3.

Staff presented an even lengthier argument, showing that Sections 16-111(i) and 16-112 of the Act, 220 ILCS 5/16-111(i) and 16-112, do not support BOMA's proposal, and that the evidence proves that the proposal is unnecessary and is "fraught with problems and additional unnecessary costs." (Staff Init. Br. at 192-195; *see also, e.g.*, ComEd Init. Br. at 14-15)

BOMA's Initial Brief argues for its proposal and alternative, but it focuses entirely on legal issues, ignoring the extensive evidence showing its proposal and alternative are unwarranted and undesirable on their merits. (BOMA Init. Br. at 3, 22-24) No other party submitted evidence or argument in support of BOMA's approach. BOMA's proposal and alternative are unjustified and harmful, contrary to the evidence, and should not be approved.

D. Other Matters

1. Staff's Rate Increase Mitigation Proposal

ComEd's Initial Brief showed that the evidence supports Staff's mitigation proposal, which relates to the CPP-B auction segment, as that proposal has been clarified and revised in rebuttal testimony. (ComEd Init. Br. at 167-169) Staff's Initial Brief also shows that the evidence supports the proposal as clarified and revised. (Staff Init. Br. at 196-201)

CECG opposed Staff's mitigation proposal on two grounds, that the proposal could add migration risk uncertainty and, as a result, lead to higher auction prices, and that it is unneeded because the Illinois auction proposal sends the proper price signal. (CECG Init. Br. at 19-20)

Dynegy did not support or oppose Staff's mitigation proposal, but Dynegy did observe that the Commission, in making its decision here, should consider the possibility that the proposal could lead to higher prices by adding migration risk. (Dynegy Init. Br. at 22-23)

Finally, BOMA's Initial Brief argues for its rate increase mitigation proposal relating to Rider 25 -- non-residential space heating -- customers, which would supersede Staff's proposal

as to such customers, and also argues, in the alternative, that if the Commission were to adopt Staff's mitigation proposal, then it should order ComEd to add a separate sub-group for Rider 25 customers in the proposal. (BOMA Init. Br. at 20-21, 21-22) BOMA's proposal and alternative are without merit, as is discussed in Section VII.D.3 of this Reply Brief.

Staff's mitigation proposal, as revised and clarified, is supported by the evidence in the record, is just and reasonable, and should be approved. ComEd recognizes the concerns raised by CECG and Dynegy, but believes that the better balance is in favor of Staff's proposal.

2. Elimination of Rider ISS

ComEd's Initial Brief shows that the Commission should reject BOMA's request that the Commission order ComEd to continue to offer service under Rider ISS-Interim Supply Service ("Rider ISS") as a separate service after the end of the transition period. (ComEd Init. Br. at 169-170) ComEd showed that the Commission lacks the authority to require ComEd to continue to offer Rider ISS, a voluntary service, as a separately priced service in the post-transition period, 220 ILCS 5/16-103(e), that BOMA's proposal is beyond the scope of this Docket, and that, in any event, it is without merit and inappropriate. (ComEd Init. Br. at 169-170)

BOMA's Initial Brief pursues its proposal in a cursory manner, ignoring the legal issue, ignoring the point that the issue is beyond the scope of this Docket, and focusing on the claim that Rider ISS has contributed to the development of a competitive retail market. (*See* BOMA Init. Br. at 21) No other party submitted evidence or argument in support of BOMA's proposal.

BOMA's position is confused. ComEd is not stating that there will be no "default" service, rather, for all eligible customers the bundled electric service tariffs will serve as "default" service. (ComEd Init. Br. at 170) ComEd opposes, however, the request that it be required to continue to offer Rider ISS as a separately priced service. ComEd is unwilling to

offer this voluntary service as a separately priced service. (*Id.* at 169-170) There is no basis in the law or the evidence for such a requirement. BOMA's proposal should be rejected.

3. Non-Residential Electric Space Heating Customers

ComEd's Initial Brief showed that the evidence does not support, and instead warrants rejection, of BOMA's proposal for rate mitigation relating to Rider 25 customers, under which they would be exempted from distribution facilities charges in ComEd's delivery services tariffs, i.e., receive free delivery service for eight out of twelve months, and of BOMA's alternative proposal that Rider 25 customers be treated as a separate subgroup in Staff's mitigation proposal, discussed in Section VII.D.1 of this Reply Brief. (ComEd Init. Br. at 170-171) ComEd showed that BOMA's proposal, especially in terms of the requested relief, which involves amending delivery services tariffs not before the Commission here, is beyond the scope of this Docket, and, in any event, it is without merit and inappropriate, for several reasons, based on testimony of ComEd's witnesses and on that of Staff's mitigation witness. (*Id.*) ComEd also cited evidence that BOMA's alternative proposal is without merit from those witnesses. (*Id.* at 171)

BOMA's Initial Brief advocates its proposal and alternative. (BOMA Init. Br. at 21-22) No other party submitted evidence or argument regarding BOMA's position, except for Dynegy, which did not support or oppose the proposal or its alternative. (Dynegy Init. Br. at 23)

BOMA's proposal and its alternative remain without merit because:

1. it is inappropriate to deal with supply-related rate impacts by adjusting the delivery rates for any customer or group of customers, a point that is reflected in Staff's mitigation proposal (Alongi / Crumrine Reb., ComEd Ex. 13.0, 56:1241-1244; *see also* Lazare, Tr. 1232-1234);

2. Rider 25 was created under the previous vertically integrated utility structure and was designed based on facts that are no longer relevant, as is reflected in the fact that BOMA, in its rebuttal testimony (and its Initial Brief) appears to have abandoned the argument that its proposal is cost-based (Alongi / Crumrine Reb., ComEd Ex. 13.0, 57:1252-1259; Alongi / Crumrine Sur., ComEd Ex. 21.0, 56:1225-1232; Crumrine, Tr. 744-745);
3. exempting customers from a distribution facilities charge would send an inaccurate price signal regarding the cost of distribution capacity (Alongi / Crumrine Reb., ComEd Ex. 13.0, 57:1260-58:1268; *see* also Crumrine, Tr. 764 (BOMA's witnesses acknowledged that they were not knowledgeable regarding ComEd's distribution planning criteria)); and
4. Rider 25 customers are not customers under a single rate but rather under multiple rates, and giving them special treatment within Staff's mitigation proposal is not justified. (Alongi / Crumrine Sur., ComEd Ex. 21.0, 45:1047-46:1059; Crumrine, Tr., 746-747, 753-755; *see* also Lazare, Tr. 1238-1239)

BOMA's proposal and alternative are not supported by the evidence and should not be adopted.

4. DASR Procedures in Anticipation of Serving New Customer Facilities

ComEd's Initial Brief stated that the Commission did not appear to be presented with any open issue on this subject, because ComEd, in light of concerns raised by CES, committed to fully specifying its proposal for how a RES could "DASR" a new customer in ICC Docket No. 05-0597, its pending rate case. (ComEd Init. Br. at 172) CES now requests that the Commission order ComEd to provide those DASR procedures in writing in the instant Docket.

(CES Init. Br. at 45-46) CES' request is inappropriate in this Docket and is supported by the evidence. CES' request should not be approved.

5. Recategorizing Certain Condominium Customers as Non-Residential Customers

ComEd's Initial Brief stated that the Commission should approve CES' proposal to recategorize certain condominium customers as non-residential for purposes of the Customer Supply Group definitions in Rider CPP. (ComEd Init. Br. at 172) CES now urges the Commission to order ComEd to "formally recognize that the common areas of condominium buildings are to be re-categorized under a commercial rather than a residential classification." (CES Init. Br. at 46) What CES actually is seeking is somewhat unclear, but it appears that CES now wishes ComEd to provide the "methodology" by which it will effectuate the recategorization, to be "formally recognized" in this Docket and then implemented in ICC Docket No. 05-0597, its pending rate case. (*Id.*) That request is untimely, and ComEd does not see how it can submit a proposed "methodology" on this subject at this point here. At most, the Order should reflect that ComEd has agreed to CES' proposal and has agreed to effectuate it in ICC Docket No. 05-0597. Any "methodological" issue should be resolved in that Docket.

6. Treatment of Uncollectibles

Please *see* Section VII.B.8.a (relating in part to supply-related uncollectibles expenses and the AAM part of Rider CPP) and Section VII.C.1 (relating in part to the supply-related uncollectibles adjustment to Supply Charges) of this Reply Brief.

7. Credit Risk and Other Administrative Costs

ComEd's Initial Brief showed that the Commission should not approve CES' proposal that ComEd recover certain additional costs from customers through some charge for specific credit costs and other administrative costs in relation to CPP-H service, because CES' proposal

in effect is another premature attempt to address in this Docket what costs should go into the CPP-H Supply Administration Charges, akin to those discussed in Section VII.C.2 of this Reply Brief, and the proposal is not justified, in any event. (ComEd Init. Br. at 172-173)

CES' Initial Brief discusses this subject (CES Init. Br. at 48-50), but that discussion alters neither the fact that CES' proposal is premature and inappropriate in this Docket, nor that the evidence in the record simply does not support the determinations that CES wishes to be made here. (ComEd Init. Br. at 172-173) CES' proposal should not be adopted.

8. Integrated Distribution Company Issues

ComEd's Initial Brief showed that the evidence does not support CES' proposal for a separate formal proceeding for the consideration of any new ComEd communication materials related to the procurement process, which is based on the grounds that ComEd is an Integrated Distribution Company ("IDC"). (ComEd Init. Br. at 173)

CES pushes this issue (CES Init. Br. at 50-52), but CES does not and cannot cite any experience in the over three years since ComEd became an IDC that warrants such a proceeding. ComEd is aware of, and complies with, its obligations as an IDC. (ComEd Init. Br. at 173)

The evidence also shows that a formal Commission proceeding to evaluate, and litigate, ComEd's communications with its customers would be burdensome and unworkable. (ComEd Init. Br. at 173) The fact that some parties might challenge education materials as "advertising" (*see* CES Init. Br. at 51) (citing Crumrine, Tr. 797) does not alter the fact that ComEd has the obligation to communicate with its customers about its rates. (Crumrine, Tr. 793-794) Nor is it an indication that the requested proceeding would be an efficient use of the parties' and the Commission's resources. No other party has supported CES' proposal in testimony or argument.

CES has not made the case for requiring other stakeholders, ComEd, Staff, and the Commission to undertake the burdens and costs of such a Docket. CES' proposal should not be approved.

VIII. CONCLUSIONS AND MIXED LEGAL / FACTUAL ISSUES

A. Legality of Rider CPP

For the reasons discussed in Section III of its Initial Brief and this Reply Brief, ComEd submits that the Commission has authority to approve Rider CPP and that the evidence shows that Rider CPP complies with all applicable legal requirements.

B. Legality of Rider PPO-MVM

BOMA argues that ComEd's Rider PPO-MVM does not implement properly the PPO required under Sections 16-110(c) and 16-112(a) of the 1997 Restructuring Law (BOMA Init. Br. at 22). It attempts to support this argument by arguing that the Supplier Forward Contracts (SFCs), which require suppliers to deliver a vertical slice of ComEd's full requirements for electricity supply, will be for an indefinite quantity and therefore cannot be traded on any exchange or market in which futures contracts are traded. (BOMA Init. Br. at 23) BOMA also claims that the price determined by an auction is not an exchange-traded or other market-traded index. (BOMA Init. Br. at 23) BOMA relies on Dr. Laffer's testimony to support its arguments, but Dr. Laffer offers nothing to support his opinions. He has no familiarity with the market in which ComEd sells and the customers in its service area buy electric power and energy and no experience with futures contracts.

"Market value" is defined in Section 16-112. That provision establishes that the Commission may determine "market value" pursuant to a "tariff that ... provides for a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the

market in which the utility sells, and the customers in its service area buy, electric power and energy.” 220 ILCS 5/16-112(a) (emphasis added). The tariffs for the competitive auction process proposed by ComEd fit squarely within the criteria for establishing the “market value” for electric power and energy under Section 16-112(a).³²

As stated above, Dr. Laffer’s opinions are not based on an understanding of electricity markets, electricity contracts or the history of the determination of market value in Illinois. Section 16-112 of the Act sets forth a broad array of methods to determine market value, including but not limited to, methods based on “futures contracts”. The SFCs and the products and prices they represent are within the market-value determination methods permitted by Section 16-112. The Commission has also interpreted Section 16-112 in prior proceedings to recognize that market value can be determined as proposed in Rider PPO-MVM.³³ As Ms. Juracek pointed out in her testimony: the auction constitutes a competitive market; the SFCs are standardized contracts that provide for the procurement of market-traded products for future delivery; the auction will result in a published index for electricity applicable to ComEd’s service territory; the SFCs are contracts that are directly related to the market in which ComEd sells, and its customers buy, electric power and energy; and the SFCs allow for assignment thereby permitting a secondary market to develop opening the opportunity for the SFCs to trade in that market (Juracek Reb., ComEd Ex. 9.0, 51:1209-1215; ComEd Ex. 3.1, § 15.3)

³² An auction by definition constitutes a “market.” An “auction market” is “[a]n organized market in which prices adjust continuously in respect to shifts in supply and demand” and can be considered “the text-book model for competitive supply.” MIT Dictionary of Modern Economics, at 20 (4th ed. 1992). The contracts resulting from the auction constitute “index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy.” 220 ILCS 5/16-112(a). These contracts are directly “applicable” to the utility’s retail market within the meaning of the statute: Under the tariff, the utility’s actual bundled retail electricity load obligation is divided into discrete segments, and the lowest bidder for a given segment is selected for the contract. Rider CPP at Sheet Nos. 250-54, 257.

³³ See, In re Commonwealth Edison Co., 2001 Ill. PUC Lexis 419, at *418 (Ill. Commerce Comm’n Apr, 11, 2001.)

The procurement method embodied in Rider CPP – an auction for the resources required to provide the very product to be used by retail customers -- produces a direct and precise assessment of market value, as called for by the 1997 Restructuring Law. Moreover, it would be illogical for the Legislature to prohibit the most objective, fair and straight forward determinant of market value — a competitive auction that results in an index price for the very product being valued. Moreover, Staff is in agreement. Staff witness Zuraski testified that a Commission approved auction provides the “market value” called for in Section 16-112 of the Act because the auction would produce contracts applicable to the market “in which the utility sells, and the customers in its service area buy, electric power and energy” (Zuraski Dir., Staff Ex. 3.0, 6:160-161)

C. Issues Concerning Compliance of Auction Process Details with Illinois Law

As reflected in the evidence in this case, and as described in ComEd’s Initial Brief, the auction process fully complies with Illinois law.

CCSAO’s claims that there may be provisions of Illinois law that are inconsistent with the Illinois Auction Proposal or with which the Commission will be unable to comply are illusory. A review of each of the provisions identified by CCSAO demonstrates that there is no such inconsistency. The Illinois Auction will be conducted in accordance with Illinois law, and the Commission will comply with all legal requirements.

1. Illinois Open Meetings Act

The Open Meetings Act requires that “[a]ll meetings of public bodies shall be open to the public unless excepted in subsection (c) and closed in accordance with Section 2a.” 5 ILCS 120/2(a). A “meeting” is defined as “any gathering of a majority of a quorum of the members of a public body held for the purpose of discussing public business.” 5 ILCS 120/1.02.

There is nothing in the Open Meetings Act that is inconsistent with the Illinois Auction process and there is no reason to assume that the Commission will fail to comply with the requirements of that act. The auction is conducted by an independent auction manager in accordance with a process specified in a tariff approved by the Commission. The Commission does not conduct the auction. To the extent that the Commission holds any meetings to take any action with respect to the auction or the results of the auction, it will comply with the provisions of the Open Meetings Act.

2. The Illinois Ethics Law

The Illinois Ethics Law defines an ex parte communication as:

any written or oral communication by any person that imparts or requests material information or makes a material argument regarding potential action concerning regulatory, quasi-adjudicatory, investment, or licensing matters pending before or under consideration by the agency.

5 ILCS 430/5-50 (b) (emphasis added)

The Illinois Auction is run by an independent auction manager in accordance with a process specified in a tariff approved by the Commission. The auction is not a matter “pending before or under consideration by” the Commission. In the event that any matters relating to the auction or its results do become the subject of a regulatory, quasi-adjudicatory, investment, or licensing matter pending before or under consideration by the Commission, the agency will comply with the requirements of the Illinois Ethics Law.

3. Regulation of Public Records

The regulation of public records provision, 220 ILCS 5/10-101, appears under Article X of the Public Utilities Act entitled: Proceedings Before the Commission and the Courts. Section 10-101 itself begins:

The Commission, or any commissioner or hearing examiner designated by the Commission, shall have power to hold investigations, inquiries and hearings concerning any matters covered by the provisions of this Act, or by any other Acts relating to public utilities subject to such rules and regulations as the Commission may establish. ... Complaint cases initiated pursuant to any Section of this Act, investigative proceedings and ratemaking cases shall be considered “contested cases” as defined in Section 1-30 of the Illinois Administrative Procedure Act (5 ILCS 100/1-30).

220 ILCS 5/10-101

The language of 220 ILCS 5/10-101 applies to “investigations, inquiries, and hearings.” In other words, it applies to “contested cases” or other formal proceedings before the Commission.

As previously explained, the auction process is managed by an independent auction manager. It is not an investigation, inquiry or hearing before the Commission. In the event that any matters relating to the auction or its results do become the subject of an investigation, inquiry or hearing, the Commission will comply with the regulation of public records provisions of the law.

4. Ex Parte Communications

The Public Utilities Act states in part that “[t]he provisions of Section 10-60 of the Illinois Administrative Procedure Act shall apply in full to Commission proceedings.” 220 ILCS 5/10-103. The Illinois Administrative Procedures Act is limited to contested cases before the Commission. The relevant portion of the statute states:

Except in the disposition of matters that agencies are authorized by law to entertain or dispose of on an ex parte basis, agency heads, agency employees, and administrative law judges shall not, after notice of hearing in a contested case or licensing to which the procedures of a contested case apply under this Act, communicate directly or indirectly, in connection with any issue of fact, with any person or party, or in connection with any other issue with any party or the representative of any party, except upon notice an opportunity for all parties to participate.

5 ILCS 100/10-60 (a) (emphasis added)

The Illinois Auction is not a “contested case” under the Illinois Administrative Procedures Act. “Contested case” is defined as follows:

“Contested case” means an adjudicatory proceeding (not including ratemaking, rulemaking, or quasi-legislative, informational, or similar proceedings) in which the individual legal rights, duties, or privileges of a party are required by law to be determined by an agency only after an opportunity for a hearing.

5 ILCS 100/1-30

The Public Utilities Act expands the definition of “contested case” to include investigative proceedings and rate cases (*see* 220 ILCS 5/10-101). However, the Illinois Auction is not an investigative proceeding or a rate case. In the event that any matters relating to the auction or its results do become the subject of an investigative proceeding or a rate case, the Commission will comply with the requirements of 220 ILCS 10-103.

5. Decisions of the ICC Being Based on Record Evidence

CCSAO also raised the concern that, in “proceedings, investigations or hearings conducted by the Commission,” decisions are required to be made on record evidence as defined in 220 ILCS 5/10-103. The Illinois Auction is not a proceeding, investigation or hearing conducted by the Commission. In the event that any matters relating to the auction or its results do become the subject of a proceeding, investigation or hearing conducted by the Commission, the Commission will comply with the record evidence requirement.

IX. OTHER ISSUES

A. Renewable Energy and Energy Efficiency Issues (Not Already Addressed Above)

The record demonstrates that the Illinois Auction proposal is sufficiently flexible to permit incorporation of renewable resource requirements, and thus meets the eighth consensus

attribute identified in the Commission's Post-2006 Initiative. (McNeil Dir., ComEd Ex. 3.0, 14:299–307.) In addition, the Commission recently adopted a policy that encouraged public utilities to make greater use of renewable and energy efficiency resources voluntarily, which makes a Commission decision regarding the purchase of such resources unnecessary in this proceeding. CCSAO's recommendation to make renewable and energy efficiency purchases specifically through the auction should be rejected.

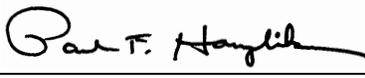
B. Additional Other Issues

CUB's supposition that testimony from ComEd and Exelon employees who hold stock of Exelon might be not be objective because of potential Exelon auction profits is unfounded. The Commission has long considered the testimony of both utility employee witnesses and witnesses for intervening parties that may have both direct and indirect financial stakes in entities that employ them or retain them, or interests in the policies that they believe in. The Commission evaluates that testimony on the merits, based on the particular witnesses' credibility, the nature of their interest, and the nature of their testimony. Just as ComEd witnesses may theoretically increase the value of stock options, experts retained by all parties may theoretically benefit financially if the policies they advocate are adopted and/or if their own stature as a testifying witness grows. However, the Commission does not dismiss credible, qualified expert testimony on that basis. Rather, the evidence is weighed based both upon its content and the witnesses' demeanor. Here, absolutely nothing in this record or in the witnesses' demeanor, in general and concerning the option, in particular, suggest that their testimony is anything but objective, or should be discounted. Nor has CUB provided any evidence whatsoever that any of these witnesses did or could have biased his or her testimony.

DES-USESC's proposal to alter the hourly default rate, advocating a monthly auction of customers with an annual peak demand over 1 MW and a quarterly auction for customers with an annual peak demand greater than 15,000 kWh but under 1 MW, is unwarranted and, contrary to claims, would not be in the best interest of consumers. Particulars of the proposal are discussed in Section V.

Respectfully submitted,

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