

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY :
:
Proposed general revision of rates, restructuring and : No. 05-0597
price unbundling of bundled service rates, and :
revision of other terms and conditions of service :

COMMONWEALTH EDISON COMPANY'S
INITIAL POST-HEARING BRIEF

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COMMONWEALTH EDISON COMPANY'S
INITIAL POST-HEARING BRIEF

Commonwealth Edison Company (“ComEd”) hereby submits its Initial Post-Hearing Brief to the Illinois Commerce Commission (the “Commission” or “ICC”). Section I is an executive summary of the key issues. It explains why ComEd’s proposed revenue requirement and basic rate structure are just and reasonable and should be adopted. Sections II through VII address in detail, with specific citations to the record, each issue in the common issue outline. Section VIII and Appendix A numerically summarize the revenue requirement. Section IX and Appendix B define acronyms and terms used during the proceeding.

I. INTRODUCTION

In the decade since passage of the 1997 “Restructuring Law,”¹ ComEd’s bundled rates have been frozen without regard to its costs or its investments. For non-residential customers, ComEd’s rates have been frozen at 1995 levels; for residential customers rates were reduced 20% below 1995 levels.

The result of the rate freeze is that customers have saved billions. It also means that while ComEd’s costs have increased dramatically, its rates have not. Since 1995, the overall cost of goods and services has risen by some 27%, and the price of many items has risen even more.

¹ The 1997 amendments to the Illinois Public Utilities Act, 220 ILCS 5/1 *et. seq.* (the “Act”), and the subsequent amendments thereto, are collectively referred to as the “Restructuring Law”.

But, ComEd's residential customers pay far less today for their electric service than they did ten years ago, and less than customers in comparable metropolitan areas. The average residential electric rates in the ten largest U.S. cities are approximately 30% higher than ComEd's current residential rate of approximately 8.6 cents per kilowatt hour, the second lowest among that group.² Residential customers in the Los Angeles area and San Francisco, for example, pay 12.9 cents per kilowatt hour. In the New York City area, the rate is well over 20 cents per kilowatt hour. Even the national average residential rate, which includes many lower-cost non-metropolitan areas, is well above ComEd's residential rate.

ComEd has, at the same time, dramatically improved its reliability of service. Outages are down 44% since 1998. More than 1.3 million of ComEd's 3.7 million customers experienced no outages in 2005. An additional 1.1 million customers had only a single outage. And, when outages do occur, ComEd restores power in less than half the time that it took in 1998.

These accomplishments are the direct result of massive expenditures ComEd undertook to enhance reliability of its distribution service, strengthen its distribution facilities and customer service systems, and add capacity to serve both new customers and growing demands of existing customers. Ten major new substations have been constructed. New control and communication technology has been added. New data management, dispatch, customer service and response, and outage management systems are in place. And, countless circuits, transformers, and other facilities have been upgraded. Since 2001 alone, ComEd has invested more than \$3 billion enhancing and reinforcing its distribution systems.³

² See generally Landon Dir., ComEd Ex. 2.0 Corr., 15:315—37:508 (comprehensively comparing ComEd's rates to inflation, costs of other services, and peer group rates). ComEd intends to cite the final admitted version of written testimony and other exhibits. All cites should be so interpreted. The final versions of ComEd's exhibits are listed in the most recent version of its Exhibit List.

³ A number of the projects included in ComEd's new plant investment are depicted in the digital video included in the record as ComEd Ex. 4.1.

During the transition, ComEd could not recover the added costs of those new investments from the vast majority of customers remaining on frozen and reduced bundled rates. Nor could it recover its increased operating costs. ComEd's request for a rate increase is, therefore, neither extraordinary nor unreasonable; it is necessary and reflects the increases in ComEd's actual, reasonable, and prudent costs. For ComEd to continue to provide reliable electric service, and as required under state and federal law, ComEd's new rates must allow it to recover these costs.

The Restructuring Law recognizes that, after the transition period ends on January 1, 2007, Illinois utilities must be permitted to charge rates that reflect their actual costs of service in the restructured environment. A ten-year rate freeze during which utilities spent billions without adjustment of most customers' rates to recover the costs incurred is a marked departure from the normal regulatory process. Had there never been a Restructuring Law, a rate freeze, or a residential rate cut of 20%, there would have been several general rate cases over the last ten years, and ComEd's added investments and increased costs would have resulted in periodic rate increases. But, by design, the Restructuring Law departed from that incremental approach, opting instead to maintain artificially low rates for a lengthy transition period. The consequence of that approach is that after the transition period, establishing rates that again cover the full costs of service will require a one-time adjustment larger than would have occurred during any individual rate case.

The need for reliable distribution service requires that rate adjustment. As John Costello, ComEd's Executive Vice President and Chief Operating Officer and the executive responsible for its operations testified:

... ComEd is clearly doing more – and thus spending more – to meet customers' needs. ... [N]o critical inquiry into ComEd's activities suggests that we should do less, that we should cut back our activities or our service to our customers. If

anything ... there is more work to be done, which will result in even more expenditures.

Costello Rebuttal (“Reb.”), ComEd Ex. 13.0 Corr., 41:918-22.

The Costs of Providing Safe, Adequate, and Reliable Service

ComEd presented compelling evidence that established ComEd’s costs of providing safe, adequate, and reliable delivery service.⁴ Delivering electricity to more than three million customers is capital-intensive. It requires enormous investments in distribution plant, such as substations, transformers, overhead and underground wires, poles, and manholes. It also requires “general” investments in office buildings, automated communications equipment that reduces the frequency and duration of outages, vehicles employees use to read meters or install and repair equipment, and the like. It also requires significant investment in “intangible” capital such as computer systems that manage work, provide customer information, and handle customer accounts and billing. The necessary capital ComEd has invested to provide delivery service, appropriately adjusted, totals nearly \$6.2 billion.

ComEd recovers this capital investment through a “return of and on” ComEd’s “rate base.” The “rate base” is the nearly \$6.2 billion in capital investments used to serve customers. The “return on” is based on a weighted average of ComEd’s overall cost of debt and equity. ComEd’s capital structure, after removal of the accounting effect of the “purchase accounting”

⁴ The Act defines delivery services are “those services provided by the electric utility that are necessary in order for the transmission and distribution systems to function so that retail customers located in the electric utility’s service area can receive electric power and energy from suppliers other than the electric utility” 220 ILCS 5/16-102. The Act, per federal law, also provides that: “An electric utility shall provide the components of delivery services that are subject to the jurisdiction of the Federal Energy Regulatory Commission (“FERC”) at the same prices, terms and conditions set forth in its applicable tariff as approved or allowed into effect by that Commission.” 220 ILCS 5/16-108(a). ComEd’s transmission costs and rates have been determined by FERC. Moreover, the means of determining ComEd’s costs of procuring electricity in the post-transition period were established by the Commission in *Commonwealth Edison Co.*, ICC Docket 05-0159 (Order Jan. 24, 2006) (the “Procurement Case”). This case thus focuses on ComEd’s “distribution” (including the customer function) costs and resulting distribution charges in both ComEd’s bundled rates (paid by customers purchasing delivery and electricity together from ComEd) and unbundled rates (paid by customers purchasing electricity separately, including from a competitor).

required by the October 2000 merger of ComEd with PECO Energy Company (described in Section III.E.1, *infra*), is comprised of 45.8% debt having an annual cost of 6.5%, and 54.2% equity with a cost of 11%. The weighted average cost of capital (and therefore ComEd's appropriate return on its rate base) is 8.94% (45.8% x 6.5% plus 54.2% x 11% equals 8.94%). ComEd's total cost of capital is the product of its \$6.2 billion rate base and the 8.94% rate of return, or approximately \$552 million. The effects of income taxes (including deferred taxes) adds an additional \$241 million of expenses.

In addition to recovering its capital investments, ComEd must pay for the expenses of the operation and maintenance of its distribution facilities, restoration of service after storms, billing and collection of customer accounts, providing service and information to customers, employee compensation including pensions and benefits, office supplies and services, accounting fees and many other items. It also pays taxes (other than income taxes) and incurs depreciation costs. ComEd's operating expenses are about \$1.165 billion.

The total cost of delivering electricity to ComEd's retail customers is the sum of the approximately \$552 million of capital costs, the \$241 million of income tax expenses, and the \$1.165 billion of annual operating expenses. After subtracting miscellaneous revenues of about \$95 million, approximately \$1.862 billion in distribution-related costs must be recovered through Illinois rates. This \$1.862 billion "revenue requirement" must then be allocated among customer classes and broken down into individual charges, taking into account the differences in the costs of delivering electricity to different types of customers and other appropriate "rate design" considerations. ComEd's tariffs reflect individual rates and charges that allocate these costs and provide for recovery of the total \$1.862 billion annual cost of service.

Other parties, however, seek to artificially reduce ComEd's revenue requirement far below its actual cost of providing service. The Citizens Utility Board ("CUB"), the Cook County State's Attorney's Office ("CCSAO"), and the City of Chicago (the "City") (together "CCC") propose a revenue requirement of about \$1.621 billion, nearly \$250 million less than ComEd's actual costs. The Staff's proposal would result in recovery of only about \$1.508 billion, or about \$360 million less than ComEd's actual costs. The Illinois Attorney General's Office (the "AG") proposes a revenue requirement of about \$1.447 billion, nearly \$420 million lower than ComEd's actual costs. Indeed, both the AG and Staff propose that ComEd actually recover less than the revenues allowed by the Commission in Docket 01-0423 — revenues based on service to fewer customers and now six-year-old costs.

There is no dispute that the enormous investments ComEd has made to serve customers were prudent, are reasonable in amount, and are being used to provide service. ComEd has managed its business efficiently. Costs have been controlled, and productivity enhanced. The resulting revenue requirement of \$1.862 billion is just and reasonable and reflects ComEd's numerous efforts to achieve operational economies while ensuring reliable service for customers. There is no room to cut \$250 million to \$400 million from the revenue requirement, as some propose. The Commission cannot blink away the reality of these costs. As Mr. Costello testified:

... just as our activities are real, so are their costs. If we are to accomplish those real activities, then ComEd's rates must be based on their real costs, not on some manipulated hypothetical construct In contrast, starving ComEd of the money it needs would take away its tools for achieving these goals.

Costello Reb., ComEd Ex. 13.0 Corr. 41:925-28.

Six key flaws account for the lion's share of the shortfall in these proposed revenue requirements. They: (1) use inaccurate and unfair capital structures to determine ComEd's

allowed cost of capital; (2) ignore the need to recover a reasonable return on the shareholders' \$803 million contribution to fund the pensions of ComEd employees; (3) ignore arbitrarily much of the general and intangible investments that support ComEd's delivery of electricity; (4) cap arbitrarily ComEd's Administrative and General Expenses; (5) disallow costs of incentive compensation plans that concretely and undeniably benefit customers; and (6) reduce arbitrarily other distribution operation and maintenance ("O&M") expenses essential to reliable service.

Throughout this proceeding, ComEd approached the testimony and proposals of Staff and Intervenors with an open mind, seeking to reach common ground wherever justly possible. As a result, ComEd voluntarily reduced its proposed revenue requirement by about \$28 million to the \$1.862 billion now recommended. But wishful thinking cannot be substituted for ComEd's real costs. To do so would shortchange the wages, benefits, and retirement of ComEd's employees, and jeopardize ComEd's ability to provide reliable service to its customers. Mr. Costello explained:

If we are to accomplish the necessary work, if we are to continue to provide more reliable and efficient service, it is essential that ComEd receive rates that cover the costs we incur in providing that service. ...

Failing to provide ComEd with rates that cover its costs is in no one's interest. Most important to me, it is not in our customers' interest.

Id. at 41:923-25, 935-36. In each of six key areas, the proposal to reduce ComEd's rates would prevent recovery of actual costs and, ultimately, hurt customers.

Capital Structure. ComEd's total cost of capital is based on its cost of debt and equity, in the same ratio as they occur in ComEd's capital structure. There is no disagreement about ComEd's \$4.341 billion actual debt balance; the dispute concerns ComEd's common equity balance. Staff, CCC, the Illinois Industrial Energy Consumers ("IIEC"), and the AG propose to fundamentally recast the 2001 transfer of ComEd's former nuclear units, which occurred at their

actual book value, into one occurring at a retroactively-reconstructed “original cost.” This fictional reconstruction would in one stroke eliminate \$2.6 billion of ComEd’s actual equity, and reduce the percentage of equity in ComEd’s capital structure from its actual 54.2% to only 37.11%. That, in turn, would increase ComEd’s leverage well above that of comparable utilities, artificially depress ComEd’s actual cost of capital, and unjustly and unlawfully bar ComEd from recovering at least \$74 million of its actual capital costs each year.

There is no basis for this reduction in equity. It is unsupported by the evidence. It also would violate the Act. The nuclear units were transferred in lawful restructuring transactions authorized by Section 16-111 of the Act, 220 ILCS 5/16-111. The accounting entries supporting ComEd’s post-transfer equity balance were submitted to the Commission in connection with its review of the transfer of the nuclear assets, and Section 16-111(g) provides that the transaction may not thereafter be reviewed “in any subsequent proceeding or otherwise.” The attempt to now review and revise those entries to retroactively increase the value of the assets to some pre-2000 “original cost” is illegal not only because it recasts the 2001 transaction, but also because Section 16-111(g) expressly and unconditionally authorizes writedowns of the “original cost” of assets in connection with such transactions.

The adjustment is also irreconcilably inconsistent with prior Commission determinations of ComEd’s capital balances. In ComEd’s 2001 delivery services rate case (Docket 01-0423), the Commission approved ComEd’s actual post-transfer common equity balance — without any artificial restatement of the nuclear units’ value — and set both ComEd’s cost of capital and rates based on a capital structure that reflected the transfer at book value, just as ComEd proposes here. Indeed, the adjustment would artificially reduce ComEd’s equity balance as of 2001, when

the transfers occurred, to more than \$2.6 billion lower than the \$5.224 billion of equity expressly approved by the Commission in Docket 01-0423.

Moreover, arguing for an artificial reduction in equity requires one to pretend not only that the value of the nuclear plants was billions of dollars more than it actually was at the time of transfer, but also, had the value been \$2.6 billion greater, ComEd would nonetheless have structured all the other aspects of the transfer in exactly the same way, and would have simply ignored the unprecedented impact on its equity. This is unsupported and unrealistic. In fact, the proposed equity subtraction would result in a highly-leveraged capital structure for ComEd with a common equity ratio that is not only significantly lower than the averages for comparable companies, but that also falls outside the benchmarks established by Standard & Poors for electric utilities similar to ComEd. Imposition of a more risky, leveraged capital structure will increase ComEd's future cost of capital, and harm not only ComEd but customers.

Pension Contribution. In March 2005, Exelon contributed \$803 million to ComEd so that the portion of the existing pension plan covering ComEd employees could be fully funded. It is uncontested that the contribution was made with actual funds, provided solely by shareholders, no portion of which was ever collected in rates from any customer. That \$803 million contribution enables ComEd to honor its commitment to its union and management employees alike to provide for their retirements. Increasing the assets in the pension plan by \$803 million also produced additional pension fund earnings that resulted in a \$30 million reduction in the pension expense that would otherwise have been included in annual costs when determining ComEd's revenue requirement.

Yet, Staff proposes to prohibit ComEd from recovering the cost of the \$803 million pension plan contribution. Rather than reflecting it in rate base as the asset that it actually is,

Staff would exclude it for arbitrary reasons, largely based on inapplicable precedent. Moreover, the increase in fund assets resulting from the \$803 million contribution undeniably leads to a \$30 million reduction in annual pension expense reflected in the revenue requirement. Staff's proposal also inconsistently reduces ComEd's costs by the full pension expense savings, despite giving ComEd no opportunity to recover the contribution that made those savings possible. Staff's proposed treatment of the pension contribution violates ComEd's constitutional right to full cost recovery and is contrary to law. Moreover, it advocates a flawed and repugnant policy. Fully funding pensions is an important priority. Disallowing pension contributions would send an alarming message to utilities and their employees throughout Illinois, and discourage utilities from making full provision for the future pension costs of their workers.

General Plant and Intangible Plant. Staff proposes to simply remove from ComEd's rate base a tremendous amount – over \$303 million – of General Plant and Intangible Plant that ComEd needs to deliver electricity to its Illinois customers. No one has even argued that \$303 million worth of assets — such as office buildings, communications equipment, repair and meter-reading vehicles, tools, or software systems — are not being used by ComEd, or are being used for some purpose other than the wires business that is ComEd's only activity. No one has pointed to any asset, tangible or intangible, included in rate base which is either not used and useful, or devoted to some non-jurisdictional function. Nor has any party shown, or even claimed, that the cost of any of these rate base assets was excessive or imprudently incurred.

Staff's proposed General Plant and Intangible Plant disallowances are based entirely on the General Plant and Intangible Plant balances established in a prior 2000 test year, under completely different circumstances. But, unlike the question of the nuclear plant transfer -- which occurred in 2001 -- ComEd's General Plant and Intangible Plant balances concern test

year assets and services, not what occurred in 2000 or 2001. IIEC takes a similar approach, seeking to limit ComEd's General Plant and Intangible Plant based on an arbitrary comparison to the plant balances approved by the Commission in the last case, and proposing an even larger disallowance of at least \$441 million.

The Commission's decision must be based on the evidence in this case. That evidence proves that ComEd's General Plant and Intangible Plant assets are at this time being used exclusively to deliver and support the delivery of electricity to ComEd customers. The evidence ComEd presented is supported by detailed studies and analyses — analyses that were ignored by those advocating disallowances. The proposed disallowances, by contrast, are not supported by studies or analyses. Elimination of \$303 million, \$441 million, or any other amount of General Plant and Intangible Plant from ComEd's rate base is inconsistent with the record and denies ComEd recovery of its actual, reasonable costs.

Administrative and General Expenses. Administrative and General (“A&G”) expenses generally relate to corporate support and overhead functions, such as Human Resources, Finance, Legal, Supply Management, and Information Technology. A&G expenses include the costs of employee pensions and benefits, including health care. ComEd's total jurisdictional A&G expenses were \$287,142,000. ComEd presented extensive, detailed evidence proving that the A&G expenses that are included in its revenue requirement are prudent and reasonable in amount, necessary, and useful in providing Illinois-jurisdictional services. No party denies that expenditures on these functions are essential to ComEd's provision of service to its customers.

Staff arbitrarily claims that ComEd's A&G expenses should be capped at the \$176,684,000 level approved, based on 2000 test year costs, in Docket 01-0423, without even adjusting for inflation. IIEC arbitrarily proposes that ComEd's A&G expenses should be

reduced below even that level, based on the illogical premise that since ComEd has been able to cut certain non-A&G costs since the last rate case, A&G must be lower, too. Yet, they identify no facts supporting a theory A&G expenses should track changes in costs such as distribution O&M, customer accounts, and customer service information expenses. They are independent costs, and it is incorrect to expect a correlation.

The evidence also discredits these claims. Some important A&G expenses — including post-9/11 security expenses and Sarbanes-Oxley Act compliance — did not even exist in 2000. Nor is there any reason to believe ComEd's A&G expenses are high. ComEd's jurisdictional A&G expenses have increased only slightly more than inflation — 14.2% — from 2000 to 2004. And, ComEd's ratio of A&G expenses to the other expenses IIEC cites is below average compared to peer utilities. The allowed level of A&G expenses must be based on the evidence regarding ComEd's actual costs, not on six-year old data, arbitrary mathematical exercises, or baseless speculation. Staff's and IIEC's adjustments must be rejected.

Incentive Compensation. Employee compensation in the United States routinely includes not only base compensation, but also incentive compensation, which motivates employees to improve their performance. ComEd is no exception. There is no challenge by opposing parties to the reasonableness of ComEd's total compensation package or its use of incentive compensation in the package. If incentive compensation were eliminated, base pay would have to be increased by the same amount in order to continue attracting and retaining an adequate and qualified workforce. Paying a portion of the required compensation levels in the form of incentive compensation, however, produces greater benefits for customers through improved focus on reliability, customer service, efficiency, and productivity that it encourages in

ComEd's workforce. Indeed, key performance indicators for fully half of the requested program costs are based directly on measurement of reliability, customer satisfaction, and cost control.

Nonetheless, Staff, the AG, and CCC oppose recovery of any incentive compensation expenses. They claim that incentive compensation expense is discretionary and may not benefit customers. The evidence proves otherwise. It shows that the total cash compensation of ComEd's employees, including incentive compensation, is reasonable and prudent. It proves that ComEd cannot attract and retain talented employees without a competitive incentive compensation package. The record also shows that ComEd's incentive compensation program provides numerous tangible benefits to customers, including increased focus on reliability, customer service, productivity, and cost control.

Distribution Operation and Maintenance Expenses. Operation and maintenance expenses are essential to providing safe, adequate, and reliable service, *i.e.*, to keeping the lights on. They relate to both specific physical facilities (*e.g.*, distribution substations, overhead and underground distribution lines, and line transformers), and functions such as repairing storm damage or managing vegetation. The costs include the salaries and wages of the personnel who perform that critical work. ComEd's final revised revenue requirement includes \$274,184,000 of distribution O&M expenses that the evidence shows to be prudent, reasonable, and necessary.

CCC proposes, based only on speculation, to reduce the Distribution O&M expenses in ComEd's revenue requirement by 4.75%, or over \$13 million. CCC's proposal is based on unsupported conjecture that ComEd's significant investments in its distribution system will result in additional, incremental net reductions in these expenses beyond the cost savings achieved in the 2001-2004 period. ComEd presented evidence regarding the actual drivers of its Distribution O&M expenses that refuted CCC's speculation, showing that the reduction in 2003

and 2004 were the result of broad steps to improve efficiency and productivity in that period, and that there is not any factual basis for assuming that the additional, incremental expense reductions that CCC hypothesizes will occur. CCC's witness, in rebuttal, was unable to provide any valid basis for this proposed adjustment. ComEd's Distribution O&M expenses should be approved based on the facts, and should not be reduced based on speculation.

Appropriate Post-Transition Rate Design

ComEd's proposed rate design reflects its status as a "wires" company and the common theme that the distribution and customer charges in ComEd's post-transition bundled and unbundled retail rates must reflect its costs as an integrated distribution company — not a generation company. ComEd's distribution system-related costs are driven by the need to meet the maximum demand of the customers using each local portion of the system, regardless of when customers use the system or the nature or purpose of such usage. Thus, most of ComEd's current bundled rates contain obsolete pricing structures based on when, or for what purpose, a customer uses electricity. In this proceeding, ComEd proposes a rate design that allows it to recover its costs of providing distribution and customer service in a manner consistent with its being a "wires" company and with cost-causation principles.

Some parties take issue with ComEd's move to cost-based distribution rates, largely because they would no longer contain pricing structures that provide a delivery rates benefit for using electricity in a certain manner or at a particular time. ComEd's proposals make sense because these factors generally do not change ComEd's distribution costs. While they are potentially relevant to generation costs, that is better addressed in generation charges and through demand-control and real-time pricing rates that ComEd continues to actively support. If the Commission were, nonetheless, to maintain tariffs that no longer reflected ComEd's delivery

costs, it would simply cross-subsidize customers. Granting one group of customers a rate that incompletely reflects the group's costs inevitably results in other customers paying more than their fair share.

ComEd proposes several cost-based tariff changes, including to:

- Reduce the number of residential and non-residential customer classes, combining the four residential customer classes into one new class, and the four largest non-residential customer classes into another. ComEd's embedded cost of service study, which is supported by Staff, demonstrates convincingly that the costs to provide distribution service to each of these groups of customers are similar enough to warrant their consolidation into a single residential and single very large non-residential class.
- Redefine maximum demand for ComEd's largest non-residential customers, based on a customer's demand during a 24-hour period rather than during the system peak period only. When ComEd was a vertically integrated utility, it was logical to differentiate demand based on when it occurred because ComEd's generation costs now captured in hourly supply prices, not rates at issue here, were closely tied to when a customer used electricity. ComEd's distribution costs are not. They are driven by distribution capacity, whenever the demand that drives it occurs. Hence, ComEd proposes to have one measure of non-residential demand. Without this change, very large non-residential customers with the ability to shift their load to non-peak periods will receive a \$31 million subsidy from other large non-residential customers.
- Eliminate Rider 25, a rate applicable only to non-residential space heating customers. This obsolete tariff was created decades ago to recognize the low winter-season costs of ComEd's former generation fleet. The response of the Building Owners' and Managers' Association ("BOMA") — to essentially give Rider 25 customers free distribution service eight months of the year — violates sound ratemaking principles and should be rejected.

ComEd also proposes to add a new tariff, Rider ECR — Environmental Cost Recovery. Rider ECR recovers the fluctuating and volatile environmental remediation costs that ComEd incurs on a regular basis, but in unpredictable amounts. Rider ECR recovers costs related to the environmental remediation of manufactured gas plant ("MGP") sites, like similar tariffs of other Illinois utilities. Staff supports recovery of MGP costs under Rider ECR. ComEd agrees, but also presented compelling evidence that Rider ECR should be used to recover all such

environmental clean-up costs, as there is no reasonable distinction between these costs and MGP clean-up-related costs. Accordingly, Rider ECR should be approved.

Commissioners' Questions

During this proceeding, Commissioners Ford and Lieberman asked the parties to address several questions primarily focused on demand response. ComEd presented supplemental testimony explaining that it has a robust demand response program, with a portfolio of programs for both residential and non-residential customers. The undisputed evidence demonstrates that ComEd has one of the largest, if not the largest, demand response programs in the country. Moreover, ComEd continues to explore ways to expand its portfolio of demand response programs, provided that such programs are effective and that ComEd is allowed to recover the costs for such programs. To that end, ComEd generally supports the CUB/City proposal to expand the existing residential real-time pricing program, subject to conditions discussed in Section VII, *infra*.

Applicable Legal Principles

The central legal principles governing this case are clear. As in all contested ratemaking proceedings, the Commission's order must be within its jurisdiction and authority, must be lawful, and must be based exclusively on the evidence in the record. *E.g.*, 220 ILCS 5/10-103, 10-201(e)(iv); *Business and Professional People for the Public Interest v. Illinois Commerce Comm'n*, 136 Ill. 2d 192, 201, 227 (1989) ("*BPI 1989*"). A Commission order is subject to reversal if it is: (1) beyond the Commission's jurisdiction or authority, 220 ILCS 5/10-201(e)(iv)(B); *Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 120 (1995) ("*Citizens 1995*"); *BPI 1989*, 136 Ill. 2d at 204; (2) contrary to law or the Commission followed procedures that are contrary to law, 220 ILCS 5/10-201(e)(iv)(C) and (D); *Citizens 1995*, 166

Ill. 2d at 120-21; *BPI 1989*, 136 Ill. 2d at 204, 240; or, (3) not supported by substantial evidence in the record, contrary to the manifest weight of the evidence, or is not based exclusively on the evidence in the record. 220 ILCS 5/10-103, 10-201(e)(iv)(A); *Citizens 1995*, 166 Ill. 2d at 120-21, 131; *BPI 1989*, 136 Ill. 2d at 204, 227, 234, 240; *Citizens Utilities Co. v. Illinois Commerce Comm'n*, 124 Ill. 2d 195, 206 (1988).

The Commission must approve rates that provide for recovery of the full costs of serving customers. The Restructuring Law unconditionally mandates that: “[c]harges for delivery services shall be cost based, and shall allow the electric utility to recover the costs of providing delivery services through its charges to its delivery service customers that use the facilities and services associated with such costs.” 220 ILCS 5/16-108(c). The Act also mandates that rates adopted in a contested ratemaking proceeding must be just and reasonable. 220 ILCS 5/9-201(c). The “just and reasonable” mandate of Section 9-201(c) of the Act means that the rates must be just and reasonable to the utility and its stockholders as well as its customers. *Business and Professional People for the Pub. Interest v. Illinois Commerce Comm'n*, 146 Ill. 2d 175, 208 (1991) (“*BPI 1991*”). See also *Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 121 (1995) (“In setting rates, the Commission must determine that the rates accurately reflect the cost of service delivery and must allow the utility to recover costs prudently and reasonably incurred” (citing 220 ILCS 5/1-102(a)(iv)) (case involving riders for certain environmental expenses)).

The full cost recovery principle embodied in the Act mirrors well-established Constitutional standards ensuring utilities the opportunity to recover their capital costs and operating expenses, including a reasonable rate of return of and on their capital investments. See U.S. Const., amend. XIV; *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989); *Federal*

Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591, 605 (1944); *Bluefield Waterworks v. Public Service Comm'n*, 262 U.S. 679, 690 (1923); Ill. Const. Art. I, § 15. Rates must enable a utility “to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risk assumed....” *Duquesne*, 488 U.S. at 310 (*quoting FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 605 (1944)).

In this case, those principles require that the Commission reflect ComEd’s proven actual investments and costs in its ComEd’s post-transition rates. This is the only lawful result, and the right result for ComEd and its customers. “ComEd must recover sufficient revenue through its retail rates to cover its costs, if it is to continue to be able to provide customers with adequate, safe, and reliable service.” Clark Direct (“Dir.”), ComEd Ex. 1.0, 6:124-26.

II. STATEMENT OF UNCONTESTED ISSUES

A. Issues That No Party Contests

1. Test Year

ComEd has used an historical test year of 2004 as the basis for ratemaking in this Docket in accordance with 83 Ill. Adm. Code § 287.20(a). *E.g.*, Hill Direct (“Dir.”), ComEd Ex. 5.0 Corr., 3:43-45. No party contests the use of 2004 as the test year.

2. Elements of Rate Base

a) 21 Capital Project Additions

The “21 capital project additions” refers to the 21 largest additions to rate base made by ComEd since its last rate case, which includes Distribution Plant, General Plant, and Intangible Plant projects, and for which ComEd had to provide detailed information under 83 Ill. Adm. Code §§ 285.6100 and 286.20. DeCampli Dir., ComEd Ex. 4.0 Corr. (entire testimony); ComEd Ex. 4.3 (Sch. F-4 Errata). No party contests the inclusion of these 21 additions in rate base.

b) Staff Adjustment Related to ComEd Schedule B-2.1

ComEd made detailed adjustments to rate base based on ComEd's *pro forma* adjustments for certain 2005 plant. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 32:686 - 33:707; ComEd Ex. 5.1 at Schedule B-2.1 Errata. Schedule B-2.1 Errata reflects corrections supported by Staff. No party disputes those corrections.

c) Pro Forma Capital Additions and Construction Work in Progress

At any time, ComEd has a substantial number of construction projects in progress for which it does not accrue Allowance for Funds Used During Construction ("AFUDC"). *E.g.*, Hill Dir. ComEd Ex. 5.0 Corr., 14:295-301. ComEd originally proposed to include \$53,449,000 (corrected) of non-AFUDC bearing Construction Work in Progress ("CWIP") in rate base. ComEd Ex. 5.1 at Schedule B-1 Revised. Staff witness Mr. Griffin (Staff Ex. 3.0) and CCC witness Mr. McGarry (CCC Ex. 2.0) objected to the CWIP addition based on the theory that costs were "double counted" with certain *pro forma* capital additions. ComEd, Staff and CCC subsequently agreed that it would be fair and appropriate for ComEd to lower the amount of CWIP in its rate base from \$53,449,000 to \$41,040,000 and Staff and CCC withdrew their proposed adjustments to CWIP and the *pro forma* capital additions. Hill, Tr. at 896:11-22; McGarry, Tr. at 910:20 – 911:6; Griffin, Tr. at 1565:8-21; ComEd Ex. 45.0; Hill Sur., ComEd Ex. 36.0 at Schedule 1 Revised, page 4. Accordingly, this issue is not uncontested.

d) Pro Forma "New Business" Capital Additions and Revenue Credit Against Operating Expenses

CCC and the AG proposed adjustments to ComEd's *pro forma* new business capital additions based on the theory that the revenue requirement did not reflect revenues that would result from the additions. McGarry Dir., CCC Ex. 2.0 Second Corr.; Effron Dir., AG Ex. 1.0).

ComEd, CCC, and the AG subsequently agreed that ComEd would add a revenue credit of \$13,751,325 to its revenue requirement, and CCC and the AG would withdraw their proposed adjustments to rate base. McGarry, Tr. at 301:3-16; Hill, ComEd Ex. 36.0 Revised, 9:188-93 and Schedule 3 Revised. Accordingly, this issue is not uncontested.

3. Elements of Operating Expenses

a) Advertising Expense Adjustment

Staff in its direct testimony suggested, and ComEd witness in its rebuttal testimony agreed, to an adjustment to remove \$349,000 of “advertising expenses” from the revenue requirement, except they agreed that the correct amount of the adjustment is \$317,000. Hathhorn Dir., Staff Ex. 1.0, 18:370 - 19:389; Hill Reb. ComEd Ex. 19.0, 58:1286-1296; Hathhorn Reb., Staff Ex. 12.0, 16:352 - 17:360. Accordingly, this issue is not uncontested.

b) Staff 2005 Wage and Salary Adjustment

Staff in its direct testimony suggested, and ComEd in its rebuttal testimony agreed to, an adjustment to remove \$1,174,000 of ComEd’s *pro forma* salary and wage increases adjustment for 2005. Ebrey Dir., Staff Ex. 2.0:627-635; Hill Reb., ComEd Ex. 19.0, 42:931-937. Accordingly, this issue is not uncontested.

c) Post-Retirement Healthcare Benefits

The AG in its direct testimony suggested a \$7,636,000 adjustment to reduce pension and post-retirement health care expenses in the test year to remove the impact of fair value accounting. Effron Dir., AG Ex. 1.0, Schedule C-2. ComEd, in its rebuttal testimony agreed, based on updated data, that a \$5,200,000 adjustment to pension and post retirement expense would be appropriate and consistent with fair value adjustments to the capital structure proposed by ComEd. Houtsma Reb., ComEd Ex. 18.0, 27:594 - 28:622. The AG in its rebuttal agreed to

the \$5,200,000 figure. Effron Reb., AG Ex. 3.0 revised, 8:8-23. No other party contests this adjustment.

d) Tax Consultants

The AG in its direct testimony suggested an adjustment to remove a \$4,600,000 charge for payments to tax consultants in 2004. Effron Dir., AG Ex. 1.0, 35:7 - 36:2. In order to narrow the issues. ComEd in its rebuttal testimony agreed to make the adjustment. Hill Reb., ComEd Ex. 19.0, 48:1058-1063. Accordingly, this issue is not uncontested.

e) Employee Arbitration Settlements

The AG in its direct testimony proposed an adjustment to eliminate certain employee arbitration settlement costs. Effron Dir., AG Ex. 1.0, 24:5 - 25:4. ComEd, in order to narrow the issues, proposed to reduce ComEd's test year employee settlement/arbitration costs by \$4,301,224 to account for a true-up credit booked in 2005. Hill Reb., ComEd Ex. 19.0, 47:1026-48:1056. The AG agreed to the revised adjustment. Effron Reb., AG Ex. 3.0 Revised, 17:21-18:9. Accordingly, this issue is not uncontested.

4. Elements of Rate Design and Tariffs

a) Rider PM

Rider PM (relating to Primary Metering Adjustments) is ComEd's proposed tariff to replace Rider 9 and is applicable to customers taking service from ComEd at 2,160 volts or greater with interval metering that utilize service at a different voltage. (ComEd Ex. 10.14 page 4) Rider PM provides for an adjustment to the measurement of electric power and energy provided to retail customers that have primary metering facilities. The metering adjustment is stated as a percentage. ComEd determined that percentage by calculating average electrical losses based on average load conditions for transformers purchased by ComEd that are typically

used to provide standard service to retail customers. Alongi/McInerney, ComEd Ex. 10.0 32:743-751 ComEd Exhibit 10.19) Staff agreed that ComEd’s data supported the calculation Linkenback, Staff Ex. 8.0 17:392-400. No other party recommended an adjustment to Rider PM.

b) Rate MSPS7

Rate MSPS7 (relating to Metering Service Provider Service) is proposed to replace Rate MSPS. Alongi/McInerney, ComEd Exhs. 10.0 lines 817-829, 10.27, 10.28, 10.29. It addresses certain housekeeping changes to reflect changes to the names of other tariffs, to remove generally applicable terms which have been moved to General Terms and Conditions, to reflect ComEd’s integration into the PJM Interconnection, LLC (“PJM”), and to update certain charges. Staff agreed that ComEd’s data supported the proposed changes (Linkenback, Staff Ex. 8.0 18:412-19:425) and no other party contested it.

c) Rate RESS7

Rate RESS7 (relating to Retail Electric Supplier Service) is proposed to replace Rate RESS. Alongi/McInerney, ComEd Ex. 10.0 lines 817–829. Similar to Rate MSPS7, it addresses certain housekeeping changes to reflect changes to the names of other tariffs, to remove generally applicable terms which have been moved to General Terms and Conditions, and to reflect ComEd’s integration into PJM. No party recommended changes or modification to Rate RESS7.

d) Rider FCA

Rider FCA (relating to Franchise Cost Additions) is proposed to replace ComEd’s Rider 16 – Franchise Cost Addition – and to reflect two changes to Rider 16 involving the introduction of two new formulae into the new Rider. Crumrine, ComEd Ex. 9.0 Corr., 25:549-26:573 and Alongi/McInerney, ComEd Exhs 10.0 lines 715-731, and 10.17. Rider FCA provides for the

recovery of certain municipal franchise costs and fees. No party suggested changes or modification to Rider FCA.

e) **Rider RCA**

Rider RCA (Retail Customer Assessments) is proposed to replace Rider 21. *Id.* Exhs 10.0 lines 679-699, and 10.15 page 2. Rider RCA provides for a renewable energy resources and coal technology development charge under the Renewable Energy, Energy Efficiency, and Coal Resources Development Law of 1997 and an energy assistance charge for the Supplemental Low-Income Energy Assistance Fund under Section 13 of the Energy Assistance Act of 1989. No party suggested changes or modification to Rider RCA.

5. **Other**

a) **Original Cost Audit**

ComEd supports the Interim Order entered April 6, 2006.

b) **Exelon GSA-Reporting Requirements**

ICC Staff Witness Hathhorn proposed new reporting requirements as a result of the repeal of the Public Utilities Holding Company Act (“PUHCA”). ComEd proposed some modifications to those requirements, which Staff has accepted. Specifically, ComEd will file a copy of its FERC Form 60 with the ICC, and provide a copy to the Manager of Accounting, on the day it is filed with FERC; ComEd will notify the ICC within 30 days of implementation of substantial changes to service company allocation factors. (A substantial change is defined by 1) a change in the allocation basis for a function, or 2) a change in the calculation of the factor that would result in an increase or decrease in total BSC costs allocated to ComEd by more than 5%, or \$10 million, whichever is greater, relative to the prior calendar year.) Additionally, ComEd will file as part of its ICC Form 21 a report of BSC corporate governance charges by function,

and the following schedules that were previously filed as part of the U-13-60 report filed with the Securities and Exchange Commission prior to the repeal of PUHCA, with detail to be provided for items that are greater \$100,000 in amount:

- Outside Services Employed - Account 923
- Employee Pension and Benefits - Account 926
- General Advertising Expenses - Account 930.1
- Rents - Account 931
- Taxes Other Than Income - Accounts 408.1 and 408.2
- Donations - Accounts 426.1
- Other Deductions -Account 426.5

B. Proposals to Which Certain Parties Have Agreed

1. Elimination of Rate 87

ComEd requested that the Commission approve a revision to Rate 87 tariff sheet to make it clear that this rate is not effective after January 1, 2007. [35th Revised Sheet No. 55 ComEd Exhs 10.0 lines 190-210, and 10.2]. Rate 87 is a grandfathered rate that is available only to certain governmental customers in Rockford and has been closed to new customers since December 1972. Separate pricing for these customers is not appropriate in the post-transition period. Crumrine Direct, ComEd Ex. 9.0 Corr., 22:485-492. Staff agrees that this is a housekeeping issue and no longer takes issue with ComEd's proposal. Hanson Reb., Staff Ex. 18.0, 3:58—4:72. However, Staff suggests that this housekeeping change should not supersede any obligation that ComEd may have under Rate 87 to provide the City of Rockford with adequate notice before canceling the tariff. *Id.* at 4:69-72. ComEd has agreed to give proper notice. Alongi/McInerney Sur., ComEd Ex. 41.0, 146-151. No other party contests this proposal.

2. Condominium Common Area Reclassification

The Coalition of Energy Suppliers (“CES”) originally took the position that ComEd’s revised General Terms and Conditions did not re-categorize certain condominium common area customer accounts from residential to nonresidential customers consistent with statements made by ComEd in ICC Docket 05-0159 (the “Procurement Case”). Domagalski Dir., CES Ex. 3.0, 30:706. ComEd’s rebuttal testimony indicated the location of this change (Sheet No. 503, ILL. C.C. No. 4 Original Sheet No. 503). Alongi/McInerney, ComEd Ex 24.0 lines 756-762. In rebuttal testimony, CES indicated that it was satisfied that ComEd properly addressed the issue. O’Connor/Domagalsik, CES Ex. 5.0, 14:298-299. No other party contests this issue.

3. Modifications to ComEd Business Processes to Aid RESs and Customers

a) Rider SBO7

The proposed Single Bill Credit contained in Rate RDS is an update of the currently effective embedded cost-based fixed credit, the Single Bill Credit, using the methodology approved in ComEd’s last delivery service rate case, Docket 01-0423. Alongi/McInerney Dir., ComEd Ex. 10.0, at 24:569-81.

In response to concerns raised by CES, ComEd agreed to make certain revisions to Rider SBO. *See* Domagalski Dir., CES Ex. 3.0 revised at 16:370-72, 17:377-80; Clark/Witt Dir., CES Ex. 2.0, at 31:766-89. While reserving the right to revisit this matter should unforeseen issues arise, ComEd is willing to eliminate the provision in proposed Rider SBO7 that precludes a Retail Electric Supplier (“RES”) from offering SBO service to a retail customer during the 12 monthly billing periods after it terminated such service. Crumrine Reb., ComEd Ex. 23.0, at 70:1503-9. ComEd Exhibit 41.6 contains the amendment to proposed Rider SBO7 that would implement this revision, if approved by the Commission.

b) Definition of “New Customer”

CES requested that ComEd modify the definition of a “new customer” so that an existing customer account would not be “finaled” (or closed and a final bill sent) as a result of a name change. Clark/Witt Dir., CES Ex. 20, 23:571-579 ComEd agreed to change the definition of “new customer” in the manner requested by CES. Meehan Rebuttal, ComEd Ex. 26.0, 15:318-26; Clark/Witt Rebuttal, CES Ex. 6.0, 2:36-42. No other party contests this issue.

c) Definition Of Retail Versus Wholesale Peak and Off-Peak Periods

CES raised certain concerns about the definition of “Peak-Period,” under ComEd’s proposed General Terms and Conditions. *See* Domagalski Dir., CES Ex. 3.0 (Rev.), at 15:330-32. ComEd recognized that further clarity is needed to distinguish the retail peak and off-peak periods from the wholesale peak and off-peak periods used by PJM Interconnected LLC. (“PJM”). Consequently, ComEd proposes to make amendments to the Definitions part of ComEd’s proposed General Terms and Conditions to provide clear definitions of the following terms: PJM Peak Period; PJM Off-Peak Period; Retail Peak Period; and Retail Off-Peak Period.

In their panel rebuttal testimony Dr. O’Connor and Mr. Domagalski testified that “[t]he revised definitions presented by ComEd are acceptable and the Coalition recommends that the Commission approve revisions that implement the Company’s clarification.” *See* O’Connor/Domagalski Reb., CES Ex. 5.0, at 13:284-87.

d) Clarification of Switching Rules

CES originally took the position that the switching rules in ComEd’s proposed tariffs are complex and unclear. *See, e.g.,* Domagalski Dir., CES Ex. 3.0, at 11:253-54. ComEd provided testimony that it is taking steps to educate customers and Retail Electric Suppliers (“RESs”) to ease the transition to these new tariffs, including revising its RES Handbook and its Customer

Handbook. Alongi/McInerney Reb., ComEd Ex. 24.0, at 31:779-84. These handbooks will be available to interested parties within approximately two months after the completion of this Docket. *Id.* ComEd also notes that it is willing to work with RESs to develop a summary of the switching rules for purposes of this RES Handbook. *Id.*

In addition, ComEd agreed to amend the 12-month restriction in Rate RCDS as a one-time transition provision such that a customer could switch to delivery service on its last regularly scheduled meter reading date in 2006. *Id.* If the Commission approves this proposal, ComEd will file an appropriate revision of Rate RCDS with its compliance filing.

CES is satisfied with ComEd's proposals regarding switching rules. O'Connor/Domagalski Reb., CES Ex. 5.0, at 14:304-13, 14:309-10, 16:350-52.

e) **Timely Revision to RES Handbook**

As stated previously in Section II.B.3.d. of this Brief, ComEd agrees to revise its RES Handbook and its Customer Handbook and make them available to interested parties approximately within two months after the completion of this Docket. Alongi/McInerney Reb., ComEd Ex. 24.0, at 31:779-84.

f) **Inclusion of "Frequently Asked Questions" on "PowerPath"**

CES requested that ComEd establish an electronic bulletin board for customers and RESs to interact with ComEd, and dedicate employees to address RES customer's service questions. Clark/Witt Dir., CES Ex. 2.0, 38:913-40:974 ComEd agreed that it would post common RES questions and responses as FAQs on the PowerPath website. Meehan Reb., ComEd Ex. 26.0, 24:516-17. CES agreed to this proposal. Clark/Witt Reb., CES Ex. 6.0, 3:53-54. No other party contests this issue.

g) Relief From Minimum Stay Requirement

See Section II.B.3.d. of this Brief.

h) Provision of Information to RESs

(i) 867 and 810 Billing Data Available after 1:00 PM

An EDI 867 transaction provides detailed meter usage information, and is sent to RESs when an account is billed. The EDI 810 transaction is the bill image of ComEd's delivery service bill, and is sent to a RES that is a customer's Single Bill Option provider under ComEd's Rider SBO – Single Bill Option ("SBO") when an account is billed. CES requested that ComEd make 867 and 810 Billing Data available electronically before 1:00 PM for same-day processing by RESs, and data submitted after 1:00 PM be dated the next business day. Clark/Witt Dir., Ex. 2.0, 29:709-715 ComEd agreed to this request, and has modified its systems on January 12, 2006. *Id.* No other party contests this issue.

(ii) Weekly Pending Disconnection Report

CES requested that ComEd provide all drop information to RESs electronically, in real time. Clark/Witt Dir., CES Ex. 2.0, 5:122-123. ComEd agreed to provide information to RESs regarding pending disconnections through a hard copy report, which could be provided on a weekly basis and CES agreed to this resolution. Meehan Reb., ComEd Ex. 26.0, 16:335-37. Clark/Witt Reb., CES Ex. 6.0, 3:43-44. No other party contests this issue.

(iii) Customer Current Rate and Supply-Type Information on PowerPath

CES requested that ComEd provide current rate and supply-type information, including customer supply group and customer delivery class information, on ComEd's PowerPath website. Clark/Witt Dir., CES Ex. 2.0, 6:150-155. ComEd agreed that it will implement these

changes in the near future. Meehan Reb., ComEd Ex. 26.0, 20:439-43. No other party contests this issue.

(iv) **DASR Eligibility on PowerPath**

CES requested that ComEd provide a DASR eligibility date on its PowerPath website. Clark/Witt Dir., Ex. 2.0, 34:822 ComEd agreed that a DASR eligibility date would be beneficial to the market participants, and agreed that, if the data is readily available, ComEd will make this information available to requestors with proper authority. Meehan Rebuttal, ComEd Ex. 26.0, 21: 446-49. No other party contests this issue.

(v) **Customers' TOU data on PowerPath**

CES requested that ComEd provide time of use (TOU) data and on- and off-peak splits. ComEd agreed to provide TOU data relating to how ComEd defines peak and off-peak service for some customers and agreed to provide such information on the PowerPath website to RESs. Meehan Reb., ComEd Ex. 26.0, 21:459-64. CES agreed to this proposal. Clark/Witt Rebuttal, CES Ex. 6.0, 3:50-52. No other party contests this issue.

i) **Allocation of Uncollectible Expenses**

CES raised the issue of the Uncollectible Adjustment Factor as it applies to Supply Charges under the BES tariffs. Domagalski Dir., CES Ex. 3.0, at 25:586-87, 25:591-93. ComEd showed that uncollectible expenses are properly allocated between electric supply and delivery customers. Crumrine Reb., ComEd Ex. 23.0, at 54:1144-56. ComEd Exhibits 10.0 and 10.8 discuss and describe how each of the four Uncollectibles Adjustment Factors for each of the BES tariffs was determined. CES and ComEd are in agreement on this issue. *See* Domagalski Dir., CES Ex. 5.0, at 13:270-74.

4. Other

a) Rider ZSS7

ComEd proposes to revise item (1) of the applicability conditions for this Rider ZSS7 to require self generating customers to have direct access to the PJM markets. This proposal more closely follows the cost of service principles and sends appropriate price signals. Crumrine Dir. ComEd Ex. 9.0 Corr., 28:615-29-637; Alongi/McInerney, ComEd Ex. 10.0, Sched. 10.14, at 5. In direct testimony, IIEC argued that self-generating customers should be allowed to elect Rider ZSS7. Stephens Dir., IIEC Ex. 1.0, 3:71-75, 20:387 - 21:415. In rebuttal, ComEd explained that Rider ZSS7 applies only to those self-generating customers that operate under an Operating Agreement, the applicable Reliability Agreement and the Open Access Transmission Tariff of the PJM to sell power and energy into the PJM market and that Rider ZSS7 is designed to recover the cost of minimal distribution facilities on a direct assignment basis for each such customer. Crumrine Reb., ComEd Ex. 23.0, 76:1641-77-1670. IIEC did not address this issue further in rebuttal. No party opposed this revision to Rider ZSS7.

III. ARGUMENT ON CONTESTED ISSUES

A. Total Revenue Requirement And Base Rate Revenue Increase

The Commission should approve ComEd's final revised proposed revenue requirement of \$1,862,185,000, which yields a base rate increase of \$317,295,000.⁵ ComEd has proved that its

⁵ This amount reflects subtraction of Miscellaneous Revenues and the "new business" revenue credit for the provision of Illinois-jurisdictional delivery services (not including transmission service). ComEd's final revised revenue requirement and the components thereof, as well as the resulting base rate increase, are set forth in ComEd Ex. 36.0 at Schedule 1 Revised at Schedule C-1. Because ComEd agreed to two proposed adjustments at the evidentiary hearing in this case, those adjustments were not reflected in ComEd's pre-filed testimony. Accordingly, ComEd prepared: (1) ComEd Ex. 36.0, Schedule 1 Revised (which consists of revised revenue requirement Schedules that, reflecting those two adjustments, set forth ComEd's final revised revenue requirement and the components thereof, as well as the resulting base rate increase); and (2) ComEd Ex. 36.0, Schedule 3 Revised (which shows the final calculation of the second of those two adjustments, replacing an earlier proposed calculation

revenue requirement is correct, just, and reasonable. Staff's and intervenors' respective alternative proposals, which are hundreds of millions of dollars lower, and their underlying proposed adjustments, should be rejected for reasons that are described in the remainder of this Brief.

Setting the Correct Revenue Requirement Is Critical for ComEd and for its Customers. Setting the correct revenue requirement is critical not only for ComEd but also for its customers. Approval of the correct revenue requirement, and of rates that allow full recovery of that revenue requirement, is essential if ComEd is to continue to provide its retail customers with adequate, safe, and reliable service. *E.g.*, Clark Dir., ComEd Ex. 1.0, 6:124-130. Denying ComEd recovery of the money that it prudently and reasonably invests to distribute electricity and keep the lights on is not a sensible option, and is contrary to the interests of customers. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., 7:129-144.

Setting rates that reflect ComEd's actual costs and expenses is essential from an economic perspective as well. Rates that under-recover costs can fail to provide ComEd with sufficient resources to build and maintain the infrastructure needed to support competitive markets, and such rates send incorrect price signals to retail customers. *E.g.*, Landon Dir., ComEd Ex. 2.0, 1:14 - 2:29, 3:49-54, 11:217-228.

Finally, establishing rates that allow ComEd to recover fully its revenue requirement is required by well recognized decisions governing the rate setting process.⁶

thereof); and ComEd offered them as attachments to ComEd Ex. 45.0, the Affidavit of Jerome P. Hill. Thus, in this Initial Brief, when ComEd refers to ComEd Ex 36.0 at Schedule 1 Revised or at Schedule 3 Revised, it is referring to items found in the record as attachments to ComEd Ex. 45.0.

⁶ See the Introduction of this Brief re legal standards. See also, *e.g.*, *Bluefield Water Works & Improvement Co. v. Public Service Comm'n of West Virginia*, 262 U.S. 679, 692-93 (1923) (holding state rate case order unconstitutional, as confiscatory); *Michigan Bell Tel. Co. v. Engler*, 257 F.3d 587, 594 (6th Cir. 2001) (holding state telephone rate "freeze" unlawful, as confiscatory); *City of Edwardsville v. Ill. Bell Tel. Co.*, 310 Ill. 618, 621 (1923) (legislative power over public utility rates does not include power to set rate that is confiscatory).

ComEd Proved Its Revenue Requirement. ComEd has proved that its \$1,862,185,000⁷ revenue requirement is correct, just, and reasonable. The uncontradicted evidence⁸ shows that ComEd's revenue requirement reflects its actual costs and expenses incurred as of and in 2004. More specifically, the evidence shows that ComEd operates on a calendar year basis for financial reporting purposes, that 2004 was the most recent calendar year for which ComEd had complete actual results when it prepared and filed its proposed rates, e.g., Hill Dir., ComEd Ex. 5.0 Corr., 7:142-143, and that the 2004 historical test year is permitted under 83 Ill. Adm. Code § 287.20(a). E.g., Hill Dir., ComEd Ex. 5.0 Corr., 3:60 - 6:114, 7:137 - 9:193, *et seq.* The test year is uncontested, as noted in Section II.A of this Brief.

The evidence also shows that each year, ComEd files, with both the Federal Energy Regulatory Commission ("FERC") and the ICC, ComEd's independently audited "FERC Form No. 1: Annual Report of Major Electric Utilities, Licensees, and Others," commonly referred to as the FERC "Form 1", e.g., Hill Dir., ComEd Ex. 5.0 Corr., 7:143-150; Lazare, Tr. at 614:8-16, 615:1-5, that the FERC Form 1 records ComEd's actual costs, including both capital costs and operating expenses, incurred as of and during the applicable year, in accordance with FERC's Uniform System of Accounts (the "USoA"), which has been adopted by the ICC with limited modifications (none relevant here), e.g., Hill Dir., ComEd Ex. 5.0 Corr., 7:146-148; Lazare, Tr. at 611:20 - 614:16, and that ComEd developed its revenue requirement by starting with the capital costs and operating expenses recorded in its 2004 FERC Form 1, identifying those costs and expenses that were incurred in order to provide Illinois-jurisdictional delivery services. E.g.,

⁷ From this point onward, all references to revenue requirement figures are after the subtraction of Miscellaneous Revenues and, where applicable, the "new business" revenue credit.

⁸ The Commission must apply Illinois law governing uncontradicted evidence. "Where the testimony of a witness is neither contradicted, either by positive testimony or by circumstances, nor inherently improbable, and the witness has not been impeached, that testimony cannot be disregarded by the trier of fact." *Bazydlo v. Volant*, 164

Hill Dir., ComEd Ex. 5.0 Corr., 7:140 - 9:193. No party has contested the accuracy of any of ComEd's 2004 FERC Form 1 data.

The evidence also shows that ComEd, after thoroughly reviewing its 2004 actual costs and expenses to establish the foundation for its revenue requirement, carefully determined and calculated the appropriate adjustments, including *pro forma* adjustments as permitted under 83 Ill. Adm. Code § 287.40, in arriving at its proposed revenue requirement. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 3:60 - 6:114, 7:137- 9:191, 32:675 - 40:868.

ComEd presented extensive testimony from highly-qualified witnesses who supported ComEd's proposed revenue requirement, including:

- the direct, rebuttal, and surrebuttal testimony of John Costello, ComEd's Senior Vice President, Operations (ComEd Exs. 3.0 Corr., 13.0 Corr., 13.1, 13.2, 30.0), supporting numerous components of the revenue requirement, including Distribution Plant, General Plant, Intangible Plant, *pro forma* capital additions, and the Materials and Supplies component of rate base, as well as operating expenses generally, Distribution Operations and Maintenance ("O&M") expenses, Customer Accounts expenses, Customer Service and Information Expenses, Administrative and General ("A&G") expenses, and post-2006 implementation expenses;
- the direct, rebuttal, and surrebuttal testimony of David DeCampli, ComEd's Vice President, Asset Investment Strategy & Development (ComEd Exs. 4.0 Corr., 4.1, 4.2, 4.3 Errata, 14.0 Corr., 31.0, 31.1), discussing the 21 largest capital additions

Ill. 2d 207, 215 (1995). *See also, e.g., Thigpen v. Retirement Bd. of Fireman's Annuity and Benefit Fund of Chicago*, 317 Ill. App. 3d 1010, 1021 (1st Dist. 2000).

included in rate base since ComEd's 2001 delivery services rate case, Commonwealth Edison Co., ICC Docket 01-0423;

- the direct, rebuttal, and surrebuttal testimony, and Affidavit, of Jerome P. Hill, ComEd's Director of Revenue Policy (ComEd Exs. 5.0 Corr., 5.1, 5.2, 19.0 (including Schedules 1-18 thereto), 36.0 (including Schedule 1 Revised, Schedule 2, Schedule 3 Revised, and Schedules 4-10 thereto), 45.0), who presents a "roll-up" of the revenue requirement and its components, including all necessary calculations and the supporting Schedules and work papers, and who also provides additional support for other components of the revenue requirement;
- the direct, rebuttal, and surrebuttal testimony of J. Barry Mitchell, ComEd's President (ComEd Exs. 7.0, 20.0, 20.4, 37.0 Second Corr.), supporting ComEd's proposed capital structure, inclusion of ComEd's pension asset in rate base and ComEd's overall rate of return; and
- the rebuttal and surrebuttal testimony of Kathryn M. Houtsma, CPA, ComEd's Vice President, Regulatory Projects (ComEd Exs. 18.0 Corr., 18.1, 35.0, 35.1, 35.2, 35.3, 35.4, and 35.5), refuting several adjustments proposed by other parties.

ComEd also presented the testimony of renowned independent experts supporting the reasonableness of particular revenue requirement components, including:

- the direct and rebuttal testimony of Richard F. Meisheid II, Managing Principal, Towers Perrin (ComEd Exs. 12.0, 27.0), supporting the reasonableness of ComEd's incentive compensation programs, including their benefits for customers, and of the programs expenses; and

- the rebuttal and surrebuttal testimony of Susan F. Tierney, Ph.D., Managing Principal, Analysis Group, and former Commissioner of the Massachusetts Department of Public Utilities (ComEd Exs. 22.0, 39.0), refuting Staff’s proposed adjustments relating to ComEd’s pension asset and pension expenses.

ComEd also presented the direct, rebuttal, and surrebuttal testimony of John H. Landon, Ph.D., Special Advisor, Analysis Group (ComEd Exs. 2.0 Corr., 2.1, 2.2 Revised, 2.3, 2.4 Revised, 2.5, 15.0, 15.1, 15.2, 15.3, 32.0 Revised, 32.1), supporting the reasonableness of ComEd’s proposed rates.

Finally, ComEd has carefully considered not only its Form 1 data and the other facts shown and referenced in its testimony, but also Staff’s and intervenors’ testimony, in arriving at ComEd’s final revised revenue requirement of \$1,862,185,000.

ComEd Also Proved Its Revenue Deficiency (the Needed Base Rate Increase).

ComEd’s proposed base rate increase – its revenue deficiency – is the difference between ComEd’s proposed revenue requirement, \$1,862,185,000, and its calculation of revenues under existing rates, \$1,544,890,000, *e.g.*, ComEd Ex. 5.1 at Schedule C-1 Errata, resulting in a revenue deficiency (base rate increase) of \$317,295,000.⁹ While the revenue requirement is disputed, there does not appear to be any contested issue as to the calculation of the revenue deficiency.

⁹ The calculation of revenues under existing rates and thus of the revenue deficiency unavoidably are conceptual figures. ComEd’s calculation of revenues under existing rates has to assume that all retail customers are taking service under ComEd’s existing delivery services rates. *E.g.*, ComEd Ex. 5.1, Hill, Tr. at 915:19 – 916:18. That approach to the calculation of revenues under existing rates is necessary, because ComEd’s existing bundled electric service rates do not break out (“price-unbundle”) the amounts being charged for Illinois-jurisdictional delivery services and, so, it is not possible to calculate ComEd’s revenues recovered under the bundled electric service rates for Illinois-jurisdictional delivery services. In fact, ComEd’s over 3 million residential customers and thousands of its non-residential customers take service under its existing bundled electric service rates, not its delivery services rates.

Staff's and Intervenors' Proposed Revenue Requirements Are Unsupported By The

Evidence. ComEd has provided compelling evidence to support its final revised proposed revenue requirement. Staff and intervenors have failed to refute that evidence.

While ComEd bears the burden of proof that its proposed rates are just and reasonable, 220 ILCS 5/9-201(c), that does not mean that it is the only party that has to prove its claims.

In proceedings before the Commission, once a utility makes a showing of the costs necessary to provide service under its proposed charges, it has established a prima facie case. *City of Chicago v. People of Cook County*, 133 Ill. App. 3d 435, 478 N.E.2d 1369, 88 Ill. Dec. 643 (1985). The burden then shifts to others to show that the costs incurred by the utility are unreasonable because of inefficiency or bad faith. *City of Chicago v. People of Cook County*, 133 Ill. App. 3d 435, 478 N.E.2d 1369, 88 Ill. Dec. 643 (1985).

Illinois Bell Tel. Co. v. Illinois Commerce Comm'n, 327 Ill. App. 3d 768, 776 (3d Dist. 2002).

Staff and Intervenors have not met their burden of going forward with the evidence. Their respective revenue requirement proposals are hundreds of millions of dollars below that of ComEd. *E.g.*, Hill Sur., ComEd Ex. 36.0 Corr., at 5:108 – 7:154. Indeed, Staff and the AG recommend a revenue requirement decrease, and CCC recommends only a small revenue requirement increase, despite the facts that ComEd has spent approximately \$3 billion on its distribution system since its last rate case, and has experienced operating expense increases in numerous areas, such as wages and employee health care expenses. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., at, 9:188–11:218; Hill Sur., ComEd Ex. 36.0 Corr., at 5:108–7:154.

ComEd has addressed each of the adjustments proposed by Staff and intervenors, showing that they are unsupported by the evidence. In many cases, they are based on invalid theories or artificial mathematical exercises divorced from test year ratemaking and the actual relevant facts. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., at, 6:115-123; Costello Sur., ComEd

Ex. 30.0, at 3:56–4:88; Hill Sur., ComEd Ex. 36.0 Corr., at 2:35–4:70. ComEd’s final revised proposed revenue requirement is supported by the evidence and should be approved.

B. Rate Base

1. Depreciation and Amortization Reserve

Overview. In determining ComEd’s rate base, the Commission must take depreciation into account. A simple example illustrates why this is so. When ComEd invests in a capital asset used to provide delivery services to ComEd’s customers, it incurs a one-time cost. This one-time cost is the historical cost of the asset and serves as the starting point for determining ComEd’s rate base. Each year, ComEd records depreciation expense, which, in effect, recognizes that plant assets provide service to customers over an extended useful life. If the useful life of an asset will be ten years, depreciation expense on a straight line basis would equal one tenth of the original cost of the asset per year for ten years. For purposes of establishing rates, ComEd’s expenses include depreciation expense. Therefore, one tenth of the original cost of the asset would be included in the revenue requirement used to set ComEd’s rates, thus enabling ComEd to recover, over time, the one-time investment it originally made in the capital asset.

Although depreciation expense allows ComEd to recover the cost of the capital asset over time, it does not compensate ComEd for the cost of the debt and equity capital used to acquire the asset. Compensation for those costs comes in the form of a return on ComEd’s rate base. The appropriate rate base for all of the capital assets used to provide delivery services to customers reflects the depreciation expense that has already been recorded. For example, if ComEd had a \$1 million assets with a ten-year useful service life, in the fourth year, cumulative depreciation expense of \$400,000 would already have been recorded, and ComEd’s rate base

would include the original \$1 million cost of the asset less the \$400,000 of accumulated depreciation, or \$600,000.

At any given time, ComEd's capital assets will include investments from many different past years, but the total historic cost of those assets is known and recorded in ComEd's books and records. Similarly, the accumulated total of depreciation expense is also known and recorded. To determine ComEd's rate base as of December 31, 2004, the Commission starts with the total historic costs of the assets and deducts the accumulated depreciation through December 31, 2004.

In its direct testimony, ComEd established the total historic cost of the capital assets used to provide delivery services and the accumulated depreciation balance reflected on ComEd's books with respect to those assets. The net of those two amounts was included in ComEd's rate base. Significantly, ComEd's approach was symmetrical. For assets being used as of December 31, 2004, ComEd deducted the accumulated depreciation expense through December 31, 2004. For the limited number of assets placed in service in 2005 and included in the rate base as *pro forma* adjustments,¹⁰ ComEd deducted 2005 depreciation as well when determining rate base values.¹¹

¹⁰ Section 287.40 of Part 287 defines *pro forma* adjustments to the historical test year as “changes affecting the ratepayers in plant investment, operating revenues, expenses, and cost of capital where such changes occurred during the selected historical test year or are reasonably certain to occur subsequent to the historical test year within 12 months after the filing date of the tariffs and where the amounts of the changes are determinable.” (Emphasis added). 83 Ill. Adm. Code § 287.40. Section 287.40 further provides that “[a]ttribution or inflation factors shall not be substituted for a specific study of individual capital revenue, and expense components.” (emphasis added). Consistent with this rule, ComEd made the appropriate, and complete, *pro forma* adjustments to the “Depreciation Reserve for the post-test year plant that comprises its *pro forma* capital additions.

¹¹ The Accumulated Reserve for Amortization and Depreciation (the “Depreciation Reserve”), was \$4,595,475,000, after subtraction of \$9,468,000 assigned to service of reselling municipalities. E.g., Hill Dir., ComEd Ex. 5.0 Corr. at 14:294 293; ComEd Ex. 5.1, Schedule B-1 Errata; Hill Sur., ComEd Ex. 36.0 Corr., Schedule 1 Revised, page 4.

Attorney witness Mr. Effron has proposed an asymmetrical treatment of historic costs and accumulated depreciation for purposes of determining ComEd's rate base. He argues that, because ComEd increased the 2004 test year rate base through *pro forma* adjustments for capital assets placed in service in 2005, an additional year of depreciation expense should be deducted from the historic cost of *all* of the other capital assets in ComEd's rate base.¹² Mr. Effron does not contend that the limited number of *pro forma* adjustments were inappropriate or that ComEd failed to reflect depreciation with respect to the assets in question. Instead, he uses the existence of entirely proper *pro forma* adjustments as an excuse to deduct an additional \$260 million from ComEd's rate base. Mr. Effron's proposed deduction would deprive ComEd of the full cost recovery to which it is entitled, and would violate fundamental test year principles, which are designed to avoid the very type of mismatched rate base values the AG asks the Commission to approve. Mr. Effron's asymmetrical, accumulated depreciation deduction should be rejected.

Mr. Effron's Proposed Adjustment Violates the *Pro Forma* Adjustment Rule and Creates an Improper Mismatching of Revenues and Expenses. Apart from his asymmetrical accumulated depreciation deduction, Mr. Effron proposes no other change to ComEd's test year rate base either because of the 2005 *pro forma* plant additions, or strictly due to the passage of one year's time, as evidenced by the lack of adjustments to eight other rate base line items on his Schedule B-1. Effron Reb., AG Ex. 3.0, Schedule B-1. His proposed adjustment reflects a change to one component of rate base for no supportable reason other than the attrition that has occurred to the book value of ComEd's plant in service at year end 2004 with the passage of one additional year. Section 287.40 specifically provides that "[a]ttrition or inflation factors shall not

¹² Effron Dir., AG Ex. 1.0, 8:8–11. Specifically, Mr. Effron asks the Commission to add another year of depreciation expense (*i.e.*, 2005) to the Depreciation Reserve for distribution plant, effectively making the test year Depreciation Reserve not the 2004 historical test year value, but, for this component of rate base only, a 2005 value. *E.g.*, Hill Reb., ComEd Ex. 19.0 Corr., at 11:245-251.

be substituted for a specific study of individual capital revenue, and expense components.” (emphasis added). Thus, Mr. Effron’s adjustment is a clear violation of the Section 287.40 prohibition of unsupported adjustments for “attrition.”

In addition to violating a specific prohibition in the Commission’s rules, Mr. Effron’s proposed adjustment is one-sided because ComEd has presented a revenue requirement that takes into account *pro forma* additions extending only to plant reasonably expected to be placed in service (and, in fact, in service) by December 31, 2005. ComEd did not propose further additions to rate base, as would be permitted under Section 287.40, for assets placed in service through August 31, 2006. *E.g.*, Hill Sur., ComEd Ex. 36.0 Corr., at 13:283-89. Further, as to the plant additions in 2005 included in rate base, ComEd’s *pro forma* adjustments represent the full, annual rate base impact on the Depreciation Reserve and Accumulated Deferred Income Taxes (both of which are reductions to rate base), even though these plant additions were not in-service for the full year 2005. Hill Sur., ComEd Ex. 36.0 corr., at 12:257-61; Effron, Tr. at 1611:11-18. Mr. Effron proposes to reduce the rate base still further for this one item without regard to the Commission’s test year and *pro forma* adjustment requirements rules. His proposal would result in a one-sided adjustment to ComEd’s rate base, which is in violation of test year principles and the Commission’s rules.

Mr. Effron’s Proposed Adjustment to the Depreciation Reserve Is Contrary to Commission Decisions on this Subject, Given the Facts of This Case. Mr. Effron argues that his proposed adjustment is consistent with Commission decisions in certain past rate cases, Effron Reb., AG Ex. 3.0, 10:21-11:12, but a review of those decisions shows that he is incorrect. At the outset, it is significant that Mr. Effron did not cite ComEd’s last rate case, ICC Docket 01-0423, in which the Commission rejected Mr. Effron’s proposed downward adjustment to the

entire Depreciation Reserve where ComEd had made *pro forma* adjustments for post-test year plant additions. *In re Commonwealth Edison Co.*, ICC Docket 01-0423 at 43 (Order, March 28, 2003) at 43. The Commission rejected that recommendation because the proposal assumed that the entire increase in the Depreciation Reserve was due to plant additions, when in fact it was a change to the entire Depreciation Reserve for all plant -- the same adjustment Mr. Effron is proposing here. *Id.* The Commission also noted that the proposed adjustment would improperly shift the test year into the future only for the Depreciation Reserve value in rate base. *Id.* Here, just as in ComEd's last rate case, the effect of the proposed adjustment would be to shift the test year improperly into the future only for accumulated depreciation. *E.g.*, Hill Reb., ComEd Ex. 19.0 Corr., at 12:254-62.

Ignoring the Commission's Order in Docket 01-0423, Mr. Effron cites *In re Illinois Power Co.*, ICC Docket. 01-0432 (Order, March 28, 2002), *In re Central Illinois Light Co.*, ICC Docket 02-0837 (Order Oct. 17, 2003), and *In re Central Illinois Public Service Co. (AmerenCIPS) and Union Electric Co. (AmerenUE)*, ICC Docket 02-0798, 03-0008, 03-0009 [Cons.] (Order, Oct. 22, 2003), (Effron Reb., AG Ex. 3.0 Corr., 11:3-12) but none of these cases supports Mr. Effron's proposed adjustment. Unlike in this case, the decisions cited by Mr. Effron involve situations in which the Commission found that historical plant in service was either declining or static, requiring further analysis of post test year *pro forma* increases in plant in service to avoid an increase to rate base when, in fact, after netting out the effect of declining plant in service and Depreciation Reserve with the *pro forma* additions, there should have been a decrease in rate base. Here, by contrast, ComEd's net plant in service increased from 2003-2004, and that increase was greater than the amount by which the *pro forma* capital additions

increased net plant.¹³ Thus, the Commission Orders on which Mr. Effron relies do not support, and the relevant facts directly undermine, his proposed adjustment.

In short, as these facts show, the cases cited by Mr. Effron in support of his proposed adjustment do not support it and, instead, given the facts, warrant its rejection. Accordingly, the Commission should reject Mr. Effron's proposed adjustment to the Depreciation Reserve.

2 & 3 General Plant - Functionalization and Amount and Intangible Plant - Functionalization and Amount¹⁴

Overview. Delivering electricity to more than 3 million customers is a capital intensive business. In addition to distribution plant facilities, such as substations, distribution transformers, overhead and underground wires, poles and manholes, it also requires "general" investments, for example, in office buildings, automated communications equipment ("SCADA") that provides data used to reduce the frequency and duration of outages, and for more familiar items like the vehicles used by employees who visit service locations to read meters. There are "intangible" capital investments as well, for example, in computer software used in the systems that provide customer information and that handle billing.¹⁵

¹³ As shown in ComEd Ex. 5.1, at Schedules B-5 and B-6, ComEd is proposing, by virtue of the *pro forma* capital additions, to increase gross plant by \$435,094,000 and net plant by \$312,536,000. These same Schedules show that gross distribution plant increased from \$9,597,741,000 in 2003 to \$10,048,269,000 in 2004, an increase of \$450,528,000, while the depreciation reserve for distribution plant increased from \$4,247,627,000 in 2003 to \$4,383,930,000 in 2004, an increase of \$136,303,000. This means that in one year – 2003 to 2004 – there was an increase in net distribution plant of \$314,225,000. The 2003 to 2004 increase in net plant at ComEd for distribution plant alone exceeds the amount of the increase in net plant that ComEd is proposing by means of the 2005 pro forma adjustments without even considering the 2003 to 2004 net increase in general and intangible plant that can be calculated from the same schedules plus ComEd Ex. 5.1, Schedule C-12, page 1, line 2, and ComEd Ex. 5.2, work paper WPB-1, page 1, lines 13-14.

¹⁴ Although General Plant and Intangible Plant are different categories of plant, some of the parties' testimony regarding these assets is intertwined. So, ComEd will address both sets of costs in this combined discussion.

¹⁵ *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 19:394-402, 19:409 - 20:417, 22:459-471; ComEd Ex. 5.2; DeCampli Dir., ComEd Ex. 4.0 Corr., 39:807-813; Hill Sur., ComEd 36.0 Corr., 23:511-519 and Schedule 7) (discussing both general and intangible assets).

When the Commission first established delivery services rates for ComEd, in ICC Docket 99-0117, it concluded that general and intangible plant presented a complex allocation question. At that time, ComEd was an integrated utility, still owning generating plants and engaged in both the business of producing and the business of delivering electricity. While the company had general and intangible plant investments, there was no simple way to determine precisely how much of the general and intangible plant related to the delivery services business (for which rates were being set) and how much related to the separate generation or “production” business. A significant amount of the testimony in the first delivery services rate case addressed this allocation question, attempting to divide (“functionalize”) general and intangible plant between ComEd’s two businesses.

The need for a complex allocation of general and intangible plant between the delivery service business and the production function has been eliminated in this proceeding, because ComEd no longer owns generating plants and no longer engages in the production of electricity.¹⁶ The general and intangible plant ComEd owned in 2004 all relates to the delivery services business because ComEd has no other business. As a result, there is no need to allocate general and intangible plant between a delivery business and a generation business.¹⁷

ComEd has proved that the general and intangible plant assets that are included in its rate base were prudently acquired, reasonable in cost, and that they are used (exclusively) and useful

¹⁶ *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., 9:173-187; Clark Dir., ComEd Ex. 1.0, at 3:57-58; Lazare Reb., Staff Ex, 17.0 Corr., 16:379-381 (“ComEd was a different utility in 2000 because it still owned generation. ComEd today is solely a transmission and distribution utility.”); Lazare, Tr. at 632:11-17 (the last time that ComEd had significant production capital costs or production operating expenses, not including purchased power expenses, was 2001); *Id.* at 643:7-13 (ComEd is “just a T&D utility” now).

¹⁷ The only allocation task that must be performed is to divide ComEd’s general and intangible plant assets between its Illinois distribution / customer business and its FERC-jurisdictional transmission business. ComEd made such an allocation, which is supported by extensive testimony and exhibits and is uncontested.

to support the delivery services business.¹⁸ No party has identified any general or intangible plant asset in rate base that does not meet those criteria.

Staff and IIEC nonetheless are asking the Commission to remove hundreds of million of dollars of general and intangible plant from ComEd's rate base on the ground that ComEd has not justified the increase over the amount approved in its last rate case, ICC Docket 01-0423, effectively arguing that the increase should be allocated to a generating or production function that does not exist or to no function at all. There is no dispute, however, that ComEd owns the general and intangible plant in rate base, and ComEd's evidence explains how it uses the plant for its delivery services business. Because ComEd does not engage in the generation or "production" of electricity, its general and intangible plant cannot have been used in that business. The "allocation" the Staff and IIEC effectively propose is entirely fictional. The cost of the general and intangible plant that the Staff and IIEC would disallow from ComEd's delivery services business would not end up in a revenue requirement for some non-delivery services business because there is none. Recovery of the cost of that plant would simply be denied forever.

As the evidence and the law discussed in this section demonstrates, the path the Commission must take is clear. If there were evidence that ComEd's general and intangible plant was unreasonably expensive or was imprudently acquired, the Commission could disallow the unreasonable or imprudent portion of the cost. However, no evidence of that type has been presented. Instead, the Commission effectively is being asked to adopt a fictional allocation to deny ComEd recovery of the cost of the general and intangible plant it uses to distribute

¹⁸ The assets in rate base do not include the general and intangible plant assets that support the transmission function. That is uncontested.

electricity to customers and provide customer service. The Commission should reject this fictional allocation and approve the full cost recovery to which ComEd is entitled.¹⁹

ComEd Proved that the General Plant and Intangible Plant Costs Included in Rate Base Belong There. ComEd has shown that the general and intangible plant assets included in its rate base were prudently acquired, that the costs incurred to acquire them were reasonable, and that the assets are used and useful exclusively in providing distribution and customer service.

The evidence of these costs was compelling. John Costello, ComEd's Senior Vice President, Operations, explained the distribution and customer service functions that could not be performed without General Plant and Intangible Plant assets. Costello Dir., ComEd Ex. 3.0 Corr., at 19:395 - 21:443. David DeCampli, ComEd's Vice President, Asset Investment Strategy and Development, showed that, out of the 21 largest capital additions included in rate base since ComEd's 2001 delivery services rate case, six are General Plant assets and five are Intangible Plant assets used to provide distribution and customer service. DeCampli Dir., ComEd Ex. 4.0 Corr., at 1:10-3:48, 16:341-20:413, 37:770-56:1168; ComEd Ex. 4.3 Corr. Mr. Costello and Mr. DeCampli supported the prudence, reasonableness, and the use and usefulness of the general and intangible plant assets in rate base. Jerome Hill discussed the "direct assignment" method ComEd followed to establish the general and intangible plant assets being used for the distribution and customer service "functions." Mr. Hill's explanation of this "functionalization" process addressed each individual General Plant Account and the software systems that comprise Intangible Plant. Hill Dir., ComEd Ex. 5.0 Corr., at 9:179-180, 9:183-188, 10:211-214, 11:221-226, 11:231-13:282, 18:372-22:470; ComEd Ex. 5.1; ComEd Ex. 5.2. See specially his

¹⁹ ComEd is legally entitled to include in rate base plant that is prudently acquired, reasonable in cost, and used and useful. *E.g.*, 220 ILCS 5/9-211; *In re Commonwealth Edison Co.*, ICC Docket 94-0065, 1995 Ill. PUC Lexis at * 5 (Order January 9, 1995), *aff'd in part and remanded in part on other grounds*, 291 Ill. App. 3d 300 (1st Dist.1997).

direct at pages 18-22 and work paper WPB-1. An independent expert, Alan Heintz, provided further support for the direct assignment method described by Mr. Hill, showing that it is the correct approach to functionalize General Plant and Intangible Plant. Heintz Dir., ComEd Ex. 11.0, at 9:181-192, 11:238-240, 13:266-269, 14:289 - 17:361.²⁰

Staff's and the IIEC's Positions Are Not Based on any Facts About ComEd's General Plant and Intangible Plant Assets. Staff and the IIEC largely ignore ComEd's factual showing of its general and intangible plant costs that are properly included in rate base. They have not identified any General Plant or Intangible Plant assets included in rate base that are not prudent, have an unreasonable cost, or are not used and useful in providing distribution and customer service. Staff and the IIEC never even seriously considered the actual assets in ComEd's General Plant and Intangible Plant Accounts.²¹

Staff's Position Is Unsupported by the Evidence and Invalid as a Matter of Law.

Instead, Staff's proposed adjustment is based on the fact that the ICC reduced ComEd's General

²⁰ After Staff and IIEC questioned the level of General Plant and Intangible Plant costs included in ComEd's rate base, ComEd provided additional evidence substantiating its costs and the methodology used to determine them. ComEd also responded to the fictional allocation arguments advanced by Staff and IIEC in support of their positions. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., 3:54-63, 9:173-187, 26:586 - 31:694; Hill Reb., ComEd Ex. 19.0 Corr., 13:280 - 25:554 and Sched. 3, 4, 5, 6, 7, 8, and 9; Heintz Reb., ComEd Ex. 25.0, 5:88-97; Costello Sur., ComEd Ex. 30.0, 1:21-25, 2:38 - 4:81, 12:248 - 14:289, 22:442 - 23:452; Hill Sur., ComEd Ex. 36.0 Corr., 14:291 - 23:523 and Schedules 5, 6, and 7.

²¹ Staff's witness admitted that, while he disagreed with ComEd's "general approach", he had identified no errors in ComEd's Schedules and work papers showing and supporting its direct assignments of General Plant and Intangible Plant. Lazare, Tr. at 633:17 - 634:7. Staff's witness further admitted that he did not specifically examine any of the General Plant and Intangible Plant Accounts, *id.* at 643:14 - 644:12; that General Plant Account 397 - Communications Equipment, which includes \$517,757,458 out of ComEd's \$1,136,816,693 in gross General Plant before functionalization (ComEd Ex. 5.2), includes costs of SCADA, but that he does not know how much, Lazare, Tr. at 647:3-20; and that all but \$5,815,979 of ComEd's gross \$258,767,979 in Intangible Plant before functionalization are costs of six software systems, and that neither he nor any other witness has claimed that ComEd's evidence regarding how those six software systems are used is incorrect. Lazare, Tr. at 644:18 - 646:3; *see also* Lazare, Tr. at 650:16 - 653:7 (including Staff's objection based on Staff's witness' lack of knowledge). IIEC's witness did not review substantial portions of ComEd's evidence on this subject, did not review the documents that ComEd made available in discovery on this subject, and performed only a superficial and incomplete review, which included no analysis of any individual General Plant and Intangible Plant Accounts and assets. *E.g.*, Chalfant, Tr. at 1663:1-11, 1663:16 - 1664:3, 1665:3-14, 1666:3 - 1686:22, 1687:16 - 1688:1, 1688:8-17; ComEd Cross Exs. 10, 11, and 12.

Plant and Intangible Plant costs in the 2001 delivery services rate case by \$405,161,000. *In re Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2003) at 41. *E.g.*, Lazare Dir., Staff Ex. 6.0 Corr., at 2:29-34, 3:61-68, *et seq.* But that reduction has nothing to do with the outcome in this proceeding. The Commission is legally required to base its ruling exclusively on the evidence in the record of this case. *E.g.*, 220 ILCS 5/10-103, 10-201(e)(iv).²² To do otherwise would be reversible error. Staff's witness agreed that, if the evidence in this case warrants a different decision than was made in a past case, the Commission should make that decision. Lazare, Tr. at 655:16-19. Because Staff's proposed adjustment is not supported by the evidence in this proceeding, it must be rejected.²³

The Order in ICC Docket 01-0423 itself rejects the position the Staff is taking here. The Commission stressed that its conclusion on the subject of General Plant and Intangible Plant was:

for purposes of this proceeding only, and without prejudging any issues that may arise in future cases concerning the allocation of general and intangible plant using other test years

In re Commonwealth Edison Co., ICC Docket 01-0423 (Order March 28, 2003) at 41 (emphasis added). *See also* Lazare, Tr. at 634:15 - 635:13; ComEd Cross Ex. 3.

²² Past Commission Orders are not legal precedents, nor are they *res judicata*. *E.g.*, *United Cities Gas Co. v. Illinois Commerce Comm'n*, 163 Ill. 2d 1, 22-23 (1994), *Mississippi River Fuel Corp. v. Illinois Commerce Comm'n*, 1 Ill. 2d 509, 513, (1953).

²³ Staff apparently now seeks to support its position based on the premise that ComEd's January 1, 2001, divestiture of its nuclear plant assets should not have substantially altered the amount of General Plant and Intangible Plant functionalized to Illinois-jurisdictional delivery services. However, when the divestiture took place, ComEd transferred the General Plant and Intangible Plant assets that supported the production function out of ComEd. The General Plant and Intangible Plant that remained at ComEd was only the General Plant and the Intangible Plant supporting the provision of Illinois-jurisdictional delivery services. Hill Reb., ComEd Ex. 19.0 Corr., 19:413-421, 21:463 - 22:493 and Sched. 4 and 7; Hill Sur., ComEd Ex. 36.0 Corr., 14:308 - 15:324 and Schedule 5; Hill, Tr. at 921:7 - 927:2; ComEd Redirect Ex. 3; Hill, Tr. at 921:7 - 927:2; ComEd Redirect Ex. 3. At the evidentiary hearing, Mr. Hill carefully walked through the facts showing that the divestiture did not substantially change ComEd's functionalization of its General Plant and Intangible Plant, and that, instead, in Docket 01-0423, the Commission's Order, by using the general labor allocator rather than ComEd's direct assignments, created a huge incorrect reduction in ComEd's rate base and thus its revenue requirement due to the divestiture. Hill, Tr. at 921:7 - 927:2; ComEd Redirect Ex. 3.

Moreover, even the general “labor allocator” approach used by the Commission in the Order in ICC Docket 01-0423 is inconsistent with the position Staff takes in this proceeding. The evidence is uncontradicted that, if the general labor allocator approach were applied just to ComEd’s General Plant and Intangible Plant additions to rate base since Docket 01-0423, then the General Plant and Intangible Plant costs included in rate base would increase by \$75,993,818. Hill Reb., ComEd Ex. 19.0 Corr., at 25:545-554 and Schedule 9; Hill Sur., ComEd Ex. 36.0 Corr., at 16:345-351. Moreover, if the general labor allocator based on the 2004 test year were applied to all of ComEd’s General Plant and Intangible Plant (not just the additions since Docket 01-0423), then the General Plant and Intangible Plant costs included in rate base would increase by \$137,834,000. Hill Sur., ComEd Ex. 36.0 Corr., at 16:351-359 and Sched. 6.

Staff’s position also overlooks the support in past Commission orders for use of “direct assignment” of costs where feasible, rather than relying on the general labor allocator approach. The Commission’s Order in *Illinois Commerce Comm’n v. Central Illinois Light Co., et al.*, ICC Docket 99-0013 (Order October 4, 2000) at 44, stated: “As a general proposition, the Commission believes that direct assignment of costs is superior to the application of general allocators if the costs are suited to direct assignment and sufficient cost data is available to make direct assignments.” The Order in Docket 01-0423 at 79, when discussing A&G expenses, expressly reaffirmed and quoted that language from the Order in Docket 99-0013.

Finally, Staff’s position is inconsistent with Section 16-111(g) of the Act, 220 ILCS 5/16-111(g), and the Commission’s Order in *Commonwealth Edison Co.*, ICC Dockets 00-0369 and 00-0394 [Cons.] (Order, August 17, 2000). The Commission reviewed and gave advance approval for ComEd’s January 1, 2001, transfer of its nuclear plant assets to Exelon Generation under Section 16-111(g), and part of ComEd’s compliance with the Order was its filing of the

journal entries showing the assets to be transferred, including general and intangible plant assets. Hill Sur., ComEd Ex. 36.0 Corr., at 15:318-19; *In re Commonwealth Edison Co.*, ICC Dockets 00-0369 and 00-0394 [Cons]. (Order, August 17, 2000) at 27. In essence, Staff is now arguing that the asset transfer may be reviewed and revised in this proceeding. Section 16-111(g) prohibits any such action, providing that: “The Commission shall not in any subsequent proceeding or otherwise, review such a reorganization or other transaction authorized by this Section, but shall retain the authority to allocate costs as stated in Section 16-111(i).” Section 16-111(g), (220 ILCS 5/16-111(i) does not authorize Staff’s position).²⁴

The IIEC’s Position Is Unsupported By The Evidence and Invalid as a Matter of Law. The IIEC’s witness presented only superficial discussion of ComEd’s General Plant and Intangible Plant costs. He pointed to the increase from the level of General Plant and Intangible Plant costs approved in Docket 01-0423, incorrectly claimed that ComEd had not presented any valid reason for that increase, and then constructed out of thin air, not evidence, his proposal that the increase in such costs should be limited so as to be proportional to the increase from the level of Distribution Plant costs approved in Docket 01-0423 to the level of approved in this case. Chalfant Dir., IIEC Ex. 2.0, 2:23-27, 2:35-3:43, 6:110-8:157.

IIEC’s position lacks any merit. Indeed, tellingly, after ComEd refuted the IIEC’s testimony here, the IIEC did not even offer any rebuttal testimony on this subject (nor cross-examine any ComEd witness on this subject). First, the IIEC’s simplistic calculations of that increase far overstate the real increase from the 2000 test year to the 2004 test year, as noted above. Second, ComEd proved that its General Plant and Intangible Plant costs included in rate

²⁴ Staff also makes a cursory fall-back argument that ComEd has not justified the increase in General Plant and Intangible Plant assets in rate base over the level approved in ICC Docket 01-0423. Staff’s (and the IIEC’s) calculations vastly overstate the real increase from 2000 to 2004. *E.g.*, Hill Reb., ComEd Ex. 19.0, 23:494-505, 23:514 -24:518, and Schedule 8. In any event, the evidence amply justifies all such assets in rate base.

base belong there, and it presented evidence refuting the IIEC's witness' claims. Third, there is no basis for the IIEC's witness claim that ComEd's evidence is insufficient. Fourth, cross-examination of the IIEC's witness revealed that his analysis and proposal are superficial and are not based on any facts about ComEd's General Plant and Intangible Plant assets. Finally, ComEd demonstrated that that proposed limitation is not supported by the facts, there is no valid basis for making such a linkage, and that, properly calculated, the increase in General Plant was not out of line with the IIEC's witness' novel theory, in any event. Hill Reb., ComEd Ex. 19.0, Corr.; 23:506-24:526 and Schedule 8; *see also* Heintz Reb., ComEd Ex. 25.0, 5:88-97. The IIEC's proposal is not supported by, and instead is contrary to, the evidence in the record. It should be rejected.

CES' Position Is Unsupported By The Evidence. CES, in its rebuttal testimony, offered only wholly conclusory testimony on this subject. *See* O'Connor/Domagalski Reb., CES Ex. 5.0, 7:150-8:168. CES' proposal to move some of these costs to the Supply Administration Charge ("SAC") should be rejected. ComEd has proved its General Plant and Intangible Plant costs included in rate base belong there. CES has not shown that any of those costs (or any A&G expenses included in operating expenses) are costs of the production function. Hill Dir., ComEd Ex. 5.0 Corr., 24:521-523; ComEd Ex. 5.2 WPC-1b; Crumrine Dir., ComEd Ex. 9.0 Corr., 46:1008-47:1013; Alongi/McInerney Dir., ComEd Ex. 10.0, 3:62-63, 15:372-16:383; ComEd Ex. 10.7; Hill Sur., ComEd Ex. 36.0 Corr., 37:832-38:855.²⁵

²⁵ ComEd agrees, however, that if Staff's incorrect and unlawful proposed adjustment were to be adopted, then, because it is based on the functionalization determination made in Docket 01-0423, the Commission would need to approve use of the SAC or some other mechanism to enable ComEd to recover fully those removed costs, including a reasonable rate of return. ComEd believes that it would make the most sense to use a mechanism other than the SAC, one that applies to all retail customers, for the same reasons ComEd has discussed as to its procurement case expenses, addressed in Section III.B.9 of this Initial Brief.

4. Pension Asset

In March 2005, Exelon contributed \$803 million in equity to ComEd to enable it to “fully fund” its portion of the Exelon pension plan. Mitchell Dir., ComEd Ex. 7.0, at 8:160-162. Exelon obtained the funds for the \$803 million equity infusion by issuing debt and obtaining tax benefits from the contribution. Mitchell Dir., Com Ed Ex. 7.0, 8:170-9:173. ComEd used the \$803 million equity infusion to contribute \$803 million to the ComEd portion of the Exelon pension plan. Mitchell Dir., ComEd Ex. 7.0, 8:170-9:173. Without the equity infusion from Exelon, ComEd would have had to issue additional debt itself, which would likely have resulted in a downgraded credit rating. Mitchell Dir., ComEd Ex. 20.0, at 17:347-357.

The effect of the Exelon contribution of \$803 million is included as an asset in rate base to allow the Exelon shareholders and bondholders who financed the loan to recover their costs. Houtsma, Tr. at 521:13-19.²⁶ Because the contribution of the funds will generate additional pension trust fund earnings, the \$803 million contribution also results in a decrease in jurisdictional pension expense of approximately \$30 million, which has been reflected in ComEd’s rate request. Houtsma, Tr. at 469:16-22; Mitchell Dir., ComEd Ex 7.0, at 9:187-189.

No party claims that fully funding the pension plan was imprudent or unreasonable, nor could they. Recent history has shown many examples where major corporations ran into trouble after funding their pension plans at minimum levels and then finding themselves, for whatever reason, in financial distress and unable to meet their pension commitments. Tierney Reb.,

²⁶ With the \$803 million cash contribution, the amount of the pension asset is \$853 million. Hill, ComEd Ex. 5.1 Appendix A, Sched. B-1, page 1 of 2. At December 31, 2004, ComEd already had a net pension asset on a jurisdictional basis of \$138.9 million. Id. As a result of Exelon’s \$803 million cash contribution to ComEd in March 2005, after pro-forma adjustments to reflect the portion of the \$803 million contribution (\$716 million) allocable to delivery services Mitchell Dir., ComEd Ex. 7.0: 191-192, and the allocation of an additional \$2 million to reselling municipalities, a jurisdictional pension asset was created of \$853 million (Hill, ComEd Ex. 5.1 Appendix A, Sched. B-1, page 1 of 2). After reflecting \$214.6 million of accumulated deferred income taxes, the net rate base effect of the pension asset is \$639.3 million.

ComEd Ex. 22.0, 12:255-13:273. Moreover, employees are keenly aware of troubles experiences by companies that have not adequately funded pension plans and now have a heightened awareness of funded status. Mitchell Reb., ComEd Ex. 20.0, at 23:478-489. Perverse financial incentives would be created by adopting adjustments that would encourage the utility to fund only the minimum requirements for a pension plan and in fact deny it cost recovery when it prudently funds more than that level. Tierney Reb., ComEd Ex. 22.0, at 12:246-49; Mitchel Reb., ComEd Ex. 20.0, at 23: 89-95.

Notwithstanding these important considerations, Staff witness Ms. Ebrey recommends not only that the pension asset be removed from ComEd's rate base, but that the reduced annual pension expense which the contribution made possible nonetheless remain. AG witness Mr. Effron recommends removing the pension asset from ComEd's rate base, but agreed that the costs of the contribution should be recovered through rates. Thus, he proposed to add to jurisdictional operating expense approximately \$27 million, representing Mr. Effron's estimate of the interest expense associated with \$803 million in debt.

The Commission should approve inclusion of the pension asset in rate base, and provide ratepayers with the corresponding benefit of the approximately \$30 million in reduced annual pension expense which that asset makes possible, because it is the right thing to do, and is good regulatory policy. Unless the pension asset is included in rate base, shareholders will not receive a return on the funds which they have invested in the pension plan prior to collection of these amounts from customers. This would be unfair and confiscatory. Moreover, without inclusion in rates of both the pension asset and the lower pension expenses made possible by the contribution that created that asset, ComEd rates will not appropriately reflect the cost to provide

service to ratepayers. ComEd's retail customers should support legitimate costs incurred to provide them with electric service . Tierney Sur., ComEd Ex. 39.0, 4:82–5: 94.

a) **Funding The Pension Plan Was Prudent, and the Cost of That Funding Should be Included In Cost of Service**

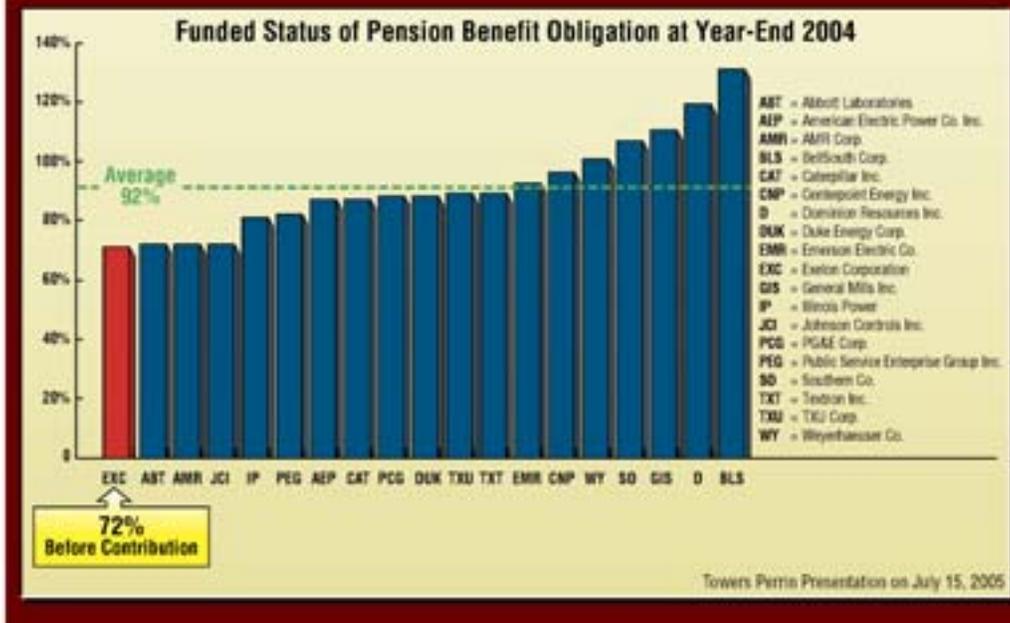
ComEd's \$803 million pension contribution in March 2005 was part of a larger effort by Exelon to fund its pension plan for all employees. Most of Exelon's employees (including all ComEd employees) participate in a corporate-wide pension plan Exelon announced last fall that it would make a \$2 billion contribution to its pension plan because it was the right thing to do, and Exelon had the financial strength and resources to do it. Mitchell Dir., ComEd Ex. 7.0 at 8:164-68. Mr. Mitchell stated directly: "We view the pension funding as a fiduciary responsibility." Mitchell Dir., ComEd Ex. 7.0, at 8:168.

The \$2 billion total contribution was ultimately funded through \$1.4 billion of Exelon debt and \$600 million in tax benefits resulting from the contribution. Of the \$2 billion of pension funding, \$803 million related to ComEd employees, and Exelon contributed \$803 million to ComEd as equity, which ComEd, in turn, contributed to the pension plan. Mitchell Dir., ComEd Ex. 7.0, 8: 170-9:173.

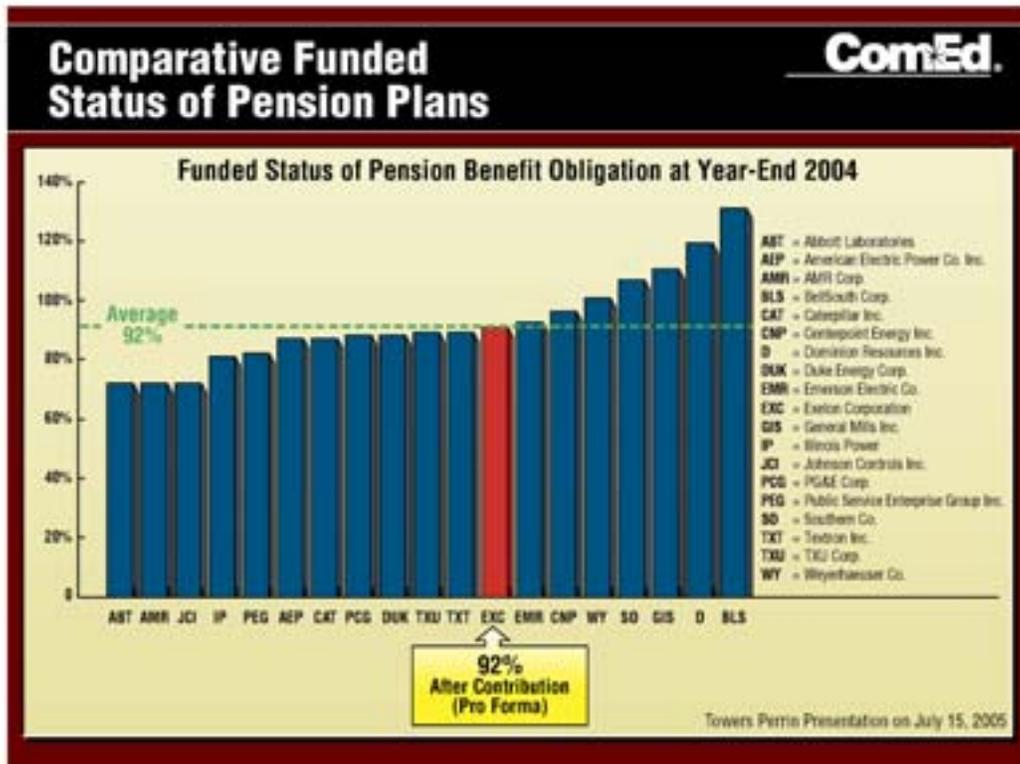
The decision to fund the plan was prudent and reasonable. A comparison of the funding status of the pension plan (in which ComEd participates) before and after the contribution to the funding status of other employers with large pension plans demonstrates that, prior to the \$803 million contribution, the 2004 funding status of the plan was at the very low end of the spectrum, as revealed by the following chart:

Comparative Funded Status of Pension Plans

ComEd.



After the contribution, the pension plan’s funding status was more in line with that of other companies and ComEd’s own goals for itself. The analogous chart, after the contribution, shows:



Mitchell Sur., ComEd Ex. 37.0 Corr., at 26: 528–28: 540.

As a result of the pension contribution, the ComEd pension plan was “fully funded.” The minimum pension liability, as prescribed by GAAP, is based on the Accumulated Benefit Obligation (ABO) funded status of the plans. Based on this measure of funded status, the pension plans from which ComEd employees participate had the following funded status (Assets/Liabilities) at the indicated time periods shown below:

December 31, 2004 – 79%

December 31, 2004 including the 2005 contribution – 101%

Mitchell Reb., ComEd Ex. 20.0, at 21:437-443. Thus, after the contribution, the Accumulated Benefit Obligation of the plan was approximately equal to (within 1% of) the funds available to meet the obligation.

The \$803 million contribution created a pension asset on ComEd's books for at least two reasons. From an accounting point of view, the pension asset represents a net prepayment position on ComEd's balance sheet related to future pension obligations. This prepaid position arises because the majority of the amount recently funded relates to pension obligations that have not yet been recognized in ComEd's financial statements. These are primarily unrecognized net actuarial losses which will be recognized in ComEd's pension expense in future periods as required by Statement of Financial Account Standard No. 87 – Employer's Accounting for Pensions. Mitchell Dir., ComEd Ex. 7.0, at 10:195-201.

From a regulatory point of view, the pension asset represents funds contributed by shareholders to satisfy future pension obligations in an amount above and beyond what has previously been collected from customers through rates. Houtsma, Tr. at 468:12-17. By including the asset in rate base, ComEd is asking for a return on these shareholder supplied funds that have been invested prior to collection of these amounts from customers. Houtsma, Tr. at 469:5-8. *See also* Mitchell Dir., ComEd Ex. 7.0, at 10:202-09. The regulatory obligation to provide shareholders with such a return is unaffected by whether the corresponding pension liabilities remain, as they now are, on Exelon's books, or whether they instead are recorded on ComEd's books. Houtsma Reb., ComEd Ex. 18.0, 16:344-17.366; Heintz Reb. ComEd Ex. 25.0, 26:523-31.

Although the \$803 million pension contribution resulted in a pension asset of \$853.9 million that is reflected in ComEd's rate base, it significantly reduced jurisdictional pension expense. By funding the pension in early 2005, investment returns earned by the pension trust funds will increase, which in turn will reduce ComEd's jurisdictional pension expense by

approximately \$30 million. ComEd included this reduction as a pro-forma adjustment to the 2004 test year. Mitchell Dir., ComEd Ex. 7.0, at 9:187-90.

b) The Accounting and Policy Issues Raised by Staff Witness Ebrey and AG Witness Efron Are Without Merit

(i) Pension Asset

(1) Staff Witness Ms. Ebrey

Pension Asset Not Offset By Pension Liability

Ms. Ebrey's first ground for opposing inclusion of the pension asset in rate base is that, in her view, no pension asset exists at all. Ms. Ebrey's theory is that under Statement of Financial Accounting Standards No. 87 ("FAS 87"), para. 35, a pension asset "is the amount by which a pension plan is over funded." Ebrey Dir., Staff Ex. 2.0, at 4:59-61. Thus, she maintains, there is no pension asset here because after the contribution, ComEd's plan was fully funded, not overfunded. Ebrey Dir., Staff Ex. 2.0, 4: 66-69. Put another way, in her view, because the pension liability recorded on Exelon. Ebrey Dir., Staff Ex. 2.0 7:125-8:154; Ebrey Reb., Staff Ex. 13.0, 5:87-6:104.

Ms. Ebrey's theory regarding the creation of and accounting for the pension asset is not only fundamentally misconceived and incorrect but, at bottom, irrelevant. Ms. Houtsma explained that a pension asset can arise in a variety of ways. One way is where funds have been contributed in excess of the obligation. This is the way of creating a pension asset on which Ms. Ebrey is focused. Another way not applicable here is where the trust fund that is used to satisfy the future obligations has generated better-than-expected asset returns, so that the available funds in the trust fund are greater than the existing obligations. Houtsma, Tr. at 471:4-11. A third way, and the one that applies in this rate case, is where the pension asset represents funds that have been contributed to a pension fund by shareholders and bondholders to satisfy future

pension obligations in an amount above and beyond what has previously been collected from customers through rates. Houtsma, Tr. at 468:13-17.

In this proceeding, there is no dispute that the funds which made the pension contribution possible were not provided by ratepayers Houtsma, Tr. at 468:18-20, but instead were provided by Exelon shareholder and bondholders. Houtsma, Tr. at 521:13-19. Thus, by including the asset in rate base in this proceeding, ComEd is simply asking for a return on the funds that have been invested by shareholders and bondholders prior to receipt of those funds from ratepayers. Houtsma, Tr. at 469:5-8, Tr. at 521:13-19. Moreover, because the contribution was funded by shareholders and bondholders, the pension asset exists for ratemaking purposes regardless of whether the pension liability related to the contribution is accounted for on Exelon's books or ComEd's books. Ms. Ebrey's belief that the pension liability which the contribution funded should be an offsetting deduction from rate base that would make the pension asset disappear (Ebrey Dir., Staff Ex. 2.0, 7:128 – 8:154) is incorrect. As Ms. Houtsma testified, liabilities that are deducted from rate base represent amounts that have been collected from customers through rates in advance of their application to satisfy a given obligation.²⁷ Houtsma Reb., ComEd Ex. 18.0 Corr., at 16:348-350. But here, although the additional liability referred to by Ms. Ebrey was recorded by Exelon in accordance with FAS 87 as an increase in the pension liability, it has never been recognized in ComEd's pension accruals, and has never been included in ComEd's cost of service for ratemaking purposes. Because it has not previously been reflected in cost of service, and it does not reflect any ratepayer supplied funds, there is no basis to deduct this

²⁷ For example, historically ComEd has deducted accumulated deferred income taxes from rate base because deferred income tax expense is included as a component of operating income and as such the customer, in effect, supplies funds necessary to meet ComEd's tax obligations in advance of when ComEd will actually be required to pay the tax obligations. Because these customer supplied funds can be used to meet ComEd's service obligations, thereby reducing the amount of the rate base that must be supported by external capital, the deferred liability is reflected as a deduction from rate base. Houtsma Reb., ComEd Ex. 18.0 Corr. At 16:350-357.

liability from rate base, regardless of whether it is accounted for on ComEd's financial statements or Exelon's financial statements. Houtsma Reb., ComEd Ex. 18.0, 16:344 – 17:366; Houtsma Sur., ComEd Ex. 35.0 Corr., 24:523-531.

Ms. Ebrey's apparent belief that the asset on ComEd's books was created by accounting entries only is another manifestation of her mistake as to how the asset was created. Ebrey Dir., Staff Ex. 2.0, at 6:103-104. Although it is correct that if the pension liability was recorded (or pushed down) on ComEd's books for accounting purposes, rather than Exelon's, ComEd's pension assets and liabilities would offset and ComEd would no longer have a net pension asset for accounting purposes, *for ratemaking purposes* it would not be appropriate to reduce rate base by the amount of the pushed down pension liability. As previously explained, the pension asset would remain for ratemaking purposes because the liability has not been recovered through customer rates.²⁸ Houtsma Reb., ComEd Ex. 35.0 Corr., at 24:531-35.

Ms. Ebrey further suggests that the pension asset is not real when she argues that the pension asset, and the capital contribution made by Exelon to provide ComEd with the cash to fund the pension contribution, both "disappear" in the financial consolidation process and do not appear on Exelon's books. Ebrey Reb., Staff Ex. 13.0, 6:107 – 7:123. This observation is not relevant. The effects of virtually all intercompany transactions are eliminated upon consolidation of Exelon's financial statements. This fact does not relieve ComEd of the obligation associated with those transactions. For instance, ComEd has a payable to BSC at the end of any month related to the services it receives from BSC. BSC records a corresponding

²⁸ Several parties – particularly BOMA – appear to be under the impression that because, when the \$803 million contribution was made (March 31, 2005), the plan was fully funded, ComEd's pension obligation was "eliminated". Houtsma, Tr. at 494: 4-12. This pension obligation elimination theory is incorrect for much the same reasons as explained above, i.e., because the pension contribution was made with funds supplied by shareholders and bondholders, it would continue to exist, and be a valid addition to rate base, regardless of whether the plan was, at the time of the contribution, fully funded, and regardless of whether some of the pension obligations are on Exelon's books but not on ComEd's books. Houtsma, Tr. at 495: 1-4.

receivable from ComEd for those services. When Exelon's financial statements are consolidated, the ComEd payable and the BSC receivable are offset against each other, and Exelon does not report either a receivable or payable. But ComEd's obligation did not disappear or cease to exist; it is simply offset, for financial reporting purposes, by corresponding items on Exelon's financial statements. Thus, the fact the pension asset "disappears" in the financial consolidation process is simply the result of required consolidation accounting practices under GAAP; it does not make the pension asset any less real. Houtsma Sur., ComEd Ex. 35.0, at 24:536 – 25:556.

Pension Funds Not Within Company's Disposition

A second reason given by Ms. Ebrey for disallowing the pension asset is that it does not represent funds within the Company's disposition and in which it has an interest. Ebrey Dir., Staff Ex. 2.0, at 9:169-183. But as Mr. Mitchell pointed out, under federal law, amounts contributed to the pension trust must be used exclusively to provide pension benefits. Mitchell Reb., ComEd Ex. 20.0, at 24:508-11. Similarly, Dr. Tierney testified that to penalize a utility by not allowing cost recovery of its pension funds because these funds are not "funds within the Company's disposition" is inconsistent with the intent of direct contribution pension plans as well of the expectations of the workforce benefited by them. Tierney Reb., ComEd Ex. 22.0, at 14:290-300. The Commission has consistently provided recovery to utilities of employee pension benefits, without regard to the fact that these benefits are provided through contributions to pension trust funds that, by law, cannot be accessed for general corporate purposes. Mitchell Reb., ComEd Ex. 20.0, at 24:511-14.

Furthermore, the pension trust funds generate investment income that reduces the amount of pension expense that is included in cost of service. In this regard, customers receive the

benefit from these trust funds despite the fact that the trust funds are not available for other corporate purposes. Indeed, as discussed in more detail, infra, despite the fact that she does not believe customers should provide a return on the pension contribution, Ms. Ebrey believes that customers should receive the benefit of the reduction in pension expense that the contribution generates. Mitchell Reb., ComEd Ex. 20.0, 24:508 – 25:522.

Discretionary Nature of Pension Contribution

A third reason given by Ms. Ebrey for opposing the inclusion of the pension asset in ComEd's rate base is "the discretionary nature of the pension contribution." Ebrey Reb., Staff Ex. 13.0, at 5:84-85, 8:147-159; Ebrey Dir., Staff Ex. 2.0, at 9:184 – 11:122. This position is shortsighted and incorrect.

At the outset, as Ms. Ebrey admitted (Ebrey Tr. 1891:9-17), it has never been the position of this Commission that a criterion for including an asset in rate base is that its creation was not discretionary. As long as the asset is used and useful and acquired at a reasonable and prudent cost, that asset goes into rate base. (Ebrey Tr. 1891:18-22). No party has challenged that the contribution to fully fund the pension obligation was reasonable and prudent.

In any event, at bottom Ms. Ebrey's argument is that shareholders should not be compensated for actions by ComEd and Exelon that go beyond the minimum pension funding requirement in the law. The effect, Ms. Tierney testified, is to discourage use of best practices with respect to pension funding. Tierney Reb., ComEd Ex. 22.0, at 11:223-28.

Mr. Mitchell also testified that although the timing of the funding involved some discretion, ultimately ComEd has a legal obligation to fund its pension obligations to its employees. To say that ComEd's decision to fund its pension obligations is "voluntary" does not properly characterize the nature of the payment and the obligation. Pension contributions would

have eventually been required and would have been even higher. Additionally, by making the payments earlier than legally required, ComEd's pension expense will be reduced and ComEd employees and retirees in Illinois are protected against the loss of their hard-earned pension benefits. Mitchell Reb., ComEd Ex. 20.0, at 25:527-34.

Further, Staff's position also fails to take into account the impact on workers of discouraging a utility from fully funding the pension plans on which its employees' retirement benefits depend. Employees consider ComEd's complete compensation package when deciding whether to work for or continue working for ComEd. A pension is a major part of that package and, thus, is a major part of attracting and retaining employees who have the experience and expertise to provide reliable service. Employees are well aware of troubles experienced recently by other companies that have not adequately funded pension plans and now have a heightened awareness of funded status. Mitchell Reb., ComEd Ex. 20.0, at 23:478-489. Thus, disallowing recovery of pension plan costs on the theory that ComEd had discretion to do the minimum is not appropriate, and the Commission should reject that approach. Mitchell Sur., ComEd Ex. 37.0 Second Corr., at 36:517-525.

Cost Impact Of Pension Asset Outweighs Benefit

A fourth argument made by Ms. Ebrey is that the customer impact of including the pension asset in rate base outweighs the benefit of the lower pension expense that results from the contribution, and therefore that the contribution is detrimental to customers and should not be included in rate base. Ebrey Reb., Staff Ex. 13.0, 9:157 – 10:192. This argument is incorrect.

An expenditure should not be excluded from cost of service solely because its inclusion would increase rates. Virtually all expenditures have the effect of increasing rates, but if they are reasonably and prudently incurred costs they should be reflected in the rate setting process. In

prior years, customers have received the benefit of substantial rate base deductions due to unfunded pension liabilities. In the last rate case, for example, the rate benefit of the unfunded pension liability deducted from the rate base more than offset the pension expense. Houtsma Sur., ComEd Ex. 35.0, 25:561-526:567. Here, ComEd has shown that funding the pension obligation now was reasonable and prudent. Therefore, shareholders and bondholders should be compensated for providing the funds that made the contribution possible.

(2) **AG Witness Mr. Effron**

Attorney General witness Mr. Effron's proposal is to remove the pension asset from rate base, but to add to jurisdictional operating expense approximately \$27 million, roughly equivalent to the after-tax interest expense associated with \$803 million in debt. Effron Dir., AG Ex. 1.0, 12:15 – 14:10. Mr. Effron's proposal attempts to compensate ComEd for the cost of the contribution, and thus is more reasonable than Staff's asymmetrical proposal completely to disallow the pension asset but preserve the lower pension expense that asset makes possible, discussed *infra*. At bottom, however, Mr. Effron's proposed disallowance should also be rejected.

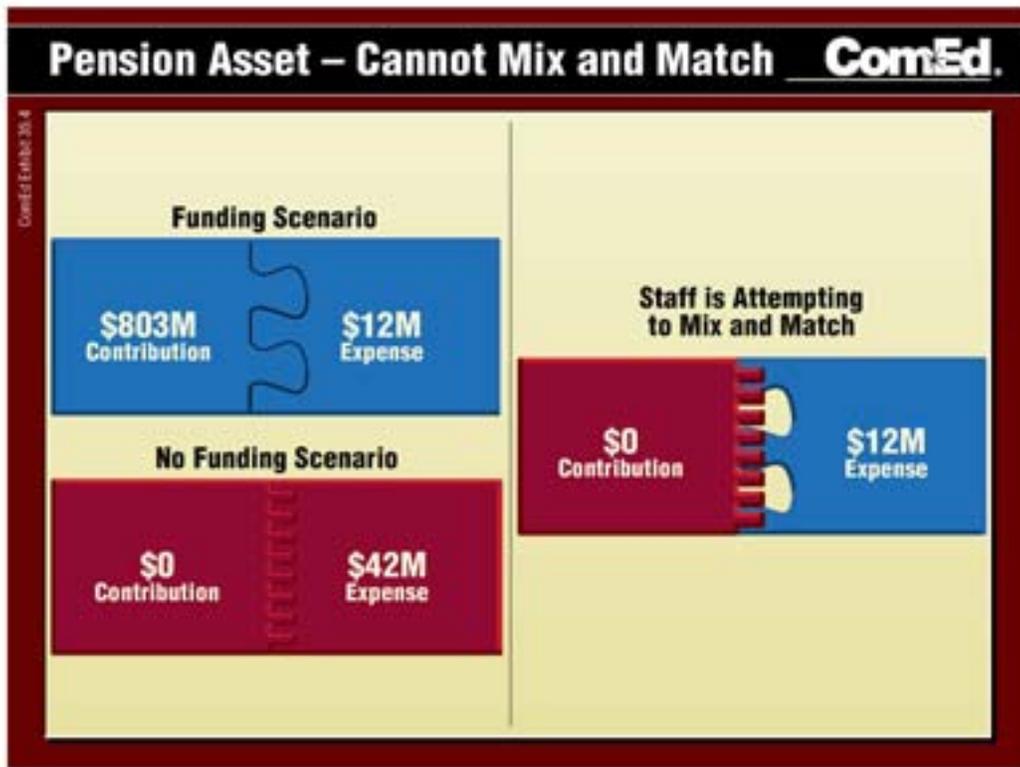
The contribution ComEd made to its pension was not funded by a debt issuance at ComEd. ComEd received an equity contribution from Exelon for a valid business purpose. As Mr. Mitchell explained, if the pension obligation had been funded by ComEd with debt, it would have put ComEd in a position similar to the one it was in before the 2004 Accelerated Liability Management program debt reduction efforts, and because its financial ratios would not have been within the S&P ranges for an A credit rating, it is likely ComEd's credit would have been downgraded. In other words, it would have effectively undone most of what Exelon needed to accomplish through the debt reduction program. Mitchell Reb., ComEd Ex. 20.0, at 17:347-557.

Maintaining acceptable credit ratings is important, and a failure to do so can have adverse consequences in terms of access to capital and the cost of capital. Entering into a period of competitive procurement of power beginning on January 1, 2007, there is even further justification for the need to maintain strong credit ratings to enable ComEd to obtain commercially reasonable terms on supplier contracts. Mitchell Reb., ComEd Ex. 20.0, at 20:415-24. Thus, for these reasons, the \$803 million is equity to ComEd and should be treated as such, and the costs ComEd recovers should match the return afforded for that source of capital. Mitchell Reb., ComEd Ex. 20.0, 18:378 – 19:390.

(ii) Pension Expense

(1) Staff Witness Ms. Ebrey

The other major pension-related issue raised by Ms. Ebrey is the appropriate treatment of pension expense. The annual pension expense level of \$11.7 million that ComEd seeks to recover is directly related to the decision to fund the \$803 million pension obligation. Ms. Ebrey proposes to disallow the pension asset arising from the pension funding from rate base, but seeks nonetheless to reflect in rates the pension expense level of \$11.7 million resulting from the contribution. This attempt to “have it both ways” is fundamentally unfair and at odds with ratemaking principles that treat costs and benefits consistently, as shown by the following chart:



ComEd Ex. 35.4. *See also* Tierney Reb., ComEd Ex. 22.0, at 15:321-22.

By fully funding the pension obligation, ComEd reduced its 2005 pension expense by \$30 million. Houtsma Reb., ComEd Ex. 18.0, at 17:371-72; Mitchell Reb., ComEd Ex. 20.0, at 25:539-40. This \$30 million reduction in expense is offset in part by changes in 2005 actuarial assumptions that result in a net 2005 jurisdictional pension expense of \$11.7 million (rounded off to \$12 million in the chart). But if the \$803 million pension contribution had not been made, 2005 pension expense would have been \$41.9 million, or \$30 million higher than the \$11.7 million pension expense supported by Ms. Ebrey. Thus, at the very minimum, if the Staff's proposed rate base disallowance of the \$803 million pension contribution were adopted, ComEd's test year pension expense would have to be increased from \$11.7 million to \$41.9 million to remove the benefit associated with the contribution. Houtsma Reb., ComEd Ex. 18.0, at 18:382-388.

Ms. Ebrey's testimony ignores these realities. Ms. Ebrey agreed on cross-examination that “all else equal”, the net change in test year pension expense of the contribution was a \$30 million reduction. Ebrey, Tr. at 1888:1-13. But despite this admission, Ms. Ebrey has not indicated that she has abandoned her argument that if the contribution had not been made, the revenue requirement would only have been \$8.6 million higher. Ebrey Reb., Staff Ex. 13.0, 9:180-10:192. This is plainly wrong. Ms. Ebrey arrived at the \$8.6 million figure by subtracting the 2004 pension expense of \$33.3 million from \$41.9 million, which is what the 2005 pension expense would have been had the contribution not been made. However, this year over year comparison is not what the change in pension expense would have been if the contribution had not been made, as shown on ComEd Exhibit 35.3 to Ms. Houtsma’s surrebuttal testimony. Houtsma Sur., ComEd Ex. 35.0, 26:571-27:593. Instead, the \$8.6 million is the net increase in pension expense in 2005 due to factors other than the pension contribution. For instance, in addition to the positive impact of the pension contribution, the 2005 pension expense was adversely impacted by lower than expected 2004 asset returns, a lower discount rate used to calculate the costs, and changes in normal FAS 87 actuarial assumptions. These adverse impacts, which total \$8.6 million, are unrelated to and would have occurred regardless of the pension contribution.

Ms. Ebrey further asserts that the positive impact on pension expense from the contribution that is reflected in the 2005 actuarial study should flow to customers in spite of her position that customers should not pay for the cost of funding that contribution. Ebrey Reb., Staff Ex. 13.0, at 11:205 – 12:235. This would be unfair and unjust. Towers Perrin, ComEd’s actuaries, included the impact of the pension contribution in the 2005 actuarial study because it had been made at the time the estimates were prepared. The fact that the pension contribution is

included in the study does not automatically mean that it should be included in rates. It is inappropriate simultaneously to disallow recovery of the cost of the contribution in rates, and include the benefit of that contribution in the form of lower pension expense. This is not “back-pedaling” as claimed by Ms. Ebrey. Houtsma Sur., ComEd Ex 35.0, 617-618. Instead, Ms. Houtsma testified, it is following the long-standing and widely recognized ratemaking principle that costs and benefits should be treated symmetrically. Houtsma Sur., ComEd Ex 35.0, at 28:618-619.

Ms. Ebrey argues that her treatment of pension expense is consistent with prior Commission orders holding that pension expense should be updated based on the latest actuarial valuation. Ebrey Dir., Staff Ex. 2.0, at 13: 262-268; Ebrey Reb., Staff Ex. 13.0, at 12: 231-235. Ms. Ebrey misapplies the Commission decisions in those orders. ComEd agrees that an updated actuarial analysis can provide an appropriate basis for a known and measurable test year adjustment and, in fact, test year data was updated to reflect the latest actuarial analysis. Hill Dir., ComEd Ex. 5.0 Corr. at 36:777-780. The problem with Ms. Ebrey’s approach, however, is that it is unjustifiably asymmetrical, in that she seeks to take advantage of a lower pension expense, whether updated or not updated, made possible only by the pension asset she seeks to disallow.

Ms. Ebrey also asserts that her asymmetrical treatment of the pension contribution and pension expense is consistent with prior commission orders (Ebrey Dir., Staff Ex. 2.0, at 14:272-280), but this is equally incorrect. Although in the recent Nicor Gas rate case cited by Ms. Ebrey (Docket 04-0779), the Commission disallowed the requested pension asset from rate base, and at the same time allowed a pension credit to reduce operating expense, the circumstances resulting in the pension asset were quite different – and meaningfully so – from the circumstances in this

case. In the Nicor Gas proceeding, the Commission determined that the pension asset should not be included in rate base because it arose from ratepayer supplied funds. The Commission first noted that in Nicor Gas' last general rate case, ICC Docket 95-0219, the Commission found that eliminating Nicor Gas' net pension asset from rate base "is consistent with past Commission orders which found that the overfunded pension asset was created from ratepayer supplied funds." *Northern Illinois Gas Co.*, ICC Docket 04-0779 (Order Sept. 20, 2005) at 22. In that Order the Commission then held:

Nicor has not presented any additional evidence since the 1996 Order to show why the Commission should arrive at a different conclusion now. It remains true that the pension asset was created by ratepayer-supplied funds, not by shareholder-supplied funds.

Id. at 23.

The circumstances with ComEd's pension asset are quite different. Here, the funds are shareholder-supplied funds, and the liability that was funded has not previously been recognized in cost of service. It is undisputed that customers have not provided the source of funds for the pension contribution. Therefore, the Nicor Gas ICC Docket 04-0779 Order is not precedent for how the pension asset and related expense reduction should be treated in this proceeding. *Houtsma Reb.*, ComEd Ex. 18.0, at 19:407-419.

The Commission's decision in the GTE case cited by Ms. Ebrey (*GTE North Inc.*, ICC Docket 93-0301/94-0041 [cons.], 1994 Ill. PUC Lexis 436 (Order Oct. 11, 1994)) is equally off the mark. There, as in the *Nicor* Order in Docket 04-0779, the Commission held that "[t]o require ratepayers to now pay a further return *on an asset they have created through rates* would be unreasonable and is rejected." *Id.* 1994 Ill. PUC Lexis 436 at *25 (emphasis added). As shown, the pension asset at issue in this proceeding was not created through rates.

At the hearings, Staff effectively conceded that neither of these cases apply to the circumstance present here. At the close of his recross of Ms. Houtsma on the pension asset issue, counsel for Staff asked, “That’s the point of my question. This is a case of first impression, isn’t it?”, to which Ms. Houtsma replied, “I’m not aware of a similar situation.” Houtsma, Tr. at 524:22 – 525:2.

In summary, the Commission should approve the pension asset, in which event the appropriate pension expense is \$11.9 million. But if, despite substantial record support, the Commission were nonetheless not to include the pension asset in the rate base, the jurisdictional pension expense should be \$41.9 million. Houtsma Sur., ComEd Ex. 35.0, 28:626 – 29:635.

(2) **AG Witness Mr. Efron**

AG witness Mr. Efron proposes an adjustment to pension expense to recognize a full year’s effect of the pension contribution. Efron Dir., AG Ex. 1.0, 23:10-24:2. As described earlier, the pension contribution was made in March 2005, and the increase in investment returns due to that contribution will reduce pension expense by \$30.2 million in 2005, which has been reflected in test year pension expense. Mr. Efron suggests that a full year’s effect of the pension contribution should be reflected, even though that effect will not be realized until 2006. *Id.*, at 23:18-19. As described earlier, many factors affect pension expense and are factored into an actuarial analysis, including discount rates, demographic experience, asset returns and other normal actuarial changes. All of these factors will impact 2006 pension expense, and Mr. Efron’s proposal to slice out just one of these factors is inappropriate and one-sided. Hill Reb., ComEd Ex 19.0 Corr., at 37:814-38:829.

5. Accumulated Deferred Income Taxes

ComEd's final revised proposed rate base figure includes a correctly calculated final revised figure of \$1,408,375,000 for Accumulated Deferred Income Taxes ("ADIT"). Hill Sur., ComEd Ex. 36.0 Corr., Sched. 1. ADIT is subtracted from plant balances in calculating rate base. (*See, e.g., id.*) Because Staff and certain intervenors propose adjustments to ComEd's plant balances in its proposed rate base, they also propose entirely derivative adjustments to ComEd's ADIT figure. However, because their underlying proposed adjustments to ComEd's plant balances are without merit, as discussed in the applicable sections of this Brief, their entirely derivative adjustments to ComEd's ADIT figure also are without merit. ComEd's ADIT figure should be approved. Staff's and intervenors' adjustments should not be approved.

6. Customer Deposits

Staff proposes to reduce ComEd's proposed rate base by \$31,477,000 (along with a related increase of \$412,000 in operating expenses) based on the theory that customer deposits are a "cost-free source of capital". Ebrey Dir., Staff Ex. 2.0, at 28:572-83 and Sched. 2.6; Ebrey Reb., Staff Ex. 13.0, at 25:520-26:537 and Sched. 13.5. Staff's proposal lacks merit, is inconsistent and unfair, and should be rejected.

First, Staff's proposal is unwarranted and one-sided. Customer deposits are a short-term liability on ComEd's books, and so customer deposits are just one of the many components that comprise ComEd's cash working capital requirements. Hill Reb., ComEd Ex. 19.0 Corr., at 25:560-62. ComEd has not included, however, cash working capital requirements in its proposed rate base. *E.g.*, ComEd Ex. 5.1. Thus, Staff has selectively picked just two components of cash working capital, customer deposits and the budget payment plan balances discussed in the next subsection of this Brief, to incorporate in ComEd's rate base. Significantly,

both cash working capital components that Staff has chosen would reduce rate base, ignoring all the other cash working components, many of which would increase ComEd's rate base. *See* Hill Reb., ComEd Ex. 19.0 Corr., at 25:562 - 26:564. That is clearly inappropriate and unfair. In *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order March 28, 2003) at 46, the Commission rejected Staff's proposed adjustment to rate base founded on budget payment plan balances for that reason, stating:

The Commission finds that ComEd's position on this issue is persuasive. While Staff makes a salient point relative to the Company's exclusion of working capital from this proceeding while in the previous DST proceeding it chose to include working capital, to simply pick out particular working capital items that would result in a downward adjustment to the Company's revenue requirement would be inappropriate. The downward adjustment sought by Staff, therefore, is not accepted.

The same reasons that prompted that ruling have been proved in this case. The Commission in that Docket did approve customer deposits as a subtraction from rate base (*id.* at 115), but ComEd had proposed the subtraction and did not make the same argument as to customer deposits there. ComEd has done so here.

Second, Staff's witness was mistaken when she called the customer deposits "cost-free", as is reflected by her agreement in rebuttal that if her adjustment were to be approved it would require the partly offsetting increase in operating expenses noted above.

Finally, Staff's witness' position is inconsistent with her proposed adjustment to remove ComEd's pension asset from rate base and, again, one-sided. As discussed in Section II.B.4, *supra*, in terms of the pension asset, ComEd's shareholders have supplied \$803 million of capital in the form of the pension contribution that created the pension asset, resulting in a \$30 million reduction in pension expenses included in the revenue requirement. To propose to disallow the inclusion of the pension asset in rate base, while simultaneously insisting that rate base be reduced by \$31,477,000 for customer deposits, is inconsistent and unfair. There is no valid basis

for denying shareholders a return on funds they have provided while giving customers a return on funds they have provided (by reducing rate base). Staff's proposed adjustment should be rejected.

7. Budget Payment Plan Balances

Staff proposes to reduce ComEd's proposed rate base by \$529,000 based on theory that budget payment plan balances are "excess funds" that ComEd may use. Ebrey Dir., Staff Ex. 2.0, 27:585-28:600 and Schedule 2.7; Ebrey Reb., Staff Ex. 13.0, 26:539-27:566 and Schedule 13.6. Staff's proposal lacks merit, is inconsistent and unfair, and should be rejected, for the same reasons as the first and third reasons that Staff's proposed customer deposits adjustment should be rejected, discussed above. Again, the Commission rejected Staff's parallel budget payments payment balances proposal, based on that first reason, in *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order March 28, 2003) at 46. The same reasons that prompted that ruling have been proved in this case.

8. Materials and Supply Inventory

ComEd has included in its proposed rate base its inventory of materials and supplies as of December 31, 2004, the last day of the test year. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 16:330-40; ComEd Ex. 5.1.

Staff proposes that the 13-month average of ComEd's materials and supplies inventory should be used instead, less a figure for accounts payable associated with the materials and supplies inventory, resulting in a net deduction from rate base of \$1,609,000 (as revised in rebuttal). Ebrey Dir., Staff Ex. 2.0, 28:602-29:625 and Schedule 2.8; Ebrey Reb., Staff Ex. 13.0, 28:568-29:594 and Schedule 13.7.

ComEd has demonstrated in the rebuttal and surrebuttal testimony of Mr. Hill that Staff's proposed adjustment is incorrect and inappropriate. ComEd showed that: (1) the 2004 year-end figure is more representative of the current inventory management policies and practices; (2) the 2004 year-end figure is within 3.4% of Staff's 13-month average, negating any notion that the year-end figure is unrepresentative; (3) Staff used a four-year average to calculate the accounts payable offset part of her proposed adjustment, not the comparable 13-month period it used to calculate the materials and supplies inventory, which is inconsistent and inappropriate; (4) had Staff used the four-year average methodology for both parts of its proposed adjustment, then the result would be a \$5,268,000 increase in the inventory (before functionalization and the accounts payable offset); (5) Staff disregarded ComEd's direct assignment of the inventory for functionalization purposes, without explanation, and substituted an arbitrary allocator, one that is based on the same point in time, year-end 2004, that Staff rejects when used to calculate the inventory in the first place; and (6) had Staff used the average of the 13-month averages over the last four years then the result would be a \$6,681,000 increase in the inventory (before functionalization and the offset). Hill Reb., ComEd Ex. 19.0 Corr., 27:604-29:649 and Schedule 10; Hill Sur., ComEd Ex. 36.0 Corr., 25:566-26:585. Staff's proposed adjustment should be rejected.

**9 & 10 Procurement Case Expenses [Rate Base Effect]
Rate Case Expense [Rate Base Effect]**

ComEd seeks to recover its estimated legal fees and expenses associated with the Rate Case and the Procurement Case through inclusion of those costs in the test year rate base. The level of test year expense for these two proceedings is set forth in ComEd Ex. 5.0, App. A Sched. WPB-2.2 and 2.3 and supporting documentation is set forth in ComEd Ex. 48.0.

Staff does not disagree with ComEd that such costs are recoverable. Hathhorn, Tr. 1720:14-18 Staff also does not object to amortizing Rate Case expenses over a three year period. There are two principal disagreements. *Id.* at 1718:22-1719-2. First, ComEd and Staff disagree as to where to recover the Procurement Case expenses -- through delivery services charges or through the supply administration charge. Staff's proposal to recover these expenses through the supply administrative charge would place the burden of recovering the Procurement Case expenses almost entirely on residential bundled customers, as opposed to ComEd's proposal which would allow recovery of these expenses from all customers through the delivery services charge. Second, if both the Procurement Case expenses and Rate Case expenses are recovered through delivery service charges, as they should be, ComEd and Staff disagree as to whether there should be a return on the unamortized balances of the Rate Case and Procurement Case expenses. Hathhorn, Tr. 1720:14-18; Hill Sur., ComEd Ex. 36.0 Corr., 26:596-598. ComEd addresses each of these disagreements in turn.

Procurement Case Expenses Should Be Recovered Through Delivery Services Rates.

ComEd seeks to recover its Procurement Case expenses through delivery services rates. Staff argues that those expenses should instead be recovered through the supply administration charge. Hathhorn, Tr. 1720:6-1721:4. The Commission should reject Staff's proposal.

Staff's proposal is inconsistent with traditional ratemaking principles in that it fails to recognize that the costs incurred in the Procurement Case are for the benefit of all customers, not just those that take supply service from one of ComEd's supply tariffs. Crumrine Reb., ComEd Ex. 23.0, at 7:138-142. ComEd currently has a statutory obligation to make supply service available to most customers under Section 16-103(a) of the Public Utilities Act. 220 ILCS 5/16-103(a). And ComEd is offering supply service options to all customers. If a delivery

services customer in the future comes back to ComEd, ComEd must have sufficient supply to meet that customers' supply needs. *Id.* at 1724:6-10. The ability of a delivery services customer to come back to ComEd for supply clearly is a benefit to that customer. Hathhorn, Tr. 1722:20-1723:2. Accordingly, the Commission's decision in the Procurement Case creates the foundation for the competitive "safety net" to be extended to retail customers under Illinois law in the post-transition period. Crumrine Reb., ComEd Ex. 23.0, 7:148-8:151.

The Procurement Case costs that ComEd seeks to recover from customers through the delivery services charge are the costs incurred so that ComEd can fulfill all of these supply obligations, including its obligations as a provider of last resort. Hathhorn, Tr. 1723:3-1724:13. By allowing ComEd to recover the unamortized balance of Procurement Case expenses through delivery services rates, the Commission will insure that all parties benefiting from the Procurement Case bear some of the related expense, *i.e.*, the expense will be passed on to both bundled and delivery service customers through the delivery services charge. Hill Dir., ComEd Ex. 5.1, Sch. C-210.

Staff's proposal that ComEd recover its unamortized balance of the Procurement Case expenses solely through the supply administration charge would impose on residential customers virtually the entire burden of the Procurement Case expenses. Hathhorn, Tr. 1726:6-17. The supply administration charge applies only to supply customers who chose ComEd as their supplier. *Id.* at 1721:5-13. All customers taking supply as well as delivery from ComEd, *i.e.*, all of ComEd's bundled customers, pay a supply administration charge. *Id.* at 1721:14-18. Most bundled customers today are residential customers. *Id.* at 1726:2-5. Delivery service only customers do not pay a supply administration charge. *Id.* at 1725:21-1726:1. Thus, ComEd's large industrial and commercial delivery customers who take service from another supplier do

not pay a supply administration charge unless they come back to ComEd for service at some later time. *Id.* at 1726:18-1727:6. For this reason, Staff’s proposal would allow large industrial and commercial customers with competitive options to avoid Procurement Case costs by switching to or staying with another supplier, and they would help pay for such costs only if they exercised their option to return one day to take supply from ComEd. *Crumrine Reb.*, ComEd Ex. 23.0, 8:159-163. In other words, under Staff’s proposal it is those customers with limited competitive options (e.g., residential and small commercial customers) who are most likely to be saddled with most of the costs of the Procurement Case.

Ms. Hathhorn tried on redirect to suggest that the benefits from the Procurement Case are “de minimis” for customers that do not take supply from ComEd. *Hathhorn Tr.* 1754:1-4. This is not credible. The General Assembly put the obligation to serve requirement in the Act. As such, the General Assembly clearly did not share Ms. Hathhorn’s view that this requirement that ComEd have sufficient supply for these potential customers is merely a “de minimis” benefit. Moreover, even these customers that ComEd is not obligated to serve have fought to maintain the supply option. *In re Commonwealth Edison Co.*, ICC Docket 05-0159, (Order, Jan 24, 2006), at 124-130. The Commission therefore should reject Staff’s proposal to include the Procurement Case expenses in the supply administration charge and instead allow recovery of these expenses through the delivery services charge.

Unamortized Balances of Rate Case Expenses and Procurement Case Expenses Should be Included in the Test Year Rate Base. ComEd also seeks to have the unamortized balance of the Rate Case expenses included in the test year rate base, as well as the unamortized balance of the Procurement Case expenses if those expenses are recovered, as they should be, through delivery services charges. The rate making principle is that ComEd should recover the

time value of money for its outlay of Rate Case and Procurement Case expenses over the period that one expects the rates to be in effect. Hill Sur., ComEd. Ex. 36.0 Corr., 26:596-98. By including the unamortized balance of these expenses in the rate base, shareholders are not earning a profit on these expenses, but rather they appropriately are being reimbursed for their “carrying costs” for the time period that will take place before they receive full reimbursement for these just, reasonable, and approved expenses. Hill Reb., ComEd. Ex. 19.0 Corr., at 30:664-67.

Staff believes that ComEd should not be allowed to recover these costs through inclusion in the test year rate base. Notably, Staff does not dispute that by removing the unamortized balance of these expenses from the test year rate base, shareholders may obtain no reimbursement for the time value of the money expended. Hathhorn, Tr. 1728:20-1729:5. However, Staff argues that the unamortized balances of these expenses should be excluded from the rate base because there is no “symmetry” to ComEd’s proposal. Specifically, Staff argues that inclusion of the unamortized balances would reimburse shareholders, but could lead to rate payers being overcharged for these expenses because the amortization period may expire before ComEd has a new rate case, *i.e.*, that there will be too long a time between the end of the effective date of the rates and the filing of new rates. *Id.* at 1729:6-20. Commission history and the facts of this case both establish that Staff’s arguments are without merit.

On cross examination, Staff agreed that a three-year amortization period is appropriate in this case for the recovery of the expenses of this rate case. Hathhorn, Tr. 1730:16-20. Moreover, a look at history shows that the Commission consistently has decided that a three or four year amortization period is a reasonable expected life of the rates set within ComEd rate case proceedings. Hill Sur., ComEd Ex. 36.0, at 26:599-27:601. History also shows that in each

instance, the Commission's decisions have been accurate in that the amortization period fairly matched the actual period between the effective date for the new rates and the filing of the next rate proceeding, particularly when one considers that in each instance, much of the rate case costs were incurred well before the Commission order approving the new rates. Hill Reb., ComEd Ex 19.0 Corr., 33:722-33:736; Hill Sur., ComEd. Ex. 36.0, 26:599-28:627; Hathhorn, Tr. 1730:20-1733:12.

What this experience shows is that had the Commission included the unamortized balances of rate base expenses in the rate base in Docket Nos. 90-0169 and 94-0065, the Commission's determination of the amortization periods would have indeed been fair symmetry in that the amortization period would have fairly matched the actual period between the effective date for the new rates and the filing of the next rate proceeding. Accordingly, inclusion of the unamortized balances in the rate base would have resulted in shareholders appropriately receiving time value for their money and ratepayers would not have been overcharged for these expenses due to amortization periods that were too short. Hill Sur., ComEd Ex. 36.0 Corr., 28:628-30.

Moreover, in each of ComEd's last two rate cases, the Commission did in fact approve recovery by ComEd in rates of the unamortized balance of rate case expenses. Hill Dir., ComEd Ex. 5.1, Sch. 2.9. Here again, the facts do not show over recovery of these costs. With respect to Docket No. 99-0117, the three year amortization period did not expire before ComEd filed a new rate case. Hill Sur., ComEd Ex. 36.0, at 27: 616-620. And as explained by ComEd witness Mr. Hill, with respect to Docket No. 01-0423, although the expected effective dates for the rates to be set in this proceeding are January 2007, a period of 4 years and 9 months, again much of the costs were incurred well before the Order issued in that case and significant costs after the

Interim Order in that case were not reflected in the revenue requirement. Hill Sur., ComEd Ex. 36.0 Corr., 27:616-28:627.

In short, Staff's proposal has absolutely no symmetry because, on the one hand, as Ms. Hathhorn admits, it may prohibit shareholders from being fully reimbursed for test year costs (Hathhorn, Tr. 1728:20-1729:5) and, on the other hand, history suggests ratepayers will not be overcharged if these costs are included in rates. Symmetry is an appropriate ratemaking consideration, as Staff recognizes, but its proposal violates it. Accordingly, the Commission should reject Staff's adjustment and allow ComEd to include the unamortized balances of the Procurement Case and Rate Case expenses included in the test year rate base.

11. Other

Not applicable.

C. Operating Expenses

1. Distribution O & M

ComEd's proposed operating expenses in its final revised proposed revenue requirement include a final revised figure of \$274,184,000 for Distribution O&M expenses, a decrease of \$3,304,000 from its original figure of \$277,488,000 (due to an adjustment made in its surrebuttal testimony). *E.g.*, Hill Dir., ComEd Ex. 5.1; Hill Sur., ComEd Ex. 36.0 Corr., 4:72-89, 5:100-02 and Sched. 1. ComEd's Distribution O&M expenses in its revenue requirement are just and reasonable and should be approved.

ComEd presented direct testimony from Mr. Costello and Mr. Hill supporting ComEd's Distribution O&M expenses included in the revenue requirement. Mr. Costello, in his direct testimony, discussed the nature of these expenses, such as distribution system maintenance expenses that help to maintain the safety and the reliability of distribution service and storm

damage repair expenses; he explained how ComEd controls these expenses; and, he discussed the net downward adjustments that ComEd had made in the amount of \$1,848,000 to these expenses, resulting in a level that he concluded was necessary, prudent, and reasonable. Costello Dir., ComEd Ex. 3.0 Corr., 27:567 - 29:617. In his direct testimony, Mr. Hill further supported and confirmed the quantification of, these expenses, including the adjustments. Hill Dir., ComEd Ex. 5.0 Corr., 23:500 - 24:513.

CCC proposes, based on an average of percentage declines in Distribution O&M expenses over three years (from 2001 to 2004), adjusted for an inflation rate of 3.45%, to reduce ComEd's Distribution O&M expenses figure by 4.75% (McGarry Reb., CCC Ex. 5.0 Corr., 11:218 - 12:223), which yields a downward adjustment of \$13,024,000 based on ComEd's final revised figure of \$274,184,000 for Distribution O&M expenses.²⁹ CCC's proposed adjustment lacks merit and should not be approved.

CCC's witness noted what he referred to as a "steady decline" in Distribution O&M expenses from 2001 to 2004, which he "suspect[ed]" was due in part to significant capital investments and ultimately attributed to productivity increases. McGarry Dir., CCC Ex. 2.0 Second Corr., 15:330 - 16:351. He acknowledged that: "It is important to understand that no one would expect the Company's expenses to continually decline." *Id.* at 16:354-55. However, he then developed and proposed that ComEd's Distribution O&M expenses be reduced by a 4.78% "productivity factor." *Id.* 16:355 - 17:370; CCC Ex. 2.02. He asserted that his proposal was not a "trend line" proposal but rather is based on the premise that ComEd's significant investments

²⁹ While CCC's entire approach here lacks any merit, as discussed below, ComEd notes that CCC's witness' calculations show that, if he had based his proposal only on the change from 2003 to 2004, then his most recent data point, his proposed adjustment figure would have been 4.7% minus 3.45%, i.e., 1.25%, not 4.75%. CCC Ex. 2.02. ComEd also notes that because CCC's proposal is based on the total level of Distribution O&M expenses, it inherently double-counts with any other adjustments that reduce the level of these expenses, including the downward adjustments that ComEd already has made to these expenses and Staff's and intervenors' proposed adjustments discussed in Sections III.C.4, III.C.5, and III.C.6 of this Initial Brief.

in its Distribution system, all else being equal, would result in additional, incremental net reductions in its Distribution O&M expenses. McGarry Dir., CCC Ex. 2.0 Second Corr., 17:372 - 18:389. CCC's witness did not provide data that supported that premise.

ComEd witness Mr. DeCampli, who has knowledge of the actual drivers of ComEd's Distribution O&M expenses, in his rebuttal testimony, refuted the speculative bases of CCC's proposed adjustment. ComEd's reductions in Distribution O&M expenses in 2003 and 2004 instead were the result of broad steps to improve efficiency and productivity, and, while the cost reductions that were achieved are expected to be sustainable, further such reductions cannot be expected to continue, which all means that CCC's proposal does not reflect operational reality. DeCampli Reb., ComEd Ex. 14.0 Corr., 13:249-64.

Mr. Costello, in his rebuttal testimony, established that a further decline in the salaries and wages expenses that are the largest component of Distribution O&M expenses (*e.g.*, ComEd Ex. 5.2 (base payroll comprises \$98,991,910 of ComEd's 2004 Distribution O&M expenses)) should not be expected to occur, noting that while ComEd experienced a substantial decline in the number of its employees in 2004, another such decline did not occur in 2005 and that such declines should not be expected.³⁰ Costello Reb., ComEd Ex. 13.0 Corr., 34:765 - 35:796. Ms. Houtsma, in her rebuttal testimony, pointed out that the Exelon Way program, the implementation of which was completed in 2004, and which reduced ComEd's total (all categories) 2004 O & M expenses by \$66 million, included, among other things, the transfer of 436 employees out of ComEd on January 1, 2004. Houtsma Reb., ComEd Ex. 18.0 Corr., 3:46-50, 12:254-56; *see also* Houtsma Sur., ComEd Ex. 35.0, 7:139 - 9:190.

³⁰ The subject of salary and wages expenses is discussed further in Section III.C.4 of this Initial Brief.

CCC's witness, in his rebuttal, was unable to provide any valid basis for his proposed adjustment. CCC's witness, in his rebuttal, also claimed that "it stands to reason" that ComEd's capital investments in its Distribution system will result in net lower Distribution maintenance expenses. McGarry Reb., CCC Ex. 5.0 Corr., 10:191-94. That is not correct, as Mr. Costello's surrebuttal testimony showed. Costello Sur., ComEd Ex. 30.0, 21:409-19. Mr. Costello also again showed that further, incremental decreases in salaries and wages expenses should not be expected. *Id.* at 21:420 – 22:434. Finally, Mr. Hill pointed out that CCC's witness' use of historical graphs to support speculation about future reductions in uncollectibles expenses without supporting information regarding the drivers of that data is an insufficient basis for an adjustment. Hill Sur., ComEd Ex. 36.0 Corr., 46:1027 – 47:1033. The same is true here.

While CCC would have it otherwise, the evidence shows that its proposed adjustment is ultimately based on nothing more than conjecture. The only real evidence of the drivers of the data points in CCC's calculation came from ComEd, and that evidence did not support CCC's extrapolation. ComEd has proven that its Distribution O&M expenses are just and reasonable and should be approved. CCC's proposed adjustment should be rejected.

2. Pension and Other Post-Retirement Expenses

Please see Section III.B.4, *infra*.

a) Fair Value Adjustment to Pension Costs

Please see Section II.B.4, *infra*.

3. Administrative & General Expenses

ComEd's actual total 2004 Administrative and General expenses, before functionalization, were \$347,636,000. *E.g.*, ComEd Ex. 5.2. ComEd's final revised revenue requirement includes \$260,909,000 of A&G expenses for Illinois-jurisdictional delivery services

(not including transmission service), a decrease of \$8,920,000 from its original proposed figure of \$269,829,000 due to adjustments made in its rebuttal and surrebuttal testimony. *E.g.*, ComEd Ex. 5.2; Hill Sur., ComEd Ex. 36.0 Corr., Sched. 1. ComEd's A&G expenses in its revenue requirement are just and reasonable and should be approved.

Under the FERC's Uniform System of Accounts (the USOA), Administrative and General expenses are recorded in Accounts 920-935. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 26:549-50. "Costs included in those Accounts generally represent corporate support and overhead costs that benefit or derive from more than one operating business unit. Major A&G expenses support areas include Human Resources, Finance, Legal, Supply Management, and Information Technology departments. Additionally, the costs of employee pensions and benefits, including health care, are included in these A&G Accounts." *Id.* at 26:550-55.

In general, [the] services [the costs of which are included in A&G expenses] are provided either internally, by ComEd employees or by other service providers, including Exelon's Business Services Company ("BSC"). In 2001, Exelon Corporation, the ultimate (indirect) parent corporation of ComEd, undertook a corporate restructuring pursuant to which the remaining generation and shared service functions were transferred out of ComEd to separate Exelon subsidiaries. In order to maximize efficiencies associated with the provision of support services that are common to multiple business units, the BSC was established to provide corporate governance, technical, and a wide array of other support services to Exelon affiliate companies. Since that time ComEd receives from BSC a wide array of support services that ComEd used to provide to itself, such as Information Technology, Human Resources, Finance, Legal, Communications, Executive Management, and Corporate Governance. These services are provided to ComEd under the terms of the General Services Agreement approved by the ICC and the Securities and Exchange Commission ("SEC"). Costs for these services are directly charged to ComEd where possible, and if costs cannot be direct charged, they are allocated to ComEd and the other Exelon Affiliates utilizing a cost-causative (*i.e.*, reflecting cost-causation) allocation factor. In all cases, services provided by BSC are provided at cost. ComEd's total unadjusted A&G expenses are reported in its 2004 FERC Form 1 are \$348 million, of which approximately 47% are for services provided by BSC.

Id. at 26:557 - 27:574.

ComEd has presented extensive, detailed evidence that proves that the \$260,909,000 of A&G expenses that are included in its final revised revenue requirement are prudent, reasonable, necessary, and useful in performing the distribution and customer functions. *E.g.*, Costello Dir., ComEd Ex. 3.0 Corr., 30:647 - 31:675; Hill Dir., ComEd Ex. 5.0 Corr., 25:547 - 28:594; ComEd Ex. 5.1, ComEd Ex. 5.2; Costello Reb., ComEd Ex. 13.0 Corr., 4:64-71, 31:696 - 34:763; Houtsma Reb., ComEd Ex. 18.0 Corr., 3:46-50, 5:90 - 7:142, 10:217 - 15:333; Hill. Reb., ComEd Ex. 19.0 Corr., 38:831 - 42:929 and Sched. 1, 12, 13, 14, and 15; Costello Sur., ComEd Ex. 30.0, 1:21-25, 14:290 - 19:373; Houtsma Sur., ComEd Ex. 35.0, 2:25-42, 3:64 - 14:307; Hill. Sur., ComEd Ex. 36.0 Corr., 34:772 - 38:855 and Sched. 1, 4 and 9.³¹

Staff and intervenors have proposed numerous adjustments to ComEd's A&G expenses. ComEd has accepted certain of their proposed adjustments, in some cases to narrow the issues. ComEd, in its rebuttal testimony accepted two of those adjustments (one in a corrected amount) and part of a third adjustment, as discussed in Sections II.A.3.d, II.A.3.e, and III.C.8, *supra*. ComEd in its surrebuttal testimony, accepted a fourth adjustment and made a fifth adjustment prompted by a data request, as discussed in Sections III.C.6 and III.C.11, *supra*.

Staff's and intervenors' remaining proposed adjustments to ComEd's A&G expenses lack merit and should not be approved.³² They are not supported by, and instead are contrary to, the evidence. They would deny ComEd recovery of prudent, reasonable, and necessary actual expenses incurred in order to perform the distribution and customer functions.

³¹ Please note that this list of ComEd testimony and attachments generally does not include ComEd testimony and attachments that respond only to Staff's and intervenors' proposed adjustments to ComEd's A&G expenses that are discussed in other Sections of this Initial Brief, i.e., Sections II.A.3.d, II.A.3.e, III.B.6, III.B.9, III.B.10, III.C.2, III.C.6, III.C.8, III.C.9, III.C.10, and III.C.11.

³² Again, only certain of Staff's and intervenors' remaining proposed adjustments to ComEd's A&G expenses are discussed within the four subsections of this Section III.C.3 of this Initial Brief. Please see the preceding footnote.

a) **Functionalization**

ComEd correctly functionalized its A&G expenses. As noted above, ComEd's actual 2004 A&G expenses were \$347,636,000. *E.g.*, ComEd Ex. 5.2, at workpaper WPC-1a, p. 1. ComEd made adjustments that removed \$25,727,000 of its actual 2004 A&G expenses, including \$17,658,000 of executive compensation expenses from BSC, from its calculations, yielding a figure of \$321,909,000, before it functionalized these expenses. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 27:575-86; ComEd Ex. 5.2.

ComEd then functionalized that remaining \$321,909,000 of A&G expenses, using the general labor allocator based on the 2004 test year, correctly determining that the amount that supported the distribution and customer functions was \$287,142,000 and the amount that supported the transmission function was \$34,767,000.³³ Hill Dir., ComEd Ex. 5.0 Corr., 27:582 - 28:594; ComEd Ex. 5.1; ComEd Ex. 5.2. Although ComEd believes A&G expenses should be directly assigned when feasible, it was not feasible in this case, and, therefore, ComEd used the general labor allocator because it was the best available method. As Mr. Hill testified: "For purposes of this proceeding, because not all of the necessary data to conclusively determine the direct assignment of ComEd's 2004 A&G expenses are readily available, the allocation of A&G expenses is based on the 2004 relationship of total delivery services (distribution and customer-related) ComEd wages and salaries included in O&M expense to the total ComEd wages and salaries included in O&M expense." Hill Dir., ComEd Ex. 5.0 Corr., 27:589 - 28:593; ComEd Ex. 5.2 (calculation of the general labor allocator based on the 2004 test year).

³³ As indicated earlier, ComEd made further adjustments after functionalization in its direct testimony that reduced the A&G expenses in its proposed revenue requirement to \$269,829,000 and ComEd made still further adjustments in its rebuttal and surrebuttal testimony that reduced the A&G expenses in its final revised revenue requirement to a final revised figure of \$260,909,000.

ComEd's allocation of all of those expenses between the distribution, customer, and transmission functions makes sense. ComEd is "just a T&D utility" now, as Staff's witness testified. Lazare, Tr. at 643:12-13. The last time that ComEd had significant production capital costs or production operating expenses, not including purchased power expenses, was 2001, as he also testified. *Id.* at 632:11-17. That leaves ComEd with only one function besides the distribution and customer functions: transmission. *See id.* at 612:18 - 613:12 (discussing the four functions: production, transmission, distribution, and customer).

ComEd's functionalization of its A&G expenses should be approved. The evidence shows that use of the general labor allocator is appropriate in this case. No party disputes that ComEd calculation of the general labor allocator based on the 2004 test year is correct. No party has shown any valid reason to reject ComEd's functionalization. No party has even proposed any other method to functionalize ComEd's A&G expenses.

Staff does not claim to have shown any error in ComEd's functionalization of its A&G expenses. Moreover, Staff does not propose any method of functionalizing ComEd's A&G expenses, and instead rests on its proposal to cap these expenses at the level of \$176,684,000 approved in ICC Docket 01-0423 (which involved a 2000 test year). *E.g.*, Lazare, Tr. at 638:2-11; Lazare Dir., Staff Ex. 6.0 Corr., 20:483 - 21:507. Even though Staff's adjustment is based on the amount approved for the 2000 test year, Staff has had to acknowledge that ComEd is not the same utility now, as noted earlier. Indeed, Staff's witness also has stated that: "The utility, as it exists today is quite different from the utility that exists in those three cases [ICC Dockets 98-0680, 99-0117, and 01-0423]. The calculations that I wish to perform that I performed in the previous incarnation of the utility are no longer possible for just a T&D utility which ComEd is now." Lazare, Tr. at 643:7-13. The uncontradicted fact, however, is that the

general labor allocator calculation has been performed, and used, by ComEd to functionalize its A&G expenses in this Docket.

Staff's remaining asserted concerns on this subject have no merit. Staff claims that the increase from the level of A&G expenses approved in ICC Docket 01-0423, \$176,684,000, to the level included in ComEd's proposed revenue requirement in the instant case somehow casts doubt on ComEd's functionalization of its A&G expenses (*e.g.*, Lazare Dir., Staff Ex. 6.0 Corr., 20:483 - 21:507, 25:625-34, 27:670-75), but Staff's asserted concerns about the increase are shown to be without merit in Section III.C.3.b, *infra*. Staff also expresses concern about the relative changes in ComEd's A&G expenses versus its distribution O&M, customer accounts, and customer service and information expenses (*e.g.*, Lazare Dir., Staff Ex. 6.0 Corr., 26:636 - 27:675), but Staff's asserted concerns about those relative changes also are shown to be without merit in Section III.C.3.b, *infra*. Finally, Staff also claims that ComEd's restructuring, in particular, the creation of BSC, and the allocation of corporate governance and other expenses for which ComEd is charged by BSC complicate the assessment of ComEd's A&G expenses (*e.g.*, Lazare Dir., Staff Ex. 6.0 Corr., 21:519 - 22:527), but Staff's asserted concerns on those subjects are shown to be without merit in Sections III.C.3.c and III.C.3.d, *infra*.

No intervenor has provided any grounds for rejecting ComEd's functionalization of its A&G expenses. The IIEC submitted direct testimony questioning the increase from the level of A&G expenses approved in ICC Docket 01-0423 to the level included in ComEd's proposed revenue requirement in the instant case, and proposing that the level be tied to the percentage decrease in the sum of ComEd's distribution O&M, customer accounts, and customer service and information expenses. Chalfant Dir., IIEC Ex. 2.0, 2:18-22, 2:35 - 6:109. Tellingly, after ComEd refuted the IIEC's testimony on this subject, as discussed in Section III.C.3.b, *infra*, the

IIEC did not even offer any rebuttal testimony on this subject [(nor cross-examine any ComEd witness on this subject)]. In any event, the IIEC's witness did not directly address the subject of functionalization of ComEd's A&G expenses, and he provided no direct or indirect grounds for rejecting ComEd's functionalization.

CES offered rebuttal testimony suggesting that Staff's witness in his direct testimony "makes the same point with respect to Administrative and General Expenses ('A&G') as he did with respect to G&I plant. That is, A&G previously allocated to supply has now been shifted to delivery service by the Company, without an adequate explanation of the service being provided." O'Connor / Domagalski Reb., CES Ex. 5.0, 9:179-83. That is incorrect in three different ways. First, Staff's witness made no such claim, as the above discussion shows. Second, A&G expenses are operating expenses. Thus, the A&G expenses at issue in ICC Docket 01-0423 were the actual A&G expenses of that Docket's 2000 test year, while the A&G expenses at issue in this Docket are the actual A&G expenses of the 2004 test year, four years later. *E.g.*, Lazare, Tr. at 655:20 - 656:13. So, the A&G expenses of 2000 are not part of the revenue requirement in this Docket, and the A&G expenses of 2004 have never before been functionalized. Thus, not one dollar has been "shifted". Finally, ComEd has provided extensive, detailed evidence that proves that the final revised \$260,909,000 of A&G expenses that have been included in its final revised revenue requirement are prudent, reasonable, necessary, and useful in performing the distribution and customer functions, as discussed above and below. No party has refuted that evidence. CES' testimony provides no basis for disallowing any A&G expenses or assigning or allocating them to the production function. Costello Sur., ComEd Ex. 30.0, 18:359 - 19:366; Hill Sur., ComEd Ex. 36.0 Corr., 37:832 - 38:855.

CES requests that, if the Commission were to find that ComEd's A&G expenses included any expenses that are not properly allocated to the distribution and customer functions and that are more properly allocated to the production function, then those expenses should be recovered through the Supply Administration Charge. O'Connor / Domagalski Reb., CES Ex. 5.0, 9:183-86. Because the evidence supports (and only supports) ComEd's functionalization of its A&G expenses, as discussed above, the predicate finding for that request should not be made.³⁴ *E.g.*, Hill Sur., ComEd Ex. 36.0 Corr., 37:832 - 38:855. ComEd's functionalization of its A&G expenses should be approved.

b) Overall Amount

As shown in the introduction of Section III.C.3, *supra*, ComEd has provided extensive, detailed evidence that proves that the \$260,909,000 of A&G expenses that are included in its final revised revenue requirement are prudent, reasonable, necessary, and useful in performing the distribution and customer functions. ComEd will not repeat those citations here.

As indicated earlier, Staff and the IIEC purport to challenge the total amount of ComEd's A&G expenses in its revenue requirement on three grounds, each of which is based on asserted concerns about changes in expense levels from those approved in ICC Docket 01-0423:

- First, Staff claims that the increase from the level of A&G expenses approved in ICC Docket 01-0423 (which involved a 2000 test year), \$176,684,000, to the level included in ComEd's proposed revenue requirement in the instant case, has not been justified and that, therefore, ComEd's A&G expenses should be capped at

³⁴ ComEd agrees, however, that, hypothetically, if, contrary to the evidence, any of its A&G expenses in its final revised revenue requirement were to be disallowed on the grounds that they should be functionalized to the production function, then the Commission would need to approve use of the SAC or some other mechanism to enable ComEd to recover fully those expenses. ComEd believes that it would make the most sense to use a mechanism other than the SAC, one that applies to all retail customers, for the same reasons ComEd has discussed as to its procurement case expenses, addressed in Section II.B.9 and III.C.9 of this Initial Brief.

the level of \$176,684,000. *E.g.*, Lazare Dir., Staff Ex. 6.0 Corr., 20:483 - 21:507, 25:627-34, 27:670-75.³⁵

- Second, Staff also professes concern about the relative changes in ComEd's A&G expenses versus its distribution O&M, customer accounts, and customer service and information expenses, because these expenses are "moving in opposite directions". *E.g.*, Lazare Dir., Staff Ex. 6.0 Corr., 26:636 - 27:675.
- Finally, the IIEC submitted direct testimony questioning the increase from the level of A&G expenses approved in ICC Docket 01-0423 to the level included in ComEd's proposed revenue requirement in this case, and arbitrarily proposing that the level be decreased by \$119 million solely because A&G expense in this case should only be allowed if it was incurred in the exact same proportion to non-A&G O&M expense as was approved in the last case, or 35.8%. Chalfant Dir., IIEC Ex. 2.0, 2:18-22, 2:35-6:109. As noted earlier, tellingly, after ComEd refuted the IIEC's testimony here, the IIEC did not even offer any rebuttal testimony on this subject (nor cross-examine any ComEd witness on this subject).

None of those Staff's and the IIEC's three claims has merit, for a host of reasons. First, as noted above, ComEd submitted extensive, detailed proof that \$260,909,000 of its A&G expenses belong in its revenue requirement. Staff's and the IIEC's claims to the effect that ComEd has not met its burden of proof are incorrect in the face of that evidence. Nor have Staff and the IIEC refuted that evidence. They have not shown that any of that \$260,909,00 of A&G expenses is anything but prudent, reasonable, necessary, and useful in performing the

³⁵ Remarkably, Staff does not adjust its proposal for inflation. Even CCC, in its proposed adjustment to ComEd's distribution O&M expenses, used a 3.5% annual inflation factor, as noted in Section III.C.1 of this Initial Brief.

distribution and customer functions. Staff has challenged certain of those expenses, but those challenges, which are discussed in Sections III.C.3.c, III.C.3.d, and the other applicable Sections herein, lack any merit. Moreover, even if any of Staff's specific proposed adjustments to any particular A&G expenses had any merit, which is not the case, that would not warrant capping all A&G expenses. The IIEC has not challenged any specific A&G expenses. ComEd proved that the A&G expenses in the revenue requirement belong there, and Staff and the IIEC's proposals to limit ComEd's A&G expenses based on levels approved in ICC Docket 01-0423 are arbitrary and incorrect and should be rejected. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., 4:64-67, 31:696-32:715, 32:725-33:740, 33:753-34:763; Costello Sur., ComEd Ex. 30.0, 1:21-25, 14:290-305; Hill Sur., ComEd Ex. 36.0 Corr., 36:805-21. As Mr. Costello stated:

[Staff's proposal] should not be adopted. The A&G expenses proposed by ComEd are its actual costs. It was money well spent. Mr. Lazare does not suggest, nor could he, that ComEd's costs of doing business have not increased over the past five years. Yet his proposal would freeze spending levels at an arbitrary point in the past that bears no relation to the costs necessary for running an efficient electric company today. This proposed adjustment would result in ComEd's recovering less than it needs to continue to provide safe, efficient, and reliable service. It would hurt our customers and our employees.

Costello Reb., ComEd Ex. 13.0 Corr., 33:756-34:763; *see also* Costello Sur., ComEd Ex. 30.0, 14:290-305. As Mr. Hill stated:

In short, the costs that make up the A&G expense[s] are the actual, real costs that ComEd incurred to provide service to its customers. Neither Mr. Lazare nor any other witness has shown that any of the ComEd's 2004 test year costs that make up the total A&G expense were unreasonable in amount.

Hill Sur., ComEd Ex. 36.0 Corr., 36:818-21.

Second, Staff's and the IIEC's comparisons of total A&G levels in ICC Docket 01-0423, which involved a 2000 test year, and this Docket, which involves a 2004 test year, are inappropriate, misguided, and incomplete, if not misleading. Mr. Hill, in his rebuttal testimony, provided an extremely detailed refutation of those comparisons, showing among other things,

that: (1) ComEd's actual total 2004 A&G expenses are \$123 million lower or 26% less than its actual total 2000 A&G expenses; (2) in 2000, ComEd still was a vertically integrated utility that owned generation assets, and if one removes the A&G expenses that were functionalized to the production function in ICC Docket 01-0423, then ComEd's non-production A&G expenses have increased by only 9.4% from 2000 to 2004 (less than the general inflation rate, as noted below); (3) that 9.4% figure compares favorably to the 31% average increase and the 11.3% weighted average increase of the 178 electric utilities that filed FERC Form 1's for those years; (4) ComEd's A&G expenses functionalized to the distribution and customer functions have increased only 14.2% from the level determined by ComEd's direct assignment study that was approved in ICC Docket 01-0423; (5) the remainder of the difference from the prior Docket to this Docket is attributable to fact-based adjustments made in the prior Docket, which makes that much of the difference a reconciling factor, not a reason to challenge the level in this Docket; (6) Staff and the IIEC ignore general inflation, which was 9.7% from 2000 to 2004; (7) Staff and the IIEC ignore salary and wage increases, in particular, which have averaged approximately 3% per year; and (8) there are A&G expenses that existed in 2004 that did not exist in 2000, including post-September 11th security expenses and Sarbanes-Oxley Act compliance expenses. Hill Reb., ComEd Ex. 19.0 Corr., 38:831 - 43:900 and Sched. 12, 13, 14, and 15. Staff's witness responded to only the fourth, fifth, seventh, and eighth of those eight points, and his responses lack merit. *See* Lazare Reb., Staff Ex. 17.0 Corr., 15:363 - 18:449; Hill Sur., ComEd Ex. 36.0 Corr., 34:772 - 35:782, 35:786 - 36:804 and Sched. 9.

Third, Staff and the IIEC place no weight on the fact that in ICC Docket 01-0423 itself, the Commission approved an increase of these expenses of \$48,807,000 or 38.2% from the level approved by the Order on Rehearing in ComEd's first delivery services rate case, ICC Docket

99-0117 (which used a 1997 test year). More recently, in *Northern Illinois Gas Company*, ICC Docket 04-0779 (Order September 20, 1995), the Commission approved a forecasted 2005 test year level of A&G expenses that was 97% higher than the 2001 actual level. Hill Reb., ComEd Ex. 19.0 Corr., 41:866-69.

Fourth, Staff's and the IIEC's claims are unreasonable, on their faces, given ComEd's actual 2004 A&G expenses, the adjustments already made by ComEd, and the amount already functionalized to the transmission function. As noted in Section III.C.3.a, *infra*: (1) ComEd's actual 2004 A&G expenses were \$347,636,000, before adjustments and functionalization; (2) ComEd made adjustments that removed \$25,727,000 of its actual 2004 A&G expenses, including \$17,658,000 of executive compensation expenses from BSC, from its calculations, yielding a figure of \$321,909,000 to be functionalized; (3) ComEd functionalized \$287,142,000 to the distribution and customer functions and \$34,767,000 to its only other function, the transmission function; and (4) ComEd made further adjustments that reduced the final revised figure for A&G expenses in its final revised revenue requirement to \$260,909,000. Staff and the IIEC suggest that only \$176,684,000 (Staff) or \$155,300,000 (IIEC) of that \$260,909,000 of actual A&G expenses should be included in the revenue requirement. That disallows \$84,225,000 (Staff) or \$105,609,000 (IIEC) of those actual expenses. Thus, Staff's and the IIEC's proposals necessarily suggest that, on top of the \$34,767,000 already functionalized to the transmission function, there is another \$84,225,000 (Staff) or \$105,609,000 (IIEC) that: (1) supports the transmission function; or (2) supports no function. That, however, is absurd. Staff and IIEC have not identified any particular A&G expenses that fall in either of those three categories. Moreover, even if they had done so as to any particular A&G expenses, which is not

the case, that would only support disallowing those particular expenses, not capping all A&G expenses.

Fifth, Staff and the IIEC have identified no facts that support their claim or supposition that A&G expenses should be more directly correlated to distribution O&M, customer accounts, and customer service information expenses, and, in fact, they are independent and it is incorrect to expect such a correlation. *E.g.*, Costello Reb., ComEd Ex. 13.0 Corr., 4:68-69, 32:716 – 33:740; Hill Reb., ComEd Ex. 19.0 Corr., 41:901-09; Costello Sur., ComEd Ex. 30.0, 15:306-18. As to the superficiality and lack of merit of the IIEC’s witness’ analysis and proposal, *see also* Chalfant, Tr. at 1663:16-1664:3, 1664:16-1665:6, 1665:11-14, 1688:2-1690:13, 1691:6-1695:19, 1702:3-11; ComEd Cross Exs. 10, 13.

Sixth, while Staff’s witness claimed that ComEd’s A&G expenses were “extraordinarily high” relative to its distribution O&M, customer accounts, and customer service information expenses (Lazare Dir., Staff Ex. 6.0 Corr., 32:796-98), he provided no data regarding any other utility’s ratio, and the opposite is true. ComEd’s ratio of A&G expenses to those other expenses is below average compared to peer utilities. Costello Sur., ComEd Ex. 30.0, 15:31917:331.

Seventh, ComEd’s costs for corporate governance and other services provided by Exelon BSC, in particular, which make up 47% of ComEd’s actual total 2004 A&G expenses, as noted earlier, are prudent, reasonable, necessary, and useful in performing the distribution and customer functions, and the increase in these expenses from BSC’s creation to 2004 is fully explained and justified, as shown in Sections III.C.3.c and III.C.3.d, *infra*.

Eighth, Staff’s witness notes that he is recommending a level of A&G expenses higher than that set using the general labor allocator in the Commission’s Interim Order in ICC Docket 01-0423. Lazare Reb., Staff Ex. 17.0 Corr., 19:47620:482. That is irrelevant and

inconsistent with his testimony on the subject of General Plant and Intangible Plant, where he refuses to accept the use of the general labor allocator for functionalization purposes, approved in the Interim and final Orders in ICC Docket 01-0423, and which would result in substantially increasing ComEd's General Plant and Intangible Plant over the level in its proposed rate base, as discussed in Sections III.B.2 and III.B.3, *supra*. Hill Sur., ComEd Ex. 36.0 Corr., 36:822 - 37:831.

Finally, the Commission's reducing ComEd's A&G expenses based on the Order in ICC Docket 01-0423 would be unlawful, reversible error, for the reasons discussed in Sections III.B.2 and III.B.3, *supra*. *E.g.*, 220 ILCS 5/10-113, 10-201(e)(iv).

c) Corporate Governance Expenses

ComEd seeks recovery of \$49,867,000 in jurisdictional corporate governance expenses paid by ComEd to Exelon BSC in the 2004 test year. Staff proposes to disallow \$663,000 of those expenses (setting aside staff's proposed cap on A & G expenses discussed above).³⁶ The corporate governance expenses which ComEd seeks to recover are just and reasonable and representative of levels for jurisdictional corporate governance expenses expected to be incurred while the rates resulting from this rate case are in effect. Accordingly, ComEd should be permitted full recovery of these costs.

(i) Ms. Hathhorn's Recommended Corporate Governance Disallowance

Corporate governance services provided by BSC include services such as accounting, financial, legal, executive, and strategic planning services. Tr. at 17341:21-1735:2. Corporate governance services are provided to ComEd by BSC under the terms of the General Services

Agreement (“GSA”) approved by the ICC and the Securities and Exchange Commission (“SEC”). Hill Dir., ComEd Ex. 5.0 Corr., 26:561-569. Costs for these services are directly charged to ComEd where possible, and if costs cannot be direct charged, they are allocated to ComEd and the other Exelon affiliates utilizing a cost-causative (*i.e.*, reflecting cost connection) allocation factor. Hill Dir., ComEd Ex. 5.0 Corr., 26:569-27:573.

The factor used to allocate corporate governance costs is called the Modified Massachusetts Formula, or MMF. ComEd and Exelon were required to use the MMF for corporate governance costs by the SEC starting in 2004. Hathhorn, Staff Ex. 1.0, at 11: 224-12:234; Tr. 1736:14-1737:7. The MMF uses three factors as inputs to its allocation formula – gross revenues, total assets, and direct labor. Hathhorn Dir., Staff Ex. 1.0, 9:177-179. The way in which the allocation of corporate governance costs for 2004 was done – indeed, must be done – is to use projected ComEd values for gross revenues and direct labor and an actual ComEd value for assets from near the end of the calendar year (here, 2003) as data inputs into the MMF to calculate the corporate governance allocation factor for the following year (here, 2004). Tr. at 1737:8-1738:21.

The reasons for use of projected values are straightforward. First, as services are rendered during the year (here 2004), the costs of these services must be allocated so that BSC can charge for the services. Houtsma Sur., ComEd Ex. 35.0, 4:69-72; Tr. at 1739:3-21. Obviously, data which are only available after the close of the books in 2005 cannot be used to charge for services as they are rendered in 2004. Second, the actual data for use in the MMF for a given year – here 2004 – is not available even at the time the books are closed for a given year,

³⁶ Staff is the only party which has supported an adjustment to this specific expense, as opposed to suggestions for adjustments to the overall costs of services provided to ComEd by BSC, which are addressed in Section III C.3.d., *infra*.

and it would be very cumbersome and problematic if actual data were required to recompute all of the cost allocations. Houtsma Sur., ComEd Ex. 35.0, 4:69-76.

Ms. Hathhorn does not challenge that the 2004 corporate governance costs in question were properly and accurately allocated under the MMF for 2004. Tr. at 1735:8 - 1737:7. Nor does Ms. Hathhorn advocate or recommend a permanent change to ComEd's on-going allocation procedures. Tr. at 1738: 15-21. Instead, Ms. Hathhorn proposes to use hindsight to recalculate the 2004 corporate governance costs actually paid, "solely for ratemaking purposes." Tr. at 1735:3 - 1739:21; Hathhorn, Staff Ex. 12.0, 6:126-128. She does this by substituting into the allocation calculation under the MMF actual 2004 data that were not available until well into 2005. This results in a different cost for corporate governance services than was actually incurred by ComEd in the test year. Hathhorn Dir., Staff Ex. 1.0, at 9: 188-192; Tr. at 1737: 8-1738: 21; 1740: 14 – 1741: 1.

Ms. Hathhorn's proposed adjustment violates test year principles. The central purpose of a test year is to avoid "mixing and matching" of revenues and expenses. *Business and Professional People for the Public Interest v. Illinois Commerce Comm'n*, 136 Ill. 2d 192, 219 (1989). Put another way, the goal is to ensure that the Commission can compare apples to apples. But if Ms. Hathhorn's adjustment is accepted, the Commission will not be comparing the costs actually incurred by ComEd in 2004 for corporate governance, as well as for other services and operations, to 2004 revenues, but instead a mixture of the actual 2004 costs for those other services and operations and a new, hindsight number never actually paid by ComEd in 2004 for corporate governance. The result is an apples to oranges comparison in violation of test year rules.

Ms. Hathhorn's proposed disallowance also ignores that another central purpose of the test year rules is to accurately predict what the cost of service will be during the period the proposed rates will be in effect. *Central Illinois Public Service Company d/b/a Ameren CIPS and Union Electric Company d/b/a Ameren UE*, 1999 Ill. PUC LEXIS 646, 16-17 (Ill. PUC 1999). Ms. Hathhorn proposes to use a methodology for calculating test year costs – hindsight use in the MMF of data available only after the year in which the services were rendered and paid for – even though in 2005 and in the years when the rates will be in effect, the costs incurred will continue to reflect allocations that use projected data inputs. Hathhorn, Tr. at 1739:3-21. Staff has submitted no evidence that its “for ratemaking purposes” methodology will be as accurate in predicting future corporate governance costs as the methodology used by ComEd – the same methodology that will be used for allocating costs and charging for services in those future years.

Not only does Ms. Hathhorn's recommended disallowance violate test year principles for the reasons stated, but at bottom her proposed disallowance does not rest on any finding that the corporate governance costs actually paid in 2004 are not just and reasonable. As Ms. Houtsma testified on cross-examination: “Well, I think Ms. Hathhorn recommended no change to the way we record and to the way BSC allocates those costs. So, you know, if she wasn't finding fault with them or indicating in any way that they were not just and reasonable, I don't believe they should be disallowed.” Houtsma, Tr. at 450:12-18.

Apparently aware of this defect in her proposed disallowance, during the hearings, Ms. Hathhorn tried to suggest on redirect that her hindsight calculation of corporate governance costs for 2004 also was “based on a reasonableness analysis.” Hathhorn, Tr. at 1753. This last-ditch effort to justify her proposed disallowance cannot withstand scrutiny.

What Ms. Hathhorn is calling a “reasonableness analysis” supporting her proposed disallowance is the discussion in her filed testimony that the proportion of corporate governance costs charged to the regulated Exelon businesses via indirect charges (as compared to direct charges) is higher than for the unregulated Exelon businesses, and her suggestion that this difference may indicate that ComEd’s 2004 corporate governance costs are overstated. Hathhorn Dir., Staff Ex. 1.0, 9:194-11:222; Hathhorn Reb, Staff Ex. 12.0, 6:119-125; Tr. at 1753:7-14. Although, these differences in the ratios of direct to indirect charges are readily explained and do not support an inference that corporate governance costs are overstated, what is absolutely clear is that Ms. Hathhorn’s actual adjustment to corporate governance costs is not in any way based on, and cannot be justified by, her testimony concerning the ratio of direct to indirect costs, for at least four separate reasons.

First, this separate analysis is presented in her direct testimony in response to the question: “In addition to your calculation of the MMF using actual 2004 inputs, does any other evidence suggest that ComEd’s 2004 corporate governance costs are overstated?” Hathhorn, Staff Ex. 1.0, 9:194-96. The very question posed to Ms. Hathhorn makes clear that her recalculation of the MMF using actual 2004 inputs was separate from her analysis of indirect corporate governance costs charged to ComEd.

Second, Ms. Hathhorn’s discussion about indirect versus direct charges was never a basis for any recommended disallowance, and certainly was not the basis of her \$663,000 disallowance. Ms. Houtsma in her rebuttal testimony testified that Ms. Hathhorn “does not recommend an adjustment based on her conclusion” concerning the different ratios of direct to indirect charges between the regulated and unregulated Exelon affiliates (Houtsma Reb., ComEd

Ex. 18.0, at 5:101-110, 6:111), an assertion never denied by Ms. Hathhorn in her responsive rebuttal testimony.

Third, the absence of any connection between Ms. Hathhorn's actual corporate governance disallowance and her direct/indirect ratio analysis is further confirmed by the fact that although Ms. Hathhorn observes that the ratio of direct to indirect charges is different for Exelon's regulated utilities than for its unregulated businesses, she never testifies that they should move in tandem or specifies what an appropriate ratio would be. She simply observes they are different, and testifies this "suggests" that indirect corporate governance costs may not be allocated fairly and equitably.

Fourth, and finally, had the difference in the ratios Ms. Hathhorn observes been used to calculate a disallowance, the disallowance would have been a vastly different number than the \$663,000 disallowance she recommends. For all of these reasons, Ms. Hathhorn's observations about the ratio of direct to indirect charges are not related either in logic or in fact to her recommended disallowance, and thus offer no support for that disallowance.

In any event, the differences in the ratios are simply an indication that direct costs are being appropriately charged to the unregulated subsidiaries, as required by the GSA, and not an indication that cost allocations are not appropriate. Houtsma Sur., ComEd Ex. 35.0, 4:86-88. Indeed, Ms. Houtsma pointed out that the amount of direct charges to a given business unit is a reflection of the level of services provided directly to that affiliate, and the volume of directly assigned services would not necessarily be expected to be proportionate among business units. In particular, Ms. Houtsma testified that the higher level of direct finance charges to Exelon Generation Company, LLC in 2004 are related to Exelon Generation's property insurance which has been appropriately directly charged to Exelon Generation rather than indirectly allocated

among all business units. Houtsma Sur., ComEd Ex. 35.0, at 4:89-5:103. Accordingly, the differences between business units in the ratio of direct to indirect corporate governance cost allocations simply reflect proper adherence to the requirement in the GSA that costs be directly charged where possible.

**(ii) Mr. McGarry’s Non-Specific Call For An
Evaluation of BSC Costs**

CCC witness Mr. McGarry suggests that because ComEd’s costs under the GSA with Exelon BSC increased from \$126.4 million in 2003 to \$253.6 million in 2004, “[t]he Commission should evaluate the charges and specifically, the rates at which these charges are incurred.” McGarry, CCC Ex. 2.0, at 21:450-52. On cross-examination, Mr. McGarry described this called-for evaluation as being “analogous to an audit” (McGarry, Tr. at 329:5), but agreed that he had not proposed any particular timing for this evaluation. McGarry, Tr. at 392:11-14. This non-specific call for an audit is not directed to corporate governance costs *per se*, but rather to all BSC costs charged to Com Ed. Accordingly, Mr. McGarry’s call for a general “evaluation” of BSC charges, as well as his additional recommendations for certain specific adjustments to BSC costs, are discussed below in Section III.C.3.(d), *infra*.

d) Exelon BSC Expenses

ComEd seeks recovery of \$143,392,000 in expenses allocated to ComEd (and recorded in A&G Accounts 920, 921 and 923) for the provision by BSC of centralized services in the test year under the GSA. Houtsma Reb., ComEd Ex. 18.0, Schedule 18.1. Staff witness Ms. Hathorn proposes a disallowance of \$10,117,000 of these costs, net of her proposed \$663,000 disallowance for corporate governance costs, discussed in Section III.C.3.(c), *supra*. Hathorn Reb., Staff Ex. 12.0, Schedule 12.8, page 2 of 2. CCC witness Mr. McGarry proposes a disallowance of \$8,467,000 of these costs on a basis inconsistent with Ms. Hathorn’s proposed

adjustment. McGarry Reb., CCC Ex. 5.0, at 39:755-758; Schedule MJM-14, page 1 of 1. In addition, he proposes that there be an “evaluation” of overall BSC costs. McGarry Dir., CCC Ex. 2.0, 21:450-52. The disallowances proposed by Ms. Hathhorn and by Mr. McGarry, as well as Mr. McGarry’s call for general evaluation of BSC costs, should be rejected.

(i) **Ms. Hathhorn’s Recommended Disallowance**

Ms. Hathhorn originally proposed a disallowance of \$23.931 million in BSC costs based on a comparison of the four-year average of BSC costs charged to certain accounts for the years 2001 through 2004 to the comparable amount of BSC costs charged to those accounts in the 2004 test year. Hathhorn Dir., Staff Ex. 1.0, Schedule 1.8, page 2 of 2. In response to the rebuttal testimony of ComEd witness Ms. Houtsma, Ms. Hathhorn agreed that her four year average failed to properly account for costs incurred by the Energy Delivery Shared Services (“EDSS”) division of BSC, an increase in costs in 2004 due to the SEC-required change to use of the Modified Massachusetts Formula (“MMF”) to allocate corporate governance cost, and an increase in 2004 costs because the sale by Exelon of its Enterprise businesses resulted in ComEd comprising a greater percentage of Exelon in 2004, which causes ComEd, under the MMF, to receive a higher allocation of corporate governance costs in 2004. Hathhorn Reb., Staff Ex. 12.0, 13:285-291, 14:292-295; Hathhorn Tr. at 1743:6-22, 1744:1-11. Accordingly, her revised proposed disallowance is now approximately \$10 million. Hathhorn Reb., Staff Ex. 12.0, Schedule 12.8, page 2 of 2.

Although Ms. Hathhorn’s recognition of the need for these changes to her originally proposed disallowance is commendable, Ms. Hathhorn’s revised four year normalization adjustment continues to be incorrect and misconceived by failing to account for increased costs due to centralization. What Ms. Hathhorn has done is to calculate a four year average of costs

for centralized services provided by BSC on the grounds of “normalization.” Hathhorn Reb., Staff Ex. 12.0, 13:285-288. But normalization adjustments to actual test year expenses are not justified where they do not more accurately portray the reasonably expected level of costs over the period of time the rates set in this proceeding will be in effect. *See, e.g., Illinois Bell Telephone Company*, Docket No. 89-0033, 1992 Ill. PUC LEXIS 633, *95-96 (November 4, 1991); *Central Illinois Public Service Company d/b/a American CIPS and Union Electric Company d/b/a American UE*, 1999 Ill. PUC LEXIS 646, 16-17 (Ill. PUC 1999). Ms. Hathhorn’s use of a four year average has exactly the opposite effect – it creates a wholly artificial number which the record in this case establishes beyond a doubt is not only well under the level of BSC expense actually experienced in the 2004 test year, but well under the level of BSC expense experienced in 2005 and expected to be experienced in subsequent years. Thus, Ms. Hathhorn’s adjustment is unfair and unjustified.

The crux of the issue has to do with changes made by ComEd on January 1, 2004, as part of the Exelon Way program. As Ms. Houtsma testified, in 2003 and 2004 Exelon embarked on the Exelon Way, one aspect of which was to centralize and consolidate common functions throughout Exelon as a means to improve performance and achieve efficiencies. As part of this reorganization, 436 employees who perform support functions such as information technology, finance, and engineering were transferred from ComEd to Exelon BSC as of January 1, 2004, and 337 of these employees were transferred to the EDSS department of BSC. Although overall ComEd costs were reduced as a result of the Exelon way, this centralization increased the portion of ComEd’s costs that are attributed to Exelon BSC in the test year. Houtsma Reb., ComEd Ex. 18.0, at 12:250-258.

Ms. Hathhorn does not challenge that 436 employees were transferred from ComEd to BSC on January 1, 2004, 337 of which went to the EDSS department at BSC. Hathhorn, Tr. 1745:9-18. She also does not challenge that as a result of this transfer, EDSS costs in the BSC accounts on which she focused went from approximately \$6.3 million in 2003 to \$24.7 million in 2004. Tr. at 1746:4-9; Hathhorn Reb., Staff Ex. 12.0, Schedule 12-8, page 2 of 2. Further, Ms. Hathhorn agrees that both Mr. Hill and Ms. Houtsma testified that the Exelon Way reorganization is at an end and therefore these employees are not going back (Hathhorn, Tr. 1749:16-1750:3), and nowhere does she present any contrary evidence. The record is clear that Exelon Way was a significant reorganization and was done to achieve long-term sustainable savings, not just a one-year temporary reorganization. As Ms. Houtsma testified, “[t]here is no realistic expectation that Exelon BSC costs recorded in Account 921/923 will revert back to the historical levels in place before 2004.” Houtsma, ComEd Ex. 18.0, at 14:308-309. It would be unrealistic (and it is incorrect) to assume that a reorganization of this magnitude, with severance costs of \$67 million, would be implemented for one year only, yet this is the result of Ms. Hathhorn’s adjustment. These facts establish both why there was a sharp increase in BSC costs in 2004 and why this higher level of BSC costs will continue in future years.

In the face of this uncontradicted evidence, Ms. Hathhorn has provided two explanations for her use of a four year normalization adjustment, neither of which can withstand scrutiny. One argument is that because she has now included EDSS in her revised analysis, the impact of centralization has already been accounted for. Hathhorn Reb., Staff Ex. 12.0, at 14:300-308. This is plainly incorrect. As can be seen from the table in Ms. Houtsma’s Surrebuttal Testimony, which reproduces a portion of Ms. Hathhorn’s Schedule 12.8, page 2 of 2, because of the transfer of the 337 employees from ComEd to the EDSS department of BSC as of January 1, 2004 – a

fact not challenged by Ms. Hathhorn – EDSS costs included in Accounts 920, 921 and 923 increased by \$18.4 million in 2004 compared to 2003. Thus, as Ms. Houtsma explains, “although Ms. Hathhorn’s average includes EDSS, and the test year amount to which she compares the average also includes EDSS, because EDSS is higher in the 2004 test year than the prior years her averaging methodology has the effect of disallowing the increase in EDSS costs that resulted from centralization.” Houtsma Surr., ComEd Ex. 35.0, 7:151-8:155.

The extent of this unsupported disallowance was illustrated during cross-examination. In essence, notwithstanding that the 2004 costs to ComEd for services by the EDSS department of BSC were \$24.7 million as a result of the transfer of employees (Hathhorn, Transcript at 1746:4-8), Ms. Hathhorn’s averaging methodology results in a number of approximately \$9 million which, when compared to the actual EDSS costs of approximately \$24 million, is short by \$15 million. Hathhorn, Tr. 1746:3-1748:6. This is completely unjustified.

Ms Hathhorn’s other argument is that she could not “accurately analyze how the centralized expenses in 2004 compare to prior years, since the expenses were recorded in different accounts and at a different entity, ComEd rather than BSC, prior to 2004” (Hathhorn Dir., Staff Ex. 1.0, at 16:329-332), and there is no data available to accurately analyze how the reorganized Exelon Way organization will compare in the future to the years 2003 and prior. (Hathhorn Reb., Staff Ex. 12.0, at 15:323-325). These assertions are also incorrect.

The record plainly shows BSC costs went up in the test year by virtue of centralization, and that this centralization has led to overall cost savings. As Ms. Houtsma testified, the centralization occurred as part of the Exelon Way program that was intended simultaneously to reduce costs and improve performance. The program had a very positive impact on ComEd’s cost structure, and that benefit is included in the test year in this proceeding. Overall, the Exelon

Way program reduced ComEd's 2004 O&M expense by \$66 million (\$59 million on a jurisdictional basis) (response to PL 4.03). This savings was achieved, in part, due to the greater reliance on shared services provided by Exelon BSC and the transfer of over 436 employees to Exelon BSC. Houtsma, ComEd Ex. 18.0, at 13:276-283. This transfer of employees to BSC reduced corresponding costs at ComEd. Hathhorn, Tr. 1746: 1-3. The centralized organization remains in place today, with the exception of only 13 employees who were transferred back into ComEd earlier this year (ComEd's response to Staff data requested DLH 15.01). Houtsma, ComEd Ex. 35.0, at 8:169-171. None of these facts has been challenged, much less shown to be incorrect, by Ms. Hathhorn. The fact that the costs are now recorded in different accounts is driven by the FERC Uniform System of Accounts, which provides for separate accounts for internally incurred payroll and service company billings.

Ultimately, as Ms. Hathhorn agreed, the issue is whether on a going forward basis, the cost level for services provided by the EDSS department of BSC is more likely to be \$9 million (the result of Ms. Hathhorn's four year "normalization" through averaging) or approximately \$24 million. Hathhorn, Tr. 1748:7-12; see also Hathhorn, Staff Ex. 12.0, 15:323-325. This is not even a close question. No record evidence, apart from the mathematics of averaging, supports a conclusion that during the years the rates established in this case will be in effect, the level of BSC costs for centralized services, and particularly EDSS services, will be anywhere close to \$9 million. Not only has ComEd provided un rebutted evidence as to why the BSC costs increased and why the level of costs resulting from the reorganization will continue in future years, but ComEd provided un rebutted evidence that BSC costs in 2005, the year following the 2004 test year, were virtually the same as in 2004. Ms. Houtsma testified that "[i]n 2005, ComEd's total BSC charges were \$256 million, almost identical to the \$254 million in 2004." Houtsma Sur.,

ComEd Ex. 35.0, 8:171-172. Ms. Hathhorn agreed that she had no reason to disbelieve these figures. Tr. at 1750:10-20. Ms. Houtsma further testified that “[t]he portion of 2005 BSC costs recorded in Accounts 920,921 and 923 was \$130 million, well in excess of the four year average of \$104.9 million proposed by Ms. Hathhorn, which demonstrates that the test year amount is much more representative of amounts to be incurred prospectively than in a four-year average that includes the pre-Exelon Way organization.” Houtsma, ComEd Ex. 35.0, at 8:172-177. Ms. Hathhorn also agreed that this comparison “doesn’t sound wrong.” Hathhorn, Tr. at 1751:5-6.

Even CUB witness Mr. McGarry has acknowledged that the effects of centralization should be removed from Ms. Hathhorn’s adjustment. McGarry Reb., CCC Exhibit 5.0, 38:746 – 39:750. Thus, ComEd witnesses have testified that these will continue, CCC witness McGarry has testified that these costs should be removed from Ms. Hathhorn’s adjustment, ComEd has provided a logical explanation of why a reorganization of the magnitude of Exelon Way would not be done for one year (the 2004 test year) only, and 2005 costs confirm that the test year costs are at a level likely to be incurred in future years. Ms. Hathhorn has supplied no affirmative evidence to the contrary.

In short, as Ms. Houtsma testified, in total, a fair consideration of identifiable events that have a sustained prospective effect on the Exelon BSC cost allocations would reduce Ms. Hathhorn’s four year historical average based adjustment down to less than \$3 million, even before the consideration of inflation. Houtsma, ComEd Ex. 18.0, 15:330-33; Ex. 18.1, Sched. 1.

**(ii) Mr. McGarry’s Recommended Normalization
Disallowances and “Evaluation”**

(1) Normalization Disallowances

Mr. McGarry's proposed disallowances based on a normalization adjustment are misconceived and incorrect for much the same reasons as applied to Ms. Hathhorn's adjustments.

Mr. McGarry agrees that Ms. Hathhorn's adjustment should be modified as ComEd has suggested to include EDSS in the analysis, and because Ms. Hathhorn has made that modification, all of the witnesses are in agreement on this point. Mr. McGarry also agrees that Ms. Hathhorn's adjustment should be reduced by the amount that is attributable to centralization, and he adopts that reduction. On this point, he and Ms. Houtsma are in agreement, although Ms. Hathhorn continues to disallow the impact of centralization. However, Mr. McGarry disagrees with Ms. Hathhorn and ComEd on two causes of increased BSC costs.

First, Mr. McGarry disallows costs related to the MMF, even though his testimony is otherwise silent on this point. Because the adoption of the MMF to allocate corporate governance costs was a change required by the SEC that will remain in effect for periods subsequent to the test year, Mr. McGarry's proposed disallowance of these costs, without explanation, is ill-founded. Houtsma, ComEd Ex. 35.0, at 10:215-11:231. His MMF disallowance, which even Ms. Hathhorn does not support, should be rejected.

Second, Mr. McGarry believes that the increases in BSC costs allocated to ComEd as a result of the sale of Enterprises should not be allowed. Mr. McGarry states that he does not believe that ComEd customers should be required to pay for an increase in allocated indirect corporate governance costs when a holding company sells or spins-off an affiliate subsidiary, because customers are not getting anything for the increase in costs. However, it is hard to imagine that Mr. McGarry believes that ComEd customers should not get the benefit of a reduction in allocated indirect corporate governance costs that would occur if an affiliate

subsidiary were added or were to expand. The nature of indirect corporate governance costs is such that they do not necessarily change with the addition or sale of an affiliate; in other words, these are costs that do not vary in exact proportion to the overall size of the holding company system. However, the allocation of these costs to ComEd may increase or decrease based on the change in ComEd's size relative to the overall size of the holding company system. It would not be any more appropriate to exclude from rates the increase in corporate governance costs allocations that occurs when an affiliate is divested than it would be for ComEd to suggest that a reduction in corporate governance costs allocations to ComEd that could occur if an affiliate were added should be treated similarly and excluded from rates. Houtsma Sur., ComEd Ex. 35.0, 11:234-12:249. Ms. Hathhorn has modified her adjustment to remove the disallowance of costs resulting from the sale of Enterprises. Mr. McGarry's suggestion that these costs should be disallowed is not correct.

(2) Proposed Evaluation of BSC Costs

Mr. McGarry's separate suggestion that there should be an "evaluation" or "audit" of BSC costs (McGarry, Tr. at 392:11-14) should also be rejected. Mr. McGarry has not provided any evidence that the BSC costs are unreasonable, and there is none.

An audit of pricing terms is not necessary to explain the increase in BSC costs since 2001. ComEd Exhibit 35.2 to Ms. Houtsma's testimony sets forth WPC-13a, which provides a history of ComEd's total billings from BSC, broken down into three categories – corporate charges, transactional costs, and Energy Delivery Shared Services. The \$119.7 million combined increase in the corporate governance charges and EDSS areas have already been explained in connection with Ms. Hathhorn's proposed disallowance -- the Exelon Way centralization (\$98 million increase in total BSC costs), the sale of Enterprises (\$13 million), and

the adoption of the MMF (\$12 million).³⁷ The transactional costs, which are the services that are billed on a rate times volume pricing basis, have actually *decreased* from \$85.4 million in 2001 to \$84.3 million in 2004. Houtsma Sur., ComEd Ex. 35.0, at 12:258-266. Therefore, there is no basis to conclude that the rates per unit of measure are unreasonable and have led to dramatic increases in costs as suggested by Mr. McGarry. Finally, it is unreasonable to narrowly focus on just one aspect of the cost structure that was impacted by Exelon Way. Although the portion of ComEd's costs that are attributable to BSC increased in 2004, this increase was offset by savings throughout other ComEd departments and, overall, the effect of the Exelon Way was to reduce ComEd's O&M expense by \$66 million in 2004, thereby reducing the costs of service in this proceeding. Houtsma Sur., ComEd Ex. 35.0, 12:268-13:273.

Mr. McGarry tries to support his call for an audit by testifying that he has reviewed the monthly billing reports that were provided in response to a Staff data request and that these billing reports do not provide evidence that the underlying rates are reasonable. McGarry Reb., CCC Ex. 5.0, at 35:692-36:715. Mr. McGarry's attempt to find support for an audit in these monthly billing reports is misconceived and incorrect. The reports reviewed by Mr. McGarry were provided in response to Staff data request DLH 16.02, which specifically asked for the detailed monthly bills ComEd received from BSC. As Ms. Houtsma explained, the purpose of the bills is to provide ComEd with detail that allows ComEd to verify the accuracy of the bill and the nature of the services it has received. These reports have nothing to do with determining the justness and reasonableness of the rates charged. Assessment of the reasonableness of the rates occurs before the services are provided and the bills are issued through the negotiation of Service Level Agreement ("SLAs"), which establish the scope and pricing of services to be provided by

³⁷ These numbers differ from those discussed with respect to Ms. Hathhorn's proposal disallowances because they reflect Mr. McGarry's focus on total BSC billings as compared to Ms. Hathhorn's focus only on

BSC to ComEd in the upcoming calendar year. It is during this process that ComEd can compare the rates for services to be received to the costs of those services in prior years to determine the reasonableness of the rates. Houtsma Sur., ComEd Ex. 35, at 13:279-288. In addition, as Ms. Houtsma testified, various areas of ComEd perform research of market based rates for services like those provided in the GSA to help determine the reasonableness of BSC charges under the GSA. Houtsma, Tr. at 363:15-364:12. There is no contrary evidence in the record. Accordingly, Mr. McGarry has provided no evidence that any of ComEd's rates are unreasonable, and his call for an audit in the absence of good reason should be disregarded.

4. Salary and Wage Expense

Recognizing that salary and wage expense at the end of the 2004 test year reflect the impact of certain permanent staff reductions related to the Exelon Way program, ComEd made a downward pro forma adjustment to that expense. Specifically, ComEd lowered that salary and wage expense by \$5,084,000 to "normalize" that expense for periods beyond 2004. Hill Dir., ComEd Ex. 5.1, Schedule C-2.13.

Attorney General witness Mr. David Effron claims that ComEd's downward adjustment did not go far enough. He states that the identified reduction in workforce related to the Exelon Way program was 228, and observes that ComEd had 404 fewer employees at the end of 2004 than it did at the beginning of that year. Effron Dir., AG Ex. 1.0, at 17:1-5. From this he concludes that ComEd must have eliminated more positions than it now claims, and thus its salary and wage expense should be lower. Effron Dir., AG Ex. 1.0, at 17:1-5. Mr. Effron also argues that, because "the average number of employees in the six months ended September 2005" was lower than the number of employees at the end of 2004, a still larger downward

Accounts 920, 921 and 923. Houtsma, ComEd Ex. 35.0, at 10:207-213.

adjustment is warranted. Effron Dir., AG Ex. 1.0, at 18:5-10. In total, Mr. Effron recommends reducing “pro forma test year wage and salary expense by \$5,488,000 beyond the adjustment recognized by the Company in its adjustment on ComEd Schedule C-2.13.” Effron Dir., AG Ex. 1.0, at 19:9-11.

Mr. Effron can justify neither his rationale for a further downward adjustment in wage and salary expense, nor the way in which he arrives at his specific downward adjustment figure. The mathematical manipulations in which Mr. Effron engages obscure the real issue, which is whether the requested level of wage and salary expense is a reasonable projection for the years the rates will be in effect – 2007 and beyond. On this issue, Mr. Effron provides no evidence at all. But even if one focuses solely on level of employees in 2004 and 2005, as does Mr. Effron, the record establishes that ComEd’s wage and salary expense for 2004 already reflects a downward adjustment for employee positions that have been eliminated and does not include any funds for temporary vacant positions for the time when such temporary vacancies existed. The record further establishes that the temporary vacancies in 2005 on which Mr. Effron is focusing are being and will be filled. His proposed adjustment should therefore be rejected.

Mr. Effron wants to lower ComEd’s salaries and wage expense further because he believes that ComEd is recovering expense for more employees than it actually pays. But this is plainly incorrect. ComEd’s 2004 wage and salary expense number is based on actual expenditures, not the number of employees. In other words, it reflects only *actual costs paid in 2004*. As ComEd witness Mr. Jerome Hill explained at hearing:

It is important that you view labor costs and not employees. The labor costs included in ComEd’s 2004 test year recorded in 2004, have not been adjusted to add back any payroll or labor costs for employees that may have been vacant or employee positions that would have been vacant over that time period.

And so what the 2004 test year salary and wages cost represent is the people and wages actually paid in 2004. It is not adjusted to remove any employees that are

currently there, who will become vacant in 2005 on a temporary basis, nor does it add back any salary and wages expense for positions that were vacant that are expected to be filled on a going forward basis.

Hill, Tr. at 932:8-933:5. Accordingly, because the salary and wages expense number reflected in ComEd's revenue requirement did not include any funds for temporary vacant positions, Mr. Effron is wrong to use vacancies as a basis for any further downward adjustment.

In his rebuttal testimony, Mr. Hill described the "significant difference" between ComEd's pro forma adjustment made before the case was filed and Mr. Effron's additional adjustment. ComEd's reduction in expenses "made for the reduction in employees due to the Exelon Way" arose because "ComEd considers and, through its revenue requirement adjustment commits, that the Exelon Way reductions will be permanent vacancies." Hill Reb., ComEd Ex. 19.0 Corr., at 43:956-59. By contrast, "Mr. Effron's adjustment incorrectly assumes that the vacant positions will result in permanent reductions to ComEd labor costs." Hill Reb., ComEd Ex. 19.0 Corr., 43:960-44:961. Indeed, Mr. Hill made clear that ComEd "could have adjusted its payroll costs upward to recognize the temporary nature of the vacant positions" (Hill Reb., ComEd Ex. 19.0 Corr., at 44:961-63), but did not do so. Therefore, no adjustment to the salary and wage expense on account of temporary vacancies is warranted.

Moreover, the testimony of John Costello, ComEd's Chief Operating Officer and the person charged with managing the "people who work to keep the lights on" (Costello Reb., ComEd Ex. 13.0, at 1:15-16), dispelled any suggestion that the vacant positions relied upon by Mr. Effron were anything but temporary. Mr. Costello testified that ComEd's proposed operating expense level (which reflects only ComEd's adjustment) "appropriately includes the costs that ComEd will incur in the future to maintain" the "work force [that] provide[s] safe, efficient, and reliable electric supply." Costello Reb., ComEd Ex. 13.0, at 34:772-75. Mr. Costello further testified that "[e]mployee levels vary throughout the course of the year

based on staffing changes” and that “[a] vacancy for a position may not be filled immediately” because ComEd takes the time necessary to ensure it hires the right person for the job. Costello Reb., ComEd Ex. 13, at 34:778-35:782. Finally, Mr. Costello summed up the impact of Mr. Effron’s proposal by explaining that it “would mean that ComEd would not be able to fill any of its current vacancies. It means that that ComEd would not be able to hire the employees it wants to hire to keep the lights on.” Costello Reb., ComEd Ex. 13.0 Corr., at 35:790-92.

Mr. Effron concedes that, unlike Mr. Costello, he has no “experience being responsible for a work force needed to operate, maintain and improve [ComEd’s] distribution system.” Tr. at 1630:6-13. Nor has Mr. Effron identified a legitimate basis to counter Mr. Costello’s testimony that ComEd needs to – and will – fill the vacancies to ensure it has a “work force for providing safe, efficient and reliable electric service.” Effron, Tr. at 1629:22-1630:5. Mr. Costello testified that temporary vacancies routinely occur, are filled, and that ComEd needs those positions to provide proper service. In fact, Mr. Costello’s testified at hearing that he has “54 people in construction schools at ComEd. I’ll be adding 15 more next week.” Costello, Tr. at 237:13-15. ComEd’s evidence – unrebutted – is that it needs to fill, has plans to fill, and will fill, these temporary vacancies, and it is already doing so. Consequently, Mr. Effron’s complaint that the positions have not yet been filled is besides the point.

Quite apart from the lack of a defensible basis for a further downward adjustment of the test year wages and salary expense figure, Mr. Effron arrived at his specific adjustment based on results-oriented mathematical manipulations which are patently unfair. At the time his written testimony was prepared, Mr. Effron had available 9 months of 2005 employee data running through September 2005. Effron Dir., AG Ex. 1.0, at 18:20-21. Instead of using that data, Mr. Effron employed a “six month average” for his employee count and based that average upon “the

six months ended September 2005.” Effron Dir., AG Ex. 1.0, at 18:20. Not surprisingly, the average employee count for the full nine months of 2005 – 5,503 – was higher than the average for the six month period Mr. Effron used – 5,482. Tr. at 1627:9-1628:5. At cross examination, it further became clear that if one looked at employee data for all of 2005 (data then available), the number would be still different – somewhere in-between Mr. Effron’s six months number and the nine-month number. Tr. at 1634:14-19. The point is that relying on short-term averages in this fashion fails reasonably to account for normal variances in employment and, as the cross of Mr. Effron demonstrated, is subject to misleading manipulation. In the past, when the Commission Staff has challenged employee counts as overstated using an average, they conducted an intensive study spanning 26 months to ensure that the figures accounted for the numerous variances that impact labor force during any given period. *See, e.g., Governor’s Office of Consumer Services v. ICC*, 242 Ill. App. 3d 172, 189-90 (1st Dist. 1992). Mr. Effron conducted no such study in this instance.

In sum, Mr. Hill explained that ComEd’s test year wages and salary figure is based on amounts actually paid and includes no wages and salaries costs in the test year related to temporarily vacant positions for the time such temporary vacancies existed; therefore, no adjustment on the basis of such vacancies is warranted. Mr. Costello established that the subject vacancies are indeed temporary, and are planned to be filled, and are being filled, in the ordinary course. By recommending a disallowance based on temporary vacancies, therefore, Mr. Effron is recommending an arbitrary, and too low, level of wage and salary expense. Further, Mr. Effron’s specific adjustment should be rejected because it is based on a results-oriented and misleading analysis of the number of ComEd employees over a limited and selective period of

time which unfairly increased the amount of his recommended (and improper) downward adjustment.

5. Severance Expense

ComEd seeks recovery of two types of severance costs in this proceeding – those that occur in the normal course of business, and those that flow from a defined cost savings initiative, *i.e.*, the Exelon Way program. The first type is recoverable as an ordinary recurring business expense. The second type – savings related to the Exelon Way program – is recoverable as a “cost savings program that is anticipated to result in annual jurisdictional savings” of more than \$1,000,000. 83 Ill. Admin. Code § 285.3215. Mr. Efron’s proposed adjustments to each of these types of severance costs should be rejected.

Severance Expense Incurred In The Ordinary Course Of Business. No one, including Mr. Efron, disputes that ComEd should recover severance costs incurred in the ordinary course of business. Efron Reb., AG Ex. 3.0, 14:14-16. However, Mr. Efron proposes reducing the requested amount by employing an average based on the years 2001 through 2005 (Efron Reb., AG Ex. 3.0, at 14:17-18), even though severance cost data for the year 2000 is in the record and available. By excluding the year 2000, Mr. Efron omits \$5.8 million in severance costs, which reduces ComEd’s annual recovery by more than \$800,000. Hill Sur., ComEd Ex. 36.0 Corr., at 39:879-889. None of the three reasons Mr. Efron offers in support of his exclusion of the year 2000 data justify his failure to use 2000 data to determine adjustments can withstand scrutiny.

First, Mr. Efron states that “the years 2001-2005 constitute a more recent five year period than the years 2000-2004.” Efron Reb., AG Ex. 3.0, 15:1-4. But as Mr. Hill stated, there is no reason to exclude the year 2000, because if an average is to be used, it should “include all

data points that are of recent vintage and are in the record.” Hill Sur., ComEd Ex. 36.0 Corr., 39:884-87. Tellingly, Mr. Effron has not objected to the use of year 2000 data to determine adjustments in other contexts. For example, Mr. Effron’s fair value adjustment to liability for pensions and post-retirement benefits other than pensions is based on the effects on the 2004 test year revenue requirement of the restatement of certain assets and liabilities to fair value at the time of the merger in 2000. Effron Dir., AG Ex. 1.0, 26:4-30:18. In addition, Mr. Effron has not taken exception to the use by other parties in this proceeding of historical averages that encompassed the 2000-2004 time period, such as Staff’s proposed adjustment for uncollectibles expense. Ebrey Dir., Staff Ex. 2.0, Sched. Mr. Effron objects to use of 2000 data here only because it suits his present purposes. Thus, Mr. Effron’s “more recent” time period argument is wholly arbitrary and should be rejected.

Second, Mr. Effron argues that including the \$5.8 million year 2000 costs in the average is improper because “the Commission has already allowed recovery of the \$5.8 million in severance costs incurred in 2000.” Effron Reb., AG Ex. 3.0 Corr., 15:5-6. But the purpose of Mr. Effron’s average is to determine a proper level of costs going forward, and therefore “[w]hether the amount may or may not have been included in determining a prior revenue requirement is irrelevant.” Hill Sur., ComEd Ex. 36.0 Corr., 39:882-84.

Third, Mr. Effron claims that ComEd “does not anticipate that any severance costs will be incurred in 2006 and 2007.” Effron Reb., AG Ex. 3.0 Corr., 15:8-9. But the portion of the exhibit to which Mr. Effron refers concerns the Exelon Way initiative, not the severance costs incurred in the ordinary course of business separate from Exelon Way. Hill Reb., ComEd Ex. 19.0 Corr., Sched. 16, p. 2. Further, there is no reference to 2006 or 2007 on the document

referenced by Mr. Effron. Hill, Tr. 874:14-875:5, 930:3-9. Accordingly, Mr. Effron has no basis for his claim that ComEd will not incur ordinary course severance costs in 2006 and 2007.

In short, none of Mr. Effron's reasons for ignoring year 2000 data is valid. Accordingly, his recommended adjustment, which constitutes a results-oriented numbers game, should be rejected.

Severance Costs Related To The Exelon Way Program. Mr. Effron also recommends disallowing the severance costs from the Exelon Way initiative entirely because they are not recurring costs and because the savings allegedly will not be recovered in rates. Neither of these arguments has merit. Effron Reb., AG Ex. 3.0, 15:12-16:16.

The Exelon Way initiative began in mid-2003 as means to reduce costs through “integration and centralization of support functions, consolidation and alignment of business units and standardization and simplification of operating processes.” Hill Reb., ComEd Ex. 19, Schedule 16, p.2.³⁸ ComEd incurred approximately \$158 million in severance costs in 2003 and 2004. Hill Reb., ComEd Ex. 19.0 Corr., at 46:1008-1010. ComEd's test year expenses in this proceeding includes \$21 million of the total severance costs related to the Exelon Way savings program, the inclusion of which results in an implied amortization period of over seven years (\$158 million divided by \$21 million equal \$7.5).³⁹ Hill Reb., ComEd Ex. 19.0 Corr., at 46:1008-1017.

³⁸ Despite Mr. Effron's suggestion to the contrary (Effron, AG Ex. 3.0, at 14:12-14), the Exelon Way program relates in no way to the ComEd/PECO merger. ComEd has incurred severance costs related to the merger (Hill, ComEd Ex. 19, at 45:993-95), but ComEd does not seek any recovery for such costs. Furthermore, the Exelon Way program did not rise out of the merger, as it was not instituted until mid-2003 – over three years after the 2000 merger – and concerns a general effort to streamline operations. Hill Reb., ComEd Ex. 19, at 45, Schedule 16, p.2. Accordingly, the requested \$21 million recovery is not a request for recovery of merger costs.

³⁹ ComEd's proposed revenue requirement does not include the effect of including the unamortized balance of such costs in rate base, which would increase the proposed revenue requirement. Hill, ComEd Ex. 19.0, at 46 n.1.

Section 285.3215 of the Commission's Rules, added in 2003, provides a mechanism for utilities to recover costs related to a "cost savings program that is anticipated to result in annual jurisdictional savings in excess of ... \$1,000,000" and the "initial costs of which are sought to be recovered in the test year." 83 Ill. Admin. Code § 285.3215. The costs to achieve the Exelon Way program savings fall squarely within the purview of Section 285.3215, and therefore recovery should be allowed. The severance costs related to the Exelon Way constitute "initial costs" of the program that are sought to be recovered in the test year, 2004. Hill Sur., ComEd Ex. 36.0 Corr., at 40:894-99. ComEd has shown that the Exelon Way initiative produced cost savings well in excess of the \$1 million threshold, that those savings are already embedded in the 2004 test year costs (Houtsma, ComEd Ex. 18.0, at 3:46-50), and that that initiative will continue to produce significant cost savings going forward – \$70 million in 2005, \$73 million in 2006 and \$75 million in 2007 (Hill Reb., Ex. 19.0 Corr., Schedule 16 p.2). Indeed, at the hearings, Mr. Hill testified that such savings will continue beyond 2007 "as long as those efficiencies are retained within the business." Hill, Tr. at 871:1-6. Accordingly, per Section 285.3215, recovery of the Exelon Way severance costs through rates is appropriate.

Mr. Effron first argues these costs should be disallowed because ComEd "does not incur these expenses on a normal, ongoing basis, and it is unlikely that such costs will be incurred prospectively unless there is another major severance program." Effron Reb., AG Ex. 3.0, at 15:20-16:1. But the entire point of Section 285.3215 is to allow recovery of the "initial costs" of "cost savings initiatives" that will produce significant savings, without regard to whether those costs recur. Indeed, Mr. Effron does not even reference Section 285.3215 in his direct or rebuttal testimony, suggesting that he prepared such testimony without regard to the terms of that section. On cross examination, however, he acknowledged that Section 285.3215 concerned cost savings

programs and did not (and could not) contend that it does not bear on this issue. Effron, Tr. at 1618:9-1619:8. Furthermore, if the severance costs were recurring, they would properly be recovered regardless of Section 285.3215, and there would have been no need for that section. As Mr. Hill testified: “Of course, these costs do not occur every year. That is precisely why the Commission provided for utilities to propose recovery of [their] initial costs for costs savings programs.” Hill Sur., ComEd Ex. 36.0 Corr., at 40:907-909. Accordingly, the fact that the Exelon Way severance costs do not recur is irrelevant to whether they can be recovered.

Mr. Effron also claims that recovery is improper because the future savings will not be reflected in rates, and therefore “the savings retained by shareholders will have more than paid for the costs of the program by the time the Commission issues an Order in this case.” Effron Reb., AG Ex. 3.0, at 16:8-12. As an initial matter, the fact that the “savings” from an initiative will cover its “costs” cannot possibly be a basis to deny recovery of the costs. No rational company would institute a savings initiative in which the initial costs exceed the expected subsequent savings, because no net savings would occur. Moreover, Mr. Hill explained that “Mr. Effron fails to mention that shareholders are absorbing cost increases above the level of costs in the test year in this proceeding in other areas of ComEd’s total costs to provide delivery services between now and the time rates from this proceeding go into effect – such as increased depreciation expense, 2006 employee salary increases, and increased health care costs to name a few.” Hill Sur., ComEd Ex. 36.0 Corr., at 41:917-921.

Moreover, and in any event, as Ms. Houtsma testified, with the centralization of support functions in Exelon BSC as a result of the Exelon Way, costs incurred directly within ComEd were reduced, and the overall effect was to reduce 2004 O&M costs by \$66 million. Houtsma Reb., ComEd Ex. 18.0 at 3:46-50. Thus, there are already savings from the Exelon Way

program that will be reflected in the rates in this proceeding. In addition, Mr. Effron does not dispute that, as a result of Exelon Way: “ComEd expects to have sustainable savings for the three years past the test year of \$70 million in 2005, \$73 million in 2006 and \$75 million in 2007;” the “Exelon W[ay] cost savings initiative has produced costs savings that are already embedded in test year costs;” and “that there will be expected savings from the Exelon W[ay] program past 2007.” Effron, Tr. 1621:20-1622:20. These facts establish a basis for recovery under Section 285.3215. Accordingly, the record is clear that ComEd properly seeks recovery of its initial severance costs for a program that will produce hundreds of millions of dollars in savings. Mr. Effron’s proposed adjustment would deny ComEd any recovery of that cost, which removes the incentive created by Section 285.2315 to initiate such programs. His recommendation should be rejected.

6. Incentive Compensation

ComEd, like nearly every major U.S. company, includes incentive compensation as part of its overall employee compensation package. Incentive compensation did not exist 60 years ago, but today it is a ubiquitous and necessary tool to recruit, to compensate and to motivate employees. ComEd witness Richard Meischeid, a compensation expert who leads consulting firm Towers Perrin’s Energy Services practice, described how employee compensation evolved from simply base salary prior to World War II to include health and welfare benefits beginning in the 1950s and 1960s, and then to comprise the total compensation package of salary, benefits and incentive compensation offered today. Meischeid Dir., ComEd Ex. 12.0, at 4:67-84. Mr. Meischeid testified without challenge that, given its wide use, “incentive compensation is not ‘additional’ or ‘optional’ compensation that ComEd provides to employees, but a required element in the compensation program and a necessary cost of doing business.” *Id.*, at 6:114-16.

Further, both Mr. Meischeid and Mr. John Costello, ComEd's Chief of Operations, testified that ComEd must offer incentive compensation in order to provide the competitive compensation package necessary to attract and to retain high-quality employees. Meischeid Dir., ComEd Ex. 12.0, at 5:107-6:112; Costello Reb., ComEd Ex. 13.0 Corr., at 23:516-19. Mr. Costello pointedly described that need, explaining the importance of incentive compensation to ComEd's ability "to continue to attract the talent necessary to provide safe, efficient, and reliable service to customers." Costello Reb., ComEd Ex. 13.0 Corr., at 16:381-85. Providing incentive compensation, in addition to base salary and benefits, is simply how modern utilities pay their employees. Meischeid Dir., ComEd Ex. 12.0, at 8:164-68. No party challenged any of this testimony.

Utilities and other corporations employ incentive compensation for a simple reason – it works. Mr. Meischeid explained that companies use incentive compensation "to focus employees on key goals in order to improve performance" because they "have found that providing monetary incentives to employees is more effective than providing salary and benefits only." Meischeid Dir., ComEd Ex. 12.0, at 5:103-06. Mr. Costello similarly testified that incentive compensation spurs employees to work harder and more efficiently. Costello Reb., ComEd Ex. 13.0 Corr., at 25:565-67. No party disputes that point. Incentive compensation therefore constitutes not only an essential element of total employee compensation, but also "one of the most powerful mechanisms companies have to drive performance." Meischeid Reb., ComEd Ex. 27.0, at 6:133-34. Thus, incentive compensation plainly qualifies as a prudent expense. At hearing, Staff witness Theresa Ebrey admitted that she neither "claim[s] that paying incentive compensation doesn't work," nor "claim[s] that paying incentive compensation is imprudent." Ebrey, Tr. at 1867:6-16.

As an integral part of total compensation, incentive compensation should not be analyzed separately from base salary when determining whether recovery of employee compensation expense through rates is proper. The only question is whether the total levels of cash compensation – base salary plus incentive compensation – are reasonable. Mr. Meischeid compared the levels of total cash compensation that ComEd pays employees in various positions to the levels of total cash compensation that ComEd’s utility peers pay to their employees in comparable positions. Meischeid Dir., ComEd Ex. 12.0, 7:147-8:158; 9:179-87. Based on that comparison, Mr. Meischeid testified that ComEd’s pay levels fall “within the competitive range versus market.” *Id.*, at 11:220-26. No party has challenged ComEd’s total cash compensation, or incentive compensation, as unreasonable or excessive.

In sum, the undisputed record establishes that ComEd’s total cash compensation levels are reasonable in amount and that, because it improves employee performance, incentive compensation is prudent. Thus, ComEd’s total cash compensation expense – base salary plus incentive compensation – merits full recovery through rates.

Notwithstanding these facts, Ms. Ebrey and Attorney General witness David Effron propose to deny ComEd recovery of the incentive compensation portion of its total cash compensation expense. Ebrey Dir., Staff Ex. 2.0, at 14:282-85; Effron Dir., AG Ex. 1.0, at 20:10-14. They do so without disputing – or offering contrary evidence – that ComEd’s total cash compensation expense (including incentive compensation) is reasonable and prudent. The proposed disallowance thus contravenes the well-established principle that rates “must allow the utility to recover costs prudently and reasonably incurred.” *Citizens Util. Bd. v. Illinois Commerce Comm’n*, 166 Ill. 2d 111, 121 (1995) (“*Citizens 1995*”). The opposition to recovery

appears driven not by a belief that incentive compensation is an improper expense, but rather simply by a desire to reduce ComEd's recovery.

Ms. Ebrey's testimony draws this improper, confiscatory motive into stark relief:

The determining factor for the recovery of incentive compensation in base rates is not related to whether the Company should offer such a plan as part of its overall compensation package. Rather, the decision to be made is who should bear the cost of the plan – ratepayers through base rates or shareholders.

Ebrey Reb., Staff Ex. 13.0 Corr., at 17:351-58 (emphasis added). In other words, Ms. Ebrey cannot dispute Mr. Costello's testimony that ComEd must offer incentive compensation to ensure it has the quality employees needed to provide safe, reliable and efficient electric delivery services, and she wants the undisputed benefits of incentive compensation to be realized – Ms. Ebrey simply does not want ComEd to recover the cost of that necessary, prudent expenditure from customers.

Ms. Ebrey and Mr. Effron attempt to disguise the confiscatory nature of their proposed disallowance by arguing that ComEd has not satisfied the Commission's test for recovery of incentive compensation expense. As an initial matter, the correct standard for recovery of employee compensation expense – base salary plus incentive compensation – is as stated in *Citizens 1995*; namely, whether that expense is reasonable and prudent. But in any event, ComEd has clearly met the Commission's separate, specific test on the present record.

a) **Summary of ComEd's Incentive Compensation Program**

ComEd's incentive compensation plan, sometimes referred to as the Annual Incentive Plan or "AIP," extends to nearly all ComEd employees, and "provides employees with the opportunity to earn cash awards based on the achievement of operational, individual and financial goals." Meischeid Dir., ComEd Ex. 12.0, at 6:119-123. Incentive compensation payments are based upon ComEd's performance with respect to certain goals, or performance

measures. The plan contains two types of performance measures: funding and allocation. As their names suggest, performance on a funding measure determines whether the plan will receive funding, and performance on an allocation measure determines how payments for incentive compensation, once funded, are divvied up among employees. *Id.*, 11:227-12:256.

ComEd's plan employs four funding measures: "1) SAIFI – System Average Interruption Frequency Index, 2) CAIDI – Customer Average Interruption Duration Index, 3) O&M and Capital Expense, and 4) EPS [earnings per share]." Meisheid Dir., ComEd Ex. 12.0, at 12:260-63. Fifty percent of plan funding is based on the SAIFI, CAIDI and O&M measures together, and the other fifty percent is based on EPS. *Id.* at 13:284-87.

The amount of funding for each measure corresponds to the performance thereunder. Three performance levels are set: threshold, target and distinguished. No funding occurs unless performance reaches the threshold level. Funding increases as performance moves to target level, and finally is capped at the distinguished level; however, payouts are assured once the threshold level is reached. Payments for incentive compensation track the measures for funding. ComEd has requested recovery of incentive compensation expense at the target level for the 2005 plan year. Meisheid Dir., Exh. 12.0, at 14:293-94.

Lastly, overall incentive compensation awards from all measures – SAIFI, CAIDI, O&M costs and EPS – may be increased or decreased based on ComEd's performance on "customer satisfaction," as measured by the American Customer Satisfaction Index Proxy (ACSI Proxy). Meisheid Dir., ComEd Ex. 12.0, at 13:272-74.

b) ComEd Has Satisfied The Commission's Test For Full Recovery Of Incentive Compensation Expense

In the past, the Commission has imposed two fundamental requirements for recovery of incentive compensation expense : (1) an "historical pattern[] of paying incentive compensation"

to serve as a basis to determine whether, and how much, incentive compensation expenses will be incurred going forward; and (2) evidence that “the incentive compensation payments provided benefits to ratepayers.” *Central Illinois Pub. Serv. Co. and Union Elec. Co.*, ICC Docket 00-0802 (Order Dec. 11, 2001) at 19; *Consumers Illinois Water Co.*, ICC Docket No. 97-0351, 1998 WL 34302196, at *17 (Order June 17, 1998) (same). Ms. Ebrey argues that ComEd has not satisfied either requirement, and Mr. Effron argues only that ComEd has not met the latter. Each is incorrect. The record amply demonstrates that ComEd has satisfied both requirements.

(i) **The Record Provides Abundant Assurance That ComEd Will Incur Incentive Compensation Expense At The Requested Level Going Forward**

Given the undisputed benefits of, and the need for, incentive compensation, ComEd has demonstrated a steadfast commitment to incentive compensation that ensures ComEd will continue to provide incentive compensation going forward. Mr. Costello, who is charged with ensuring that ComEd has the personnel necessary to provide proper service, described incentive compensation as “an actual and longstanding cost.” *Costello Reb.*, ComEd Ex. 13, at 23:520-21. He went on to explain that ComEd will not cancel incentive compensation because that would disadvantage ComEd in the market for quality employees:

ComEd has been committed to using an incentive compensation program for years, and intends to continue to use it as a vital part of its overall compensation package. Without an incentive compensation component, ComEd would not be providing a competitive compensation package and most likely would see a loss of quality employees with an inability to attract new ones.

Id., at 23:515-19. This testimony is not disputed.

The uncontested record establishes that “for each of the past four years, ComEd has paid total incentive compensation at levels *above* target.” *Hill Reb.*, ComEd Ex. 19.0, at 51:1116-17.

Thus, because ComEd seeks recovery at target level and its payout history establishes that ComEd has paid above target for each of the past four years, recovery at target level is proper.

Against that backdrop, Ms. Ebrey advances three arguments against recovery of incentive compensation expense grounded upon the notion that ComEd might not incur incentive compensation expenses in the future, or will not do so at the requested level (*i.e.*, target). The record refutes each of Ms. Ebrey's arguments.

**(1) Incentive Compensation Payments Have
Consistently Exceeded The Target Level**

Ms. Ebrey worries “that the goals in the plan may not be met and thus no cost would be incurred by the Company yet ratepayers would have provided funding.” Ebrey Dir., Staff Ex. 2.0, at 18:358-59. That concern has no basis in the record. Again, “for each of the past four years, ComEd has paid total incentive compensation at levels *above* target.” Hill Reb., ComEd Ex. 19.0 Corr., at 51:1116-17 (emphasis original). Thus, ComEd consistently incurs incentive compensation expense, and does so at levels above the target level at which it requests recovery. In the face of that evidence, Ms. Ebrey's argument rests on pure speculation, and cannot be sustained.

Moreover, in her Direct Testimony, Ms. Ebrey appeared to labor under the misconception that a failure to meet “goals in the plan” would mean “no cost would be incurred by the Company.” Ebrey Dir., Staff Ex. 2.0, at 18:358-59. But as explained above, funding occurs when performance on a funding performance measures reaches the *threshold* level – a level below target. Costello Reb., Ex. 13.0, at 22:494-97. As such, ComEd's consistent record of above-target payouts even more compellingly demonstrates that it will incur incentive compensation expense in future years. In rebuttal, Ms. Ebrey retreated from her initial position by acknowledging that funding indeed occurs at the lower threshold level, but then changes

course and argues that her concern is that, with funding at the threshold level, ComEd “would still provide the target level of cost although ComEd would pay out at a reduced level.” Ebrey Reb., Staff Ex.13.0 at 20:404-13. Concern that ComEd will incur a reduced level of expense differs from concern that ComEd will incur no expense at all. But as discussed in subpart (3) below, ComEd’s record of above-target payouts also assuages any concern about below-target payouts.

**(2) ComEd Will Not Discontinue Its
Incentive Compensation Program**

Ms. Ebrey contends that, because ComEd executives have the option to cancel the AIP, “it is certainly feasible that in any given year, the incentive compensation plan could be discontinued.” Ebrey Dir., Staff Ex. 2.0, at 21:446-56. This argument is pure speculation.

Mr. Costello laid to rest any unease about whether ComEd will simply cancel its incentive compensation program by flatly stating that “ComEd does not intend to eliminate its compensation program.” Costello Reb., ComEd Ex. 13.0 Corr., at 22:514. The status of incentive compensation as “an actual and longstanding cost” and ComEd’s need to recruit and to motivate quality employees further eliminates any realistic possibility that ComEd will cancel its incentive compensation program. *Id.*, at 23:515-21. Ms. Ebrey acknowledged at hearing that she did not know whether ComEd intended to cancel incentive compensation, and that she had no basis to refute any ComEd testimony about such intentions. Ebrey, Tr. 1871:16-1872:8.

The mere fact that ComEd executives have the option to eliminate incentive compensation provides no basis on which to conclude that they will exercise that option. Indeed, as Ms. Ebrey admitted on cross examination, ComEd could easily reduce or eliminate a number of costs, such as reducing fringe benefits for non-union employees, lowering executive base pay

or laying off union employees. Ebrey, Tr. 1871:5-15. Such possibilities cannot warrant denying or reducing recovery of the associated costs. The same holds true for incentive compensation.

(3) ComEd's Record Of Above-Target Payouts Assures That Recovery At Target Level Reflects The Likely Future Expense

Ms. Ebrey opposes incentive compensation recovery because she claims “there is insufficient data to analyze, based upon historical data, what the [incentive compensation] payout would be in the future.” Ebrey Dir., Staff Ex. 2.0, at 22:477-80. She asserts this lack of “historical data” stems from the structure of ComEd’s incentive compensation plan having changed “from a very basic plan with limited goals in 2002, to a much more complex plan in 2003-2004 and back to a simpler plan in 2005.” *Id.*, at 22:471-77. Ms. Ebrey’s position lacks merit.

The structure of ComEd’s incentive compensation plan has in fact changed somewhat over the past four years, but that does not render ComEd’s track record of above-target payouts inadequate as “historical data” that predicts above-target payout levels in future years. Mr. Costello explained that the changes to the plan “have not been fundamental.” Costello Reb., ComEd Ex. 13.0 Corr., at 19:441. Throughout the relevant period, “the fundamental goals established by the plan, such as reliability, efficiency, customer satisfaction and earnings, have remained the same.” *Id.*, at 19:444-46. Those changes:

primarily concern only the number of different metrics to measure those fundamental goals. Thus, whether ‘simple’ or ‘complex,’ incentive compensation was paid or not paid based upon the same core goals that constitute the heart of the present plan.

Costello Reb., Ex. 13.0, at 19:447-50. Accordingly, because prior versions of ComEd's plans embraced the same fundamental goals as the current plan, ComEd's payment record serves as a reliable guide to ComEd's likely payouts going forward.⁴⁰

Additionally, even if a company paid out below target level in a given year, that does not mean recovery at the target level is improper. Mr. Meischeid testified that "[b]y design, incentive compensation payments vary from year-to-year based on performance, with some years above, some years below, and some years at or around target." Meischeid Reb., ComEd Ex. 27.0, at 3:51-54.⁴¹ In general, however, payouts more often occur at or above target than below target. Mr. Meischeid studied the payout history of 24 utilities over the 2001-2004 time period at issue here, and found that the percentage of companies paying at or above target in a given year ranged from a low of 57% (2001) to a high of 80% (2003). *Id.*, 3:54-4:81. These results, combined with Mr. Meischeid's finding that the structure of ComEd's incentive compensation plan "is highly similar to typical utility industry practices" (Meischeid Dir., ComEd Ex. 12, at 14:296-302), further demonstrate that recovery is proper at the target level. Mr. Meischeid's testimony and ComEd's above-target level payouts for the past four years foreclose any argument that the record does not support recovery at the target level.

Faced with ComEd's Rebuttal Testimony, Ms. Ebrey abandoned the "plan changes" argument on rebuttal, and took a different tack. Ms. Ebrey claimed that the requested recovery at

⁴⁰ Furthermore, denying recovery for incentive compensation on the basis that ComEd altered its incentive compensation plan would unfairly punish ComEd for working to improve its compensation program. As with all aspects of their businesses, companies, including ComEd, regularly review their incentive compensation programs "to make incremental modifications over time to improve their programs' effectiveness." Meischeid Reb., ComEd Ex. 27, at 4:95-5:96. Denying recovery to a company seeking to improve its incentive compensation plan would create a perverse incentive to maintain less effective programs for fear that changes would jeopardize the ability to recover the expenses.

⁴¹ Relatedly, because ComEd's incentive compensation plan has four funding measures, an above-target payout on one measure can "make-up" for a below-target payout on another measure, producing an aggregate payout at above the aggregate target level (the level at which ComEd seeks recovery). Costello Reb., ComEd Ex. 13, at 22:499-507.

target level is not reliable because the aggregate target level of incentive compensation has decreased since 2002. Ebrey Reb., Staff Ex. 13.0, 18:372-19:386. Ms. Ebrey claims that “[w]ithout a sufficient explanation” of “why the targets have varied significantly from year to year, I cannot agree that any ‘target’ level is representative of the level of costs that will be incurred during the life of the rates to be set in this proceeding.” *Id.*, 18:372-19:399.

Mr. Costello provided Ms. Ebrey’s requested “sufficient explanation” in his Surrebuttal Testimony. First, it is important to note that the “variances” Ms. Ebrey described occur in the aggregate target level of incentive compensation for all employees, and not at the individual employee level. Ms. Ebrey does not (and could not) assert that ComEd has reduced the target level of incentive compensation at the individual employee level. Additionally, the significant “variance” in the aggregate target levels constitutes a decrease. Ebrey Reb., Staff Ex. 13.0, at 19:392-93 (describing a total decrease of 24.4% from 2002 to 2005). This should come as no surprise because, as discussed extensively in connection with other issues, the number of ComEd employees has significantly decreased during this same time period. Mr. Costello described how the drop in employee count explains the drop in aggregate target incentive levels:

Naturally, all employee compensation expenses are reduced when the total number of employees is reduced, and incentive compensation is no exception. ... [T]he number of employees eligible for incentive compensation decreased substantially between 2002 and 2005, falling from 6,545 in 2002 to 5,597 in 2005. A corresponding significant decrease in the target levels of incentive compensation over the same period is therefore to be expected. Furthermore, a disproportionate number of the total reduction occurred among high-level employees (pay grades E04 and above); the proportion of total employees at those high-level grades decreased by roughly a third from 2002 to 2005. High-level employees, in turn, have a disproportionate amount of the total incentive compensation dollars.

Costello Sur., ComEd Ex. 30.0, at 8:165-75. Thus, because fewer employees received incentive compensation in 2005 than in 2002, and the decrease in employee count was much higher among employees who received a disproportionately high amount of incentive compensation, the

decrease in employees from 2002 to 2005 decreased the aggregate target level of incentive compensation. *Id.*, at 8:175-78. Finally, “because no further material reductions in ComEd’s employee count are expected[,] there is no reason to expect ... a related decrease in the target level of incentive compensation from 2005.” *Id.*, 8:178-9:181. These facts undermine Ms. Ebrey’s position that the decrease in aggregate target levels renders ComEd’s above-target level payout history unreliable as support for recovery at the 2005 target level.

(ii) **Incentive Compensation Benefits Customers**

The second part of the Commission’s specific incentive compensation test concerns customer benefit. The undisputed record clearly establishes such benefit.

First, ComEd’s compensation expert Mr. Meischeid has testified that companies employ incentive compensation to focus employees “on key goals in order to improve performance,” and because they “have found that providing monetary incentives to employees is more effective than providing salary and benefits only.” Meischeid Dir., ComEd Ex. 12.0, at 5:103-04. Indeed, that is why nearly every investor-owned utility uses incentive compensation. *Id.*, at 8:165-68. On cross examination, Ms. Ebrey did not deny the basic truth that incentive compensation works. Tr. at 1867:13-16. No party has contended that the improved employee performance that results from incentive compensation fails to benefit ComEd’s customers.

Second, the undisputed record evidence demonstrates that, without incentive compensation, ComEd could not “continue to attract the talent necessary to provide safe, efficient and reliable service to customers.” Costello Reb., ComEd Ex. 13.0 Corr., at 16:381-85. Mr. Meischeid testified that, absent incentive compensation, ComEd cannot offer a competitive compensation package. Meischeid Dir., ComEd Ex. 12.0, at 5:107-6:112. No witness countered ComEd’s testimony on this subject. And, no party has argued, nor seriously could argue, that the

ability to compete for the high-quality employees necessary to provide safe, reliable and efficient electric services afforded by incentive compensation does not benefit ComEd's customers.

Ignoring this evidence, Ms. Ebrey and Mr. Effron assert that ComEd has not adequately demonstrated that its incentive compensation plan benefits customers, meriting disallowance of plan expenses. Ms. Ebrey contends that ComEd's incentive compensation plan is "dependent upon financial goals which benefit shareholders and not ratepayers." Ebrey Dir., Staff Ex. 2.0, at 15:303-16:323. Additionally, both Ms. Ebrey and Mr. Effron assert that ComEd has not provided "tangible" or "quantifiable" evidence of customer benefit. Neither argument has merit.

(1) Half Of ComEd's Incentive Compensation Plan Funding Flows From Operational Goals

Ms. Ebrey avers that because 50% of the funding for ComEd's incentive compensation plan is based on an EPS measure, and another 25% percent relates to the O&M costs measure, the plan depends upon financial goals that benefit shareholder, not customers. Ebrey Dir., Ex. 2.0, at 15:303-16:312. As an initial matter, Ms. Ebrey rests her position on the assumption that the extent to which an incentive compensation plan bases funding on "financial" goals, such as EPS, the plan inherently does not benefit customers. For the reasons explained further below, that assumption proves false on this record. In this subsection, ComEd addresses only Ms. Ebrey's contentions regarding ComEd's non-EPS funding measures.

Financial goals are those based on net income, EPS or other earnings-based measures, whereas operational goals are those based upon business functions such as O&M costs, reliability, safety and customer service. Meischeid Dir., ComEd Ex. 12.0, at 16:331-44. Ms. Ebrey acknowledges that ComEd can recover "that portion of total incentive compensation costs" that are "based on operational" measures (Ebrey Reb., Staff Ex. 13.0, at 21:430-36), and admits that the funding measures based upon the CAIDI and SAIFI reliability measures are

operational goals (Ebrey Dir., Staff Ex. 2.0, at 16:324-27). Ms. Ebrey wrongly asserts that the O&M costs measure, which bases funding on whether ComEd keeps those costs below certain levels, is a financial goal. In so doing, Ms. Ebrey ignores ComEd's most recent delivery services rate case, in which the Commission found recovery proper because the plan "reduced operating expenses and created greater efficiencies." *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2002), at 121 (emphasis added).

Furthermore, although a reduction in O&M costs could correspond with increased earnings, "financial" goals trigger incentive compensation payments only when earnings targets are hit. But the O&M costs measure will trigger incentive compensation payments whenever the cost target is hit – even if earnings fall. Costello Reb., ComEd Ex. 13.0, at 18:425-26. As such, O&M costs are not based on earnings, and thus are not "financial." Additionally, the level of O&M costs reflects "the efficiency and effectiveness of operations." Hill Reb., ComEd Ex. 19.0, at 49:1083-84. More efficient and effective operations unquestionably benefit customers. Indeed, at hearing Ms. Ebrey answered "yes" when asked if "customers benefit from their utility's providing service with greater efficiency." Tr. at 1862:8-11. These benefits include freeing up funds for other useful work and, over time, lower rates because, all things being equal, rates set in future rate cases will be lower when O&M costs are lower than they would be if the O&M costs were higher. Costello Reb., ComEd Ex. 13.0, at 18:427-31. Given those benefits, the Commission has regularly recognized that incentive compensation programs that reward employees for lowering operating costs benefit customers. *See Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2002); *Consumers Illinois Water Co.*, ICC Docket 03-0403 (Order, April 13, 2004), at 14-15; *Northern Illinois Gas Co.*, ICC Docket 95-0219 (Order, April

3, 1996), at 27. Thus, the O&M costs measure constitutes an operational goal that the Commission has determined benefits customers.⁴²

Ms. Ebrey also points to the so-called “shareholder protection feature” in ComEd’s incentive compensation plan to support her position that ComEd’s incentive compensation plan has an improper shareholder focus. Ebrey Dir., Staff Ex. 2.0, at 16:312-23. That feature curtails funding based upon the operational goals (CAIDI, SAIFI and O&M costs) if commensurate financial performance is not achieved, but only to the extent that such payouts are “above target level.” *Id.*, at 16:315-18. In other words, that “feature can never be used to lower [operational] payments below the target level.” Costello Reb., ComEd Ex. 13.0 Corr., at 18:412-14. And, as Mr. Costello explained in his Rebuttal Testimony, because “ComEd is not seeking recovery for payments which exceed the target level ..., this feature has no impact whatsoever on the incentive compensation expenses sought in this proceeding.” *Id.*, at 18:415-17.

**(2) ComEd Has Adduced Abundant
Evidence Of Customer Benefit**

Both Ms. Ebrey and Mr. Effron challenge the adequacy of the evidence of customer benefit provided by ComEd. Ms. Ebrey asserts that ComEd must “provide the detailed evidence of objectives measured by tangible or quantifiable results and the specific dollar savings or other tangible benefits conferred upon ratepayers from its incentive compensation plan.” Ebrey Dir., Staff Ex. 2.0, at 24:520-22. Similarly, Mr. Effron claims that ComEd must prove that incentive compensation will “reduce expenses and create greater efficiencies in operations.” Effron Dir., AG Ex. 1.0, at 20:8-10. Ms. Ebrey and Mr. Effron demand more than the Commission requires,

⁴² The only support Ms. Ebrey offers for her position is a cite to a 12-year old Commission Order in Docket No. 93-0183. Ebrey Reb., Staff Ex. 13.0, at 21:427-30. The Orders cited above post-date Ms. Ebrey’s, and thus better reflect the Commission’s current position. Regardless, the uncontested facts in this case demonstrate that the O&M costs goal benefits customers, and therefore recovery for that expense is warranted.

or properly could require. The record in this proceeding contains all conceivable evidence of customer benefit from ComEd's incentive compensation program, including tangible benefits, and therefore must satisfy the Commission's test.

The evidence of significant benefits to employee performance, recruitment and more efficient operations brought about by incentive compensation are set forth above. The record also contains evidence of more specific, tangible customer benefits. For instance, ComEd's reliability has improved dramatically. Mr. Costello testified that CAIDI – the measure of outage duration – “improved from 142 minutes in 1999 to 109 minutes in 2005” and SAIFI – the measure of outage frequency – “improved from 1.42 outages in 1999 to 1.13 outages in 2005.” Costello Reb., ComEd Ex. 13.0 Corr., at 21:469-71. Similarly, “customer satisfaction has been a component of ComEd's incentive compensation plans dating back to at least 2001. During that time period, ComEd's performance on the American Customer Satisfaction Index (“ACSI”) Proxy has steadily improved from a 62.8 score in the first quarter of 2001 to a 70.8 score in the first quarter of 2005.” Costello Sur., ComEd Ex. 30.0, at 9:197-201. Finally, ComEd's O&M costs decreased by \$66 million in 2004 (Houtsma Reb., ComEd Ex. 18.0 Corr., at 7:141), which has reduced the cost of service in this proceeding to customers' direct benefit. Improved reliability and customer satisfaction and lower operating costs plainly constitute tangible customer benefits.

These tangible benefits apparently do not satisfy Ms. Ebrey, who further demands that ComEd “quantify” the precise impact of incentive compensation on those (and all other) measures. Nor do they satisfy Mr. Effron, who apparently finds customer benefit only through specific, quantifiable “reduce[d] expenses” and “greater efficiencies,” because the record clearly contains abundant, uncontested evidence that incentive compensation indeed reduces expenses

and creates efficiencies. Those demands are not realistic. Mr. Meischeid testified that such evidence simply is not available, explaining that “[g]iven the broad array of factors that influence employee performance, including variables that come into play at the individual, company and market levels, there are substantial difficulties in isolating the precise impact a particular incentive compensation program had upon employee performance.” Meischeid Reb., ComEd Ex. 27.0, at 6:122-25. Ms. Ebrey and Mr. Effron insist upon evidence that ComEd, or any other utility, simply cannot provide. As such, their approach to incentive compensation serves only to thinly disguise a pre-determined decision to deny recovery: *i.e.*, they purport to base their opposition to recovery on a test, but that test can never be met.

Importantly, however, the inability to quantify customer benefit from incentive compensation does not mean customers do not in fact benefit. Mr. Meischeid testified:

Well-designed incentive plans using key performance indicators benefit everyone – customers included. Employees come to understand why they are doing what they are doing and how their activities tie into the activities of the unit and the company itself. As a result, productivity rises, more attention is paid to cost control and more focus is given to customer service. They promote greater teamwork, more productivity, quality, cost control and employee involvement.

Meischeid Reb., ComEd Ex. 27.0, 6:137-7:143 (emphasis added). The measurable improvement in ComEd’s reliability, operating costs and customer satisfaction proves Mr. Meischeid correct.

Moreover, contrary to Ms. Ebrey’s above-described assumption that financial measures do not benefit customers, the financial measures of ComEd’s incentive compensation plan do benefit customers because they bring about a well-balanced plan: “plans that combine operational and financial measures appear to produce the most positive results – improved productivity, higher quality, enhanced customer satisfaction and lower costs” (Meischeid Reb., ComEd Ex. 27.0, at 7:144-46) – all of which inure to the benefit of customers. That effectiveness explains why ComEd, and nearly all utilities, use a plan that combines operational

and financial measures. Meischeid Dir., ComEd Ex. 12.0, at 16:333-35. Furthermore, “[g]iving short shrift to one of the goals used in a well-designed incentive compensation system is likely to provide less value to a company’s customers and owners in the long run.” Meischeid Reb., ComEd. Ex. 27.0, at 7:146-48.

Finally, and significantly, ComEd’s entire incentive compensation plan – both the operational and the financial aspects – has a customer satisfaction overlay that brings the entire focus of the plan to that most basic customer benefit. As Mr. Costello described:

The total incentive compensation payout would increase, decrease or remain the same based upon whether ComEd [improved, fell or remained the same compared to peer utilities using the ASCI Proxy]. The improved customer satisfaction represents another tangible benefit to customers from incentive compensation, and the customer satisfaction goal imbues the entire AIP – including the earnings per share component – with a direct customer benefit.

Costello Sur., ComEd Ex. 30.0, at 10:202-11. Accordingly, contrary to Ms. Ebrey’s assertion that the “shareholder protection feature” (which applies only to above-target payouts for which ComEd does not seek recovery) focuses ComEd’s plan on shareholder benefit, the customer satisfaction overlay, which does apply to the entire plan and can increase or decrease the entire award, strongly focuses ComEd’s incentive compensation plan on customer benefit.

In sum, the record demonstrates that incentive compensation benefits customers through: increased customer satisfaction; improved service reliability; more efficient, lower cost operations that lead to lower rates over time when compared to less efficient operations; improved employee performance; enhanced ability to attract and to retain high-quality employees; and better employee productivity. Those numerous benefits satisfy the Commission requirement that incentive compensation benefit customers. By claiming that more is required, Ms. Ebrey and Mr. Effron advance an unsupportable interpretation of the Commission’s test. Simply put, if Ms. Ebrey and Mr. Effron’s test for recovery of the expenses of a well-designed

incentive compensation plan that includes a balance of operational and financial measures has not been met on this record, then it cannot be met on any record. And if it can never be met, then the test serves only as a pretense for denying, with confiscatory effect, ComEd's recovery of a widely used, and vital, cost of doing business. That result would wrongly deny ComEd its entitlement to recover all prudent and reasonable expenses. *See Citizens 1995*, 166 Ill. 2d, 121.

c) **As A Necessary Component Of Total Compensation, ComEd Should Recover Its Incentive Compensation Expense Because It Is Reasonable And Prudent**

As set forth above, ComEd has met the Commission's specific test for recovery of incentive compensation expense. In reality, however, recovery of incentive compensation should be determined under the "reasonable and prudent" test used for expenses generally. ComEd's incentive compensation expense is in fact reasonable and prudent, meriting recovery.

Before incentive compensation fully emerged as a ubiquitous method of compensating employees, it made sense to ensure that a utility seeking recovery for incentive compensation was not merely experimenting with the latest trend, but actually was committed to the program. But as the uncontested record shows, nearly every utility now uses incentive compensation as part of its total compensation package because of the positive impacts on employee performance and recruitment. Accordingly, there is no reason to suspect that ComEd's use of incentive compensation is any more novel or temporary than its payment of base salary or health benefits. Thus, although the record also demonstrates ComEd's individual commitment to incentive compensation, such further proof should not be needed.

Similarly, prior to incentive compensation gaining wide acceptance, it was perhaps not unreasonable to view it as an "extra" cost that required separate justification of customer benefit for recovery. But now that it forms an essential part of total employee compensation, such

justification is no longer required. As a standard part of total compensation, the only question is whether the amount is reasonable. Moreover, if incentive compensation did not provide benefits, it would not have gained wide acceptance. Those benefits are well-documented on the record.

An insistence on a separate justification for incentive compensation not only has outlived its usefulness, but affirmatively inflicts harm by producing unreasonable results and perverse incentives. For instance, as an undeniably essential component of ComEd's compensation package needed to attract high-quality employees, it is undisputed that ComEd would have to increase some other aspect of compensation (such as base salary) as a substitute (albeit an inferior one). *Costello Reb.*, *ComEd Ex. 13.0 Corr.*, at 16:382-85. It also is undisputed that improving ComEd's ability to recruit high-quality employees and to motivate them to improve performance is prudent, and that ComEd's total cash compensation levels are reasonable. And, Ms. Ebrey acknowledged on cross examination that, for revenue requirement purposes, it makes no difference whether the amounts paid are for incentive compensation or for base salary. *Tr.* at 1875:12-22, 1876:1-2.

Those facts coalesce to present the following unreasonable scenario. Assuming for simplicity that ComEd's total employee cash compensation totaled \$100 million and consisted entirely of base salary, recovery of that expense would occur without further analysis because no party contends that ComEd's total cash compensation levels are not reasonable or prudent. But, if \$10 million of that \$100 million total represented ComEd's incentive compensation expense, then recovery of that same \$100 million in total expenses is permitted only if ComEd shows that the \$10 million in incentive compensation expenses provides an independent, "quantifiable" benefit to customers. Requiring such independent justification is irrational because no party disputes that that incentive compensation works to improve employee performance and offer

other benefits, and Staff has expressly stated that it does not want ComEd to eliminate its program and the benefits that flow therefrom. Put another way, if ComEd would not need a separate justification of the final \$10 million of the \$100 million in total cash compensation expense when it takes the form of additional base salary, then it should not need a separate justification for that final \$10 million in expenses just because it takes the form of incentive compensation – especially because incentive compensation provides benefits base salary cannot.

That unreasonable scenario leads to the perverse incentive. Mr. Costello testified that denying ComEd recovery of the incentive compensation portion of total compensation:

generates the perverse incentive for ComEd to drop incentive compensation and pay the difference in additional base salary. In that instance, ComEd would recover its full compensation expense. But that result would not benefit ComEd's customers, as ComEd's employees would not have the targeted focus on improving performance and the other motivational benefits provided by incentive compensation would be lost – benefits that no witness has even questioned.

Costello Sur., ComEd Ex. 30.0, at 12:237-42. Thus, imposing a separate justification encourages utilities to drop incentive compensation, which would eliminate the acknowledged benefits to employee performance, but offer them nothing in return because customers would pay the same rates if base salary were increased to offset the elimination of incentive compensation.

Finally, Staff's presumed answer to ComEd's argument regarding the perverse incentive — that it does not recommend that ComEd stop paying incentive compensation, but only that ComEd not recover for it — is no answer at all. That position amounts to an admission that incentive compensation is reasonable and prudent, but that recovery should nevertheless be denied because Staff believes that ComEd will continue to pay incentive compensation, and customers will continue to reap the benefits, in any event. Staff's position thus reflects a confiscatory goal for denial of a legitimate expense that is unlawful, and reversible error.

7. Uncollectibles Expenses

ComEd has correctly included \$15,803,000 of uncollectibles expenses in its operating expenses in its final revised proposed revenue requirement. ComEd's actual 2004 uncollectibles expenses were \$37,054,000, of which ComEd correctly determined that \$13,129,000 was related to Illinois-jurisdictional delivery services (not including transmission) revenue at present rates. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 25:536-45; ComEd Ex. 5.1; Hill Reb., ComEd Ex. 19.0 Corr., 53:1170-54:1188; Hill Sur., ComEd Ex. 36.0 Corr., 42:950-43:969 and Sched 10. ComEd also correctly determined that the incremental increase in uncollectibles expenses that it would experience, based on its final revised proposed revenue requirement and its uncollectibles rate of 0.85%, is \$2,674,000. *E.g.*, Hill Reb., ComEd Ex. 19.0 Corr., 52:1146 - 53:1169; Hill Sur., ComEd Ex. 36.0 Corr., 42:950 - 45:1019 and Schedule 1 Revised, pages 1, 6. The figure of \$15,803,000 of uncollectibles expenses in the revenue requirement is the sum of the foregoing \$13,129,000 and \$2,674,000 figures. That \$15,803,000 is part of the final revised total of \$146,979,000 of Customer Accounts Expenses (under the USoA, uncollectibles expenses are recorded in Customer Accounts Expenses, Account 904) included in the revenue requirement. *E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., at 24:517-519; Hill Sur., ComEd Ex. 36.0, Sched 1.)⁴³

ComEd employs prudent and reasonable practices in managing its uncollectibles expenses. *E.g.*, Costello Dir., ComEd Ex. 3.0 Corr, at 29:619-32. No party has submitted any claim, much less evidence, to the contrary.

Staff proposes to disallow \$1,988,000 of ComEd's 2004 test year uncollectibles expenses in the revenue requirement, and to reduce its incremental uncollectibles expenses, based on the

⁴³ A utility in a rate case can include such incremental uncollectibles expenses in its Customer Accounts Expenses by means of a calculation outside of the Gross Revenue Conversion Factor, as ComEd did, or by including its uncollectibles rate in its Gross Revenue Conversion Factor. This is a presentation question. The results are mathematically identical either way. (*E.g.*, Hill Sur., ComEd Ex. 36.0 at Schedule 1 Revised, pages 1, 6)

calculating an uncollectibles rate of 0.72% based on a five-year average of total revenues and uncollectibles expenses and then using that lower rate both to disallow that \$1,988,000 and to reduce the incremental uncollectibles expenses. *E.g.*, Ebrey Dir., Staff Ex. 2.0, at 25:536-547 and Schedule 2.5.

Staff's proposal is arbitrary and incorrect. ComEd submitted detailed evidence showing that to be the case. The use of the 2004 uncollectibles expenses amount to determine the uncollectibles expenses to be included in the revenue requirement rather than a five-year average is more appropriate and accurate than Staff's proposal, because the test year amount reflects ComEd's improved policies and practices for managing uncollectibles expenses, including stricter credit policies, implemented internal risk scoring systems, and other system changes, as illustrated by the fact that the total actual 2004 uncollectibles expenses are lower than the total actual uncollectibles expenses in 2003, 2002, and 2001. ComEd Ex. 5.1 at Schedule C-16; Hill Reb., ComEd Ex. 19.0 Corr., at 52:1146-1158. In addition, ComEd's uncollectibles rate of 0.85% is more appropriate and accurate than Staff's figure. As noted above, the jurisdictional test year uncollectibles expenses and uncollectibles rate of 0.85% are based on a detailed analysis of 2004 uncollectibles expenses and jurisdictional delivery services revenues by customer class, which is more appropriate and accurate than Staff's five-year average. A methodology based on total expenses and revenues is consistent with ComEd's determination of all other components of its jurisdictional cost of service. *E.g.*, Hill Reb., ComEd Ex. 19.0 Corr., 52:1146-53:1169; Hill Sur., Com Ed Ex. 36.0 Corr., 42:950-44:1019 Staff's proposal is without merit.

CCC proposes to disallow \$3,748,636 of ComEd's 2004 uncollectibles expenses, and \$18,021 of its jurisdictional 2004 outside collection agency expenses, based on first using a

general allocator to estimate the portion of ComEd's actual 2004 uncollectibles expenses that is for jurisdictional services and then further reducing the result based on the hypothesis that uncollectibles expenses will decline over time. McGarry Dir., CCC Ex. 2.0 Second Corr., at 23:511-17, 24:534-41.

CCC's proposal, too, is arbitrary and incorrect. ComEd submitted detailed evidence showing that to be the case. CCC provides no valid basis for rejecting ComEd's careful direct assignment of its actual 2004 uncollectibles expenses, CCC's simplistic general allocator is inappropriate and less accurate, and CCC's hypothesis regarding future decreases in uncollectibles expenses is pure speculation and is not a valid basis for an adjustment. Hill Reb., ComEd Ex. 19.0 Corr., 53:1170-55:1210; Hill Sur., ComEd Ex. 36.0 Corr., 45:1020-46:1033.

Finally, the AG in its calculations has assumed an uncollectibles expense rate of 0.64% (Effron Dir., AG Ex. 1.0, at 4:2-5 and Sched. A), but the AG's assumption relies entirely on the ratio between ComEd's total actual 2004 uncollectibles expenses, before functionalization, and ComEd's total actual 2004 revenues, before functionalization. The AG offered no other basis for its assumption, and no supporting evidence. There is no basis for rejecting ComEd's detailed analysis based on actual 2004 data, which is supported by the evidence, as shown above, in favor of the AG's inappropriate and less accurate assumption. ComEd's uncollectibles expenses in the revenue requirement should be approved. Once again, the AG's methodology is clearly result-driven with the objective to find the lowest figure possible regardless of how weak or inconsistent the methodology material and support for the AG's proposal.

8. Charitable Contributions

ComEd's final revised proposed revenue requirement includes a revised figure of \$3,660,000 of charitable donations, based on its actual 2004 donations, but accepting four of

Staff's proposed downward adjustments thereto. ComEd Ex. 5.1 at Schedule C-2.4; Hathhorn Dir., Staff Ex. 1.0, Sched. 1.9; Hill Reb., ComEd Ex. 19.0 Corr., 57:1269-75.

Charitable contributions are an appropriate component of the revenue requirement. Section 9-227 of the Public Utilities Act, 220 ILCS 5/9 227, states that: "The Commission shall be prohibited from disallowing by rule, as an operating expense, any portion of a reasonable donation for public welfare or charitable purposes."

Staff's revised proposal on this subject proposes only one additional disallowance, i.e., ComEd's contribution of \$50,000 to the Illinois Manufacturers' Association (the "IMA"). Hathhorn Reb., Staff Ex. 12.0, at 16:337-40; Staff Ex. 12.9. Staff's proposal is based on its conclusion regarding the primary purpose of the IMA. *Id.* However, ComEd's contribution was to the IMA's "Research on Education in Illinois" program, and is a charitable contribution. Hill Sur., ComEd Ex. 36.0 Corr., 46:1039-41. Staff's adjustment, therefore, should be rejected. ComEd's charitable contributions in the revenue requirement should be approved.

9 & 10 Procurement Case Expenses [Rate Base Effect]
Rate Case Expense [Rate Base Effect]

Please see Section III B 9/10, *supra*.

11. Environmental Expenses

Please see Section III.H.4, *infra*. To the extent that Rider ECR is approved without modification, no adjustment need be made to the test year revenue requirement. However, if Rider ECR is not approved as proposed by ComEd, Section III.H.4, *infra* at 209, sets forth the changes that must be made to the test year revenue requirement.

12. PSEG Merger Savings.

Exelon has proposed to merge with Public Service Enterprise Group ("PSEG"), the parent company of Public Service Electric and Gas Company ("PSE&G"), a New Jersey electric

and gas utility. Houtsma Reb., ComEd Ex. 18.0 Corr., at 20:438-42; Effron, AG Ex. 1.0, at 31:1-4. That proposed merger, which has not yet been approved by state and federal authorities, is currently projected to close in mid-2006 (Houtsma, ComEd Ex. 18.0 Corr., at 21:464-470), but even AG witness Mr. Effron agrees that that projected closure date is uncertain. Tr. at 1594:19–1595:10. If the merger were to be approved in mid-2006, the earliest projection of any actual savings to ComEd from the merger is mid-2007. Houtsma Reb., ComEd Ex. 18.0 Corr., at 22:483. Even this projection does not take account possible reductions to merger savings that could result from conditions on the merger that may ultimately be imposed by the New Jersey Board of Public Utilities, (“New Jersey BPU”) or the Department of Justice, (“DOJ”). Houtsma Reb., ComEd Ex. 18.0 Corr., at 21:458-461. Accordingly, any projected savings from the merger will not occur within 12 months of the filing of the tariffs that initiated these proceedings (i.e., by August 31, 2006), and are neither known nor measurable changes, nor changes determinable in amount, as would be required to meet the criteria of Part 287.40 of the Illinois Administrative Code for a pro forma adjustment to test year expenses. If the merger is closed, and savings achieved starting in 2007, those savings can be taken into account in determining ComEd’s revenue requirement in the next rate case.

Not to be deterred by facts or by Commission rules, AG witness Mr. Effron recommends that ComEd’s test year operating expenses be reduced by \$20.561 million to reflect alleged annual merger “savings” which he derived by mathematical manipulations of ComEd’s projections from the New Jersey proceeding. This adjustment should be rejected for at least four separate and independent reasons.

First, even if the merger were to close by August 31, 2006, which has not been established on this record,⁴⁴ and even if it were assumed that the standards for projecting savings in the merger proceeding are the same as required by Part 287.40, there would be no valid basis for disregarding Exelon's estimates and substituting Mr. Effron's. The Exelon estimates of merger savings do not show any net merger savings until mid-2007, well beyond the cut-off date of August 31, 2006 for pro forma changes to test year costs.

Second, Exelon's estimates of merger savings in the New Jersey proceeding in fact do *not* meet the standards of Part 287.40. As Ms. Houtsma testified, "[t]he fact that an estimate can be prepared with confidence in a merger proceeding does not mean that it can meet the standard required for inclusion in a rate case test year." Houtsma Reb., ComEd Ex. 18.0 Corr., at 21:461-63.

The merger savings projected by Exelon are not "known and measurable" nor "determinable" as required by Part 287.40, in part because the merger is currently subject to numerous regulatory approvals, including approvals by the New Jersey BPU and the DOJ. Not only are these proceedings still pending, but even if the merger is approved, when the merger will be approved, whether there will be conditions imposed that impact the savings that can be realized, and when the savings will begin to be realized is uncertain. Houtsma Reb., ComEd Ex. 18.0 Corr., at 21:452-61. Moreover, even if the merger were approved and closed in mid-2006, there is a significant ramp-up period before any merger savings could be fully achieved and there

⁴⁴ The Commission must base its determinations in this case on the record. E.g., 220 ILCS 5/10-113. As of the close of the record, the merger has not occurred and uncertainty remains as to if or when it will occur and what conditions will apply if it does occur. Mr. Effron admits that unless there is a merger, there can be no merger savings. Tr. at 1595:11-19. He also admits that the timing of the close of the merger is now more uncertain than it appeared when he developed his proposed adjustment. Tr. at 1594:19 – 1595:5. Accordingly, for these reasons alone, the Commission may not lawfully consider savings which are uncertain from what is still a potential Exelon/PSEG merger that the record does not establish will close by August 31, 2006.

are significant up-front costs that will be incurred to achieve those savings. Thus, no net savings are projected for ComEd from the merger until at least mid-2007, well beyond August 31, 2006. Houtsma Reb., ComEd Ex. 18.0 Corr., at 22:477-83. In addition, as is evident from the table at page 22 of Ms. Houtsma's testimony, over 70% of the expected net savings to ComEd from the merger would occur in 2008 and 2009. Such far distant savings, which Mr. Effron's use of averaging makes appear will occur in 2006, even though they will not, are far outside the time period allowable for a pro forma adjustment. Houtsma REb., ComEd Ex. 18.0 Corr., 21:467-22:490.

Third, if Exelon's merger savings estimates are not "known and measurable" and "determinable", Mr. Effron's are even less so, since he starts with Exelon's projections and simply reduces Exelon's projections of expected four year *gross* savings by 50% to "avoid disputes." This back of the envelope estimate by Mr. Effron, which on its face is ambiguous and uncertain, is not based on any study or analysis presented in this proceeding of what is required to produce the savings. Houtsma, ComEd Ex. 18.0, at 23:498-506. Moreover, as Mr. Effron conceded at the hearings, even if the merger were to close by August 31, 2006, ComEd would not achieve the annual merger savings he projects of \$20.6 million. Tr. at 1596:19-21, 1598:2-18; 1600:10-20. Mr. Effron has provided no estimate of what amount of savings would occur by August 31, 2006, and absent that showing, his merger savings adjustment fails to meet the Part 287.40 requirement.

Fourth, and finally, over the four year period Mr. Effron testifies is appropriate for estimating savings (Effron Dir., AG Ex. 1.0, at 37 n.7), Mr. Effron's proposed adjustment assumes total savings of \$82,244,000, which is more than double Exelon's estimate of net savings to ComEd from the merger over this same period of \$43.4 million. Houtsma Reb., Com

Ed Ex. 18.0 Corr., at 22:477-83. Thus, use of Mr. Effron's proposed estimate would lead to a cumulative revenue shortfall for ComEd over four years of almost \$40 million, which would be both unfair and confiscatory. This is particularly true because ComEd will have had no opportunity to establish through evidence and hearings what those savings might actually be once the merger goes through and all conditions imposed on the merger are known.

13. Depreciation Expenses

ComEd's final revised revenue requirement correctly includes \$321,002,000 of depreciation expenses. *E.g.*, Hill Sur., ComEd Ex. 36.0 at Sched. 1, Revised, page 1. This is essentially the "return on" its capital investments to which ComEd is entitled. The other parties' proposed adjustments to ComEd's depreciation expenses in this case are entirely derivative of their respective proposed adjustments to plant discussed in Sections III.B (several subsections) and III.C.6, *supra*. Because their underlying proposed adjustments to ComEd's plant balances are without merit, as discussed there, their entirely derivative adjustments to ComEd's depreciation expenses also are without merit. ComEd's figure should be approved. The other parties' adjustments should not be approved.

14. Payroll Taxes

ComEd's final revised proposed operating expenses include a correctly calculated final revised figure of \$147,759,000 for "Taxes Other Than Income Taxes". Hill Sur., ComEd Ex. 36.0 Corr., at Sched. 1 Revised, page 1. One element of Taxes Other than Income Taxes is payroll taxes. (*E.g.*, Hill Dir., ComEd Ex. 5.0 Corr., 29:621-31, Appendix A:6-18; ComEd Ex. 5.1 at Sched. C-1 Errata, C-18) Staff proposed two adjustments to ComEd's payroll taxes figure as such, each of which ComEd has accepted (one in rebuttal and the other in surrebuttal) and each of which already is reflected in ComEd's final revised proposed revenue requirement.

Hill Reb., ComEd Ex. 19.0 Corr., at 60:1331-35 and Schedule 1; Hill Sur., ComEd Ex. 36.0 Corr., at 5:96-99 and Sched. 1 Revised at pages 1, 2, and Sched. 4. Because Staff and certain intervenors propose adjustments to elements of the compensation that ComEd pays its employees, they also propose entirely derivative adjustments to ComEd's payroll taxes figure. However, because their underlying proposed adjustments to ComEd's employee compensation are without merit, as discussed in the applicable sections of this Brief, their entirely derivative adjustments to ComEd's payroll taxes figure also are without merit. ComEd's payroll taxes figure should be approved. Staff's and intervenors' proposed adjustments should not be approved.

15. Income Tax Expenses

ComEd's final revised proposed operating expenses include a correctly calculated final revised figure of \$240,757,000 for income taxes. Hill Sur., ComEd Ex. 36.0 Corr., at Sched. 1 Revised, page 1. Staff and intervenors have proposed adjustments to ComEd's income taxes figure, but their proposed adjustments are entirely derivative of other of their proposed adjustments to ComEd's revenue requirement. *E.g.*, Hill Sur., ComEd Ex. 36.0 Corr., at 52:1180-83. Because their underlying proposed adjustments to ComEd's revenue requirement are without merit, as discussed in the applicable sections of this Brief, their entirely derivative adjustments to ComEd's income taxes figure also are without merit. ComEd's income taxes figure should be approved. Staff's and intervenors' proposed adjustments should not be approved.

16. Gross Revenue Conversion Factor

Please see Section III.C.7, *supra*.

17. Exelon GSA

Please see Sections II.A.5.b, III.C.3.c, and III.C.3.d, *supra*.

18. Other

Not applicable.

D. Revenues

1. Weather-Normalization

There does not appear to be a material contested issue on this subject.

2. Increase in Non-DST Revenues

In the context of how the subject has been raised in this case, “non-DST” revenues are those revenues of ComEd that are not attributable to an Illinois-jurisdictional delivery services tariff and are not miscellaneous revenues (or part of the “new business” revenue credit). BOMA witness Michael McClanahan asserted in his direct testimony that ComEd had not justified the reason for its non-DST operating revenues number of \$3,883,066,000 for 2004. McClanahan Dir., BOMA Ex. 2.0, 4:83-6:123. ComEd witness Mr. Hill in his rebuttal carefully explained how Mr. McClanahan had erred, why his assertion should be rejected, and why this is only a presentation item that does not affect the revenue requirement. Hill Reb., ComEd Ex. 19.0 Corr., 5:101-8:156. Mr. McClanahan did not respond in his rebuttal testimony.

3. Other

Not applicable.

E. Rate of Return

ComEd’s actual before-tax costs of capital are approximately \$552.003 million annually, or 29.64% of ComEd’s total delivery revenue requirement. ComEd Ex. 36.0, Sch. 1 Rev. at 6:3,22. Allowing ComEd to recover its capital costs is just and reasonable and an unquestioned legal requirement. *Bluefield Water Works & Improvement Co. v. Public Serv. Comm’n*, 262 U.S. 679, 692-93; 43 S. Ct. 675; 67 L. Ed. 1176, (1923); *Federal Power Commission et al. v. Hope*

Natural Gas Co., 320 U.S. 591, 603 (1944); *Business & Professional People for Public Interest v. Illinois Commerce Com.*, 164 Ill. 2d 175, 195-96, 585 N.E.2d 1032, (1991); Mitchell Reb., ComEd Ex. 20.0, at 2:33-6; Kight Tr. at 1822:3-20; Bodmoer Tr. at 1223:12-21. Full recovery of ComEd's reasonable capital costs is also beneficial to customers, essential to ComEd's ability to continue to provide efficient and reliable service, and keeps costs down in the long term. Mitchell Dir., ComEd Ex. 20.0, at 2:26-29; Kight Dir., Staff Ex. 4.0 Corr., at 2:31-41. The Commission should approve rates based on ComEd's established actual cost of capital.

As with all utilities, ComEd's capital costs include the interest and related charges paid to borrow money (cost of debt) and the costs incurred to attract and maintain investments in common stock (cost of equity).⁴⁵ While costs of equity are not "billed" to the utility in the same way as, for example, most distribution operating expenses, they are just as real – and just as appropriately and essentially recovered in rates. *New Landing Utility, Inc. Proposed General Increase in Water and Sewer Rates*, 04-0610, 2005 Ill. PUC LEXIS 340, 32-34 (Final Order, 2005); *Peoples Gas Light and Coke Co. v. Slattery*, 373 Ill. 31, 68 (1939); *Public Utilities Com. ex rel. City of Springfield v. Springfield Gas and Electric Co.*, 29 Ill. 209, 216 (1919). In ComEd's case, its capital costs include its 6.50% cost of debt and 11.00% cost of equity, and they reflect ComEd's "A-" credit rating (on its first mortgage bonds) and a correspondingly balanced capital structure with approximately 54% equity. Mitchell Dir., ComEd Ex. 7.1, Schedule D-1.

As with all utilities, ComEd's costs of debt and equity are set by the capital markets, not by the Commission. Capital costs are based on investors' expectations of return related to risks associated with the investment, taking into account its growth prospects, operational riskiness,

⁴⁵ Perhaps because these costs are applied to the level of rate base investment, they are also sometimes called "rate of return" or "return of and on investment," but they remain real costs.

regulatory environment, and fundamental credit measures. Mitchell Reb., ComEd Ex. 20.0, at 2:30-32; Hadaway Dir., ComEd Ex. 8.0, at 10:208-17; Janous, Tr. 1942:17 – 1944:13. The Commission’s job is to correctly the market signals that concerning the rates of return that it demands, not to second-guess the market or to substitute a lower cost to reduce rates. Moreover, since the capital markets are both national and highly competitive, ComEd’s capital costs are influenced heavily, if not dictated, by the returns available on competing investments, especially utility equity and new utility debt. For this reason, it is established law that “a proper rate of return for a regulated utility is one that is commensurate with the returns on investments in other enterprises having corresponding risks.” *Illinois Bell Tel. Co.*, ICC Docket 82-0802, 1983 Ill. PUC LEXIS 1, 16 (1983).

It is also basic constitutional law, long reflected in Commission precedent, that “[t]he return to the equity owner ... should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.” *Illinois Bell*, 1983 Ill. PUC LEXIS at 221, *quoting FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). A utility’s management is responsible for making the business decisions about its financial objectives and how its investments will be financed. It is the Commission’s task to review those decisions for prudence and reasonableness, not to second-guess them. *Public Utilities Commission v. Springfield Gas Co.*, 291 Ill. 209, 218-19 (1920); *Iowa-Illinois Gas & Electric Co. v. Illinois Commerce Com.*, 19 Ill. 2d 436, 442 (1960). So long as management’s actions are reasonable and prudent, the utility need not prove that its decisions were “optimal” or the lowest-cost approach that could be devised, with hindsight, at the time of the case. *People ex rel. Hartigan v. Illinois Commerce Comm’n*, 214 Ill. App. 3d 222, 227-28 (1991).

The Commission should allow ComEd a rate of return that matches its actual cost of capital in order to allow ComEd to remain financially strong. It benefits consumers to have capital costs reflected accurately, since this reduces capital costs in the long term and enables the utility to continue to meet its service and reliability obligations at reasonable rates. Mitchell Reb., ComEd Ex. 20.0, at 2:26–29, 29:622–625, 30:640–642; Kight Dir., Staff Ex. 4.0 Corr., at 2:31-41. As the Commission observed in regard to Illinois Power:

[The] Commission is faced with the need to allow Illinois Power sufficient revenues to maintain interest coverage ratios at levels which will maintain maximum affordable credit ratings and allow the financing of the balance of Clinton construction at the lowest possible cost in accordance with the Hope and Bluefield capital attraction test. *Fed. Power Comm. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Co. v. Pub. Serv. Comm.*, 262 U.S. 679 (1923). Both Illinois Power and its ratepayers have a common interest in maintaining the maximum affordable credit rating so as to avoid a derating and resulting higher interest charges. This is necessary since the total cost of the plant, and a reasonable shareholder return on investment, are all costs which are paid by the consumer. The lower these costs are today, the lower rates are in the future.

Illinois Power Co., ICC Docket 80-0365 & 80-0544 [Cons.], 1981 Ill. PUC LEXIS 18, 140-41 (1981). This reflects the constitutional requirement that the “return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.” *Bluefield Waterworks & I. Co. v. Public Service Comm'n*, 262 U.S. 679, 693, (1923); accord, e.g., *Commonwealth Edison Co.*, 1993 Ill. PUC LEXIS 84, 144-45 (1993).

1. Capital Structure

A utility's total capitalization has a capital structure comprised of its sources of capital — in this case common equity and long-term debt.⁴⁶ Normally, the cost of equity and debt for a company will be significantly different. Therefore, using a capital structure for ratemaking that differs from the actual capital structure significantly distorts the capital costs included in rates. Since capital costs are actual costs that must and should be recovered, it is critical that the capital structure be set accurately. Substitution of an artificial capital structure is nothing less than rejection of ComEd's actual costs in favor of an imaginary construct. It amounts to an express denial of cost recovery — in the case of the artificial capital structures now advocated by some parties, a huge denial of cost recovery, amounting to over \$75 million annually (after tax).

Moreover, even where a hypothetical capital structure is properly used in lieu of the actual capital structure, that hypothetical structure should reflect and respect appropriate management of the utility, and not be simply a mathematical technique to understate costs or an effort to replace a prudent management approach with some other approach that the proponent prefers. It would be particularly unfair and inappropriate for rate-making purposes to use an artificial capital structure for ratemaking that no witness recommends actually be used to finance the company, while rejecting capital structures that the record fails to show to be imprudent. Yet, that is exactly what ComEd's opponents advocate here.

In this case, ComEd proposes to use its actual capital structure, after a *pro forma* adjustment to remove a one-time fair value step-up in equity that occurred due to the merger accounting, and a measurement period ending June 30, 2005. Mitchell Dir., ComEd Ex. 7.0, at

⁴⁶ Some utilities also rely on preferred stock or short term debt as a permanent source of financing. ComEd does not. Therefore, no short-term debt or preferred stock are included in ComEd's capital structure, and the cost of such sources of capital are not relevant here. Mitchell Dir., ComEd Ex. 7.0, at 3:56-63; ComEd Ex. 7.2, Schedule D-2; Kight Dir., Staff Ex. 4.0 Corr., at 11:201-08.

6:118-23. This capital structure reflects the actual adjusted 54.20% equity and 45.80% debt and is based on ComEd’s actual audited book balances of debt and equity.⁴⁷ Mitchell Dir., ComEd Ex. 7.1, Schedule D-1. No party disputes ComEd’s proof of its 54/46 capital structure, the actual debt and equity balances on its books from which it is derived, or the appropriateness of the measurement period ComEd used. That actual capital structure – together with the percentage costs of debt and equity discussed *infra* – defines the actual cost that ComEd incurs in attracting and maintaining the capital that ComEd uses for its only current business: to purchase, operate, and maintain its delivery facilities and to provide delivery service with them.

Staff, CCC, IIEC, and the AG argue that the Commission should substitute an artificial capital structure with much greater leverage than either ComEd or similar utilities actually have. *See, e.g.*, Kight Dir., Staff Ex. 4.0 Corr., 4:74–6:112; Gorman Dir., IIEC Ex. 3.0 Corr, 14:322-25, 18:416-422; Bodmer Dir., CUB/CCSAO Ex. 1.0 Second Corr., 20:597-21:549. The capital structures – actual and artificial – proposed in this case and their effects on the revenue requirement (all other things being equal) are shown in the table below.⁴⁸

	Percent of		Effect on Recovery of ComEd’s Costs of Changes in the Capital Structure at:	
	Equity	Long-Term Debt	ComEd Debt and Equity Costs	Staff Debt and Equity Costs
ComEd Actual “54/46” Capital Structure	54.20%	45.80%	ComEd recovers its actual costs	\$26.9 million under-recovery
Hypothetical “50/50” Capital Structure	50.00%	50.00%	\$18.4 million under-recovery	\$43.4 million under-recovery
Artificial “37/63” Capital Structure	37.19%	62.81%	\$74.5 million under-recovery	\$93.4 million under-recovery

⁴⁷ For ease, ComEd will refer “in shorthand” to capital structures by their equity and debt percentages, rounded to the nearest percentage point. Thus, ComEd’s actual capital structure would be abbreviated as “54/46.”

⁴⁸ The “Effect on Recovery of ComEd’s Costs of Changes in the Capital Structure” reflects the after-tax effect on the total revenue requirement based on changes in the capital structure alone, calculated using the updated rate base proposed by ComEd (ComEd Ex. 45.0). The effect of the capital structure change does vary depending upon the annual costs of debt and equity and, therefore, the impact of the different capital structures is presented at the costs of debt and equity proposed by both ComEd and Staff.

Because the proposals of Staff, CCC, IIEC, and the AG depart from ComEd's actual capital structure, they understate ComEd's actual capital costs. In the case of the artificial 37/63 capital structure, that departure is radical and irreconcilable. The 37/63 capital structure alone denies ComEd recovery of more than \$74 million in costs each and every year. Moreover, even if the 37/63 capital structure were not a wholly unrealistic capital structure for ComEd (which it is), a company that could support such a capital structure would have a very different cost of equity, a difference that is completely ignored by Staff, CCC, IIEC, and the AG. Hadaway Sur., ComEd Ex. 38.0, at 2:30–39 (when leverage increases, the cost of equity increases). This result is confiscatory and, as discussed further below, not sustainable.

Apart from its illegal and confiscatory effect, the record does not support either the purported reason for rejection of ComEd's actual capital structure or the use of a radical artificial replacement. The law on the recognition of utility capital structures is clear. ComEd is entitled to manage its own business affairs. *Public Utilities Commission v. Springfield Gas Co.*, 291 Ill. 209, 218-19 (1920); *Iowa-Illinois Gas & Electric Co. v. Illinois Commerce Com.*, 19 Ill. 2d 436, 442 (1960). A key management function is the choice of a reasonable capital structure. In order to disturb a utility's capital structure, it is necessary that the actual capital structure be proven to be unreasonable. As noted above, suggesting that another capital structure is reasonable, or that another structure might be "optimal" or "lower cost" is not sufficient. *Hartigan*, 214 Ill. App. 3d at 227-28. Indeed, it is acknowledged that there is a range of capital structures that are reasonable. Gorman Dir., IIEC Ex. 3.0 Corr., 17:400-18:412; Mitchell Reb., ComEd Ex. 20.0, at 4:65-73, 16:341-43; Mitchell Sur., ComEd Ex. 37.0 Second Corr., at 23:462-68.

a) **ComEd's Capital Structure is Reasonable**

ComEd demonstrated that its actual capital structure is reasonable. Mitchell Reb., ComEd Ex. 20.0, at 2:26-29, 3:49-9:192; Mitchell Sur., ComEd Ex. 37.0 Second Corr., 23:462-68. It was chosen for sound business reasons. Mitchell Dir., ComEd Ex. 7.0, at 5:91-103, 7:144-8:156. It is comparable to previously approved capital structures and the capital structures of other financially sound utilities. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 19:384-20:291. It also results in reasonable credit metrics. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 15:313-16:340. The record proves, without contradiction, that ComEd's management carefully considers its levels of debt and equity and has managed the capital structure to maintain a reasonable A- credit rating. Mitchell Reb., ComEd Ex. 20.0, at 2:26-29, 3:49-9:192; Mitchell Sur., ComEd Ex. 37.0, at 8:157-75. It also proves that ComEd has consistently maintained a level of equity consistent with both past equity balances and the undeniable need to maintain a level of equity sufficient to allow the utility to maintain its financial strength when risks inevitably materialize. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 16:341-17:345.

By contrast, no witness testifies that an A- credit rating is *per se* unreasonable. No witness testifies that ComEd's liability management program, which reduced the amount of outstanding debt, was imprudent. No witness testifies that, historically, ComEd had too much equity or that it is unreasonable for ComEd to maintain a \$5.194 billion equity balance. Hill Sur., ComEd Ex. 36.0 Corr., Schedule C-3, at 1. Indeed, capital structures consistent with a strong credit rating have been approved for ComEd in each of its last three rate cases. *Commonwealth Edison Co.*, ICC Docket 94-0065 (Final Order, January 9, 1995); *Commonwealth Edison Co.*, ICC Docket 99-0117 (Final Order, August 26, 1999); *Commonwealth Edison Co.*, ICC Docket 01-0423, 224 P.U.R. 4th 357, 336-37 (Final Order, March 28, 2003). ComEd does not have to prove its actual capital structure is the "best" capital

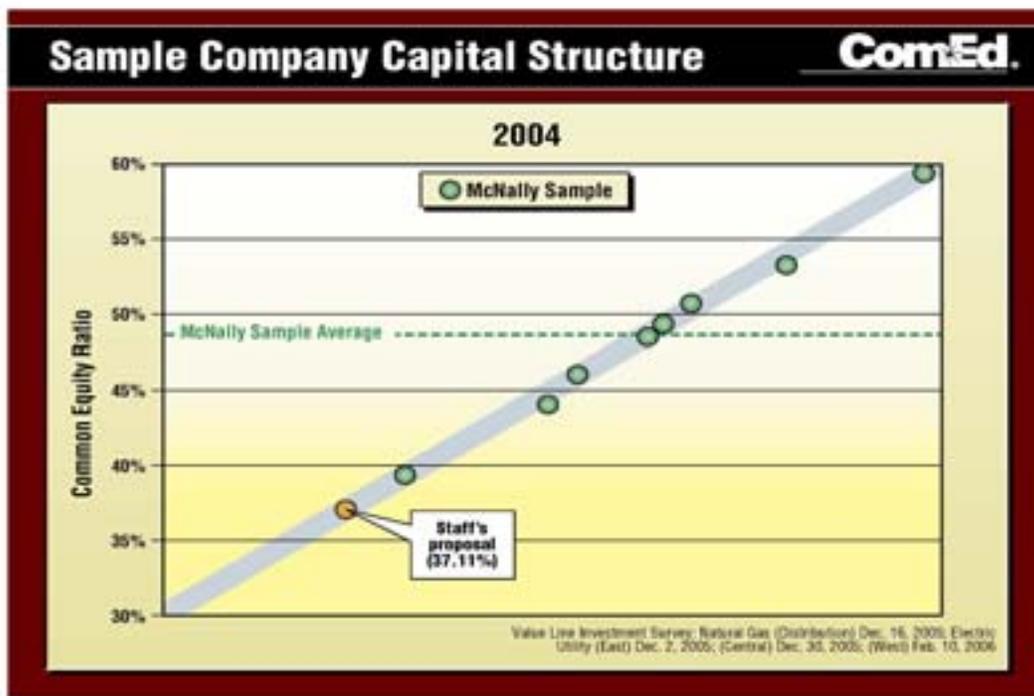
structure or the only prudent capital structure, only that it is reasonable. It bears repeating that ComEd has thereby met its burden of proof.

Two other important facts appear in the testimony of even the advocates of the extreme 37/63 artificial capital structure. **First**, even the witnesses advocating its use for ratemaking purposes take care never to advocate that ComEd actually practice what they preach and issue debt sufficient to become financed by 63% debt. Gorman, Tr. 2004:2–2005:4. To put it bluntly: they ironically advocate basing rates on a capital structure that they do not expect or want ComEd to actually use.

Second, it is also noteworthy that the direct testimony of IIEC witness Gorman advocated strongly for a hypothetical 50/50 capital structure, observing correctly that equity percentages in the 50% range both comport with past Commission Orders and can be reconciled with the leverage ratios of ComEd's peers. Gorman Dir., IIEC Ex. 3.0 Corr., at 16:363-72. Although, in his rebuttal testimony, Mr. Gorman ultimately supported the artificial 37/63 capital structure (based on mistaken arguments about transfer of the former ComEd nuclear assets discussed below), Mr. Gorman certainly did not disavow or repudiate his earlier, forthright testimony about the reasonableness of a capital structure with approximately 50 % equity and without excessive leverage.

It is not ComEd's burden to prove the unreasonableness of alternative capital structures. Yet, in this case the record plainly shows that the 37/63 capital structure is not reasonable. This leverage ratio is far outside that of typical utilities and is higher than any comparable company included in Staff's own sample of comparable companies, as illustrated by equity ratios of the

Staff companies, which are depicted in the chart below. Mitchell Sur., ComEd Ex. 37.0 Second Corr., at 18:367–19:395.⁴⁹



Similarly, Staff witness Kight’s argument that a capital structure with 37% equity is consistent with a range of financially sound utilities is crippled by her improper inclusion of the non-profit and functionally unregulated cooperative, Old Dominion Electric. When Old Dominion is excluded “all of the remaining utilities have common equity ratios of at least 41.6% and two had common equity ratios in excess of 60%. None of the remaining companies had common equity ratios nearly as low as the 37.11%” Mitchell Sur., ComEd Ex. 37.0 Second Corr., 6:120-23.

⁴⁹ Mr. McNally argues that the average needs to be adjusted for short-term debt balances. Even assuming, which the evidence does not show, that these balances are properly included in the regulatory capital structure (and, for many utilities, e.g., Nicor Gas, they are not), Mr. McNally also needs to rely on the flawed and inconsistent argument that TFI debt should simply be ignored to claim that 37% is anything but the aberrationally low level of equity that it plainly is. McNally, Tr. 1803:17– 1806:17; 1807:4–1808:3

Mr. Bodmer's similar efforts actually rely on companies with lower credit ratings and distort the overall conclusion that "despite [the] relatively weak S&P bond ratings [of the companies he cites], all but five of which have ratings below "A-," the average of the common equity ratios for the 25 electric companies was 48%." *Id.*, at 11:213-15. The record, in sum, shows that the 37/63 capital structure is not consistent with ComEd's current credit rating (Mitchell Reb., ComEd Ex. 20.0, at 3:47-53; Kight, Tr. 1841:9-1842:14), and that arguments to the contrary rely on ignoring the importance of total debt ratios and the impact that the capital structure would have on revenues going forward. Mitchell Reb., ComEd Ex. 20.0, at 2:26-29, 3:49-9:192; Mitchell Sur., ComEd Ex. 37.0 Second Corr., 8:157-175

Finally, when the Commission determines that a utility's capital structure is unreasonable, the appropriate ratemaking response is to use a reasonable hypothetical capital structure that reflects prudent management of the utility and, insofar as reasonable, reality. *Hartigan*, 214 Ill. App. 3d at 228. No party seriously contends – flawed arguments about the transfer of nuclear assets aside – that there is anything unreasonable about a capital structure in the 50/50 range. Indeed, IIEC witness Gorman actively proposed one. Gorman Dir., IIEC Ex. 3.0 Corr., 16:361-72. Unlike the 37/63 structure, a balanced capital structure can result in appropriate credit metrics and a very reasonable overall cost of capital, both absolutely and in comparison to other utilities against which ComEd competes in the capital markets. While ComEd strongly believes that it has more than met its burden of proving the reasonableness of its actual capital structure, should the Commission disagree, the proper response is not to mechanically apply an equity adjustment that leads to unprecedented high leverage for ComEd, not to ignore ComEd history of prudent management decision-making regarding its own equity balances, not to impose a capital structure out of line with ComEd's peers, and not to impose a

capital structure that no witness advocates ComEd actually use. Adopting the artificial 37/63 capital structure would do just that.

b) ComEd Has Fully Adjusted for the Unicom/PECO Merger; Additional “Adjustments” for the Transfer of ComEd’s Former Nuclear Assets are Unjustified, Contrary to Prior Decisions, and Illegal

Being unable to prove that ComEd’s actual 54/46 capital structure is unreasonable, the parties supporting the 37/63 capital structure claim that their artificial highly leveraged proposal is required by the need to undo the effect of “purchase accounting” – shorthand for the accounting entries required by law and by GAAP upon a merger like the Unicom/PECO merger – as it relates not to the merger but the value of nuclear assets subsequently transferred to an affiliate in early 2001.

The evidence shows, however, that the Unicom/PECO merger and the transfer of the former ComEd nuclear assets were two distinct transactions, separated by months, separately authorized by the Act, and separately reviewed by the Commission. The evidence also demonstrates without doubt that ComEd fully adjusted for the effect of the merger accounting on its equity balance. Mitchell Reb., ComEd Ex. 20.0, 13:262–16:334; Mitchell Sur., ComEd Ex. 37.0 Second Corr., 12:243–15:310; Houtsma Reb., ComEd Ex. 18.0 Corr., 25:543–27:591; Houtsma Sur, ComEd Ex. 35.0, 16:352–23:510; Kight, Tr. at 1827:6-21. The net effect of the merger fair value accounting on ComEd’s equity balance was \$2.296 billion and 100% of that amount has been removed from equity in ComEd’s 54/46 capital structure. Mitchell Sur., ComEd Ex. 37.0, Second Corr., at 12:243-48.

The claim that ComEd’s equity should be reduced further is not about the effect of the merger itself, but about the value at which ComEd’s former nuclear assets were transferred more than five years ago. The fact that the merger required the write down of the assets to their fair

value is not in question. Rather, the claim is that when the assets were transferred some time thereafter, instead of being transferred at their then current – and actual – book value they should have been written up to their prior “original cost.”

This argument is based on faulty assumptions. It is contrary to the record, contrary to past Commission determinations of ComEd’s capital structure and equity balance, and seeks both an unlawful second review of the long-completed transfer transaction and an illegal result.

In summary:

1. The merger, the transfer of the assets, and the capital structure resulting after both the merger and the transfer were complete, have all been previously reviewed and approved by the Commission, not once but several times, both in transfer proceedings and in the context of ratemaking. There is no basis for a retroactive, inconsistent, and confiscatory determination now. Indeed, the Act specifically and unequivocally bars such a result in this case.
2. The transfer was implemented, and the resulting equity balance set, as required and authorized by law. ComEd was required by law and GAAP to transfer its nuclear assets at their actual book value at the time of the transfer, not at a retroactively reconstructed original cost. There is no contrary requirement under the Act for assets to be transferred at original cost. To the contrary, the write-down of the original cost of plant assets is specifically and expressly authorized by the Act. Moreover, if there had been a contrary requirement, the Commission could not approved the transfer under Section 16-111, nor to the capital structure in ComEd’s last rate case that reflected the transfer as it actually occurred.
3. If ComEd had been required to transfer the assets at a retroactively reconstructed original cost, the transaction could not possibly have been the same. If an imaginary speculative transfer at a retroactively increased “original cost” had been required in 2001, the structure of the transfer would itself have been different, the consideration would have been different, the accounting would have been different, and the resulting capital structure would have been different. It is grossly unfair to ComEd to insist on changing by some \$2.6 billion the value of the assets transferred while at the same time insisting that nothing else can change at all.

First, there is no doubt that the transfer of the nuclear assets and the resulting effect on ComEd’s equity balance, capital structure, and delivery rates have all been reviewed by the Commission in several prior Commission proceedings.

ComEd transferred its nuclear assets under the authority Section 16-111 of the Act. Initially, the transfer, its terms and structure, and its effect on ComEd's equity were all addressed in the Commission's Section 16-111 proceeding that reviewed the transfer. *Houtsma Sur., ComEd Ex. 35.0, 17:372-18:391*. The transfer was accomplished in accordance with the law, and with the Commission's determination in the notice proceeding dealing with the transfer. *Id.* The law required that the accounting be in accordance with GAAP, and GAAP required that the assets be transferred at book value at the time of the transfer. The accounting entries – including the effect on equity – resulting from the transfer were both described to the Commission in advance and submitted when finalized. *Houtsma Surr., Ex. 35.0, at 3:56-58, 17:374-18:391* There is, in short, no doubt that the entries, including the equity entries, were in compliance with the law and that the transaction was implemented as the Commission reviewed and accepted it.

Retroactive review of the transfer in an effort to recast it for ratemaking purposes as involving both assets with a \$2.6 billion greater book value and a correspondingly reduced balance in ComEd's equity – is unlawful and expressly prohibited by Section 16-111(g) of the Act. Section 16-111(g)(4) ensures that “[t]he Commission shall not in any subsequent proceeding or otherwise, review such a reorganization or other transaction authorized by this Section....” Indeed, the Commission has already found that the nuclear unit transfers are covered by this prohibition of Section 16-111. *Commonwealth Edison Company, ICC Docket 05-0159* (Order Jan. 24, 2006) (the “Procurement Order”) at 51.

The Commission also considered ComEd's equity balance and established the proper post-merger and post-transfer capital structure for ComEd in *Commonwealth Edison Co.*, Docket No. 01-0423. That rate case was initiated shortly after the completion of both the merger and the transfer, and established a capital structure for ratemaking. In that case, the Commission made

no reduction to ComEd's equity based on any notion that the nuclear assets had to be, or should have been, transferred at original cost rather than at book value. *Commonwealth Edison Co.*, Docket No. 01-0423, (Int. Order, April 1, 2002)⁵⁰ ("01-0423 Interim Order"), at 112 & App. A at Sch. 1. What is more, although Staff proposed other adjustments not relevant here, throughout the proceeding it steadfastly recommended that ComEd's capital structure and equity balance, for ratemaking purposes, be based on its actual book equity balance. Kight, Tr. 1840:21-1842:17, *quoting*, in part, J. Freetly (Staff) Dir., *Commonwealth Edison Co.*, Docket No. 01-0423 Staff, Ex. 5.0, at 9:143-46. The Interim Order cites and adopts the capital structure sponsored in J. Freetly (Staff) Supp. Reb., Staff Ex. 27.0 and 27.1 ("Freetly 01-0423 Supp. Reb.).⁵¹ Staff advocated no reduction in equity to reflect a retroactive increase to the "original cost" of the transferred nuclear assets.

The Commission's determination in Docket 01-0423 is not only inconsistent with the rationale offered for the 37/63 capital structure, it is wholly inconsistent with the equity balance which the proponents of the 37/63 capital structure ask the Commission to now use. In Docket 01-0423, the Commission found that ComEd's equity balance as of the end of 2001 was \$5.224 billion, a value very similar to the current equity balance. The Commission further found that this equity balance should be used in deriving the approved rates. Staff witness Freetly testified in that Docket that ComEd's actual capital structure "fairly represents the proportion of debt and

⁵⁰ The Commission essentially approved ComEd's capital structure twice in the context of Docket 01-0423. ComEd's equity balance was expressly considered and approved in the Commission's initial rate order (the "Interim Order"), which followed a full evidentiary hearing on rate issues but preceded the audit of certain distribution expenses and assets. The Commission's Amending Interim Order of April 10, 2002, made no relevant change. The Commission then adopted and approved revised rates in a final, post-audit, order. The Commission made no change to the equity balance or capital structure between the Interim and the Final Orders. *In re Commonwealth Edison Co.*, ICC Docket 01-0423 at 43 (Order March 28, 2003)

⁵¹ The Interim Order cites and adopts the capital structure sponsored in J. Freetly (Staff) Supp. Reb., Staff Ex. 27.0 and 27.1. Ms. Freetly's testimony explains that "balance of common equity shown on Schedule 27.1 was derived using a forecasted December 31, 2001 balance of common equity and adding \$125 million to reflect the amount of the receivable from Exelon for the year 2001." *Id.* at 2: 28-30.

equity that will be outstanding during the period that rates will be in effect”, *i.e.*, through the transition period. Freetly 01-0423 Supp. Reb. at 33-34. No witness here testified that there was any way to reconcile the \$5.224 billion Commission-approved equity balance with the artificial \$2.561 billion equity balance the 37/63 capital structure now requires. Mitchell Reb., ComEd Ex. 20.0, 7:141-150; Kight, Tr. 1841:9-1842:14.⁵² Indeed, the events of the past five years suggest that ComEd’s equity balance would, if anything, be equal or higher than the 2001 balance the Commission approved (Mitchell Reb., ComEd. Ex. 20.0, 5:100-6:122, 7:141-150) and Staff candidly conceded that they are unaware of any event that would account for a significant decrease in equity, let alone one of the huge magnitude that the 37/63 capital structure necessarily implies. Kight, Tr. at 41:7–1842:17.

This is not merely an argument that precedent should be respected. The Commission’s decision in Docket 01-0423 established ComEd’s equity balance and capital structure for the purpose of ratemaking. Parties arguing for the artificial 37/63 capital structure ask the Commission not just to now reject that decision, but also to retroactively reverse for ratemaking purposes, the Commission’s determination of the equity balance that should support rates. Indeed, CCC, IIEC, and Staff are simply trying to retroactively eliminate more than \$2.6 billion of equity that the Commission has expressly approved. This is plainly unsupported, illegal, and confiscatory.

Second, the transfer of ComEd’s nuclear assets at a book value reflecting the fair value write-down was mandated by GAAP and expressly authorized, for Illinois law purposes, by the Act. There is no doubt in the record that the nuclear assets were properly written down, and lawfully transferred, and that GAAP requires that transfer to occur at book value. Houtsma Sur.,

⁵² The derivation of the 37/63 capital structure and the \$2.561 billion equity balance it requires is illustrated in Kight Dir., Staff Ex. 4.0 Corr. Sch. 4.1.

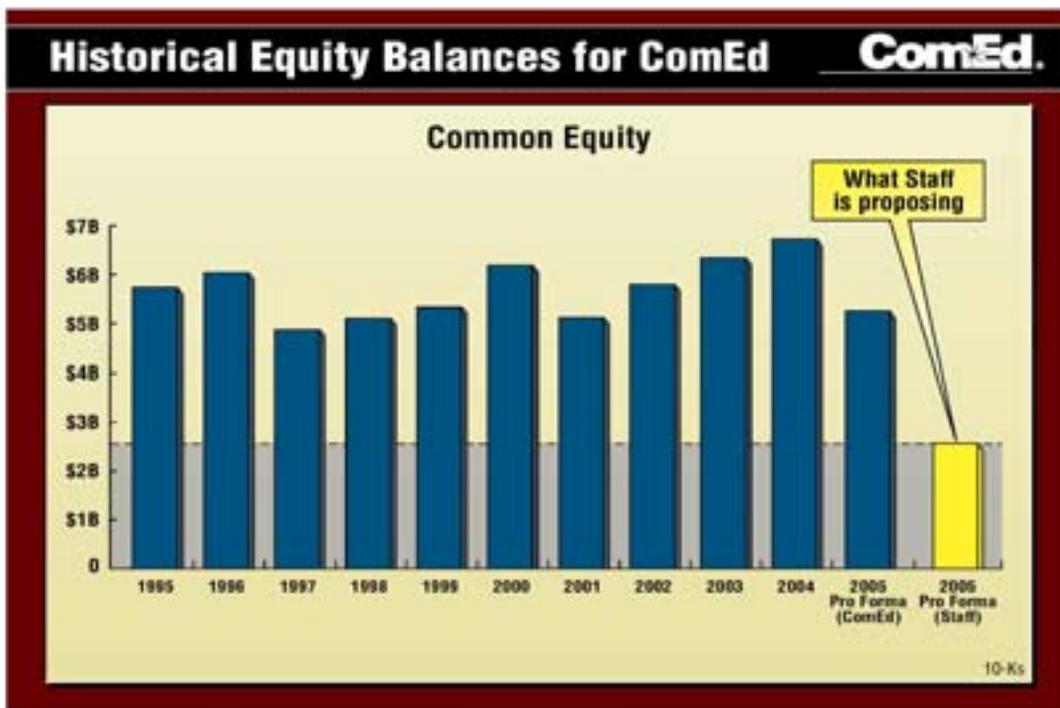
ComEd Ex. 35.0, 17:372 – 18:391. Nor is there any doubt that the equity balance implied by the artificial 37/63 capital structure is inconsistent with GAAP and ComEd’s audited financial statements. Houtsma Sur., ComEd. 35.0, 17:374-18:391; Kight, Tr. 1819:23-1825:17. ComEd simply could not have lawfully executed the asset transfer transaction in the manner suggested by Staff and others. Houtsma, Tr. 435:11-15.

But, even more importantly, the advocates of the artificial 37/63 ignore the fact that the Act specifically authorizes just the type of write down of original cost that ComEd undertook during the transition period. Section 16-111(g)(4) specifically empowers electric utilities “without obtaining any approval of the Commission other than that provided for in this subsection and notwithstanding any other provision of this Act or any rule or regulation of the Commission that would require such approval” not only to transfer assets, but to “record reductions to the original cost of its assets.” 220 ILCS 5/16-111(g)(4). This provision, which is neither addressed – nor even acknowledged – at any time by any Staff or intervenor witness, expressly authorizes the write-down that the 37/63 capital structure requires be reversed. The Commission is simply without jurisdiction, having found the transfer of the nuclear assets to be compliant with Section 16-111, to now reverse the write-down. Doing so in this case would be directly contrary to Section 16-111(g)(4) and would constitute reversible error.

Third, the proponents of the artificial 37/63 capital structure ask the Commission to assume that, had ComEd been required to transfer the assets at value (billions of dollars above book), it still would have structured the transfer in exactly the same way. Houtsma Sur., ComEd. Ex. 35.0, at 18:386-89. Of course, there is no evidence to support this unlikely assumption. Once the value of the plants is assumed to be different by billions of dollars, there is no basis in logic, fairness, business judgment, or common sense for assuming that the value is the only

element of the transaction that would have changed and that everything else would have remained the same. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 13:275-15:305. Yet, this is precisely what the proponents of the artificial 37/63 capital structure ask. *Id.* at 13:275-80.

The artificial 37/63 capital structure becomes even less plausible when the resulting impact on equity is considered. According to its proponents, the entire impact of the \$2.6 billion in retroactively increased value should have reduced equity. Yet, the fact is that ComEd has consistently managed its capitalization to achieve an equity balance above \$5 billion, as illustrated in the chart below. The equity balance that would have resulted from a transfer where



nothing but the value is changed would be plainly inconsistent with that practice, and results in an equity balance that the historical facts show would have been unacceptable. This is especially important given that ComEd could have avoided the impact on equity – even if it had been required to transfer the plants at a greater value – by structuring the nuclear asset transfer in any

number of different ways, such as receiving some cash for at least some portion of the asset value. Knight, Tr. at 1835:1-22.

The notion that any increase in the assumed value of the plants should only reduce ComEd's equity is further belied by the original financing of the plants. There is no doubt that the nuclear plants were financed with proceeds from both debt and equity. Houtsma Surr., ComEd Ex. 35.0, 17:374-18:391 Houtsma Tr. at 1836:9-16. Yet, the proponents of the 37/63 capital structure urge the Commission to ignore that fact, as well, and seek to deduct the retroactively calculated "original cost" only from equity. Houtsma Surr., ComEd Ex. 35.0, 17:374-21:459. As with the argument discussed above, the proponents do this despite the fact that there were plausible alternative structures for the transfer transaction that ComEd could have used at the time to avoid this impact, had it any reason to suspect that the transfer would later be recast as anything other than one of the book entries described in its Section 16-111 filing. Houtsma Surr., ComEd Ex. 35.0: at 2:460-69; Knight, Tr. 1835:1-22.

What the proponents of the artificial 37/63 capital structure are doing is trying to confiscate over \$75 million (after-tax) annually in real capital costs by arguing now that the lawful transfer of the nuclear assets should be treated as something other than what it was. As a result, they claim ComEd's capital structure should be set inconsistently with reality, inconsistently with the capital structures of its peers, and inconsistently with past Commission decisions. This request is not only contrary to the evidence, it is illegal.

In short, the unrefuted testimony in this record is that the transaction would either not have occurred if the result would have been what Staff now suggests or, if it had, it would have been structured much differently. The result, in either case, is that the resulting capital structure

would not be anything like what Staff and others now speculate. For this reason as well, adopting the artificial 37/63 capital structure is unjust, unreasonable, and unfair.

c) **Other Arguments For An Artificially Leveraged Capital Structure Are Unsupported And Incorrect**

Other arguments made by opponents of ComEd's actual capital structure are similarly unconvincing.

IIEC claims that a deduction must be made from equity because rate base does not closely correspond to total capitalization, and that "goodwill" does not "support" the provision of delivery service. This is a seemingly appealing but wholly sophistic argument. First, there is no reason whatsoever that rate base and capital structure should match, or even be close in value. For example, in Docket 01-0423, the Commission approved a \$12.198 billion capital structure and a net rate base of \$3.579 billion – less than 29.4% of the capital structure. *Commonwealth Edison Co.*, Docket No. 04-0143 (Interim Order, April 1, 2001) at 112; *Commonwealth Edison Co.*, Docket No. 04-0143 (Amendatory Interim Order, April 10, 2001), at 2, Finding (5). Here, IIEC would have the Commission believe that a capital structure of \$9.582 billion is somehow incredible when compared to a proposed rate base of \$6.174 billion – over 64.4% of the capital structure. Any such inference is plainly specious.

In fact, numerous factors cause capital structure and rate base to properly diverge over the years, and total capitalization may properly be more than, equal to, or in some cases even less than rate base. Capital structure is a current, largely market-based construct, that is altered by the cumulative retained earnings, dividends, capital contributions, and refinancings that occur over the years and decades. None of these factors has any effect on rate base, which is largely

historical, and derived from depreciated original cost.⁵³ That depreciation occurs regardless of the requirements of the capital markets and regardless of the capitalization. It is senseless to speak as if the total value of the capital structure needs to tie to the value of rate base or to suggest that utility capital is not supporting utility activities if it does not.

Moreover, if equity “supports” goodwill as Mr. Gorman suggests, it does so only in the most trivial sense that if goodwill is impaired, equity is reduced. “Goodwill” requires no payments and uses no cash. No portion of ComEd’s capitalization is sequestered to support the business of “maintaining goodwill.” It is utterly unfounded to imagine that ComEd has isolated and dedicated nearly \$5 billion in equity to “support” goodwill in some non-utility way. The facts are clear: ComEd’s entire capital structure – including all of its equity and debt – supports its utility business.⁵⁴

Indeed, the total amount of the capital structure is largely irrelevant for ratemaking (it may indirectly affect risk and thus capital cost components). No one – least of all ComEd – claims that ComEd should earn a return on anything more than its rate base. For ratemaking purposes, all that matters is the ratio of debt and equity in the capital structure, and IIEC’s argument is an excuse to reduce only one part of the capital structure in order to artificially skew the ratio and artificially depress the overall weighted average cost of capital.

The arguments in the rebuttal of Staff witness Kight and IIEC witness Gorman about TFI debt are red herrings. ComEd proposes its actual capital structure. ComEd proposes no artificial adjustment for TFIs and relies on no such adjustment to support its capital structure. Mitchell,

⁵³ Rate bases may also be set based on fair value of assets, and the law requires that rates not be confiscatory as compared to fair value. Fair value rate bases are not at issue here, however.

⁵⁴ ComEd reiterates that no portion of goodwill is included in rate base or the capital structure. It does not seek any return of or on goodwill. Goodwill is a residual accounting entry required to reconcile the merger purchase price with total equity, as ComEd’s witnesses testified and even witnesses supporting artificial capital structures agreed. Houtsma, Tr. 403:10-22; 480:4-16; Bodmer, tr. 1221:7-22

ComEd 37.0 2nd Corr., 22:446-449 To the extent that this testimony is purely defensive — *i.e.*, that ComEd is “crying wolf” about the risks of ComEd having a 37/63 capital structure — it is also deeply flawed. The notion that the rating agencies will view 37% equity as “really” 45% simply because they will ignore TFIs when calculating debt ratios is incomplete and flawed. If the agencies choose to back out the TFIs for debt ratio purposes, they will also back out the revenues required to pay TFI interest and retire the TFIs. Mitchell Reb., ComEd Ex. 20.0; 21:406-23:457; Kight, Tr. 147:16-21. If Staff and/or IIEC invite the Commission to view the 37/63 capital structure as one that is somehow magically less leveraged by simply disregarding the TFI balances and forbidding their “replacement” by other debt, they surely cannot also ignore the fact that such a fictional TFI-less ComEd would also have considerably less revenue and would be, in fact, a weaker – not stronger – company. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 28:458-68.

Moreover, defending the use of an artificial capital structure for setting rates that will not be charged until 2007 with an argument that the rating agencies will ignore TFI debt quantified in terms of its 2005 balances simply introduces yet another flawed fiction. TFIs are temporary — and rapidly shrinking in amount. ComEd’s TFIs will be gone by the end of 2008 and will be much diminished well before the proposed rates even go into effect. Kight, Tr. 1817:19-1818:15. Rating agencies are not foolish and are well aware of this fact. It is neither fair nor reasonable to impose on ComEd a capital structure that neither reflects its actual test year capital structure, nor the capital structure that rating agencies would expect when the rates are being charged.

2. Cost of Long Term Debt

ComEd's cost of long-term debt is 6.50%. This is ComEd's actual cost as of June 30, 2005, the capital structure measurement date. ComEd's use of its actual debt cost is consistent with the filing requirements of 83 Ill. Admin. Code Part 285.4000 - 4030. Mitchell Dir., ComEd Ex. 7.0, 3:64-66, 6:122-23; Mitchell Reb., ComEd Ex. 20.0 Corr., at 28:591-601.

Staff suggests that ComEd's debt cost be reduced to 6.48% (Kight Dir., Staff Ex. 4.0 Corr., at 3:48-50), but the ending balances and amortization amounts behind that suggestion are not correct. When the correct balances and amortization amounts are used – as shown in ComEd Exhibits 20.5a and 20.5b – ComEd's cost of long-term debt is 6.50%, just as ComEd is proposing. Mitchell Reb., ComEd Ex. 20.0, 28:602-29:609, ComEd Ex. Ex. 20.5. Although Staff witness Kight claimed that she did not use ComEd Ex. 20.5b, asserting that “not all numbers reflect straight line amortization” (Kight Reb., Staff Ex. 15.0 Second Corr., at 5:70-72), the balances and amortization amounts reflected in that Exhibit are accurate and in accordance with applicable accounting and amortization principles.⁵⁵ Thus, it is such actual balances and amounts – not Staff's modified ones – that should be used in computing ComEd's cost of long-term debt. Mitchell Sur., ComEd Ex. 37.0 Second Corr., 24:478-87.

Much more untenable is CCC's claim that ComEd's long-term debt cost should be cut to 6.23%. Asserting that the computation of that cost should not include debt maturing before or soon after ComEd's new rates go into effect in 2007, CCC witness Edward Bodmer suggested substituting a hypothetical cost based on Exelon Corporation's cost for debt issued in 2005. Bodmer Dir., CCC Ex. 1.0 Second Corr., at 33:982-985. Such a hypothetical cost is

⁵⁵ IIEC initially agreed with ComEd's proposed cost of long-term debt (*i.e.*, 6.50%), but subsequently switched to adopting Staff's position of 6.48%. Gorman Dir., IIEC Ex. 3.0 Corr., at 19:438-446; Gorman Reb., IIEC Ex. 7.0, at 2:35-37. In making this switch, however, IIEC offered nothing to support Staff's position, and thus IIEC's adopted position is invalid for the same reasons that Staff's is.

inappropriate on multiple grounds. Fundamentally, it is based on another corporation's debt, not ComEd's. In contrast, ComEd included the actual cost of its own debt – that is, the debt that it actually is required to pay – when determining its weighted average cost of capital. That actual cost of debt, not some hypothetical one, is the appropriate test when determining ComEd's cost of capital. Mitchell Reb., ComEd Ex. 20.0, 26:559-27:565. Moreover, Mr. Bodmer's hypothetical cost was based on debt issued in mid-2005, when interest rates were at an historically low level, from which they have since increased. Mitchell Reb., ComEd Ex. 20.0, at 27:565-74.

Mr. Bodmer's hypothetical cost also includes \$300 million of short-term debt, even though such debt does not belong in the capital structure. Mitchell Reb., ComEd Ex. 20.0, at 27:580-84; Bodmer Dir., CCC Ex. 1.01. Short-term debt is not properly included in ComEd's capital structure and, even if short-term debt could be included — which all other parties agree is not the case — the \$300 million in debt Mr. Bodmer proposes included is not even ComEd's debt. Bodmer Dir., CCC Ex. 1.0 Second Corr., at 32:951-54. Mr. Bodmer's proposed adjustment is inconsistent with the filing requirements in 83 Ill. Admin. Code Sections 285.4000 through 4030 noted above. As ComEd President Barry Mitchell indicated, although these filing requirements are not determinative, Mr. Bodmer's proposal would render incorrect the calculation of ComEd's cost of debt as called for by such requirements. Mitchell Reb., ComEd Ex. 20.0, at 28:591-601.

More generally, Mr. Bodmer's proposal is yet another example of CCC's overall effort to ignore ComEd's actual costs. CCC does not question ComEd's use of June 30, 2005 for an historic measurement period date. Nor does it question ComEd's computation of its cost of long-term debt. Bodmer Dir., CCC Ex. 1.0 Second Corr., at 33:1004-07. And it does not suggest that

such cost was imprudent or unreasonable. Yet, CCC asks the Commission to ignore these facts, to go well beyond even the *pro forma* period, and to use hypothetical debt costs that reflects interest rates at their lowest point in recent history, and a cost of borrowing that has nothing to do with the cost that ComEd will incur for debt even between now and 2007. The Commission should reject this unsubstantiated and improper effort.

3. Cost of Common Equity

ComEd has proposed a cost of common equity (“COE”) of 11.00%. This proposal is based on the widely accepted discounted cash flow (“DCF”) model and risk premium methods (including the capital asset pricing model (“CAPM”)), which together provide the “most reliable cost of equity estimate.” Hadaway Dir., ComEd Ex. 8.0, at 1:15-21, 16:338-17:369, 23:495-503, 36:826-38:873.

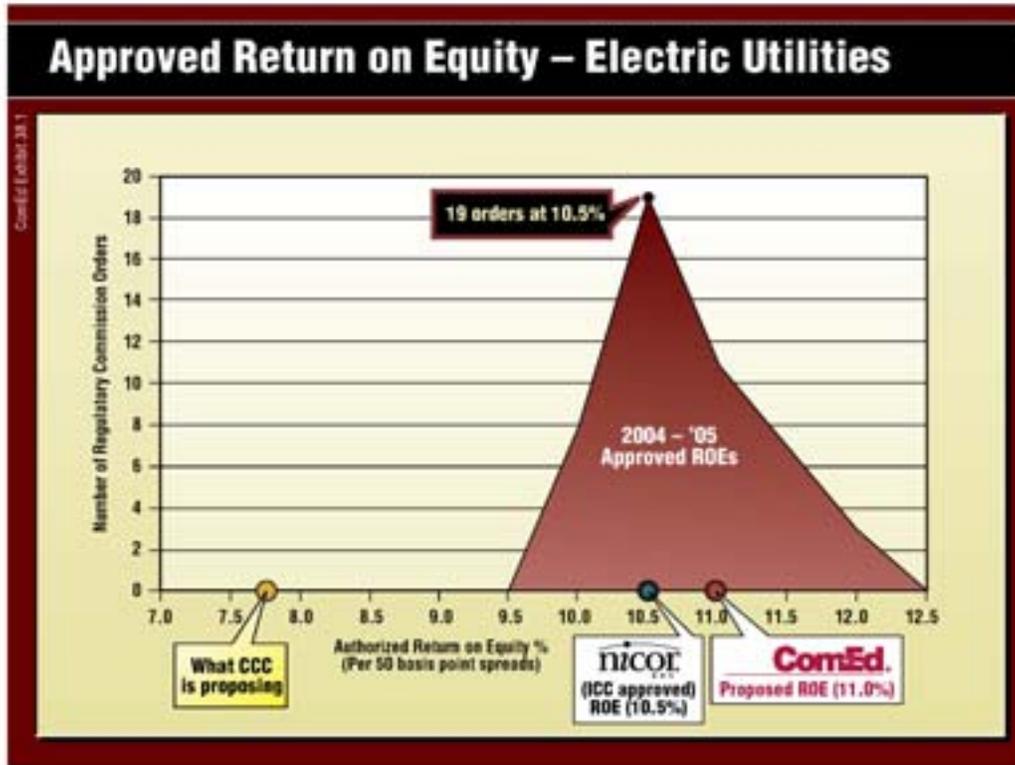
Dr. Samuel Hadaway, who conducted these analyses for ComEd, used a comparable company approach, following the United States Supreme Court’s traditional *Hope* and *Bluefield* requirements⁵⁶, and drawing on companies tracked by *Value Line Investors Service* (“Value Line”), a “widely-followed, reputable source of financial data.” The comparable companies comprised regulated gas local distribution companies and electric utilities with risk profiles similar to ComEd’s. Both of these groups are “useful proxies” that the Commission has accepted for establishing COEs on several prior occasions. Dr. Hadaway used multiple measures to ensure comparability, restricting his sample to companies that, among other things, have bond ratings of at least triple-B plus (BBB+), have received at least 66% of their revenues from domestic utility sales, are currently paying dividends, with no dividend cuts in the last two years

⁵⁶ *Federal Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co. v. Public Service Comm’n of West Virginia*, 262 U.S. 679 (1923).

and have no current merger activities. Hadaway Dir., ComEd Ex. 8.0, 2:35-3:47, 5:106-11, 6:114-19.

In his risk premium analysis, Dr. Hadaway used *Moody's* average public utility bond yields and projected single-A utility rates, and reviewed historical authorized and electric utility and gas distribution utility returns. Dr. Hadaway developed a CAPM estimate of the cost of equity for each group. Under current market conditions, this combination of approaches was the most reliable method for estimating ComEd's COE. Hadaway Dir., ComEd Ex. 8.0, at 3:48-58.

At the same time, other parties' proposed COEs – 10.19% (Staff), 9.90% (IIEC), and 7.75% (CCC) – are deficient in multiple respects and should be rejected. Fundamentally, each of these proposals is significantly below the COEs approved in recent years for electric utilities in the United States. For instance, in the fourth quarter of 2005, the average COE allowed in eleven cases was 10.75%. Thus, the COEs being proposed by other parties here constitute a “departure for the trend of rising capital costs,” and are “well below the mainstream” of COEs in the United States. Hadaway Reb., ComEd Ex. 21.0, 1:21-2:30; ComEd Ex. 38.1. This conclusion is particularly apparent with respect to CCC's proposal, which is not only 300 basis points below the national average, but also 244 basis points below Staff's already low proposal, and still 215 basis points below IIEC's even lower suggestion. Hadaway Reb., ComEd Ex. 21.0, at 17:381-93. The proposal is, indeed, substantially below any COE determined for any utility anywhere in the United States in the last two years. ComEd Ex. 21.1. The chart below illustrates the extent to which CCC's proposed COE is skewed away from reality.



In contrast, ComEd’s proposal of 11.00% is right around the national average. This COE makes sense, given the operating and capital risks that ComEd faces – such as continued dependence on kilowatt-hour volumes to recover costs, competition from self-generation and distributed generation, regulatory lag, potential disagreements over appropriate expenses and operating decisions, and responsibilities as the ultimate provider of last resort. Indeed, these kinds of risks have been noted by rating agencies and resulted, for instance, in ComEd’s having a higher risk profile than most distribution utilities, as well as in the recent downgrading of the long-term rating on ComEd’s senior unsecured debt. Hadaway Reb., ComEd Ex. 21.0, at 2:41-45, 3:64-4:91.

The contrast in proposed COEs is even more stark when ComEd’s capital structure is considered. As noted above, ComEd has proposed a equity ratio of 54.2%, which is based on its actual historical capital structure as of June 30, 2005, and includes a voluntary adjustment to

eliminate the nearly \$2.3 billion equity impact resulting from the required use of purchase accounting to reflect the Unicom/PECO merger. Mitchell Sur., ComEd Ex. 37.0 Second Corr., at 12:248-53. This equity ratio lines up well with the equity ratios of the companies in Dr. Hadaway's comparables groups, which averaged 51.8% for the LDC group and 45.7% for the electric utilities. Hadaway Reb., ComEd Ex. 21.0, 15:347-62.

Staff, IIEC, and CCC, however, are also pushing for a 37% equity ratio, dramatically lower than is reasonable for ComEd. Yet, as noted above, they have failed to consider what the cost of equity of such a hypothetical highly leveraged company would be. Kight Reb., Staff Ex. 15.0 Second Corr., 8:127; Gorman Reb., IIEC Ex. 7.0, 11:236-45; Bodmer Reb., CCC Ex. 4.0 Corr., at 2:50-51, 18:543-19:551; Hadaway Reb., ComEd Ex. 21.0, 6:131-7:144, Hadaway Sur., ComEd Ex. 38.0, 7:162-8:165. As a result, these other parties' proposed COE is mismatched with the comparable company groups proposed by Staff and IIEC, each of which involved companies with less leveraged capital structures. Hadaway Sur., ComEd Ex. 38.0, at 2:30-33. Mr. McNally's electric group, for example, had an average COE in 2004 of 48.8% and has a projected equity ratio for 2008-2010 of 52%. Hadaway Reb., ComEd Ex. 21.0, 6:131-7:144.

a) GDP Growth Rates

In preparing his DCF analysis, Dr. Hadaway used GDP growth rates to gauge long-term growth expectations. The DCF model calls for very long-term growth rates, and such expectations are more closely predicted by broader measures of economic growth – like GDP – than by near-term analysts' estimates. Hadaway Sur., ComEd Ex. 38.0, 17:397-18:405. GDP data, therefore, allowed Dr. Hadaway to look beyond the present low-inflation environment that has driven near-term growth estimates far below where they were just five years ago. Hadaway Reb., ComEd Ex. 21.0, at 8:170-77.

Staff's and IIEC's proposed COEs are flawed because their DCF models fail to consider very long-term growth expectations. Mr. McNally used growth rates projecting earnings for only the next five years, and Mr. Gorman used growth rate estimates of only three to five years. Hadaway Reb., ComEd Ex. 21.0, 7:149-8:177, 11:240-47; Hadaway Sur., ComEd Ex. 38.0, at 5:97-103. These shorter-run growth rates reflect today's historically low rates of inflation and analysts' less than optimistic outlooks for the electric utility industry, which together skew DCF estimates abnormally low. Hadaway Sur., ComEd Ex. 38.0, at 10:216-24.

b) Investment Bank Analysis

As noted above, CCC's proposed COE is aberrational and unfounded. Its proponent, Edward Bodmer, stands alone in declaring that the COE proposals of every other witness and the accepted methodologies on which they all rely, are all unreasonable. Given that his results are more than a hundred basis points below any COE recently approved in the United States, it is not surprising that Mr. Bodmer used no methodology accepted by regulators to estimate COE for ratemaking purposes. Rather, he got to his result by speculating about the conclusions of three investment banks in connection with the comparative valuation of Exelon Corporation ("Exelon") and Public Service Enterprise Group ("PSEG") in connection with their merger. Hadaway Reb, ComEd Ex. 21.0, 18:406-19:424. This approach is improper, as discussed in the following subsection.

First, CCC's proposed COE relies on an improper mixture of "apples and oranges." CCC witness Bodmer took the investment banks' valuation analyses (the "apples"), or more precisely his "reverse engineered" assumptions about them, and used them for the different purpose of setting a regulated utility's COE (the "oranges"). The two efforts – calculating a discount rate for use in a fairness opinion and determining the cost of equity that the market requires that a

utility earn for ratemaking purposes – are very different in purpose and methodology. Hadaway Surr., ComEd Ex. 38.0, at 4:311-13.

A fairness opinion in a context like the proposed Exelon-PSEG merger is intended to provide a relative valuation of the two companies' stock at a certain point in time. In doing this kind of study, investment banks use various methodologies, which may or may not be similar to those appropriately used in a regulatory proceeding like this rate case. In such a regulatory proceeding, on the other hand, the purpose of estimating a utility's cost of capital is to allow the utility a reasonable return on its rate base. That return includes a return on equity that is set by the market, rather than under Mr. Bodmer's implicit assumption that utility stocks should trade at book value (discussed in the next subsection). Hadaway Reb., ComEd Ex. 21.0, at 21:426-32; Hadaway Surr., ComEd Ex. 38.0, 14:314-322.

These contrasts are apparent here. For instance, Lehman Brothers (one of Exelon Corporation's investment banks) used internal forecasts and analyses of Exelon's financial performance and capital expenditures rather than, for example, a typical regulatory DCF analysis based on data known to the public and revealed in stock prices. Also, Lehman Brothers conducted its analysis as of a specific point in time in the past, as opposed to determining a required rate of return for the future. Hadaway Surr., ComEd Ex. 38.0, 14:323-330.

In addition, as noted above, cost of capital in a regulatory proceeding is estimated for application to a utility's rate base – *i.e.*, its historical, depreciated investment. An investment bank, meanwhile, may derive implied returns based on market-based valuations of those same assets, including the additional cost the utility would need to incur in order for it to assemble the same mix of investments at current market prices. It would therefore be inappropriate to apply

the latter type of rate of return, which is based on a market-priced portfolio of assets, to a rate base defined by original cost. *Id.* at 15:331-338.

There are other differences, as well. For example, valuation analysis uses market-based capital structure weights, while regulatory analysis uses book weights. Moreover, valuation analysis relies on an estimate of the incremental, after-tax cost of debt, while regulatory analysis calls for the known and measurable embedded, pre-tax cost of debt. Hadaway Reb., ComEd Ex. 21.0, 19:432-36.

In light of the foregoing differences in purposes, data, and methodologies, use of investment banks' fairness opinions to set regulatory returns is unreliable and inappropriate. Accordingly, CCC's suggested COE, based on such opinions, should be rejected. Hadaway Sur., ComEd Ex. 38.0, 14:311-16:360.

c) **Market to Book Ratio**

Mr. Bodmer also errs in suggesting that utility stocks should trade at book value. When confronted with the fact that utility market-to-book ratios are greater than one, Mr. Bodmer claims that "regulatory commissions have been granting returns in excess of the cost of capital to utility companies." Bodmer Dir., CCC Ex. 1.0 Second Corr., 44:1368-1370. Mr. Bodmer simply ignores the numerous other factors than can affect the price at which a holding company's stock trades. Moreover, instead of recognizing that such ratios highlight the unreasonableness of his own proposed COE, Mr. Bodmer implies that regulatory commissions around the country have been consistently wrong. This stance just underscores how far out of the mainstream Mr. Bodmer is. Hadaway Reb., ComEd Ex. 21.0, 17:385-393.

4. Overall Cost of Capital

ComEd seeks to recover its cost of capital, as is its right. The record shows that ComEd’s overall cost of capital is 8.94% – less than its most recently approved 8.99%. That cost is derived from its actual capital structure, actual embedded cost of debt, and the most reasonable estimate of its cost of equity. It is derived as follows:

<u>Line No.</u>	<u>Class of Capital</u> (A)	<u>Amount</u> (B)	<u>Percent of Total</u> (C)	<u>Cost or Earnings</u>		
				<u>End of Year</u> (D)	<u>Cost Reference</u> (E)	<u>(C X D) Weighted Amount</u> (F)
1	Short-term Debt	(1) \$ -	0.00%	0.00%	D-2	0.00%
2	Long-term Debt	4,388,487	45.80%	6.50%	D-3	2.98%
3	Preference / Preferred Stock	-	0.00%	0.00%	D-4	0.00%
4	Common Equity	(2) <u>5,194,283</u>	<u>54.20%</u>	11.00%	D-6	<u>5.96%</u>
5	Total Capital	<u>\$ 9,582,770</u>	<u>100.00%</u>			<u>8.94%</u>

ComEd’s requested cost of capital is based on its actual and reasonable capital structure, while opponents argue for an artificial capital structure with 63% debt that is well out of the norm for both ComEd and comparable utilities and is inconsistent with the maintenance of its financial ratings. Moreover, that artificial capital structure is premised on a view of the January 2001 transfer of ComEd’s nuclear assets that is not only fiction, but biased fiction, and its acceptance would be both inconsistent with the Commission’s own prior decisions and flatly illegal under the Act. ComEd’s embedded cost of debt is accurate, and its estimated cost of equity is reasonable. Staff’s estimate departs most significantly in its rejection of the use of a growth rate that fully reflects long-term trends. IIEC also uses accepted techniques, although its application of them is inferior to ComEd and Staff. On the other hand, CCC rejects all methodologies of estimating cost of equity accepted in Illinois – or anywhere in the United

States – in favor of an unsubstantiated, inaccurate, and incomplete effort to “reverse engineer” merger fairness opinions based on older data, created for a different purpose, and that attempt to measure different results using different methodologies. Not surprisingly, this effort yielded a bizarre result that is well below any rate of return awarded to any electric or gas utility anywhere in the U.S. since 2004. These attempts to depress ComEd’s capital costs should be rejected.

F. Cost of Service Issues

1. Embedded Cost of Service Study

ComEd’s embedded cost of service study (“ECOSS”), for purposes of this proceeding, allocates Distribution and Customer-related costs to retail delivery classes and develops the appropriate unit costs. (Heintz Dir., ComEd Ex. 11.0, at 5:90-102. Subject to certain appropriate adjustments, the ECOSS’ input costs generally are the same costs booked to ComEd’s accounts in the test year. *Id.*

Generally, there are two types of cost studies filed in utility rate cases: an ECOSS, which utilizes historical relationships among booked costs and the volumes of services delivered by the utility; and a marginal cost of service study, which employs analyses and estimates of incremental changes in costs, as these changes are related to (caused by) incremental changes in volumes of services forecasted to be delivered in the future. *Id.* at 5:98-102.

ComEd has used an ECOSS in prior rate case proceedings before the Commission, primarily to determine the jurisdictional revenue requirement. *See e.g.*, Orders, ICC Dockets 90-0169, 94-0065, 99-0117, and 01-0423. *Id.* at 5:103-07. For purposes of establishing delivery service charges, ComEd generally supports the use of a marginal cost of service study. Crumrine Dir., ComEd Ex. 9.0 Corr., at 43:925-36. However, in light of the fact that the Commission has approved and used an ECOSS in the last two ComEd delivery service rate cases (ICC Dockets

99-0117 and 01-0423), and in the interest of narrowing the issues in this case, ComEd proposes the use of an ECOSS for both interclass revenue allocation and rate design purposes. *Id.* Notwithstanding this proposal, ComEd continues to reserve the right to propose the use of a marginal cost study in future proceedings. *Id.*

The basic structure and functioning of the ECOSS submitted in this proceeding is substantially similar to ComEd's ECOSSs filed and approved in ICC Docket Nos. 99-0117 and 01-0423. Heintz Dir., ComEd Ex. 11.0, at 6:108-13. Staff has not proposed any adjustments to ComEd's proposed ECOSS in this proceeding. *See* Lazare Dir., Staff Ex. 6.0 Corr., at 36:878-80. The record demonstrates that the ECOSS is reasonable and, therefore, should be approved.

2. Minimum Distribution System

The cost causation methodology underlying ComEd's proposed ECOSS is consistent with the ECOSS submitted in its two previous delivery service rate cases. Consistent with this accepted methodology, and the Commission's Orders approving those prior ECOSSs, ComEd's proposed ECOSS does not reflect the minimum distribution concept. Heintz Reb., ComEd Ex. 25.0, at 2:27-29.

IIEC asserts that ComEd's ECOSS "generally follows well accepted principles concerning cost causation..." but it also asserts that the ECOSS does not "reflect the concept of a minimum distribution system." *See* Chalfant Dir., IIEC Ex. 2.0, at 9:161-62, 13:253-54. As such, IIEC requests that the Commission require ComEd to recognize a minimum distribution component in its next delivery service rate case, or provide the basis for such an allocation by providing either a minimum system study or a zero intercept analysis. *See id.* at 15:304-07. BOMA makes a similar criticism of ComEd's proposed ECOSS. *See* McClanahan Dir., BOMA Ex. 2.0, at 12:260-14:306.

The Commission has soundly rejected the minimum distribution system and zero-intercept concepts in the past and should do the same here. For example, in Dockets 99-0121 and 00-0802, the Commission rejected Ameren's proposal to employ the zero-intercept method of identifying the portion of distribution costs said to be related to connecting customers to the system, so that these costs could be allocated to customer classes on a basis other than demand, and charged through a customer charge. *See Central Illinois Public Service Co.*, ICC Docket 00-0802 (Order, Dec. 11, 2001). In that case, the Commission agreed with Staff, finding that:

[a] utility's system is designed in an integrated manner to deliver electricity to customers in quantities to meet all customer demands and individual components of the system cannot be identified for purposes of connecting customers only.

(*Id.* at 42). Furthermore, in rejecting Ameren's proposal and accepting Staff's method, the Commission stated:

[i]n the Commission's view, Staff's method is consistent with the fact that distribution systems are designed primarily to serve demand, and the Commission agrees with Staff that attempts to separate the costs of connecting customers to the electric distribution system from the costs of serving their demand remain problematic.

(*Id.*)

The minimum distribution system and zero-intercept concepts are attempts on the part of IIEC and BOMA to shift costs away from non-residential customers to residential customers. (Heintz Reb., ComEd Ex. 25.0, at 7:142-47). No new information has been provided in this proceeding that would lead the Commission to change its prior conclusions. Accordingly, BOMA's criticism of ComEd's ECOSS is without basis and should be ignored. Likewise, the Commission should deny the request of IIEC to require ComEd to incorporate minimum distribution or zero-intercept concept in its next rate case.

3. Marginal Cost of Service Services/Considerations

As previously noted, ComEd continues to reserve the right to propose the use of a marginal cost study in future proceedings.

4. Other

a) Weighting Factors

ComEd provided an explanation regarding the development of the weighting factors used to derive certain allocators employed in ComEd's ECOSS. (Heintz Reb., ComEd Ex. 25.0, at 9:182-92). ComEd's weighting factors are not arbitrary. ComEd witness Heintz testified that ComEd's work papers showing the development of these weighting factors have been submitted pursuant to the filing requirements under Part 285 of the Commission's Rules. 83 Ill. Adm. Code 285. In addition, the spreadsheet versions of the work papers have been provided in ComEd's response to a data request from the Attorney General (AG 4.03). (*Id.*) ComEd also provided explanations of the development of specific weighting factors in responses to data requests from Staff for Services (PL 3.32), Standard Meter (PL 3.33), Meter Reading (PL 3.34), Customer Account (PL 3.35), and Customer Information (PL 3.36). (*Id.*)

BOMA took issue with the weighting factors. (*See* McClanahan Dir., BOMA Ex. 2.0, at 14:307-23). In both direct and rebuttal testimonies, one of BOMA's witnesses maintains that certain weighting factors should be very similar for different non-residential delivery service customer classes. (*Id.*; McClanahan Reb., BOMA Ex. 4.0, at 9:198-214). However, nowhere in this testimony does BOMA offer any explanation as to why these weighting factors should be similar. Accordingly, BOMA's proposal regarding the weighting factors is baseless and should be rejected.

G. REVENUE ALLOCATIONS

1. Equal Rates of Return

ComEd's proposed rate design assigns the revenue requirement to each customer class in a manner consistent with the established methodology proposed by ComEd and accepted by the Commission in past cases. *See, e.g., Commonwealth Edison Co.*, ICC Docket 99-0117 (Order, Aug. 26, 1999); *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, Mar. 28, 2003). Specifically, ComEd proposes to assign the revenue requirement on an Equal Percentage of Embedded Cost ("EPEC") basis. *See, e.g., Crumrine Dir.*, ComEd Ex. 9.0 Corr., at 43:937-44:944; *see also* ComEd Ex. 10.9. This method should be adopted because it eliminates interclass subsidies, on an embedded cost basis, between rate classes.⁵⁷

2. Class Risk Differentials

CUB-CCSAO proposes that the Commission depart from a benchmark allocation methodology in favor of one that shifts portions of the revenue requirement to the non-residential classes based on speculation rather than on a cost basis. *See, e.g., Heintz Reb.*, ComEd Ex. 25.0, at 6:125-7:134; *Crumrine Reb.*, ComEd Ex. 23.0, at 37:794-99. Specifically, CUB-CCSAO recommends that only 97.5% of the residential class' costs be allocated to the residential class. *See Ruback Dir.*, CUB-CCSAO Ex. 3.0, at 29:601-03. The "basis" for this proposal is CUB-CCSAO's unsupported, and completely speculative conclusion, that the "residential class is less risky." (*Id.*) This proposal simply is another attempt to improperly shift costs away from the residential class: costs which then must be recovered from other classes of customers.

⁵⁷ ComEd notes that while it supports the EPEC method in this case, it reserves the right to raise this allocation method's counterpart, Equal Percentage of Marginal Cost ("EPMC"), in the future if a marginal cost of service study is proposed.

The record contains no evidence to support the conclusion that the residential class is less risky to serve than other classes. CUB-CCSAO provides no basis or logic for this conclusion. Rather, an examination of the evidence demonstrates the opposite—that the residential class is more risky, in terms of ComEd’s cash flow, than other classes. Crumrine Reb., ComEd Ex. 23.0, at 39:831-44. One example of this is the fact that the type of metering used for the residential class tends to focus cost recovery on volumetric rates rather than demand. *Id*) This is problematic for cost recovery, as many factors beyond the control of ComEd affect a customer’s consumption decisions (including income, weather, and personal preferences, etc.). *Id*. On the other hand, for most other customer classes, revenue recovery is largely determined based on demand, which is generally less volatile. *Id*. The residential class also tends to have greater turnover and a higher concentration of uncollectible accounts. These factors all inhibit ComEd’s ability to recover its costs from residential customers. *Id*.

In conclusion, CUB-CCSAO’s class risk argument is a transparent attempt to shift costs from the residential class to other classes. In this sense, it is no different than IIEC’s proposed minimum distribution system concept or CUB-CCSAO’s proposed P&A allocation methodology. See Sections F.2 and III.H.2, respectively. The Commission should reject these arbitrary and unsupported methodologies and, instead, continue to strive for cost-based rates that are designed to achieve the elimination of interclass subsidies, as it has done in past cases.

3. Other

Not applicable.

H. RATE DESIGN

1. Customer Class Delineations

For ratemaking purposes, customers are grouped into classes based on the cost characteristics of those classes. ComEd's proposed customer classes, on an individual class basis, are broad enough to include all customers that cause ComEd to incur costs in the same pattern, but narrow enough such that customers that cause costs in different patterns are not grouped together. Crumrine Dir., ComEd Ex. 9.0 Corr., at 31:699-701. Proper customer class delineations avoid, to the extent possible, the creation of intra-class subsidies. *Id.* at 32:703-05.

ComEd's existing customer classes for bundled electric service were designed prior to the 1997 Amendments to the Act, when ComEd was a vertically integrated utility that produced or purchased and sold all of the services necessary for customers to obtain bundled electric service. *Id.* at 32:706-21. At the time the existing bundled electric service customer classes were developed, a customer's load shape and end-use characteristics generally were key cost drivers. *Id.* However, ComEd no longer owns generation facilities and, therefore, customer classes need to be designed based on its cost structure as a "wires" company, or an electricity distribution company. *Id.* End-use characteristics and customer load shape do not contribute to distribution costs to any significant degree. *Id.* As such, ComEd's distribution costs do not vary significantly according to the usage pattern of the customer. *Id.* Accordingly, ComEd has proposed customer class designations to reflect the cost of service characteristics for its new role as a distribution company. *Id.*

a) **Residential**

ComEd's distribution costs incurred to serve residential customers are very similar. As such, four separate residential classes are no longer warranted.⁵⁸ ComEd's proposed rate design consolidates the current four residential classes into one residential class. The current residential classes are:

- Single-Family Without Space Heat
- Multi-Family Without Space Heat
- Single-Family With Space Heat
- Multi-Family With Space Heat

(Crumrine Dir., ComEd Ex. 9.0 Corr., at 33:725).

The AG is the only party that presented testimony contesting ComEd's proposed consolidation of the residential class. *See* Rubin Dir., AG Ex. 2.0, at 4:82-5:93, 5:95-103; Rubin Reb., AG Ex. 4.0, at 5:91-14:299. However, the AG did not present any evidence indicating that ComEd's distribution costs to serve these customers are sufficiently different to warrant retaining the current four residential rate classes. Instead, the AG attempted to show that cost differences exist, but only presented speculative conclusions that were discredited by ComEd witnesses. Accordingly, ComEd's proposal to have one residential class should be approved.

(i) **Single- And Multi- Family**

The current distinction between single-family and multi-family residential rate classes should be eliminated because ComEd's ECOSS indicates that there is little cost difference in serving these two classes of customers. Crumrine Dir., ComEd Ex. 9.0 Corr., at 36:765-72.

⁵⁸ Four purposes of simplicity, this Brief refers to four existing residential customer classes when technically there are five if Fixture Included Lighting is included. While this class also is a current residential customer class, it is being retained as a generic class that applies to both residential and nonresidential customers. No party has opposed this treatment.

Specifically, the per customer costs of delivering electricity to single-family residences is not significantly different from the costs of serving multi-family residences. *Id.* The record demonstrates that there is very little difference between single- and multi-family customer charges or single- and multi-family metering service charges in ComEd’s currently effective delivery service tariff, Rate RCDS.⁵⁹ *Id.* The following are ComEd’s unit costs for the four existing residential classes based upon its currently filed ECOSS⁶⁰:

Unit Delivery Cost for Current Residential Sub-Classes

Current Residential Sub-Classes	Customer-Related Costs (\$ per Customer per Month)*	Metering-Related Costs (\$ per Customer per Month)*	Distribution Facilities-Related Costs (\$/kWh)*
Single-Family Without Space Heat	\$7.74	\$2.52	\$0.0229
Multi-Family Without Space Heat	\$5.91	\$2.52	\$0.0220
Single-Family With Space Heat	\$8.02	\$2.52	\$0.0200
Multi-Family With Space Heat	\$5.86	\$2.52	\$0.0199

(*Id.* at 36:773-75). This table indicates how small the cost differences are between single-family and multi-family customers. With ComEd’s proposed residential monthly Customer Charge for the combined residential customer class at \$7.13, this proposed charge is roughly within \$1 per month of the calculated costs of the current single-family and multi-family groups. Crumrine Reb., ComEd Ex. 23.0, at 15:308-12. As ComEd witness Paul Crumrine states in his rebuttal testimony, “[v]iewing this in total dollars, \$1 a month is not significant enough to warrant the

⁵⁹ The current delivery service charges are based upon the ECOSS filed in Docket No. 01-0423 and approved by the Commission. (Crumrine Dir., ComEd Ex. 9.0 Corr., at 36:765-72).

⁶⁰ The Four Residential Classes workpaper to ComEd Ex. 11.1, submitted pursuant to Part 285, the standard information requirements for public utilities. 83 Ill. Admin. Code 285.

extra complexity of maintaining separate customer classes for multi- and single-family residential customers.” *Id.*

The AG asserted that the percentage difference in costs between the current classes is too great to allow for consolidation. Rubin Dir., AG Ex. 2.0, at 15:311-16:330. This concentration on mechanical percentage changes ignores the remaining cost structure and the relative usage of customers in those classes. *See e.g.*, Crumrine Reb., ComEd Ex. 23.0, at 15:297-313, 16:335-17:361. Multi-family residential customers generally have much lower usage than single-family dwellings because multi-family residences tend to be smaller, have fewer occupants, and fewer electric-powered fixtures and appliances. *Id.* at 15:314-19. Multi-family residences also tend to remain unoccupied much longer and more often than single-family housing. *Id.* Therefore, while the percentage increase may be higher for multi-family customers, the monthly dollar increase generally will be smaller. *Id.* Simply stated, a large percentage of a small number is still a small number.

The AG also asserts that meter installation and reading costs are lower for multi-family residences. Rubin Dir., AG Ex. 2.0, at 17:357-18:382, 19:409-20:417. The AG provides no analysis for its conclusion other than a series of speculations that do not reflect reality. For example, Mr. Rubin claims that “when 50 or 100 meters are being installed in the same location, there is not 50 or 100 times the amount of travel.” *Id.* at 20:412-14. This statement is baseless. Aside from the fact that ComEd does not generally install meter banks of the size Mr. Rubin claims, it simply is unreasonable to assume that one meter-installer could carry 50 or 100 meters to an individual location. Crumrine Reb., ComEd Ex. 23.0, at 19:395-97. Therefore, multiple trips would be needed or multiple installers would be sent to that location. *Id.* The AG also fails

to consider that groups of meters are commonly installed in a single trip to a new development of single-family homes. *Id.* at 19:397-400.

Additionally, the AG ignores the fact that ComEd's service territory is a mix of urban and suburban areas that contain both single- and multi-family dwellings. *Crumrine Reb., ComEd Ex. 23.0*, at 18:373-83. Meters of single-family dwellings tend to be easily found and accessed due to their relatively uniform location on the outside of the residence. *Id.* Meanwhile, multi-family meters tend to be inside the structure in locked utility/meter closets and the location of these closets is rarely uniform. *Id.* Multi-family dwellings also are usually located in urban areas with significant traffic congestion. Each of these factors has an impact on costs, and all were ignored by the AG. Consequently, the AG's speculations regarding meter installation and reading efficiency related to multi-family customers should be ignored.

The Commission also should reject the AG's proposal to maintain the single- and multi-family split for the purposes of applying Staff's bill impacts mitigation proposal. *Rubin Dir., AG Ex. 2.0*, at 5:101-3. As previously discussed, customers in multi-family dwellings tend to have lower energy bills compared to single-family dwellings. *Crumrine Reb., ComEd Ex. 23.0*, at 16:342-17:343. Therefore, it is not consistent with the purpose of Staff's bill impacts mitigation proposal, which focuses on customers' overall bills. *Id.* Additionally, the Commission's Order in the Procurement Case did not direct ComEd to apply Staff's proposal to multi- and single-family dwellings separately. Accordingly, the AG's proposal should be rejected.

Finally, ComEd notes that an Edison Electric Institute survey completed in 2004 indicates that only one of the twenty-five utility respondents indicated that a distinction was made between single- and multi-family dwellings in the rate structure. *Crumrine Reb., ComEd Ex. 23.0*, at 17:355-58. Thus, ComEd's proposal is consistent with the practices of the

overwhelming majority of utilities surveyed in the United States that do not differentiate between single- and multi-family dwellings. Crumrine Sur., ComEd Ex. 40.0 Corr., at 22:494-23:496.

For the foregoing reasons, ComEd's proposed consolidation of the current single- and multi-family residential rate classes into a single class is reasonable and should be approved by the Commission.

(ii) Space Heating And Non-Space Heating Residential Customers

For purposes of determining distribution rates, the distinction between space heating and non-space heating customers is no longer relevant. As a distribution company, ComEd's costs generally are not affected by the characteristics of the customers' end-use of the electricity. Crumrine Dir., ComEd Ex. 9.0 Corr., at 35:757-36:775. Rather, it is the size of the customer's maximum load on the distribution system that drives ComEd's distribution costs—not how that load is used during the course of the day, week, month or year. *Id.* Hence, it is the per kWh cost of delivering electricity to residential space heat customers is not significantly different than the cost of delivering electricity to non-space heat residential customers. *Id.* No party has produced any evidence indicating otherwise. Accordingly, the separate residential space heating designation should be eliminated.

The AG proposed separate distribution rates for space heating and non-space heating residential customers. Rubin Dir., AG Ex. 2.0, at 21:445-52. The AG's proposal is flawed for a number of reasons. First, the AG improperly relies on a miniscule difference in distribution costs between these customer classes of between 0.20 cents per kWh (\$0.00199 per kWh) and 0.23 cents (\$0.00229 per kWh). *Id.* at 20:428-29. This difference is generally within the ECOSS' margin of error. Crumrine Reb., ComEd Ex. 23.0, at 20:424-25. (Rubin "is attempting to ascribe a degree of accuracy to the cost study that cannot be reasonably imputed."). Indeed,

the very small difference between residential space heat and non-space heat distribution costs cited by the AG demonstrated that distribution costs generally are not related to the use of electricity. Rubin Dir., AG Ex. 2.0, at 20:428-29. In sum, the AG has failed to provide any cost justification for distinguishing between these customers for pricing purposes. Crumrine Reb., ComEd Ex. 23.0, at 20:428-29.

b) Non-Residential

In this proceeding, ComEd is proposing to restructure and consolidate the following non-residential classes:

Current	Proposed
0 kW up to and including 25 kW Over 25 kW up to and including 100 kW	Small Load Delivery Class
Over 400 kW up to and including 800 kW Over 800 kW up to and including 1000 kW	Large Load Delivery Class
Over 1000 kW up to and including 3000 kW Over 3000 kW up to and including 6000 kW Over 6000 up to and including 10000 kW Over 10,000 kW	Very Large Load Delivery Class

Crumrine Dir., ComEd Ex. 9.0 Corr., at 37:795-38:807.

The record demonstrates that the underlying cost of service for the listed groupings of current classes is sufficiently close to justify combining the classes. *Id.* at 38:811-15. This consolidation is supported not only by ComEd’s ECOSS in its last delivery service rate case, which showed a very similar cost among these classes, but also by the illustrative ECOSS filed

in this case which confirms the similarity of the costs. Crumrine Reb., ComEd Ex. 23.0, at 25:525-29.

ComEd originally proposed to retain a separate delivery service customer class for the two railroad customers. *See* Crumrine Dir., ComEd Ex. 9.0 Corr., at 40:863-71; ComEd Ex. 11.1. In surrebuttal testimony, ComEd has offered an alternative proposal in response to the testimony offered by the CTA. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 31:730-32:742, 32:750-752. This proposal eliminates the proposed railroad class. A complete discussion of ComEd's proposal concerning the railroad class is found in the section addressing Rate BES-RR.

Finally, ComEd proposes to subsume the existing "Delivery Service Pumping Customers" class into the Watt-Hour and the four new demand-based customer classes based on kW demands (Small Load, Medium Load, Large Load, and Very Large Load) at the individual pumping station premises, or, if applicable, into the High Voltage Delivery Class. The cost to provide distribution service to pumping customers is much the same as the cost to provide distribution service to other non-residential customers with similarly sized loads. Crumrine Dir., ComEd Ex. 9.0 Corr., at 41:877-89. Again, customer end-use characteristics do not contribute to distribution costs to any significant degree. Therefore, these customers can, and should, be subsumed into the appropriate delivery class. Additional discussions on issues raised by the Illinois Association of Wastewater Agencies ("IAWA") are addressed in the Section below entitled: "Municipal Pumping Class in Demand-based Categories."

(i) **Railroad Class**

ComEd's initial filing maintained a separate rate class for railroad traction power customers. In response to concerns raised by the CTA regarding standard service, ComEd

modified its proposal to eliminate the railroad class and provide one-line service as standard to each railroad traction power substation. A detailed discussion of this issue can be found in the Section of the Brief addressing Rate BES-RR, Section III.H.19 *infra*.

(ii) Very Large Load Customer Class

(1) The Over 10 MW Customer Class Should be Eliminated

A separate class for over 10 MW (*i.e.*, 10,000 kW) customers is no longer warranted. ComEd presented extensive factual evidence that overwhelmingly supports this result. *See* Crumrine Dir., ComEd Ex. 9.0 Corr., at 37:797-38:818; Crumrine Reb., ComEd Ex. 23.0, at 23:481-30:649; and Crumrine Sur., ComEd Ex. 40.0 Corr., 27:584-38:847; *also see* ComEd Ex. 10.9; Heintz Reb., ComEd Ex. 25.0; and ComEd Ex. 24.2. The parties that oppose this result have not presented compelling evidence to the contrary.

ComEd’s initial filing and direct testimony provided support for the conclusion that the underlying cost of service for its four largest demand-based non-residential customer classes was sufficiently close to justify combining these classes. Crumrine Dir., ComEd Ex. 9.0 Corr., 38:811-15; Crumrine Reb., ComEd Ex. 23.0, 23:491-25:523. This conclusion was consistent with the results of the ECOSS filed in ComEd’s last delivery service case (ICC Docket 01-0423), which indicated very similar distribution costs among the classes that ComEd proposes to consolidate into the Very Large Load Class. *Id.*; Order, Docket 01-0423. The following table summarizes that results of that study:

Unit Distribution Costs for Customers Using Over 1,000 kW

Customer Class	Embedded Unit Distribution Facilities Cost
Over 1,000 kW up to and including 3,000 kW	\$5.52/kW

Over 3,000 kW up to and including 6,000 kW	\$5.71/kW
Over 6,000 kW up to and including 10,000 kW	\$5.61/kW
Over 10,000 kW	\$5.54/kW

Crumrine Reb., ComEd Ex. 23.0, at 24:506-08. This table shows that the unit costs for distribution facilities range from \$5.52/kW to \$5.71/kW for these four classes. *Id.* In other words, the distribution facilities average unit costs differ by less than 3.5%. *Id.* As such, the costs for these customer classes is similar enough to justify the consolidation of these four current delivery customer classes into the proposed Very Large Load Delivery Class.

These results were subsequently reaffirmed in this proceeding when ComEd reran its ECOSS, for illustrative purposes, separating the Over 10 MW customers from the other customers in the proposed Very Large Load Delivery Class. *See* Crumrine Reb., ComEd Ex. 23.0, at 25:524-33; Heintz Reb., ComEd Ex. 25.0, at 4:82-5:87; ComEd Ex. 24.2. The illustrative ECOSS corroborates ComEd's proposal to consolidate the classes, indicating that the distribution facilities' costs for the Over 10 MW [\$5.46/kW] and the 1-10 MW class [\$5.45/kW] are virtually identical. Crumrine Reb., ComEd Ex. 23.0, at 25:524-33; ComEd Ex. 24.2. In ComEd's surrebuttal testimony, the illustrative ECOSS was revised based on changes in ComEd's revenue requirement. This revised illustrative ECOSS shows substantially the same result. *See* ComEd Ex. 41.7, p. 1 of 2, column (C)⁶¹. Accordingly, the appropriateness of the proposed Very Large Load Delivery Class cannot credibly be disputed. The Commission should adopt ComEd's proposed Very Large Load Delivery Class and reject the proposals of the other parties to maintain delivery rate class distinctions that have no cost, or evidentiary, justification.

⁶¹ The Very Large Load Delivery Class I in this exhibit corresponds to customers with load over 1 MW up to and including 10 MW. The Very Large Load Delivery Class II in this exhibit corresponds to customers with load above 10 MW.

(2) If the Over 10 MW Class is Retained, the Move Toward Cost-based Rates Should be Phased-in and Linked with the 24-Hour MKD Issue

As previously demonstrated, a separate Over 10 MW customer class is unnecessary. However, ComEd has offered an alternative proposal, in the event that the Commission concludes that an Over 10 MW customer delivery class should be maintained. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., 7:129-10:200. This proposal would phase-in the Distribution Facility Charge (“DFC”), moving this charge toward cost of service between this case and the next delivery service rate case that ComEd files. *Id.* If the Commission chooses this approach, it is critical that the 24-hour MKD be approved, as the two issues are linked, as discussed below.⁶² *Id.*

Under ComEd’s current tariffs, a nonresidential customer is assigned to a customer delivery class based on the highest 30-minute demand during the Demand Peak Period (*i.e.*, 9 am to 6 pm, Monday through Friday, excluding certain days recognized as holidays) in the preceding twelve (12) months. *See* ComEd Rate RCDS, Sheet No. 119.1. Additionally, the current DFC for the Over 10 MW delivery class is \$2.34 per kW, whereas the DFC for the three delivery classes for customers with loads over 1 MW up to 10 MW ranges from \$4.46 per kW to \$4.64 per kW. *Id.* Finally, ComEd currently measures a customer’s MKD (to which the DFC applies) only in the Demand Peak Period in the current billing month. Together, these factors establish a perverse incentive for customers that have very large and highly flexible loads to shift load from off-peak to peak periods for one 30-minute period a year in order to be classified as an Over 10 MW customer, and obtain the much lower DFC. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., 8:171-9:178. Under such a scenario, ComEd must size the distribution facilities to meet the

⁶² A complete discussion of the MKD issue can be found in Section II.H.22 *infra*.

customer's maximum demand, but the customer would pay for that investment in all but the one month tout of the year. *Id.*

To solve this problem, ComEd is proposing:

- that non-residential customers be assigned to a customer class based on the customer's highest 30-minute established in the previous 12 months (*i.e.*, on a 24-hour basis);
- that standard distribution facilities provided to non-residential customers be determined based on the customer's highest 30-minute demand established in the previous 12 months (*i.e.*, on a 24-hour basis);
- demand charges (*i.e.*, the DFC) that are intended to recover the costs for the provision of standard distribution facilities be applied to a 24-hour MKD; and
- the inappropriate subsidy that currently exists in the Over 10 MW DFC be eliminated.

See Crumrine Dir., ComEd Ex. 9.0 Corr., 34:746-35:764, 44:960-45:981; ComEd Ex. 10.1, proposed Rate RDS, proposed General Terms and Conditions Original Sheet No. 524. Taken together, these four changes provide a consistent approach to setting rates. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., at 10:212-16. However, certain parties in this case propose to retain the Over 10 MW customer class and maintain a significant price differential between the Over 10 MW class and the over 1 MW up to and including 10 MW classes, as well as maintain the current MKD definition as described in Section III.H.1.(b)(2) of this Brief.

With respect to maintaining an Over 10 MW class, IIEC, DOE, and BOMA each propose some form of an "across-the-board" increase for the current DFC that applies to the Over 10 MW class. *See* Stephens Dir., IIEC Ex. 1.0, at 16:302-4; Swan Reb., DOE Ex. 1.0, 10:258-11:264; Brookover/Childress Reb., BOMA Ex. 4.0, at 7:167-71. None of these parties provide any compelling evidence to justify this blatant attempt to maintain a subsidy that is for the benefit of

these high demand customers. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., at 29:630-30:674⁶³.

As ComEd has explained, an across-the-board increase is not cost-based in this case because:

[A]n across-the-board increase to current DST rates would serve to perpetuate a rate design that is based upon an incongruous juxtaposition of: (1) an embedded cost study for a test year that will be a decade old at the time the increase becomes effective; (2) a split between residential and nonresidential cost allocations based upon the embedded cost study filed in Docket No. 01-0423 for the 2000 test year; (3) a marginal cost based high voltage credit computed in the last rate case and based upon 2000 test year data; and (4) a subsidy memorialized in the ICC order in the last rate case that benefits customers with demands over 10 MW at the expense of all other nonresidential customers. The result of this combination is the current rate design, which does not reflect ComEd's current costs. Approval of an across-the-board increase to current rates would not be reflective of ComEd's current costs to serve and it would result in the perpetuation of existing undesirable subsidies.

Crumrine Sur., ComEd Ex. 40.0 Corr., at 30:663-74.

Without factual evidence to support their claims, all of these parties resort to using simple percentage increases in the proposed DFCs to claim that the Over 10 MW class should be maintained, in the interest of mitigating rate impacts to these large customers. Stephens Dir., IIEC Ex. 1.0, at 8:Table 2; Chalfant Dir., IIEC Ex. 2.0, at 8:146-53; Brookover/Childress Dir., BOMA Ex. 1.0, 13:284-14:289, Swan Reb., DOE Ex. 1.0, at 10:242-49. Again, the percentage changes simply do not tell the whole story. As ComEd witness Crumrine testified:

[I]t is important to point out that the proposed Very Large Load Delivery Class would pay less than 1.25 cents/kWh for delivery, under ComEd's proposal. (See ComEd Ex. 10.9). It is notable that the HVDS delivery class would pay less than half a penny per kWh for delivery under ComEd's proposal. (*Id.*) Compare this to the residential class, which would pay over 3.50 cents/kWh, and the watt-hour non-residential class that would pay roughly 4 cents/kWh for delivery, under ComEd's proposal. (*Id.*) The use of percentages in this case simply does not tell the whole story.

⁶³ In fact, the only cost evidence provided by the parties, suggests that a large subsidy exists between these customer groups. Crumrine Sur., ComEd Ex. 40.0 Corr., at 29:633-38, citing Stephens Reb., IIEC Ex. 5.0, at 13:283-86.

Crumrine Reb., ComEd Ex. 23.0, at 28:598-605. Thus, the Commission should reject attempts to shift the Commission's focus away from the evidence that ComEd's proposed delivery classes are cost-based and appropriate.

However, ComEd does recognize that rate continuity and rate impacts have been taken into account by the Commission. *See, e.g.,* Crumrine Reb., ComEd Ex. 23.0, at 38:802-03. Although, as previously noted, interested intervenors have failed to present a proposal that presents a coherent approach to ratemaking. Therefore, if the Commission does wish to phase-in the increase for the Over 10 MW customers, ComEd proposes that the Over 10 MW customer class DFC be set at \$3.86 per kW, which is one-half of the difference between the current Over 10 MW rate and the resulting rate based on ComEd's ECOSS filed in this case. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., 7:146-8:157. Further, ComEd requests that the Commission formalize its long-standing policy of setting rates based on costs by requiring a full movement to cost-based rates for this Over 10 MW class in ComEd's next rate case, whenever that may be filed. (*Id.* at 7:141-44).

In sum, the purpose of ComEd's rate design proposal is to create a consistent set of tariffs that set prices and conditions in a coherent manner. Rate design issues are inextricably linked through the operation of the tariffs. If the Commission wishes to phase-in the rate increase for the Over 10 MW class, it should also approve ComEd's proposed 24-hour MKD. *Id.* at 8:158-67. Without the approval of the 24-hour MKD as part of this proposal, customers with highly flexible loads that use dedicated distribution facilities primarily outside of the current Demand Peak Period will not only receive a subsidy in the form of a below cost DFC, but also will receive an intra-class subsidy as discussed in Section II.H.22.b of this Brief. The Commission

should not perpetuate both subsidies. Therefore, these two issues are necessarily linked and should be decided together.

(iii) **High Voltage Class Rates**

ComEd is proposing to create a High Voltage Delivery Class because high voltage customers primarily use the ComEd distribution system operating at or above 69,000 volts to obtain electric power and energy. These customers do not utilize a significant portion of ComEd's overall distribution system and, therefore, have a different cost of service than customers that utilize the ComEd distribution system at levels below 69,000 volts. Crumrine Dir., ComEd Ex. 9.0 Corr., 38:819-39:833. ComEd currently provides a bill credit to high voltage customers under Rider 11 – Service at 69,000 Volts and Higher (“Rider 11”) for bundled electric service customers and Rider HVDS – High Voltage Delivery Service (“Rider HVDS”) for delivery service customers.⁶⁴ Going forward, ComEd proposes this new delivery class to recognize the difference in cost to serve such customers. *Id.* The record demonstrates that this proposal also will allow for a more simplified billing procedure by applying standard delivery service charges for the High Voltage Delivery Class. *Id.*

BOMA witnesses Brookover and Childress propose that ComEd maintain its current practice of providing a high voltage credit through Rider HVDS to mitigate the price increases proposed by ComEd. Brookover/Childress Dir., BOMA Ex. 1.0, at 14:293-299; Brookover/Childress Reb., BOMA Ex. 3.0, at 8:169-9:186. This proposal lacks merit because the record shows that these customers will be treated the same under ComEd's proposal as they are today. Crumrine Reb., ComEd Ex. 23.0, at 28:606-29:22. Specifically, the High Voltage Delivery Class is created to be reflective of the distribution costs incurred by ComEd to serve

such customers. *Id.* Customers in the High Voltage Delivery Class will, in effect, be receiving the high-voltage credit through a reduced demand charge relative to other non-residential customers. *Id.* Thus, the maintenance of the current credit, in addition to the lower demand charge would essentially provide an unwarranted double benefit to this class. *Id.* BOMA's proposal should be rejected.

The Commission also should reject DOE witness Dr. Swan's proposal that the High-Voltage Delivery Class be separated into two subclasses. Swan Reb., DOE Ex. 1.0, at 11:274-79. Dr. Swan asserts that there are two types of customers—those that take service over 69 kV and those that do not. *Id.* He states that an intra-class subsidy will result if this class is not split. *Id.* However, this position ignores that customers in this class pay less than ½ cent per kWh for delivery service. Alongi/McInerney Reb., ComEd Ex. 24.2. A proper rate design must contain reasonable trade-off to avoid creating too many rate classes or setting too few. Crumrine Sur., ComEd Ex. 40.0 Corr., at 36:814-37:831. DOE's proposal would not improve price signals and it would further complicate the billing process for ComEd. (*Id.*) Therefore, this proposal should be rejected.

(iv) Other Classes

(1) Municipal Pumping Customers

As discussed in Section II.H.1.(b), ComEd is proposing that a water pumping customer be treated the same as any other customer with similar demand and, therefore, be subsumed into the appropriate delivery service class for that customer's demand level. Issues raised by the IAWA are addressed in the Section III.H.23 *infra* entitled: "Municipal Pumping Class in Demand-based Categories."

⁶⁴ The proposed High Voltage Delivery Class will replace Rider 11 and Rider HVDS. (Crumrine Dir., ComEd Ex. 9.0 Corr., at 38:819-39:833).

2. Relative Class Annual Utilization of Distribution Facilities

ComEd's ECOSS utilizes class NCP and CP demands to allocate distribution costs in a manner consistent with previous Orders approving ComEd's prior ECOSSs. Heintz Reb., ComEd Ex. 25.0, at 5:106-7; *See e.g.*, Order, Docket 01-0423. In particular, ComEd's allocation methodology reflects the Commission's position that the interclass revenue allocation should be based on the principle of cost-causation, and that "distribution systems are designed primarily to serve demand." *See id.* at 5:107-6:111; *See also Central Illinois Public Service Co.*, ICC Docket 00-0802 (Order, Dec. 11, 2001), at 42.

CUB-CCSAO proposes to depart from this long-standing methodology in favor of an allocation methodology that gives significant weight to the kWh consumption by class. *See, e.g.*, Ruback Dir., CUB-CCSAO Ex. 3.0, 16:323-17:344, 19:385-94. CUB-CCSAO's "Peak and Average" ("P&A") allocators would replace the NCP and CP allocators used in the ECOSS. *Id.* These P&A allocators give equal weighting to each class' share of kWh consumption (as provided in ComEd's filed ECOSS) with each class' share of NCP or CP, as the case may be. *Id.*

CUB-CCSAO's P&A method is arbitrary and results driven. Heintz Reb., ComEd Ex. 25.0, at 6:118-24, 7:136-40. CUB-CCSAO's desired result is to reduce the interclass allocation to the residential class produced by the ECOSS. *Id.* at 7:136-40. In other words, CUB-CCSAO seek to shift costs away from the residential class and on to non-residential customers. By proposing its P&A allocation methodology, CUB-CCSAO is asking the Commission to abandon its long-standing reliance on the NCP and CP methodology in favor of a methodology that has no cost basis whatsoever. *Id.* at 6:111-14, 7:140-42.

This issue is indicative of the "tug of war" between various customer groups in this case that seek to shift costs to other customer classes. *Id.* at 7:142-47. For example, while IIEC's minimum distribution system proposal (discussed in Section III.F.2 *supra*) attempts to shift costs

to the residential class, CUB-CCSAO's P&A proposal attempts to do the opposite. (*Id.*) For this reason, it is imperative that the Commission adhere to established cost-causation principles and reject arbitrary methods of allocating costs.

ComEd's proposed ECOSS carefully reflects the Commission's decisions over recent delivery service rate cases. Heintz Sur., ComEd Ex. 42.0, at 4:68-71. Staff recognizes this fact and has proposed no changes to the ECOSS. Indeed, Staff witness Peter Lazare states: "I have found no issues that would prevent its acceptance for ratemaking in this case. Further, it is consistent with studies approved by the Commission in previous DST rate cases." *See* Lazare Dir., Staff Ex. 6.0 Corr., at 36:878-80. Accordingly, CUB-CCSAO's unsupported and arbitrary allocation methodology should be rejected.

3. Environmental Cost Rate Redesign

ComEd's Customer Charge is a fixed monthly charge that is designed to recover the customer-related costs that do not vary by the amount of electricity delivered to customers. Alongi/McInerney Dir., ComEd Ex. 10.0, at 19:474-20:482. The Customer Charge recovers costs such as those related to billing, payment processing, and other customer services, as well as certain costs associated with uncollectible accounts. *Id.*; *see also* ComEd Ex. 11.1.

Staff witness Mr. Lazare proposes an adjustment that would shift 20% of the costs to be recovered in the fixed Customer Charges to the usage-based DFC. Lazare Dir., Staff Ex. 6.0 Corr., at 40:1000-43:1055. In effect, Staff seeks to shift \$70 million out of the Customer Charge and have ComEd bear the risk to collect such money through the customer's usage charge. Staff offers a set of inconsistent and unsupported claims in an attempt to buttress this flawed proposal. *See id.* Rather than analyses or study to support the impact of its proposal, Staff only offers conjecture.

According to Staff, a lower fixed charge in conjunction with a higher usage charge will create an economic incentive for customers to reduce their energy usage. Lazare Dir., Staff Ex. 6.0 Corr., 40:1000-43:1055. Staff maintained that “[t]he impact of electricity usage on global warming is a factor to consider in the design of electricity rates” *Id.* at 37:912-13 (emphasis added) and that the result of his proposal would be to “enable ratepayers to make consumption decisions that are more efficient from an overall societal standpoint.” *Id.* at 42:1043-44 emphasis added.

In rebuttal testimony, Staff changed its position claiming that the purpose of the proposal is not to reduce customer usage—but “[r]ather, it is to incorporate into delivery charges environmental costs resulting from the generation of power to meet ratepayer demands.” Lazare Reb., Staff Ex. 17.0 Corr., at 28:701-03. Staff then proceeded to assert that there would be no impact on ComEd revenues because “[i]f bills for some customers rise, then bills for others would decline. The proposal would be a zero sum game from a revenue standpoint.” *Id.* at 32:809-10. Staff is wrong.

If adopted, Staff’s proposal would seriously impede ComEd’s ability to recover its costs. The reasons for this result appear in Staff’s own testimony. Specifically, it is implausible for Staff to assert that its proposal is not aimed at lowering usage. This aim is plainly noted in Staff witness Lazare’s direct testimony. Lazare Dir., Staff Ex. 6.0 Corr., 37:912-13, 40:1000-43:1055. If usage is reduced, all else being equal, then ComEd’s ability to recover its costs is at risk. Even assuming *arguendo* that Staff’s goal is not usage reduction, then one must ask—what is the point? *See* Crumrine Sur., ComEd Ex. 40.0 Corr., at 48:1093-98. How can an adjustment that was expressly designed to aid global warming work if it does not reduce usage? Clearly, Staff’s position defies logic.

The crux of the problem is that Staff's goal, while laudable, is ill-conceived. Staff witness Lazare admits that his proposed 20% shift is "based on judgment"—not study or research. Lazare Dir., Staff Ex. 6.0 Corr., at 43:1058. Staff does not cite any evidence or provide any analysis regarding the impact of the proposal on usage. In reality, the impact on usage only can be determined through a study of the price elasticity of demand and no such study has been produced by Staff, who is advancing this proposal. Crumrine Sur., ComEd Ex. 40.0 Corr., at 49:1109-18. Thus, it is impossible for the Commission to determine what impact a shift of dollars from the Customer Charge to the DFCs would have on customer usage. Crumrine Reb., ComEd Ex. 23.0, at 41:868-85. In other words, any rate design that reduces customer usage also must factor in a corresponding upward adjustment to the billing determinants to account for the reduction in revenues that would otherwise occur. *Id.*

Staff's proposal is deficient in other respects. For example, Mr. Lazare claims that ComEd's rates "fail to take into account...the environmental cost of producing power." Lazare Dir., Staff Ex. 6.0 Corr., at 37:909-13. However, the purpose of this case is to set delivery rates—which by definition, exclude the cost of generating power. Accordingly, Staff's use of the Customer Charges and DFCs to account for power production issues is flawed from the start.

IIEC also opposes Staff's adjustment. IIEC's witness Stephens recognized that "[t]he most efficient pricing is to have delivery charges that are based on the cost of delivery and, more particularly, to have customer charges recover customer-related costs and to have demand charges recover demand-related costs." Stephens Reb., IIEC Ex. 5.0, at 21:485-88. Mr. Stephens also is correct in his statement that it would be "purely speculative to assert that such marginal changes [on the total customer bills] (some of which are decreases) would elicit any meaningful reduction in pollutants...." *Id.* at 22:500-2.

In sum, Staff witness Mr. Lazare is seeking to arbitrarily shift approximately \$70 million from the Customer Charge without any analysis as to the effect of this proposal on ComEd and its customers. This flawed proposal should be rejected.

4. Rider ECR

ComEd proposes that all of its incremental environmental remediation costs be recovered through a new rider, Rider ECR, rather than through base rates.⁶⁵ As ComEd witness Paul Crumrine explained, ComEd, like any other regulated utility, is entitled to recover its prudently incurred costs. The main issue between the parties in testimony was how ComEd's environmental costs were to be recovered. As the record evidence demonstrates, ComEd's incremental environmental costs, which it proposed be recovered through Rider ECR, are unpredictable, volatile and fluctuating. A rider will ensure that ComEd recovers, and its customers pay, only the costs incurred, no more and no less.

What Environmental Expenses Would Be Recovered Through a Rider. The record contains clear evidence that ComEd incurs costs relating to environmental clean-up or remediation at various sites, and that these costs are prudent and reasonable. ComEd is entitled to recover these costs, which are incurred as a result of a constantly evolving set of both state and federal environmental laws with which ComEd must comply if it is to avoid civil and criminal penalties and stay in business. *Fernandes & McCauley Reb.*, ComEd Ex. 28.0, at 7:140-49, 8:162-74, 13:279-87, 14:315-19, Attach. C. ComEd carefully monitors such costs and has put in place a number of procedures to ensure that the environmental costs that it incurs are reasonable. These procedures include a competitive bidding process for selecting outside contractors that extends across all Exelon business units to leverage the greatest savings, task-based estimates

and billing, reporting requirements to monitor the status of each project, and evaluation of ComEd employees' efforts to manage costs as part of performance reviews. *See generally* Fernandes & McCauley Reb., ComEd Ex. 28.0, at 15:328 - 17:375. No party introduced any evidence that would show that ComEd's environmental costs are unjust or unreasonable. In fact, the witness for the City of Chicago ("City") specifically stated that the City did not oppose recovery of such costs. Walter, Tr. at 680:1-6.

ComEd proposed only that incremental environmental remediation costs be recovered through its proposed Rider ECR, rather than through base rates. Incremental environmental remediation costs include all outside contractor costs related to remediation at both sites related to historic manufactured gas plants ("MGP") and non-MGP sites where contamination has occurred, for example, from adjacent sites or because of contamination left by prior owners. These costs also include emergency response work performed by outside contractors (Fernandes/McCauley Reb., ComEd Ex. 28.0, at 11:242-12:262), but do not include internal costs or payments made to affiliates for work performed by the affiliate Fernandes/McCauley Tr. at 2096:3-7. Staff supported rider recovery only for MGP costs. Ebrey Tr. at 1904:16-18. Although IIEC witness Mr. Gorman opposed rider recovery in his pre-filed testimony, during the hearings he acknowledged that the Commission has already permitted the recovery of MGP remediation expenses through a rider and stated that IIEC is "not suggesting the Commission should reverse any findings already made." Tr. at 2045:5-10. City witness Mr. Walter similarly indicated that the Commission has previously approved rider "recovery of MGP-related remediation costs." Walter Reb., City Ex. 2.0, at 3:53-4:55.

⁶⁵ ComEd Ex. 23.3 reflects the revisions to proposed Rider ECR that ComEd offered in response to Staff's proposed changes thereto. *See also* proposed changes in Crumrine Sur., ComEd Ex. 40.0, Corr. at 72:1635-48.

If the Commission allows only MGP-related costs to be recovered through a rider, \$1,466,667 must be added into the test-year revenue requirement. Hill Sur., ComEd Ex. 36.0, 47:1065 - 48:1080. And, in the event the Commission requires that all such costs be recovered through base rates, then \$11,577,201 must be added back into base rates. *Id.* at 48:1083 - 49:1107. Both of these amounts were calculated using a methodology previously approved by the Commission in Docket No. 01-0423. *Id.* at 48:1073-75, 1091-94.⁶⁶

IIEC witness Mr. Gorman and Staff witness Ms. Ebrey also suggested in testimony that ComEd's incremental environmental remediation costs should not be recovered from delivery services customers. The Commission, however, has previously and unequivocally rejected that position, noting that these costs "are corporate expenses that should not be bypassed by any retail customer." *Commonwealth Edison Co.*, ICC Docket No. 01-0423, (Order, Mar. 28, 2002), at 105. Further, the Illinois Supreme Court has similarly recognized that payment of environmental remediation costs "allows a utility to remain in business and to continue to provide service to its customers," and are a "necessary expense of utility operations" that the utility is entitled to recover. *Citizens Util. Bd. v. Ill. Commerce Comm'n*, 166 Ill.2d 111, 123 (1995). Thus, all customers benefit from, and should contribute to, recovery of these costs.

The suggestion by Staff witness Ms. Ebrey and City witness Mr. Walter that recovery of non-MGP costs, whether by rider or otherwise, should be deferred to a separate proceeding should be rejected as well. ComEd is entitled to recovery of both its MGP and non-MGP costs, which, as described above, are virtually identical in nature, and no party has disputed either that ComEd incurs such costs or that these costs were not prudently incurred. As Mr. Crumrine

⁶⁶ As Mr. Hill explained in his Surrebuttal Testimony, Mr. Gorman's proposal that ComEd need only add back \$3 million to the test year revenue requirements if Rider ECR were rejected "is simply wrong." Hill Sur., ComEd Ex. 36.0, Corr. at 52:1169-78.

stated in his Surrebuttal Testimony, “[t]his rate case proceeding is exactly the appropriate place to consider the implementation of such a rider mechanism. It should be noted the genesis of MGP riders was, in fact, utility rate cases.” Crumrine Sur., ComEd Ex. 40.0, Corr. 67:1517-20 (*citing* ICC Docket. 90-0127 (Order on Remand June 8, 1994); ICC Docket No. 91-0010 (Order Nov. 8, 1991)). Moreover, Rider ECR provides for annual reconciliation proceedings through which the Commission will review whether the costs ComEd seeks to recover were prudently incurred. Such proceedings therefore ensure, going forward, that the costs ComEd seeks to recover are prudent and that rates are just and reasonable.⁶⁷ There is no need for a separate proceeding to approve either recovery of these costs or their recovery through a rider.

Why Rider Recovery is Appropriate. Both the courts and the Commission have recognized that the rider is the form of rate best suited to the recovery of costs that are volatile, fluctuating, and hard to predict. The Illinois Supreme Court has stated that “a rider mechanism is effective and appropriate for cost recovery when a utility is faced with unexpected, volatile, or fluctuating expenses.” *See Citizens Util. Bd.*, 166 Ill.2d at 138 (*citing City of Chicago v. Ill. Commerce Comm'n*, 13 Ill.2d 607 (1958)). In addition, this Commission, in the “Coal Tar Cases,” which looked at the recovery of costs associated with MGP sites, designated cost-tracking riders as the “preferred method” for the recovery of MGP site remediation costs. *See Commonwealth Edison Co.*, ICC Docket Nos. 91-0080 through 91-0095 (Cons), 1992 Ill. PUC Lexis 379 at *136 (Order, Sept. 30, 1992). The Commission there explained that “[g]iven the wide variations in and the difficulties in making forecasts of the scope, costs and timing” of these

⁶⁷ Mr. Crumrine also stated that “were ComEd to have filed the rider separately, it is my understanding that such a filing would likely have been attacked as forbidden ‘single-issue ratemaking’ – an argument that has been used to challenge riders in the past. Therefore, while this case is the appropriate venue in which to consider ComEd’s rider proposal, the Commission should make clear in its order in this proceeding that such legal challenges will not be allowed in the event it concludes that a separate proceeding is necessary.” Crumrine Sur., ComEd Ex. 40.0, at 67:1529-1534.

types of costs (*id.* at 133), a rider “allows the recovery of no more than the costs incurred by the company as they are paid” and “provides for a reconciliation to match actual costs against actual collections and determine the prudence and reasonableness of the expenditures paid” *Id.* Consistent with this policy, the Commission has approved numerous riders for recovery of MGP site remediation costs.⁶⁸

Presumably because the Commission in the Coal Tar Cases provided for rider recovery of MGP-related environmental remediation costs, Staff witness Ms. Ebrey and others have suggested that rider recovery of ComEd’s incremental environmental costs should be limited only to MGP-related costs. *See* Ebrey Reb., Staff Ex. 13.0, 31:652-54; Gorman, Tr. 2045:5-10. Such a limitation, however, is not supported by either fact or law. As ComEd witnesses Allan Fernandes and Peter McCauley detailed, the MGP/non-MGP distinction is purely arbitrary, because environmental laws do not distinguish between these types of costs. Fernandes/McCauley Reb., ComEd Ex. 28.0, 7:140-49. In both instances, ComEd incurs remediation and clean-up costs to comply with environmental laws and regulations that are constantly evolving.⁶⁹ Further, both types of costs vary widely from year to year.⁷⁰ In fact, it is

⁶⁸ As ComEd witness Mr. Crumrine testified, ComEd is unaware of any case in which a utility has been denied general permission to recover MGP costs through a rider. (Crumrine Sur., ComEd Ex. 40, at 64:1462 - 65:1480). Both prior to and following the Commission’s ruling in the Coal Tar Cases, numerous riders were placed into effect to recover prudently incurred MGP site remediation costs: (1) Riders GEAC, EEAC and EEAC delivery services, filed by Central Illinois Public Service Company (now Ameren CIPS); (2) Riders GEA and EEA, filed by Illinois Power Company (now Ameren IP); (3) Riders C and 1B, filed by Interstate Power and Light Company; (4) Standard Rider 12 (now Rider 12), filed by Nicor Gas Company; (5) Riders R, E (now Rider GEAC) and EEAC delivery services, filed by Union Electric Company (now Ameren UE); (6) Rider TAR, filed by Central Illinois Light Company (now Ameren CILCO); (7) Rider 11, filed by North Shore Gas Company; (8) Rider 11, filed by Peoples Gas Light & Coke Company; and (9) Riders 10 and 14, filed by Iowa-Illinois Gas and Electric Company (now MidAmerican Energy Company). A history of these riders and their related dockets is set forth in *Illinois Commerce Commission On Its Own Motion*, ICC Docket Nos. 04-0104 through 04-0108 (Cons.), 2004 Ill. PUC Lexis 78, at *1-4 (Order, Feb. 19, 2004) and *Illinois Commerce Commission On Its Own Motion*, ICC Docket Nos. 04-0109 through 04-0112 (Cons.), 2004 Ill. PUC Lexis 77, at *1-3 (Order, Feb. 19, 2004).

⁶⁹ *See* Attachment C to Fernandes/McCauley Reb., ComEd Ex. 28.0 for a description of the constantly-changing nature of the state and federal environmental laws under which ComEd is potentially liable.

⁷⁰ An analysis of the incremental environmental remediation costs incurred by ComEd for both MGP and non-MGP sites between the years 2001 and 2004 shows wide fluctuation in these costs. Actual outside contractor

notable that neither Mr. Gorman nor any other witness challenged ComEd's figures that show the volatile and fluctuating nature of environmental remediation costs. Crumrine Sur., ComEd Ex. 40.0, Corr. 66:1508-10; Fernandes/McCauley Sur., ComEd Ex. 44.0, 3:49-51. Because such costs are volatile, fluctuating and unpredictable, it is very difficult to make a test-year estimate that would both ensure adequate cost recovery by ComEd and avoid overpayment by its ratepayers. *See* Hill Tr. at 838:2-839:1; Fernandes/McCauley Reb., ComEd Ex. 28.0, 2:38-41. In short, both MGP and non-MGP costs should be recovered through Rider ECR.

Arguments raised by witnesses for IIEC and the City also offered no basis for denying rider recovery. IIEC witness Mr. Gorman misstated the Commission's standard for rider recovery when he argued that rider recovery should not be allowed unless failure to provide for it would impair the utility's ability to earn its return of equity. Gorman Reb., IIEC Ex. 7.0, 24:567-25:596. First, the impact on a utility's ability to earn its authorized return never has been the standard for approving such riders. Crumrine Sur., ComEd Ex. 40.0, Corr. 65:1486-88. Second, this position is inconsistent with the argument that Mr. Gorman made in the Coal Tar Case. *Id.* at 65:1488-66:1493. In that case, he "testified that because remediation expenditures will fluctuate significantly from year to year, including a representative amount as a test year expenditure would in effect be asking the Commission to allow an expense that is not known and measurable," and "recommended that the Commission may want to consider extraordinary treatment for remediation expenditures." *Commonwealth Edison Co.*, ICC Docket Nos. 91-0080 through 91-0095 [Cons], 1992 Ill. PUC Lexis 379 at *113-14 (Order, Sept. 30, 1992); *see also* Crumrine Reb., ComEd Ex. 23.0, at 62:1320-34.

and legal costs incurred for MGP sites over this period ranged from a low of \$11.1 million to a high of \$43.1 million, while outside contractor and legal costs for non-MGP sites ranged from a low of \$119 thousand to a high of \$1.3 million. (Fernandes & McCauley Sur., ComEd Ex. 44.0, Attach. 2).

The argument made by City witness Mr. Walter – that the delay in ComEd’s filing of Rider ECR somehow suggests that environmental remediation costs are not as volatile or unpredictable as ComEd alleges (Walter Reb., City Ex. 2.0, at 2:23 - 3:40) – is also unfounded. This argument ignores the history of the Coal Tar Cases and the restrictions of the 1997 Restructuring Act, pursuant to which ComEd has been subject to a “rate freeze” since December 1997. Crumrine Sur., ComEd Ex. 40.0, at 69:1561-72. Indeed, it was not until after the rate freeze was already in effect that ComEd received more accurate information such that it increased its estimated liability from \$25 million to \$93 million for MGP sites alone, an estimate that has already been superseded. Fernandes & McCauley Reb., ComEd Ex. 28.0, at 6:130-35.

When the Commission approved rider recovery for MGP site remediation costs in the “Coal Tar Cases,” it recognized that the rider mechanism was the “preferred method” of recovery because utilities were required to incur such costs under existing environmental laws and those costs are volatile, fluctuating, and hard to predict. Neither the Commission nor the courts limited the standard for rider recovery to MGP costs, and both MGP and non-MGP costs meet that standard. *See* Crumrine Sur., ComEd Ex. 40.0, Corr. 66:1503-18. Because Rider ECR conforms with the standards previously identified by both the Commission and the courts, and allows ComEd to recover no more and no less than the actual costs it reasonably incurs in remediating environmental contamination, it should be approved.

5. Rider AC7

ComEd proposes to replace its current Rider AC with Rider AC7. Crumrine Dir., ComEd Ex. 9.0 [Corr.], at 23:502-13. Proposed Rider AC7 will continue to compensate residential customers for reducing load by permitting ComEd to install a direct load control (“DLC”) device that cycles a customer’s central air conditioning unit compressor. *Id.* Current

Rider AC has approximately 64,000 residential customers signed up for this service, which translates into over 75 MW of demand response from this customer group. *Id.* Proposed Rider AC7 maintains the same pricing as existing Rider AC. *Id.*

In surrebuttal testimony, ComEd's proposed technical modifications to Rider AC7 and Rider CLR7 in order to provide an appropriate transition for customers from ComEd's existing interruptible/curtailable riders to Rider AC7 and Rider CLR7, as well as clarifying how compensation under Rider CLR7 is provided. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 7:152-8:181. The need for these modifications became apparent as ComEd began to implement the auction process pursuant to the Commission's Order in the Procurement Case. Crumrine Sur. Ex. 40.0 Corr. at 81:1833-43.

These modifications are largely the result of a technicality, stemming from the creation of the new rates book and will not impact the compensation to such customers. Alongi/McInerney Sur., ComEd. Ex. 41.0 Corr. at 7:153-8:181. The modification is reasonable and should be approved.

6. Rider CLR7

ComEd proposed a technical adjustment to Rider CLR7. This modification is discussed in the discussion of Rider AC7 in Section III.H.5, *supra*. Rider CLR7 also is discussed in the discussion of Riders ISS, 13, 26, 27, 30 and 32 in section III.H.7 *infra*.

7. Elimination of Riders ISS, 13, 26, 27, 30, 32

a) Riders 13, 26, 27, 30, and 32.

Consistent with the fact that ComEd no longer owns generation and must procure all of its energy through the wholesale market, ComEd proposes to consolidate its core demand response programs for non-residential customers into Rider VLR7 and Rider CLR7, which

provide market-based incentives. Crumrine Dir., ComEd Ex. 9.0 Corr., 19:415-20:430. Therefore, ComEd proposes to remove its current, and outdated, demand response Riders 13, 26, 27, 30, and 32 from its Schedule of Rates. *Id.*

Generally, demand response riders compensate customers for the curtailment of load under defined conditions. *Id.* ComEd's proposed consolidation of these riders is necessary because Riders 13, 26, 27, 30, and 32 rely on incentives that are inconsistent with the PJM incentives for demand response. *Id.* With ComEd's entry into PJM, ComEd's service territory is part of a market environment where the value of demand response is visible. ComEd's proposed Riders VLR7 and CLR7 are market-based and essentially pass through the values from PJM. These riders can be made available to any qualifying non-residential customer, regardless of whether they remain on ComEd supply or take service from an alternative supplier. *Id.* Accordingly, ComEd's proposal eliminates potential mismatches between market values and ComEd incentive payments.

The IAWA recommends retention of Riders 13, 26, 27, 30, and 32 because it claims that some customers have made investments in standby generating equipment based on the current suite of riders. Menninga Dir., IAWA Ex. 1.0, 9:166-10:191. In addition, the IAWA erroneously asserts that Rider CLR7 "only recognizes the reduction in use at the time of curtailment, and may not even cover the associated fuel cost to run the standby equipment" that the IAWA members have installed. *Id.* at 9:171-73. In reality, Rider CLR7 provides a market-based payment to customers who can commit specified amounts of firm demand response, regardless of whether or not a curtailment is ever called under the tariff. Crumrine Reb., ComEd Ex. 23.0, 75:1614-76:1642. Indeed, PJM places a value on firm demand response capability through its Active Load Management ("ALM") program which customers can participate

through Rider CLR7. *Id.* Accordingly, IAWA members (as well as certain other customers with generating facilities and discretionary load) can continue to receive fixed annual payments for every kilowatt of their respective abilities to firmly curtail load through Rider CLR7, just as they did on Rider 32. *Id.*

IAWA also ignores Rider VLR7, which compensates customers for every kilowatt-hour curtailed based on the PJM compensation structure. Rider VLR7 is a voluntary program, and there are no penalties for non-compliance as there are under Rider CLR7.

Staff correctly summarizes the rationale for ComEd's proposal to discontinue these tariffs post-2006:

[T]he Company's proposed changes are consistent with the direction ComEd is taking towards a reliance on the PJM market and the auction process to secure the supply component of bundled service bills. Given the direction the Company is headed, it would be difficult and costly to maintain these existing riders [meaning Riders ISS, 13, 26, 27, 30, and 32].

Lazare Dir., Staff Ex. 6.0 Corr., at 45:1093-97. Accordingly, consistent with the fact that ComEd is no longer a vertically integrated utility, Riders VLR7 and CLR7 employ a market-based approach to valuing energy and capacity demand response that is consistent with the current wholesale market structure. ComEd's proposal to consolidate Riders 13, 26, 27, 30, and 32 into Rider VLR7 and Rider CLR7 is reasonable and should be approved.

b) Rider ISS.

Rider ISS, meanwhile, provides supply services for up to approximately 90 days to customers that are dropped by their suppliers. Crumrine Dir., ComEd Ex. 9.0 Corr., 19:404-09. ComEd voluntarily proposed Rider ISS as a transitional service, as part of ComEd's first delivery services rate case. *Id.* However, Rider ISS, as currently designed, is no longer necessary or even appropriate in the post-transition period. Therefore, ComEd proposes to remove Rider ISS should be removed from ComEd's Schedule of Rates. *Id.*

8. Elimination of Rider 25 – Electric Space Heating (“Rider 25”)

Rider 25 is an outdated tariff. This rider currently provides a specific energy charge with no demand charges in the non-summer months for non-residential electric space heating load customers. It was created when ComEd was a vertically integrated utility, and contains a price structure that reflects the costs of a vertically integrated electric utility. Hence, Rider 25 reflected the difference in ComEd’s generation costs between summer and non-summer periods. Crumrine Reb., ComEd Ex. 23.0, at 32:678-84. Now, ComEd no longer owns generation and, therefore, a customer’s end-use characteristics have no material effect on ComEd’s cost to provide service. *Id.* Moreover, the record indicates that the costs to provide distribution service to non-residential space heat customers is no different than other non-residential customers. *Id.* at 35:739-49. Accordingly, Rider 25 is no longer cost-based, and its continuance would provide an improper subsidy to these customers. There is no basis or justification in the record to support such a subsidy.

BOMA is the only party disputing the elimination of Rider 25. BOMA proposes that customers with “electric space heat meters” be exempted from DFCs under ComEd’s proposed Rate RDS for eight months out of the year. Brookover/Childress Dir., BOMA Ex. 1.0, at 11:237-39. In effect, BOMA requests free delivery service for two-thirds of the year. In addition, BOMA requests that the provision of this free delivery service also should be extended to apply to “buildings that are currently eligible to be served under ComEd’s heating with light service.” *Id.* at 11:239-40.

BOMA’s proposal for free delivery service for two-thirds of the year is unreasonable and devoid of any cost-justification. Crumrine Reb., ComEd Ex. 23.0, at 31:669-71, 35:739-49; Crumrine Sur., ComEd Ex. 40.0 Corr., at 38:854-65. Exempting customers from legitimate demand charges sends an inappropriate price signal concerning the costs of distribution capacity.

Id. Exempting customers from paying legitimate demand charges also creates a \$48.9 million subsidy that other non-residential customers would have to fund. Crumrine Sur., ComEd Ex. 40.0 Corr., at 38:861-63. This is plainly unfair to other non-residential customers and conflicts with the long-held rate design principle of allocating costs to cost-causers.

BOMA presented no evidence whatsoever to indicate that the costs of providing distribution service are somehow different for non-residential space heat customers. They could not, because it cannot be disputed that distribution investment is driven by demand, not energy usage. *Id.* at 39:873-74. The record indicates that non-residential space heating customers commonly have demands in the non-summer months that are at a similar level to their demands in the summer months. *Id.* at 39:879-81. ComEd witness Paul Crumrine testified:

[I]t makes no difference to the poles, wires, and transformers in place and ready to serve the customer how that customer uses electricity once it is delivered to the meter. The Commission, in both of ComEd’s previous DST cases, has recognized this aspect of distribution rate design. There has been no separation or distinction made for non-residential space heating customers in the design of DFCs since the inception of open access in 1999, and there is no reason for ComEd to set its rates based upon what that customer does with the electricity on its own premises.

Id. at 39:881-88.

What BOMA raises in this proceeding is a supply issue—not a distribution cost issue. Crumrine Reb., ComEd Ex. 23.0, at 33:697-710; Crumrine Sur., ComEd Ex. 40.0 Corr., at 40:898-903. BOMA claims that Rider 25 customers would “have no other option than being served under ComEd’s standard rates, which would effectively eliminate the substantial rate discount they currently receive.” Brookover/Childress Dir., BOMA Ex. 1.0, at 10:223-25. However, the record demonstrates that the “substantial rate discount” that these customers receive is due to the fact that they are bundled customers, and that their discount was created while ComEd still owned generation assets. Crumrine Reb., ComEd Ex. 23.0, at 32:678-84;

Crumrine Sur., ComEd Ex. 40.0 Corr., at 40:898-903. Rider 25 was created largely to “recognize the low off-peak season costs of ComEd’s generation fleet during the time when ComEd was a vertically integrated utility and owned generation.” Crumrine Sur., ComEd Ex. 40.0 Corr., at 40:898-903. Thus, it is inappropriate to deal with supply-related rate impact through the delivery service tariffs.

Finally, BOMA’s complaints regarding the insufficiency of the Commission-approved bill impacts mitigation proposal in the Procurement Case do not belong in this Docket. Brookover/Childress Reb., BOMA Ex. 3.0, at 6:122-7:150. BOMA raised this issue in the Procurement Case and lost. The Commission already has made its conclusion concerning this proposal and has determined that the bill impacts mitigation proposal, and the customers to which it applies, is appropriate. *See* Procurement Order. The Commission also rejected BOMA’s request for a separately defined Customer Supply Group in Rider CPP. *Id.* Just like any other segment of non-residential customers, former Rider 25 customers will be charged an appropriate market-based price that will be applicable to their respective Customer Supply Group. *See id.*; *See* ComEd Exs. 7.0, 13 and 21.0, filed in the Procurement Case.

In conclusion, the end-use characteristics and load shape of customers do not contribute to ComEd’s distribution costs to any significant degree. Crumrine Reb., ComEd Ex. 23.0, at 35:740-41. Accordingly, ComEd’s proposal to eliminate Rider 25 should be adopted.

9. Rider DE

Rider DE – Distribution System Extensions is proposed to replace current Rider 2, with modifications and the inclusion of a formula to use in determining the cost of an extension to the distribution system. (ComEd Ex. 10.14). The CTA indicated confusion with respect to its

application. Anosike Dir., CTA Ex. 1.0, at 11:23-33. ComEd fully addressed this concern and its proposal should be adopted. Alongi/McInerney Reb., ComEd Ex. 24.0, 43:1085-44:1111.

10. Rider NS

ComEd proposes to recover its costs for providing non-standard services and facilities through Rider NS, which replaces current Rider 6. Generally, non-standard services and facilities costs are related to the facilities and services that a customer requests that are in excess of a standard installation. *See* ComEd Ex. 10.1.

a) Reserved Distribution System Capacity Charge.

Reservation of distribution system capacity is a non-standard service. “The most common example of such a nonstandard service requirement is a customer’s request for a service arrangement that included automatic switching to an alternate Feeder.” ComEd’s reserved distribution system capacity charge is not new and the proposed language in Rider NS clarifies that reservation of distribution system capacity is a non-standard service under ComEd’s existing Rider 6 and under ComEd’s proposed Rider NS. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 23:527-30. Moreover, ComEd witnesses Alongi and McInerney specifically testified that:

ComEd recovers the cost to reserve distribution and transmission system capacity in order to serve such retail customer’s electric power and energy requirements that is requested or required by a retail customer from such customer under the rider as a non-standard service and facilities charge. This change is for the purposes of clarification and codifies existing ComEd practice.

See ComEd Ex. 10.14.

The CTA takes the position that it should not pay for reservation of capacity. The CTA did not provide any persuasive evidence to support its position why it should receive this service for free. *See* Anosike Dir., CTA Ex. 1.0, 8:171-10:204; Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 12:311-21:527. On the contrary, the record demonstrates that ComEd is entitled to recover its

costs associated with reservation of capacity. Staff agrees and does not oppose proposed Rider NS. Hanson Reb., Staff Ex. 18.0, at 2:23-27.

The CTA is incorrect in its assertion that ComEd may not have “full reserved capacity” on its system, as evidenced by the events initiated by the 2004 fire at its CTA Ravenswood traction power station. Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 20:486-500. In fact, the record demonstrates that the opposite is true. ComEd witness DeCampli testified that it was the CTA fire that damaged both lines serving that CTA traction power station. Specifically, “the fire caused damage to both ComEd 12,000 volt service lines at the CTA Ravenswood traction power substation and also damaged a CTA conduit on the CTA’s Ravenswood property in which one of ComEd’s 12,000 volt service lines was located.” DeCampli Sur. Corr., ComEd Ex. 31.0, at 8:170-77 (emphasis added). Thus, the fire that the CTA cites “was a double contingency—not a single contingency.” *Id.*

The Ravenswood fire demonstrates that reservation of capacity does exist on ComEd’s system—the reservation of distribution system capacity allowed for power to be restored the next day. Mr. DeCampli testified:

ComEd determined that repairs to the first ComEd line could not be made quickly because the CTA conduit in which it was located was badly damaged. However, ComEd made repairs to the second ComEd line and service to the CTA Ravenswood traction power substation was restored the next day. ComEd continued to provide service to the CTA Ravenswood traction power substation through that single ComEd line for over a week while the CTA repaired the CTA conduit that was damaged in the fire. Once the CTA repaired its conduit, ComEd restored two-line service.

Id. at 8:178-9:184. He further testified:

The fact that service was provided to the CTA Ravenswood traction substation using only the alternate ComEd line for over a week, clearly demonstrates that sufficient reserved capacity was available on the alternate ComEd distribution line to serve the entire CTA Ravenswood traction power substation load.

Id. at 9:184-88. Accordingly, the CTA's assertion that ComEd may not have "full capacity reserved" on its system is without merit should be ignored.

Similarly, the CTA is mistaken in its assertion that its traction power substations, as configured with two lines, enhance ComEd's distribution service to customers other than the CTA. Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 16:392-93. This assertion was totally discredited when ComEd witness DeCampli explained that:

In the event of an interruption to a line serving a CTA traction power substation with such an arrangement of normally closed circuit breakers, every other customer served on that line, except the CTA, will experience a service interruption. In other words, other customers served by the same lines that serve such a CTA traction power substation, do not receive 'enhanced' service reliability simply because they are served by those same lines, unless such customers also request and pay for an arrangement of automatic switching facilities.

DeCampli Sur., ComEd Ex. 31.0 Corr., 6:135-7:141. He reiterated this point during cross-examination. DeCampli, Tr. at 1004:11-1006:7.

In conclusion, the CTA's various arguments are baseless. The charge for reserved distribution system capacity is intended to recover the cost from the cost-causer of distribution system capacity that is reserved to accommodate the automatic transfer of a customer's load from one ComEd line to another. ComEd's costs associated with providing this non-standard service should be recovered from the cost-causer. Staff agreed that "ComEd is certainly entitled to recover its costs for such capacity." Hanson Dir., Staff Ex. 7.0, at 9:192. Accordingly, the CTA's arguments should be rejected and Rider NS should be adopted as modified in the ComEd's rebuttal testimony. Alongi/McInerney Reb., ComEd Ex. 24.0, 21:546-22:559.

b) Standard Service Construction Costs

See discussion of BES-RR in Section III.H.19, *infra*.

c) **Effect on Existing Contracts**

See discussion of BES-RR in Section III.H.19, *infra*.

d) **Rider NS and Elimination of Rider 8**

As a matter of housekeeping, current Rider 8 should be eliminated. This seldom used rider provides a small credit (20.533¢/kW) to approximately 25 customers who have installed their own transformers. *See Alongi/McInerney Reb., ComEd Ex. 24.0, 21:546-22:559.* The record indicates that in the past 10 years less than 35 customers have opted to install their own transformers and utilize Rider 8. *Id.* 25:636-26:657. Thus, ComEd proposes to provide a standard transformer allowance under Rider NS to replace the Rider 8 credit. *Id.* This will likely result in lower Rider NS monthly rental charges for many of the current Rider 8 customers. *Id.* Indeed, for many of these customers, the reduction in Rider NS rental charges would exceed the Rider 8 credit that they currently receive. *Id.* Thus, ComEd's proposal allows billing to be simplified for these customers and itself. *See id.*

Staff takes the position that the elimination of Rider 8 will raise the monthly electric cost for a large percentage of the 225 customers. *See Linkenback Dir., Staff Ex. 8.0, at 13:293-300.* Staff recommends that ComEd either pay Rider 8 customers a one-time payment covering their loss of future credits, thereby allowing Rider 8 to be eliminated, grandfather existing Rider 8 customers, or incorporate the existing Rider 8 credit elsewhere in ComEd's tariffs. *See id.* at 12:284-90.

Staff's proposal should be rejected. In light of the small amounts involved and the minimal number of customers affected, Staff's proposal is not necessary. *See Alongi/McInerney Reb., ComEd Ex. 24.0, 26:664-27:689.* Nevertheless, in rebuttal testimony, ComEd stated that it is agreeable to provide a one-time transition payment to each Rider 8 customer in an amount that

is equivalent to one year of Rider 8 credits, based on the customer's average Rider 8 credits received over the most recent three year period. *Id.* This alternative proposal is reasonable and should be approved

11. Rider POG

ComEd proposes to replace its current Rider 4 – Parallel Operation of Customer's Generating Facilities ("Rider 4") with Rider POG – Parallel Operation of Retail Customer Generating Facilities ("Rider POG"). Rider POG differs from Rider 4 in that it utilizes hourly spot prices from PJM to determine ComEd's avoided energy costs. ComEd then uses this cost information to develop its standard energy payment to certain electricity generating facilities, known as Qualifying Facilities ("QFs") under Section 210 of the Public Utilities Regulatory Policies Act of 1978, 16 U.S.C. §824a-3. Crumrine Dir., Com Ed Ex. 9.0 Corr., 26:590-27:604.

Staff asserts that Rider POG should not be approved at this time. Linkenback Dir., Staff Ex. 8.0, at 7:135-50). In rebuttal testimony, Mr. Linkenback takes the position that an annual fixed avoided energy cost rate is needed "[i]f the Commission wants to continue to promote small power producer production in Illinois." Linkenback Reb., Staff Ex. 19.0, at 4:79-81.

Staff's position is problematic for various reasons. First, Staff's recommendation is not consistent with the Commission's decision in the Procurement Case. As explained in the testimony of ComEd witness Crumrine, adoption of an annual fixed avoided energy cost would conflict with the intricate decisions made as part of the Procurement Case that dictate which load is displaced by QF operation, depending on the QF's size. Crumrine Sur., ComEd Ex. 40.0 Corr., at 76:1712-78:1753. In other words, a result of the Commission's Procurement Case Order is that ComEd's avoided energy costs are the PJM spot market prices. *Id.* On cross-

examination, Staff's witness agreed that ComEd's method to determine avoided costs under Rider POG was reasonable. Linkenback, Tr. at 2075:22-2076:9.

Moreover, setting an annual fixed avoided energy cost would jeopardize ComEd's full cost recovery. On cross-examination, Staff's witness admitted as much. Linkenback, Tr. at 2077:19-2078:2. Simply stated, Staff's recommendation requires ComEd or Staff to accurately predict ComEd's avoided energy costs or PJM spot market prices. This is unreasonable and could result in a situation where ComEd is penalized for guessing incorrectly.

In contrast to Staff's fixed price proposal, ComEd's proposal to utilize spot market-based purchase rate will send the appropriate price signals to QFs. Spot market prices would create a clear incentive for QFs to manage their output and generate electricity at times when there is a scarcity of supply—that is, when prices are high. Crumrine Sur., ComEd Ex. 40.0 Corr., at 78:1754-69. On the other hand, a fixed annual purchase rate, with seasonal and/or time-of-day differentiation, would send a price signal that is muted by the averaging that normally occurs in such calculations. *Id.* This would not give QFs the maximum incentive to actually be on the system and generating at the times of highest market prices. *Id.*

In addition, the Commission already has determined that the appropriate price that ComEd should offer to retail customers that utilize self-generation is an hourly price based on the PJM spot price (Procurement Case). There is no reason that qualifying facilities taking service under Rider POG should receive a price signal any different than that which the Commission has already determined to be appropriate for self-generating customers.

Finally, during the cross-examination of ComEd witness Crumrine, Staff inquired whether ComEd was amenable to the addition of language to the compensation section of

proposed Rider POG. The following language, shown in legislative style, was proposed in ComEd Ex. 49.0:

Unless the customer negotiates a different compensation arrangement with the Company pursuant to 83 Illinois Administrative Code Part 430, for ~~For~~ a retail customer taking service under Option C or Option D, the Company compensates the retail customer for output from such retail customer's electric generating facility that is sold to the Company.

ComEd is amenable to this modification to Rider POG. However, it is not clear at this time whether Staff supports this language as an alternative to ComEd's proposal.

In sum, ComEd's proposal is more reasonable than Staff's proposal in that it incorporates the actual benefit of QF generation to the marketplace. For the reasons stated herein, ComEd's proposed Rider POG should be approved.

12. Rider GCB7

In updating its tariffs for the post-transition period, ComEd proposes to replace its current Rider GCB with Rider GCB 7 – Governmental Consolidated Billing 2007 (“Rider GCB7”). Crumrine Dir., ComEd Ex. 9.0 Corr., at 26:574-89. Proposed Rider GCB7 allows certain governmental customers to consolidate their billings by selecting a single day each month as the due date for payment of bills. Rider GCB7 does not contain provisions establishing separate demand charges for these customers, based on maximum and coincident demand of the governmental accounts. *Id.* Rather, the proposed rider applies the charges under the BES tariffs applicable to these accounts, respectively. *Id.*

ComEd proposes Rider GCB7 because consolidated billing of this type is required by the Act. *See* 220 ILCS 5/16-125A. ComEd's proposal meets this requirement. *Id.* at 26:574-89. In addition, Rider GCB7 is required because of changes arising from the Procurement Case. (*Id.*) Specifically, because the cost of capacity is embedded in the auction clearing price for full

requirements electric supply, Rider GCB7 removes the demand charge provisions from Rider GCB to avoid imposing such costs on these customers twice. *Id.* Thus, Rider GCB7 applies the pricing under the applicable BES tariffs to such accounts. *Id.*

The City asserts that ComEd's proposed Rider GCB7 allegedly nullifies the Act's mandate that certain governmental units in the Chicago area receive a "rate reduction." Walter Dir., City Ex. 1.0, 4:67-69, 6:102-6, 6:111-13. The City's argument is without merit because Section 16-125A of the Act does not mandate a rate reduction. Rather, Section 16-125A provides that the utility's tariffs have to provide for "governmental customers to work cooperatively in the purchase of electric energy to aggregate their monthly kilowatt-hour energy usage and monthly kilowatt billing demand." 220 ILCS 5/16-125A (emphasis added). Proposed Rider GCB7 provides for such aggregation.

The City suggests that "a method needs to be found that will allow the Alliance members to consolidate the accounts to achieve rate reductions on the delivery services side of their bills." Walter Dir., City Ex. 1.0, at 6:112-13. The problem with this assertion is that it ignores that ComEd is a distribution company, and that the distribution rates must reflect ComEd's costs. ComEd witness Crumrine explains this as follows:

Because there are distribution facilities in place to serve Midway Airport that are distinct and different from those in place to serve the Daley Center, for example, and those distinct and different distribution facilities are separated by neighborhoods, expressways, and any number of roadways and alleys and cannot be sized to take advantage of any sort of diversity between the loads at the different premises, there is no valid reason to account for a coincidence of demand on the delivery portion of their bills.

Crumrine Reb., ComEd Ex. 23.0, at 58:1225-31.

Accordingly, the City essentially is asking the Commission to grant it a discount that is not cost-based. *Id.* at 58:1231-38. The problem, of course, is that this requires other customers to bear the costs that the City is seeking to avoid. *Id.* This is an unreasonable position and

should be rejected. The evidentiary record establishes that ComEd's proposed Rider GCB7 is reasonable and consistent with the Act. Accordingly, Rider GCB7 should be approved.

13. Rider QSW

No party has raised any substantive issue with respect to ComEd's proposed Rider QSW, which replaces ComEd's existing Rider 3. However, Staff witness Mr. Hanson suggests that references in this rider to Rider POG should be changed to Rider 4 should the Commission reject ComEd's proposed Rider POG. Hanson Dir., Staff Ex. 7.0, 13:272-79.

As stated elsewhere in this brief, Rider POG should be approved. However, in the event that it is rejected for some reason, ComEd asks to replace the text of the proposed Rider POG with the text of existing Rider 4, as appropriate, and retain the references to Rider POG in Rider QSW to maintain consistency within ComEd's proposed tariffs, thereby achieving Mr. Hanson's objective. Crumrine Reb., ComEd Ex. 23.0, 74:1580-90.

14. Rider TS -CPP

Rider TS-CPP is not relevant to the instant case. This rider was filed and fully considered by the Commission in the Procurement Case. *See* Order, Docket 05-0159. Although CES' direct testimony expressed a desire to have ComEd include an "informational" copy of Rider TS-CPP – Transmission Services (Competitive Procurement Process) ("Rider TS-CPP") in this case, its rebuttal testimony was silent on this issue. Domagalski Dir., CES Ex. 3.0 Corr. ComEd did not address this rider in testimony. *See* Alongi/McInerney Reb., ComEd Ex. 24.0, 25:629-34. CES' proposal should be rejected.

15. Rider TAX

Rider TAX is not at issue in this proceeding. While the CTA alluded to this rider by a cursory reference to municipal taxes Anosike Dir., CTA Ex. 1.0, 12:246-48, this reference was

fully addressed by ComEd witnesses Alongi and McInerney. Alongi/McInerney Reb., ComEd Ex. 24.0, 46:1146-57. The CTA did not refer to this rider in rebuttal testimony. *See generally* Anosike/Zika Reb., CTA Ex. 3.0 Corr. Accordingly, Rider TAX should be approved.

16. Rider ML

ComEd's proposed Rider ML contains the monthly rental charges for meter-related facilities and replaces ComEd's existing Rider 7. The determination of a monthly rental charge is provided in ComEd Ex. 10.18. Alongi/McInerney Dir., ComEd Ex. 10.0, 31:732-32:742; ComEd Ex. 10.18.

CUB and City raised certain issues with respect to the level of hourly energy pricing or real time pricing ("RTP") meter costs. Thomas Dir., CUB Ex. 1.0, 14:275-16:315. With regard to their residential RTP proposal, CUB and the City originally took issue with four components of the Rider ML charges: 1) RTP meter service life; 2) RTP meter purchase price for residential RTP program discussed elsewhere in this brief; 3) RTP meter reading charges; and 4) RTP meter exchange costs.

During the hearings, an agreement was reached between ComEd, CUB and the City with respect to residential RTP meter price and RTP meter service life. Tr. at 2385:18-2387:9. This agreement is reasonable and should be approved by the Commission.

There is one remaining issue between ComEd and CUB-City with respect to Rider ML meter rental charges. With respect to the meter exchange costs, CUB-City incorrectly asserts that ComEd should include productivity gains if ComEd is incorporating inflation in the labor rates. Thomas Reb., CUB-City Ex. 2.0 Corr. 14:312-23. The incorporation of productivity gains is inappropriate because the time estimates for performing meter exchanges used in the determination are based on fully trained employees. Alongi/McInerney Sur., ComEd Ex. 41.0

Corr., at 14:328-35. In addition, the expected 4% per year increase in hourly employee wage rates in the determination of meter exchange charges is not an “inflation” factor as CUB-City suggests. On the contrary, it is based on the current Collective Bargaining Agreement between ComEd and its employees. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., 14:328-35. CUB-City’s claims should be rejected. Accordingly, Rider ML, as modified by the previously noted agreement reached between ComEd and CUB-City should be approved.

17. Rider RESALE

Rider RESALE is proposed to replace Rider 12 – Conditions of Resale or Redistribution of Electricity by the Customer to Third Persons (“Rider 12”). The purpose of Rider RESALE is to clarify that a reseller must resell electricity at a rate that does not exceed the average cost per kilowatt-hour that the reseller incurs for the electricity it resells. *See* Crumrine Dir., ComEd Ex. 9.0 Corr., 27:606-14; ComEd Ex. 10.14. The reason for the new Rider RESALE is to update the rate-limiting provision in Rider 12, which currently references Rate 6 – General Service and Rate 6L – Large General Service, to reflect that fact that Rider 12 customers today have a broader range of supply options. *Id.* Certain parties took issue in their direct testimony regarding this rider stating that it is outdated and a landlord should be able to charge varying electric rates to tenants due to the fact that tenants load profiles may warrant different rates. Stephens Dir., IIEC Ex. 1.0, 21:422-23:475; Childress/Brookover Dir., BOMA Ex. 1.0, 14:301-18:401. ComEd agreed to revise the rider to satisfy these concerns. Alongi/McInerney Reb., ComEd Ex. 24.0, 23:596-24:628. BOMA and CES now agree with the revised Rider RESALE. Childress/Brookover Reb., BOMA Ex. 3.0, 9:188-99; O’Connor/Domagalski Reb., CES Ex. 5.0, 3:57-4:68; Stephens Reb., IIEC Ex. 5.0, 20:446-56.

However, Staff, in rebuttal testimony, asserted that it has concerns regarding the modified Rider RESALE proposal. Staff is of the opinion that landlords that resell electricity should be certified as Alternative Retail Electric Suppliers (“ARES”). Schlaf Reb., Staff Ex. 20.0, 14:324-16:367. ComEd takes no position with respect to Staff’s proposal. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., 17:385-92). It is for the Commission to decide whether such a building owner should be certified as an ARES. *Id.*

18. Rate RDS (CTA)

See discussion of BES RR in Section III H.19, *infra*.

19. Rate BES-RR

a) Introduction

In its initial filing in this Docket, ComEd proposed to maintain a separate class for its two railroad traction power customers, CTA and METRA, and to provide bundled service for that railroad class under proposed Rate BES-RR – Basic Electric Service – Railroad (“Rate BES-RR”). As discussed in detail below, ComEd offered modifications of its initial proposal to accommodate certain concerns raised by CTA during the course of this Docket. METRA and the CTA currently are served under long-standing contracts that were filed and approved by the Commission: the (1) Electric Service Agreement Between Commonwealth Edison Company and Northeast Illinois Regional Commuter Railroad Corporation (“NIRCRC”) (commonly known as METRA), dated June 1, 1986, as amended, and (2) the Electric Service Agreement Between Commonwealth Edison Company and the CTA, dated August 1, 1958, as amended. IF the Commission accepts ComEd’s rate design proposals with respect to these customers, the contracts will have to be modified to conform them to the Commission’s Order. (*See e.g.*, ComEd Ex. 10.1.

ComEd's initial proposal for Rate BES-RR has been modified in response to certain issues raised by the CTA in its direct and rebuttal testimonies. Specifically, in response to CTA direct testimony expressing concerns with respect to how ComEd's proposed Rate BES-RR limits CTA's access to multiple suppliers. Anosike Dir., CTA Ex. 1.0, at 11:218-26. ComEd's rebuttal testimony proposed to include appropriate revisions to Rate BES-H, Rate BES-RR, and Rate RDS in its compliance filing pursuant to the Commission's Order in this Docket in order to address the CTA's concern.

Additionally, in response to CTA's concerns regarding standard service and CTA's request for ComEd to provide one line as standard service Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 2:34-36, 23:560-64, ComEd offered a compromise proposal in the surrebuttal panel testimony of Alongi and McInerney. *See* Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., 26:596-27:634, 32:750-33:759. This proposal provides the CTA and METRA with the one line standard per traction power substation that the CTA requested in testimony. Adoption of this proposal also eliminates the need for a separate Railroad Delivery Class and Rate BES-RR. In addition, subject to modifications necessary to conform the contracts to the Commission's Order in this docket, the CTA and METRA contracts would remain in place. The proposed tariff changes for this compromise proposal are set forth in CTA Cross Exhibit 2.0 and METRA Cross Exhibit 1.0.

In summary, ComEd's clarifying language for reserved distribution system capacity and its surrebuttal panel testimony offer to provide one-line service as standard to each railroad traction power substation are reasonable and should be approved. Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, at 24:514-17.

The remainder of this discussion of railroad customer issues addresses the following:

- Standard service for railroad customers
- Retention of the railroad customer contracts
- CTA's Request to be Billed at a Distribution Rate No Higher than Customers Over 10 MW

For purposes of clarity and brevity, this brief will focus on these issues in the context of ComEd's compromise proposal.

b) Standard Service For Railroad Customers

ComEd's initial filing proposed a single point of supply standard for each railroad customer. *See* ComEd Ex. 10.1. In other words, any additions to either railroad system would be considered a non-standard facility subject to charges under Rider NS, unless such addition were to result in an increase in the entire load of the railroad customer's integrated electric traction power system that would require an increase in the railroad customer's standard installation. *Alongi/McInerney Reb.*, ComEd Ex. 24.0, at 39:983-89. This proposal was a continuation of the practice initiated under an amendment to the CTA contract in 1998. *Id.*; *See also* *Crumrine/Alongi Sup. Rep.*, ComEd Ex. 47.0, at 24:500-17. Specifically, the 1998 amendment to the CTA contract, as a condition of CTA's desire to take service under Rate 6L – Large General Service ("Rate 6L") and Rider GCB, specifically incorporated Rider 6. *Alongi/McInerney Sur.*, ComEd Ex. 41.0 Corr., at 24:561-25:570. Thus, the 1998 amendment adopted a single point of service standard for the entire CTA traction power system load consistent with standard service under Rate 6L. *Id.* Since 1998, ComEd has applied and CTA has paid non-standard services and facilities charges for services based on the single electric service station standard consistent with Rate 6L and Rider 6. *Id.*

ComEd subsequently amended its original proposal in this Docket in response to CTA testimony asserting that "[t]he initial service line to each individual CTA traction power substation should be considered standard service by ComEd and not subject to the company's

proposed Rider NS.” Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 2:34-36. In response, ComEd witnesses Alongi and McInerney testified that “ComEd is amenable to providing one service line to each individual CTA traction power substation as a standard service, subject to Commission approval and contingent on certain conditions described in more detail herein.” Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 26:603-5.

ComEd’s agreement to provide one service line to each individual CTA substation as CTA suggests (Anosike/Zika Reb., CTA Ex. 3.0 (Rev.), at 21:537-22:540) eliminates the need for a separate railroad class and Rate BES-RR. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 28:665-29:682. ComEd has not identified all the specific tariff revisions that would be necessary to implement this proposal, but an initial attempt to do so can be found in CTA Cross Ex. 2.0 (Attachment 5). At a minimum, this proposal would affect Rate RDS, Rate BES RR, and General Terms and Conditions. *Id.* This proposal would preclude the need to retain a separate railroad delivery class for purposes of applying charges for delivery service, and also would preclude the need for a separate bundled service rate for railroad customers (*i.e.*, Rate BES RR).

The benefit of this compromise proposal is that it treats the CTA in a fashion similar to other non-residential customers that impose similar costs on ComEd’s distribution system. This proposal is beneficial to the CTA because it can significantly lower the CTA’s charges under Rider NS for future upgrades to its system.

ComEd’s agreement to provide one service line to each individual CTA traction power substation is subject to Commission approval and contingent on certain conditions. Each CTA traction power substation would be classified as a separate retail customer. As such, each such substation would be considered individually for determining the applicable delivery service class, determining standard distribution facilities, and applying delivery service charges. The

following items provide specific aspects of the treatment of each CTA traction power substation as a separate customer:

- The DFC would be applied to the MKD determined separately for each such CTA traction power substation;
- The standard service provided by ComEd would be those off-property facilities necessary to serve the incremental new traction power system load at the individual CTA traction power substation;
- The standard service provided by ComEd for each CTA traction power substation would be subject to a refundable advance deposit as provided in Rider DE – Distribution System Extensions;
- The single point of delivery standard for the CTA’s total traction power system load provided for under the 1998 Amendment of the CTA’s contract would cease to be effective;
- Each existing and new CTA traction power substation would be billed on a separate retail customer account and the CTA could elect to receive a summary bill of such accounts; and
- ComEd’s offer and these same attendant conditions would apply to ComEd’s other railroad traction power customer, Northern Illinois Regional Commuter Railroad Corporation (“NIRCRC”). This condition maintains consistency among similarly situated railroad customers.

Id. at 27:616-34.

These conditions are consistent with the rate design to recover the cost of providing such standard service to each individual railroad traction power substation. Further, these conditions also are consistent with the rate design and standard service provided for other retail customers classified in the same customer class based upon the customer’s demand established at the customer’s individual premises. (*Id.*) ComEd also outlined the types of service requests that would be considered non-standard under this proposal. These criteria are set forth in the surrebuttal panel testimony of ComEd witnesses Alongi and McInerney. *Id.* at 28:642-60. These criteria are consistent with the provision of such non-standard services and facilities

provided under Rider NS to other retail customers, relevant provisions of the railroad contracts, as well as cost-causation and cost recovery-principles. *Id.* at 28:661-64.

ComEd's compromise proposal provides the CTA with its request for a single-line standard to each railroad traction power substation. This proposal is just and reasonable and treats the CTA in a manner that is consistent with ComEd's proposed treatment of other non-residential customers that impose similar costs on the distribution system. However, if the Commission does not approve this compromise proposal, then ComEd requests that its initial proposal that included a separate Railroad class and bundled service Rate BES-RR be approved as amended in ComEd's rebuttal testimony. *See Alongi/McInerney Reb.*, ComEd Ex. 24.0, at 41:1023-43:1084. The original proposal, which also was unopposed by Staff, is reasonable.

c) **Retention Of The Railroad Customer Contracts**

As previously noted, Staff has taken the position that the railroad contracts can be terminated. *See Hanson Dir.*, Staff Ex. 7.0, 11:242-12:262. Indeed, each of the contracts specifically provides that the contract is subject to Commission approval and modification. The CTA contract provides as follows:

SECTION 26.02. This agreement is entered into on behalf of Edison subject to approval by Illinois Commerce Commission and shall be subject to modification by proceedings before such Commission to the same extent and upon the same grounds as any filed rate of general applicability.

CTA Cross Ex. 1.0.

Similarly, the METRA contract provides as follows:

SECTION 15.02. This agreement is entered into on behalf of METRA and Edison subject to approval by the Illinois Commerce Commission and shall be subject to modification by proceedings before such Commission to the same extent and upon the same grounds as any filed rate of general applicability. Service hereunder shall also be subject to the provisions of Edison Rider 6 (Optional or Non—Standard Facilities) and Rider 7 (Meter Lease), as they may be on file from time to time with the Commission, to the extent such provisions are not inconsistent herewith.

METRA Cross Ex. 1.0.

Although Staff is correct that the Commission can terminate these contracts, ComEd is not proposing to do so. In fact, in order to ensure that the relevant provisions of the CTA contract, the METRA contract, and other similar contracts (*e.g.*, Chicago Park District) remain intact, ComEd proposes, subject to the Commission's approval, to incorporate appropriate language in its General Terms and Conditions that would make it clear that the relevant provisions of these tariff contracts continue to apply in all such circumstances (*i.e.*, for situations in which such contract customers take delivery service under Rate RDS as well as for situations in which such contract customers receive full requirement electric supply from ComEd). If the Commission agrees that such a revision is appropriate, ComEd proposes to include the appropriate revisions in its compliance filing at the conclusion of this Docket. This issue is addressed in the panel testimony of Messrs. Alongi and McInerney. Alongi/McInerney Dir., ComEd Ex. 10.0 at 8:203, Alongi/McInerney Reb., ComEd Ex. 24.0 at 11:304, Alongi/McInerney Sur., ComEd Ex. 41.0 Corr. At 29:676-82.

Although these contracts need not be terminated, ComEd proposes to treat these customers in a fashion that is consistent with the costs that these customers impose on the distribution system. Accordingly, if the Commission accepts ComEd's rate design proposals with respect to these customers, the contracts will have to be modified to conform to the Commission's Order.

d) CTA's Request to be Billed at a Distribution Rate No Higher than Customers Over 10 MW

The CTA witnesses make several erroneous assertions regarding the elimination of the over 10 MW customer class. *See, e.g.*, Anosike/Zika Reb., CTA Ex. 3.0 Corr., 1:27-2:31, 2:40-46. In particular, CTA witnesses Anosike and Zika assert that:

The Commission should leave in place the delivery service tariff for customers whose loads are 10 MW or greater as recommended by the IIEC. The CTA's distribution facilities price as reflected in the railroad class should be no higher than the price that customers in the greater than 10 MW class are charged.

See e.g., id. 1:27-2:31. These arguments are addressed in Section III.H.1.b of this Brief. However, whether the Commission accepts or rejects ComEd's proposals with respect to the treatment of over 10 MW customers is irrelevant for purposes of the CTA. The record on this issue is abundantly clear: there simply is no justification in the record to allow CTA, or any non-residential customer with multiple non-contiguous locations in ComEd's service territory, to be billed at a distribution rate no higher than that for a customer with a load of 10 MW or more at a single contiguous location. *See, e.g., Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 19:401-20:415.*

As discussed in Section III.H.1.b in this Brief, ComEd has offered an alternative proposal which conditionally retains an over 10 MW customer class. This alternative does not apply to the railroad customers. *See Crumrine Sur., ComEd Ex. 40.0 Corr., at 8:156-57.* While the CTA asserts that it is served in the same way as other customers with loads of 10 MW or more (Anosike/Zika Reb., CTA Ex. 3.0 Corr., at 2:40-46), the record indicates otherwise. The record indicates that the CTA and METRA together take service for traction power at 70 different locations in ComEd's service territory. *See, e.g., id.* at 22:547-49. These locations are non-contiguous and the load at each traction power substation is typically between 1 and 5 MW, and none exceeds 10 MW individually. *Id.* In contrast, other customers with loads of 10 MW or more are typically served at a single location. *Id.* Furthermore, each of those 70 railroad traction power substations is served through two ComEd 12,000 volt lines. Whereas, most other customers with loads of 10 MW or more that are not in the High Voltage Delivery Class are

typically served through one or two 34,000 volt ComEd lines or one to five 12,000 volt ComEd lines. *Id.*

ComEd witnesses Crumrine and Alongi testified that:

[A]lthough CTA claims it should be charged like customers that have load over 10 MW, the massive amount of distribution facilities required to serve CTA's geographically dispersed traction power substations—which in 1998 included 162 miles of underground primary feeder cable in conduit, 18 miles of overhead primary feeders, involving over 20 different ComEd substations and approximately 60 different feeders—is much different than the distribution facilities required to serve any single customer with load over 10 MW. Rather, with the exception of the automatic load transfer capability that CTA requires, the service to CTA's geographically dispersed traction power substations (of which there was 57 in 1997) is more like providing service to a retail chain of grocery stores, each of which is billed as an individual customer.

Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 19:405-20:415 (footnote omitted).

In sum, the CTA is not at all like an over 10 MW customer. There is no evidence whatsoever to support a finding that the distribution costs to serve two customers with 70 separate non-contiguous locations are similar to those of a customer served at one contiguous location. Indeed, the record overwhelmingly indicates otherwise. Thus, whether the Commission accepts ComEd's conditional proposal, or otherwise decides to retain the over 10 MW class, such a decision should not affect the two railroad customers.

e) **Miscellaneous Railroad Issues**

CTA witness Zika questioned the increase in the Distribution Loss Factor ("DLF") for the CTA. Zika Dir., CTA Ex. 2.0, at 8:156-59. ComEd witness DeCampli fully explained DLFs, how they are calculated, and the reasons for the increase in the Railroad Delivery Class DLF. (DeCampli Reb., ComEd Ex. 14.0, 17:338-21:413. The CTA did not present any credible evidence on this issue and, therefore, CTA's comments on this issue should be rejected.

The CTA also expressed concerns regarding provisions in ComEd’s proposed General Terms and Conditions that the CTA interpreted as potentially requiring “unexplained changes in [CTA] infrastructure.” Anosike Dir., CTA Ex. 1.0, at 10:205-17. The provisions that Mr. Anosike refers to are not new. These provisions are restatements of currently effective tariffs on file with the Commission contained in ILL. C.C. Schedule No. 9 – Information and Requirements for the Supply of Electric Service (“ILL C.C. No. 9”), which ComEd proposed to incorporate into General Terms and Conditions. ComEd witnesses Alongi/McInerney went on to explain each of those existing provisions in detail. *See* Alongi/McInerney Reb., ComEd Ex. 24.0, at 44:1112-45:1145.

20. General Terms and Conditions

ComEd proposes various modifications to its General Terms and Conditions. The notable amendments are summarized in ComEd Ex. 10.21.

The only item at issue⁷¹ with respect to these changes is ComEd’s proposed removal of a service by which residential customers can receive an energy audit. *See* Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., at 19:434-21:479. ComEd proposed to remove the energy audit language that is currently contained in ComEd’s existing Terms and Conditions because it is outdated and refers to a program that was once mandated by law but has long since been discontinued. *See e.g., Id.* 20:451-21:479. This service has not been used by a single customer in at least 13 years. (*Id.*) While in testimony Staff witness Hanson took issue with the removal of this service, during cross-examination Mr. Hanson agreed that the issue of energy audits should be addressed in the upcoming energy efficiency rulemaking orders pursuant to the Commission’s procurement

⁷¹ Issues raised by CES regarding the definition of “peak period” and recategorization of certain condominium common areas as nonresidential customers were addressed to the satisfaction of CES and, therefore, no longer at issue. (*See* O’Connor Reb., CES Ex. 5.0, at 13:284-87, 14:298-99). Issues raised by the CTA regarding General Terms and Conditions are discussed in Section III.H.19 of this Brief.

Order. *See e.g.*, Hanson Dir., Staff Ex. 7.0, at 4:79-82; Tr. 1169:12-1170:3; Order, Docket No. 05-0159.

ComEd agrees with Staff that it is reasonable to address the issue of energy audits in the upcoming energy audit rulemaking. With this understanding, there are no contested issues with respect to ComEd's proposed General Terms and Conditions. Accordingly, the proposed modifications are reasonable and should be approved.

21. Demand Charge

See Discussion of Proposed Change in Definition of Maximum kW Delivered in Section III.H.22 *infra*.

22. Proposed Change in Definition of Maximum kW Delivered

ComEd's proposal to change the way usage for certain large customers is defined for billing purposes has been one of the most misunderstood issues in this case. *See, e.g.*, Crumrine Sur., ComEd Ex. 40.0 Corr., at 10:208-11:237. With the confusion created due to incorrect and misleading assumptions and assertions made by many of the parties, it is important to understand the context for ComEd's proposal.

ComEd recovers the costs of providing standard distribution facilities differently from different customer segments:

- For residential and non-residential customers with only watt-hour metering, the distribution facilities costs are recovered through a per kWh charge because the metering in place for these customers is only capable of registering kWh usage. ComEd charges a per-kWh DFC, which is applied to all kWhs provided to the customer during the billing month, no matter when they are consumed.
- For non-residential customers with load under 400 kW,⁷² ComEd recovers distribution facilities costs through a per kW (*i.e.*, demand) DFC. This is because these customers generally have meters that record the customer's highest demand,

⁷² With the exception of customers that elect different metering or optional services that require different metering (*e.g.*, hourly pricing).

no matter when that demand occurs (*i.e.*, on a 24-hour basis), and ComEd charges them based on the highest 24-hour demand in the billing month.

- For customers with loads over 400 kW that have meters that can record a customer's demand at regular intervals over the day, ComEd currently charges such customers only for the maximum demand during the billing month that is recorded in the currently effective Demand Peak Period, defined to be from 9 am to 6 pm, Monday through Friday, excluding certain days recognized as holidays.

Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, at 4:82-5:98.

It is largely this last group of customers that are affected by ComEd's proposal to modify the definition of billing demand, which is called the Maximum Kilowatts Delivered or MKD.⁷³ The MKD currently is measured for this group of customers as the highest 30-minute demand during the Demand Peak Period in a billing month. *See* ComEd's Rate RCDC, Sheet No. 117. ComEd is proposing that the MKD be determined on the highest 30-minute demand in the billing month, no matter what time of the day that occurs (*i.e.*, a 24-hour MKD). *See* Crumrine Dir., ComEd Ex. 9.0 Corr., 44:961-45:981; Crumrine/Alongi Sup., ComEd Ex. 46.0, 22:470-77; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 5:94-98. Several observations are critical for understanding the context of ComEd's proposal.

First, while there is an implication from certain parties that rejection of ComEd's proposed 24-hour MKD is simply maintaining the *status quo*, this assertion is incorrect. The issue is far more comprehensive than merely retaining a current tariff condition. ComEd's proposal provides a coherent basis for (a) the determination of the delivery classes applicable to customers; (b) the determination of the standard distribution facilities provided to customers; and (c) the determination of the charges applicable to customers for those standard distribution

⁷³ The MKD is multiplied by the distribution facilities charge ("DFC") to obtain the total charge for the distribution facilities in the billing month. The DFC is one part, albeit for large load customers the most important part, of the customer's overall monthly bill. Note that some customers under 400 kW that have interval metering would be affected by ComEd's proposal as well.

facilities. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., 10:208-16. Rejecting ComEd's 24-hour MKD proposal would cause a disconnect between these various tariff conditions.

Second, the Commission already has determined that customers should be grouped based on a 24-hour demand basis for the creation of supply groups in the Procurement Case. ComEd's proposed 24-hour MKD is a consistent approach to classifying customers, which minimizes customer confusion between delivery and supply categories and sends better price signals to customers. *See id.* 10:218-11:223.

Third, the vast majority of ComEd's customers would not be affected by this proposal. As already noted, only those customers with interval demand recording ("IDR") metering, generally customers with over 400 kW of demand, would be affected by this proposal. Of these customers, only those that have large demands outside the Demand Peak Period would see any noticeable change in MKD relative to the current definition. *See id.* at 11:225-27; Crumrine Reb., ComEd Ex. 23.0, 10:206-9.

Fourth, the customers affected by this proposal are ComEd's largest load customers. Because of the size of the demand of these customers, ComEd generally must install facilities that are sized to meet that customer's maximum demand. This means that shifting load from peak to off-peak not only does not, but cannot, have an effect on the manner in which ComEd sizes its distribution facilities to serve these customers. The effect of these customers shifting load is that other non-residential customers that cannot shift load to off-peak pay for these costs. *See id.* 10:206-11:215, Crumrine Sur., ComEd Ex. 40.0 Corr., 11:224-33; Crumrine/Alongi Sup., ComEd Ex. 46.0, 21:444-22:459.

Finally, while ComEd has provided extensive testimony on the reasons why its proposed MKD definition is justified, and those reasons will be discussed in more detail herein, this issue

fundamentally boils down to one of fairness. *See* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 4:72-75. ComEd's current tariffs only bill customers for usage during the predefined Demand Peak Period. *See* Crumrine/Alongi Sup., ComEd Ex. 46.0, 27.4. It does not take sophisticated and detailed knowledge of the distribution system to realize that a customer who largely uses the distribution system outside of the Demand Peak Period receives a free ride under the current MKD definition. While ComEd must size its distribution facilities to meet this customer's maximum demand, the customer only pays for those facilities to the extent that maximum demand occurs in the Demand Peak Period. This violates one of the most fundamental principles of rate design (*i.e.*, customers should pay for the costs they cause the utility to incur) and is blatantly unfair to other customers who have to pay for this subsidy. *See* Crumrine Reb., ComEd Ex. 23.0, 11:218-31; Crumrine Sur., ComEd Ex. 40.0 Corr., 15:310-16; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 4:70-78. The Commission has a long history of implementing tariffs that are cost-based, to the extent possible, and it should continue that approach in this case and approve ComEd's proposed MKD definition.

a) **ComEd's Proposed MKD Definition is Based on the Reality of Distribution System Design**

One of the issues that parties have created confusion over how the proposed MKD relates to what investments ComEd must incur to serve its customers. ComEd's proposed MKD definition reflects the manner in which ComEd's distribution facilities are sized, and in turn matches the cost-causation for these facilities better than using a Demand Peak Period to set MKD. ComEd witnesses Messrs. Crumrine and Alongi clearly state how ComEd must design and invest in its system:

ComEd must design the distribution system such that the facilities on the system are sized to meet the expected maximum demand on those particular facilities, whenever it occurs. This means that localized demand is a critical planning

criteria and ComEd must invest in these facilities to meet the maximum demand expected to be placed on the facilities. For very large load customers, ComEd will have to size the facilities dedicated to serve these customers to meet that customer's maximum demand, whenever it occurs.

Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 8:148-53.

While there should be no dispute that ComEd must invest in distribution facilities in this manner, certain parties have confused the record by suggesting alternative theories of distribution planning and investment. Anosike/Zika Sup., CTA Ex. 4.0, 2:31-39. ("ComEd distribution system is built to meet the maximum demand on the system"); Lazare Dir., Staff Ex. 6.0 Corr., 50:1211-14 ("the distribution system...is designed to serve groups of customers... [W]hat drives these costs are not the demands of individual customers, but rather groups of customers.")). Obviously, these two parties disagree on the design parameters for the distribution system and, therefore, both cannot be correct. In fact, neither is correct.

The IIEC, on the other hand, correctly notes that "the costs...ComEd incurs in providing delivery service are driven by the highest total demand on each piece of distribution equipment used to provide service." (IIEC Verified Comments at 2 (emphasis added) (Note the variance of this conclusion with the CTA and Staff's theories about distribution planning). Unfortunately, the IIEC also claims it is "the time of day that customers establish their high demands [that is] a critical factor in the utility's actual facilities costs." *Id.* As testified to by ComEd witnesses Messrs. Crumrine and Alongi, it is not relevant what time of day customers affected by this proposal reach their maximum demand for the purposes of distribution planning and investment, it is the customer's maximum demand on ComEd's facilities that drives ComEd's investment. Crumrine Reb., ComEd Ex. 23.0, 10:211-11-215; Crumrine Sur., ComEd Ex. 40.0 Corr., 15:319-27; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 10:200-03, 10:214-11:222.

Staff witness Mr. Lazare has further muddied the waters by making a misleading conclusion concerning the 24-hour MKD issue based on the manner in which ComEd allocates its distribution costs in the embedded cost of service study. *See* Lazare Dir., Staff Ex. 6.0 Corr., at 50:1211-19; Lazare Reb., Staff Ex. 17.0, 38:938-39:962; and Lazare Sup., Staff Ex. 23.0 Corr., at 2:38-47. While it is true that ComEd allocated distribution plant based on either non-coincident peak (“NCP”) or coincident peak (“CP”) demand as Mr. Lazare claims, that does not support the use of a Demand Peak Period for setting the MKD for the customers that will be affected by this proposal. *See* Heintz Reb., ComEd Ex. 25.0, at 2:29-33; Crumrine Sur., ComEd Ex. 40.0 Corr., at 17:367-18:383. Mr. Lazare’s confused approach takes no account of facilities that are dedicated (or largely dedicated) for the use of a single customer, nor does it recognize the real planning criteria that ComEd must use in investing in its system (*i.e.*, ComEd must size individual distribution facilities to meet the maximum demand on those individual facilities). *Id.* 17:370-18:381.

ComEd provided a graphical illustration of how one large customer, the CTA, influences the sizing of feeders at its Clark Street traction power substation. *See* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 13:269-14:287; ComEd Ex. 47.6 and ComEd Ex. 47.7. What is clear from these graphs is that the CTA load, which peaks outside of the current Demand Peak Period, influences the sizing of the feeders that deliver electricity to that substation. *See* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 13:279-14:287. No party to this case has disputed this data. In turn, Mr. Lazare, nor any other party, has provided any evidence, at the customer level, to support the contention that the current definition of MKD better reflects cost causation, even though these parties had four opportunities to do so.

To support his conclusion, Mr. Lazare references cost allocations that have been traditionally used to allocate overall distribution costs among rate classes. *See* Crumrine Sur., ComEd Ex. 40.0 Corr., at 17:370-71. The MKD issue is a rate design issue, as it deals with the design of individual tariffs; it is not a revenue requirement allocation issue *per se*. By using this high-level data, which is appropriate for the ECOSS, Mr. Lazare glosses over the real issue of how ComEd must plan its distribution system for large customers and, in turn, how tariffs should be designed. *Id.* at 17:372-75. Further, as Mr. Crumrine points out, while distribution costs are not allocated based on the individual customer's demand, these costs also are not allocated on the individual customer's Demand Peak Period (which is Mr. Lazare's preferred MKD definition). *Id.* at 17:375-77. Therefore, Mr. Lazare's claim that 99% of the distribution costs are allocated based on peak period demands has no bearing on the 24-hour MKD issue.

To crystallize this concept, Messrs. Crumrine and Alongi provide an example based on a highly stylized hypothetical situation posited by the IIEC. In IIEC's hypothetical there are three customers: A, B, and C that all have 10 MW of maximum demand where A and B reach their maximum demands during the Demand Peak Period and C reaches its maximum demand outside of the Demand Peak Period. 11 EC Verified Comments at 3. Customer C sets a 5 MW demand during the Demand Peak Period. Under the IIEC theory of distribution planning (and presumably the other parties would agree) ComEd would size the system to meet the "peak period" maximum demand of 25 MW (10 MW for A, 10 MW for B, and 5 MW for C). However, as ComEd experts testify, this is not correct. *See e.g.*, Crumrine Reb., ComEd Ex. 23.0, at 10:202-11:215; Crumrine Sur., ComEd Ex. 40. Corr., at 10:202-11:237, 13:264-90, 14:291-301. ComEd would have to install dedicated distribution facilities to serve each customer. If this were an actual situation, ComEd would size its facilities to meet the 30 MW of

load, not the 25 MW. Therefore, it is the maximum demand of these customers, not the time at which they reach that maximum demand that drives the investment costs. *See* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 10:214-11:222.

Finally, certain parties have alleged that ComEd's proposed MKD definition ignores the benefits of diversity of demand on the system. *See, e.g.,* Lazare Dir., Staff Ex. 6.0 Corr., at 50:1209-19; Stephens Dir., IIEC Ex. 1.0, at 18:347-50; Menninga Dir., IAWA Ex. 1.0, at 8:145-50; Anosike Dir., CTA Ex. 1.0, at 6:108-11; Zika Dir., CTA Ex. 2.0, at 7:143-51. As shown earlier, such claims are based on a faulty understanding of the types of customers the 24-hour MKD proposal would affect and a complete misunderstanding of how ComEd plans and invests in its distribution system. *See* Crumrine Reb., ComEd Ex. 23.0, at 10:206-11:215. These claims hold no value and should be ignored.

ComEd has supported its MKD proposal with consistent and sound testimony concerning the manner in which it plans and invests in its distribution system. Other parties and Staff have provided a mish-mash of conflicting theories and assertions concerning distribution planning and investment, all of which fail under even superficial examination. ComEd is the only party to provide a consistent and logical argument that links its 24-hour MKD proposal to the manner in which investment in the distribution system actually occurs. Therefore ComEd's proposed 24-hour MKD is consistent with cost causation principles and should be adopted.

b) ComEd's Proposed MKD Definition Eliminates a Current Intra-Class Subsidy in the Non-residential Customer Classes

Under the current MKD definition, an intra-class subsidy exists between customers who utilize the system more in the off-peak and customers that cannot shift load to the off-peak periods. *See* Crumrine Reb., ComEd Ex. 23.0, at 11:218-31; Crumrine Sur., ComEd Ex. 40.0 Corr., at 15:319-16:335. Large load customers who utilize the distribution system in the off-

peak period currently are receiving a subsidy from those customers that cannot or do not utilize the distribution system in this manner. These customers have largely dedicated facilities that are sized to meet the maximum demand on those facilities at any time of the day. Therefore, utilizing billing units for the Demand Peak Period only creates a subsidy that is largely paid for by customers consuming during the Demand Peak Period. (*Id.* 6:Table 1). Mechanically, this subsidy occurs because, while the total revenue requirement allocated to a customer class does not change, the number of billing units used to calculate the DFC change will be different under the current MKD definition and the 24-hour MKD definition. Under a 24-hour MKD these billing units will be larger, which results in a lower DFC for all customers in the class. Under the current MKD, the Demand Peak Period billing units are lower which results in a higher DFC for all customers in the class. That higher DFC largely falls on customers that consume during the Demand Peak Period. *Id.* at 15:326-16:335. ComEd has estimated this subsidy is roughly \$31 million, or about 3.5% of ComEd's proposed total revenue requirement for the non-residential classes. *See* Crumrine Reb., ComEd Ex. 23.0, at 11:229-31.

Rejection of ComEd's proposed MKD definition would unfairly transfer these costs from customers that have the flexibility to shift significant amounts of load to the off-peak periods to the majority of non-residential customers that do not have this capability. Crumrine Reb., ComEd Ex. 23.0, at 11:216-26; Crumrine/Alongi Sup., ComEd Ex. 46.0, at 24:500-17; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 4:68-6:123. Furthermore, this proposal would affect a very small number of ComEd's non-residential customers. Crumrine Reb., ComEd Ex. 23.0, 10:202-11:215; Crumrine/Alongi Sup., ComEd Ex. 46.0, 21:442-22:459; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 5:99-6:105. That is, currently, a very small group of the ComEd's

largest load customers avoid paying their fair share of distribution costs. *Id.* ComEd's 24-hour MKD proposal rectifies this situation and moves its tariffs closer to reflecting cost causation.

c) **State Regulators Recognize the Importance of Off-Peak Demands in Setting Distribution Prices**

In response to questions from Commissioners Ford and Lieberman, ComEd conducted a survey of all retail jurisdictions in the United States that have some form of restructuring in place as of January 1, 2006. *See* Crumrine/Alongi Sup., ComEd Ex. 46.0, 24:498-520; Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, 14:288-15:320; ComEd Ex. 47.1. The results of that survey are summarized in the following table.

Utility Billing Demand Survey

Maximum Billing Demand Determination	Number of Utilities in Survey	Percent of Total
1. 24-Hour clock	12	32%
2. Some recognition of off-peak demand	12	32%
3. On-peak demand with ratchet	8	21%
4. On-peak demand without ratchet	6	16%
Total	38	100%*

* May not sum to 100 due to rounding.

Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, at 15:320.

The conclusion from this research is clear. The majority of utilities in the survey utilized off-peak demand in setting prices either through the use of a 24-hour MKD (32%) or through some other method of valuing off-peak demand (32%). Of those that did not explicitly use off-peak demands, over half used a pricing tool called a demand ratchet. A demand ratchet uses the highest MKD from a specific time (*e.g.*, the highest MKD in the previous 12 months) to set the

billing demand for any given month. That is, the MKD for the current billing month is set based upon the highest MKD set over a specific time frame prior to the current month. (ComEd Ex. 47.1 provides a description of the demand pricing which includes the specific ratchet provisions for those tariffs that include a ratchet.) Only a minority of utilities (6 of the 38 in the survey) use a monthly Demand Peak Period MKD for billing purposes without a ratchet, which is how the MKD is currently determined in ComEd's tariffs. *See* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, at 15:314-19.

Furthermore, ComEd was the only party to provide such a comprehensive survey of state jurisdictions for the record, although both Staff and IIEC reviewed a very limited number of tariffs. *See* Lazare Sup., Staff Ex. 23.0 Corr., 6:139-8:198; 11 EC Verified Comments, IIEC Ex. at 7. In addition, both Staff and the IIEC leave the impression that the MKD, as currently defined in ComEd's tariffs, is used equally with policies that recognize off-peak usage in the MKD. This simply not the case, as the majority of state regulators have approved tariffs that recognize that off-peak demand is an important factor in distribution pricing. (32%+32%=64% from the Utility Billing Demand Survey table, *see also* Crumrine/Alongi Sup. Rep., ComEd Ex. 47.0, at 14:299-301). Therefore, ComEd's proposed 24-hour MKD that recognizes that off-peak demand as a critical factor in setting distribution tariffs is largely in line with the rest of the country. ComEd's current MKD definition, that utilizes no demand ratchet and measures MKD in the Demand Peak Period is out of step with the rest of the country. ComEd's proposed 24-hour MKD is consistent with the majority of distribution tariffs in the United States for utilities that have some form of restructuring and should be accepted.

23. Single Monthly Peak Vs. Average of 3 Peaks for Municipal Pumping

See Discussion of Proposed Change in Definition of Maximum kW Delivered in Section III.H.22(a), *supra*.

24. Municipal Pumping Class in Demand-based Categories

ComEd is proposing that water and sewage pumping customers be treated in the same manner as other customers with similar demands. Crumrine Reb., ComEd Ex. 23.0, at 35:753-58). Thus, ComEd is proposing that these customers take service under the appropriate delivery service class for each such customer's demand level. Crumrine Dir., ComEd Ex. 9.0 Corr., 40:872-42:897. This result is reasonable and the record does not support any other conclusion.

Similar to other parties in this docket, (*e.g.*, the CTA and the City), the IAWA is seeking to maintain the aggregation of load across non-contiguous locations for purposes of setting maximum demand. Menninga Dir., IAWA Ex. 1.0, at 7:125-28. This request is unreasonable.

The IAWA suggests that the aggregation of load as it proposes recognizes the "benefits to the distribution system associated with this distribution of demand." Menninga Dir., IAWA Ex. 1.0, at 6:102-4. However, a pumping customer, just as any other customer, causes costs on the delivery system based on the individual maximum demand at each geographically separate pumping station. *See* Crumrine Dir., ComEd Ex. 9.0 Corr., 41:880-42:889; Crumrine Reb., ComEd Ex. 23.0, at 36:767-74. As ComEd witness Paul Crumrine testified:

Pumping sites located in various parts of a municipality require ComEd to install facilities to meet the maximum demand of each facility and, therefore, ComEd's delivery costs are localized. From ComEd's perspective as a delivery service company, there is no reason to treat pumping customers any different from other similarly sized non-residential customers. Mr. Menninga has provided no compelling argument to rebut this point.

Crumrine Reb., ComEd Ex. 23.0, at 36:769-74.

The argument raised by the IAWA is similar to the arguments of other parties (*e.g.*, CTA and the City), requesting the ability to aggregate load at non-contiguous locations. These parties essentially ask the Commission to ignore distribution costs and provide these customers with a subsidy. As such, the IAWA's proposals are not cost-based and should be rejected.

25. Credit for CTA's Own Transformation and Distribution

CTA witnesses Anosike and Zika assert that CTA does not believe that ComEd has charged the CTA only for the cost of facilities that are reasonably assignable to the CTA. Anosike/Zika Sup., CTA Ex. 4.0, at 9:240-46. The CTA made a similar unsupported statement in direct testimony, but did not address it in rebuttal testimony. *See Zika Dir.*, CTA Ex. 2.0, at 6:111-14.

ComEd's ECOSS determines ComEd's cost to serve customers based on ComEd's costs. *See generally Heintz Dir.*, ComEd Ex. 11.0. Additionally, ComEd provided an analysis prepared in 1997 which demonstrates that ComEd considered only the CTA's proportional use of each individual primary feeder and each ComEd transformer substation in developing the underlying basis for the nonstandard service charge under Rate 6L and Rider 6, which is consistent with the cited provision of Rider 6 to charge only the cost of facilities that are reasonably assignable to the customer. *See Crumrine/Alongi Sup. Rep.*, ComEd Ex. 47.0, 22:468-75; ComEd Ex. 47.5. CTA's equipment has no bearing on ComEd's costs. The CTA's assertions have no basis and should be ignored.

In addition, see discussion of BES-RR in Section III.H.19, *supra*.

26. Supply Administration Charge

The costs that ComEd will incur to administer the supply function for bundled electric service customers, including associated administration and general ("A&G") costs, should be

recovered from the bundled electric service customers that cause these costs. *See generally* Crumrine Dir., ComEd Ex. 9.0 Corr., 46:1007-48:1031. Accordingly, ComEd proposes that each proposed BES tariff contains a corresponding Supply Administration Charge (“SAC”). *Id.*; *See also* ComEd Ex. 10.1 and ComEd Ex. 10.7.

The record demonstrates that ComEd’s proposal fairly apportions the costs incurred by ComEd to provide bundled electric service to customers. *See* Crumrine Dir., ComEd Ex. 9.0 Corr., at 46:100-48:1031; Crumrine Reb., ComEd Ex. 23.0, 48:1020-49:1041. Specifically, ComEd proposes that these costs, which are fixed in nature, be recovered through a fixed SAC per month for each BES tariff. *Id.* ComEd proposes to allocate these costs utilizing a two step process: 1) first, the costs are allocated between each of the BES tariffs based on the total kWhs that ComEd provided to each of the Customer Supply Groups, and 2) the costs are allocated to each group utilizing the expected number of customers to arrive at a fixed per customer charge for each BES tariff. Crumrine Dir., ComEd Ex. 9.0 Corr., at 46:1007-48:1031; Crumrine Reb., ComEd Ex. 23.0, 48:1020-49:1041.

While Staff does not oppose the concept of recovering a SAC charge through the BES tariffs, Staff asserts that the SACs should be “recovered on a usage basis,” as opposed to the per customer basis proposed by ComEd. Lazare Dir., Staff Ex. 6.0 Corr., at 49:1188-92. This position is not reasonable for three reasons. First, Staff’s underlying assumption that the “level of [these] costs bears a closer relationship to usage than to the number of customers” is flawed. *See id.* 48:1181-49:1185; Crumrine Dir., ComEd Ex. 9.0 Corr., at 47:1006-48:1031; Crumrine Reb., ComEd Ex. 23.0, 48:1020-49:1041. The only support for this conclusion is Staff’s speculation that if ComEd provides less bundled supply that it would result in lower costs. Crumrine Dir., ComEd Ex. 9.0 Corr., 46:1007-48:1319; Crumrine Reb., ComEd Ex. 23.0,

48:1020-49:1041. However, there was absolutely no evidence proffered in this case or in the Procurement Case to support the assumption that a reduced supply obligation would in turn reduce administrative costs. (*Id.*; Procurement Order. In contrast, the record demonstrates that the costs reflected in the SAC are relatively fixed and do not vary with the volume sold or the number of customers served. *See, e.g.,* Crumrine Reb., ComEd Ex. 23.0, 49:1044-46. Staff's assumption is unfounded and should be rejected.

Second, while these costs are fixed in nature, ComEd proposes that they be allocated to the various customer groups based on usage. As indicated previously, the first step of the allocation involves allocation of the costs to each BES tariff based on the total kilowatt-hours. *Id.* at 48:1020-27. ComEd proposes to allocate such costs in this manner because they are, in a limited sense, incurred to provide supply. *Id.* However, consistent with traditional ratemaking principles, ComEd proposed a fixed charge for the recovery of fixed costs. *Id.*

Third, aside from lacking support in the record, Staff's proposal is not practical. With proposed SACs of as little as a penny per month for residential customers, it makes no sense to convert this charge into a per kWh charge. *Id.* at 49:1042-55. The record demonstrates that for most BES customers, the costs allocated to them are such relatively small amounts that converting the monthly charge to a per kWh charge would create a meaningless distinction. ComEd's proposed allocation is just under \$520,000. *Id.* With usage estimated at over 26 billion kWhs per year, the residential charge would just about round to zero on a per kWh basis (approximately 0.001 cent per kWh). (*Id.*; *See also* ComEd Ex. 10.7). Staff's suggestion of a per kWh charge for supply related costs is baseless and unreasonable. Accordingly, it should be rejected.

The Commission also should reject CES' arbitrary and unsubstantiated recommendation to "allocate no less than one-fourth of call center costs to supply." O'Connor/Domagalski Reb., CES Ex. 5.0, at 11:226-27. CES' proposed percentage is pulled out of thin air. Crumrine Sur., ComEd Ex. 40.0 Corr., at 60:1358-61:1377. It has no basis whatsoever and is a transparent attempt to create "headroom" by artificially increasing the cost of BES rates. *Id.* As such, the proposal is unreasonable and should be rejected.

27. Real Time Pricing Meters and Energy Smart Pricing Plan

CUB and the City propose that ComEd: 1) include residential real time pricing ("RTP") meters in the standard meter charge for residential customers; 2) work to expand the size of the Energy Smart Pricing Plan; and 3) provide RTP meters for every residential customer interested in RTP Programs (collectively "the Proposal"). Thomas Dir., CUB Ex. 1.0, at 5:81-88, 9:161-10:185. ComEd supports this Proposal subject to certain conditions discussed herein.

The Proposal seeks to socialize across all residential customers the cost of providing IDR meters to customers who request them. Crumrine Reb., ComEd Ex. 23.0, 43:925-44:952. Under the Proposal, ComEd would add the program costs to ComEd's revenue requirement for residential customers and reflect such costs in the residential Customer Charge. *Id.* All residential customers would pay the same Customer Charge, regardless of the tariff under which they take service. By allocating the costs in this manner, all residential customers would bear the same percentage of the total costs associated with this program. *Id.*

ComEd supports this Proposal, subject to two conditions. *Id.* at 46:996-47:1014. The first condition is that the program must contain a cap in the tariffs for the number of residential customers for which ComEd would waive metering installation and removal costs. *Id.* The cap should be equal to the total number of residential Rate BES-H customers assumed in whatever

cost scenario or alternative analysis the Commission ultimately adopts. *Id.* In rebuttal testimony, CUB witness Mr. Thomas supported the “Current Administrator High Estimate,” which is based on the Community Energy Cooperative (“CEC”) estimate of 70,000 customers enrolling within three years. *See* Thomas Reb., CUB Ex. 2.0, at 7:144-55. Thus, ComEd is willing to waive the associated fees for no more than 70,000 customers at any point in time. Crumrine Sur., ComEd Ex. 40.0 Corr., at 52:1180-91. This cap is necessary in light of the uncertainties surrounding when and how many customers will respond to this program in the post-2006 environment. *Id.* at 53:1196-99.

ComEd’s support for the Proposal also is predicated on the Commission’s rejection of Staff witness Lazare’s proposal to shift 20% of the costs reflected in the Customer Charges to the DFCs. Crumrine Reb., ComEd Ex. 23.0, at 47:1008-14. This condition is necessary because Staff’s proposal has the potential of jeopardizing ComEd’s cost recovery and the Proposal would result in an increase in the costs to be recovered through the Customer Charge. Consequently, this result would exacerbate the many problems associated with Staff witness Lazare’s cost shifting proposal. *Id.*

CUB and the City responded to ComEd’s conditional support with three conditions of their own. First, ComEd should equally share the risk of the program with customers. Thomas Reb., CUB Ex. 2.0, at 7:151-52. This condition is not reasonable because the estimated number of participating residential customers is the “primary driver of the cost estimates” (Crumrine Reb., ComEd Ex. 23.0, at 46:987-89; Crumrine Sur., ComEd Ex. 40.0 Corr., at 53:1196-99), and there are “obvious uncertainties surrounding when and how many customer[s] will respond to this program in the post-2006 environment...” Crumrine Reb., ComEd Ex. 23.0, at 47:1005-7; Crumrine Sur., ComEd Ex. 40.0 Corr., at 52:1180-91. The estimate adopted should be as

accurate as possible in order to minimize the risk of overpayment and underpayment for both customers and ComEd. Crumrine Sur., ComEd Ex. 40.0, 53:1204-14. However, ComEd believes that it is no more reasonable that residential customers bear the risk of overpayment if the Commission should adopt the Proposal and overestimate the number of residential participants than it is for ComEd to bear the risk of under-recovery if the Commission underestimates the number of residential participants. Accordingly, ComEd cannot agree to this condition. *Id.*

Their second condition is that “IDR meters should be made available for RTP programs offered by alternative suppliers.” Thomas Reb., CUB Ex. 2.0, Corr. 7:152-53. CES witness Ms. Meffe suggests that CUB’s proposal be made “competitively neutral between ComEd and RESs.” Meffe Reb., CES Ex. 7.0 Corr., 14:317-15:327. It is not clear what is meant by the phrase “competitively neutral.” Crumrine Sur., ComEd Ex. 40.0 Corr., 54:1220-31. ComEd interprets “competitively neutral” to mean that if a RES were to provide residential customers a real time, market-based energy pricing service analogous to ComEd’s Rate BES-H, then such customers also should receive a waiver on the otherwise applicable metering and meter exchange charges and fees. *Id.*

If the Commission accepts this Proposal, ComEd would have no objections to making this Proposal “competitively neutral” under two conditions. First, ComEd reiterates that the proposed cap must be approved because including RESs in the Proposal would place upward pressure on the number of participating customers. *Id.* at 54:1232-55:1246. Second, in implementing a competitively neutral program, ComEd recommends that any RES seeking to provide RTP to residential customers must:

(1) provide a sworn statement to ComEd that all such customers are, in fact, on an hourly energy pricing program, where the hourly prices directly reflect PJM Interconnection, L.L.C. (“PJM”) spot prices;

(2) provide advance notice to ComEd of when pricing in the customer’s contract changes to something other than hourly energy pricing, so that the IDR metering can be exchanged as it would for a Rate BES-H customer;

(3) agree to submit to a periodic audit conducted by Staff (for which ComEd will reimburse the Commission for its travel and business expenses) of its applicable customer contracts; and

(4) assume financial responsibility for all charges and fees waived for such customer in the event it is determined that such customers are not or are no longer on a legitimate hourly energy pricing service from the RES.

Id. at 55:1247-56:1267.

Finally, ComEd agrees to the third and final condition that “the Commission should order ComEd to work closely with stakeholders in an effort to actively educate customers about the benefits of RTP programs.” Thomas Reb., CUB Ex. 2.0, Corr. 7:153-55. ComEd is willing to work with stakeholders in an effort to educate customers about RTP. Crumrine Sur., ComEd Ex. 40.0 Corr., 56:1268-77. However, ComEd notes that such education efforts must fairly present both the potential advantages and disadvantages associated with RTP programs. (*Id.*) Indeed, RTP may not be the right choice of rate for all residential customers, as Mr. Thomas recognizes. *See* Thomas Reb., CUB Ex. 2.0, Corr. 8:178-9:182. Thus, this CUB condition should be a non-issue.

Staff, meanwhile, took the position that further research is needed on residential RTP to determine that “enough system-wide benefits would be gained to justify the proposed cross-subsidy, even at the very small level proposed by ComEd in ComEd Ex. 23.1.” Schlaf Reb., Staff Ex. 20.0, 6:144-7:147. ComEd agrees that there may be cross-subsidy issues, but takes the position that “this is a matter worthy of the suspension (at least, temporarily) of traditional

ratemaking practices....” Crumrine Reb., ComEd Ex. 23.0, at 44:946-49; Crumrine Sur., ComEd Ex. 40.0 Corr., at 56:1294-1303.

Finally, should the Commission share Staff’s opinion that further research is needed before implementing the Proposal, ComEd’s revenue requirement must be adjusted to recover the costs associated with the experiment. *Id.* In sum, ComEd supports CUB’s residential RTP program subject to the aforementioned conditions.

28. Distribution Loss Factors

See miscellaneous railroad issues, Section III.H.19.e, *supra*.

29. Replacement of Rider 28 with Rider LGC

ComEd proposes to replace ComEd’s existing Rider 28 with Rider LGC. *See* ComEd Ex. 10.1 and ComEd Ex. 10.3. There are no substantive changes between existing Rider 28 and ComEd’s proposed Rider LGC. Alongi/McInerney Reb., ComEd Ex. 24.0, 15:389-91; ComEd Ex. 10.15. Indeed, arguments very similar to those raised by the City were rejected when the Commission approved Rider 28. *See* ICC Dockets 91-0146 and 91-0217, [cons.] (Order, Feb. 11, 1992). Thus, Rider LGC is reasonable and should be approved.

The purpose of Rider 28 and its proposed replacement, Rider LGC, is to recover the incremental costs incurred by ComEd in the event a local government unit requires ComEd to provide a service, or otherwise install, remove, replace, modify or maintain its facilities in a manner that is different from the manner in which ComEd would otherwise be required. *See, e.g.,* Alongi/McInerney Reb., ComEd Ex. 24.0, 15:385-91. Rider 28 currently recovers, and Rider LGC is proposed to recover, these additional costs directly from the ComEd’s retail customers located within the boundaries of such local government unit imposing the additional requirements. *See* ComEd Ex. 10.1, ComEd Ex. 10.2.

ComEd presented detailed evidence explaining that the differences between Rider 28 and proposed Rider LGC are not substantive. (*See* Alongi/McInerney Reb., ComEd Ex. 24.0, 15:392-16:407; ComEd Ex 24.4). In rebuttal testimony, ComEd provided the changes between the riders in legislative style. *Id.* This exhibit demonstrates that the changes are minor in nature and simply add clarity and organizational structure to the existing tariff language. *Id.* Additionally, ComEd also represented that it intends to administer Rider LGC “in the same manner” as Rider 28. Alongi/McInerney Reb., ComEd Ex. 24.0, 17:438-43.

The City is the only party that took issue with Rider LGC.⁷⁴ However, the City’s primary argument, that Rider LGC gives ComEd too much discretion, is baseless. Indeed, in approving Rider 28, the Commission rejected this same argument. *See* ICC Dockets 91-0146 and 91-0217, [cons.], (Order, Feb. 11, 1992). Moreover, the City never references any specific new language that supposedly grants this “discretion.” (*See, e.g.,* Walter Dir., City Ex. 1.0, 8:143-46). The City’s assertions are unsupported and the Commission should reject them.

The City’s assertion that Rider LGC may impair the City’s rights under the existing franchise agreement with ComEd is equally meritless. (*See* Walter Reb., City Ex. 2.0, 8:131-41). The City asserts that subsection (d) of proposed Rider LGC would impair the City’s right under its franchise agreement with ComEd because the franchise agreement requires ComEd to remove at its expense any utility facility in the public way when the City has determined that such removal is necessary for certain purposes. *Id.* The City misunderstands the language in the Rider for two reasons. First, the record demonstrates that subsection (d) is a clarification of an existing practice. (*See* Alongi/McInerney Reb., ComEd Ex. 24.0, 15:402-16:406). Second, the City’s concern is not justified because a “like-for-like” replacement and relocation of ComEd’s

existing standard facilities for a road widening public improvement are not subject to the provisions of the rider. This is the reason for the “otherwise required” language in subsection (d). *See id.* at 16:415-422.

The evidence demonstrates that the differences between Rider 28 and proposed Rider LGC are not substantive and do not change the purpose of the rider. Accordingly, Rider LGC should be approved.

30. Other

In light of the magnitude of changes being proposed by various parties in this proceeding, as well as the fact that the final Commission Order is scheduled to be entered several months in advance of the beginning date on which charges under the proposed tariffs would apply (*i.e.*, January 2, 2007), ComEd requests 30 days from the time the final order is entered in which to file its compliance tariffs. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., 39:901-40:925.

There also are two housekeeping proposals regarding ComEd’s proposed rates. (*See id.*; Alongi/McInerney Dir., ComEd Ex. 10.0, at 9:216-31). First, ComEd proposes that the Commission, in its order in this proceeding, direct ComEd to file a new Schedule of Rates with a new schedule number (*e.g.*, Schedule ILL. C.C. No. “XX”) within a reasonably short period of time after the mandatory transition period ends (*e.g.*, within eight months). This is necessary because ComEd’s current set of rates will remain in ComEd’s Schedule of Rates, but will no longer be operational at the end of the mandatory transition period. (*Id.*)

Second, to facilitate a customer’s ability to locate information in the new Schedule of Rates, ComEd requests that the Commission’s order in this proceeding provide a variance to the

⁷⁴ While Staff originally took issue with a provision in proposed Rider LGC, Staff witness Hanson stated in rebuttal testimony that the issue had been resolved to his satisfaction. *See* Hanson Dir., Staff Ex. 7.0, at 7:145-49; Hanson Dir., Staff Ex. 18.0, 2:29-3:44.

tariff sheet numbering requirements contained in 83 Ill. Admin. Code 255.30(c), and instead allow ComEd to file its new post-2006 Schedule of Rates (*i.e.*, Schedule ILL. C.C. No. “XX”) using the proposed tariff sheet numbering structure shown in ComEd Ex. 10.5.

IV. RETAIL COMPETITION ISSUES

A. Clarification of Tariffs for Post-transition Period

ComEd has agreed to work with RESs to develop a summary of the switching rules for purposes of the RES Handbook. Alongi/McInerney Reb., ComEd Ex. 24.0 30:765-35:896. CES appears to be satisfied with ComEd’s “...willingness to work with RESs to ensure that ComEd has clear and easy to follow switching rules.” O’Connor and Mr. Domagalski Reb., CES Ex. 5.0 at 14:304-17:369.

B. General Account Agency

ComEd’s Information Technology (“IT”) and business process were appropriately established for a one-on-one relationship between ComEd and its customers, permitting a customer to appoint an agent to act on the customer’s behalf. Agency issues in the open access environment were the subject of discussion and a Commission Order in ComEd’s last delivery services rate case, ICC Docket No. 01-0423. Meehan Reb., ComEd Ex. 26.0 11:225-34.

CES’ recommendation that ComEd modify its IT and business processes to allow for different types of General Account Agents (“GAA”), and to permit appointment of agents to begin acting at a future date, is inappropriate and should be rejected. CES’ proposal confuses the duties and rights of a RES with that of a GAA, essentially treating the two entities as synonymous, which is inappropriate and not in keeping with the Act or ComEd’s tariffs. Crumrine Reb., ComEd Ex. 23.0 77:1673-79:1720; Meehan Reb., ComEd Ex. 26.0 4:92-7:153. Additionally, operationally, the proposal to create multiple agents that are “stacked” by both type

of agency and effective date is problematic in several senses. First, there is no place to record multiple agents, whether current or future, in ComEd's billing system. Meehan Reb., ComEd Ex. 26.0, 8:154-59; Meehan Sur., ComEd Ex. 43.0, 3:52-54. Second, it could create confusion if customers appointed multiple agents to perform the same function, potentially providing conflicting instruction to ComEd. Meehan Reb., ComEd Ex. 26.0, 9:185-10:216; Meehan Sur., ComEd Ex. 43.0, 2:40-46. Third, given the lack of certification requirements, the Commission should be cautious so as not to create a situation in which an unscrupulous agent could make changes to a customer's account that the customer did not intend. Meehan Reb., ComEd Ex. 26.0, at 10:217-224; Meehan Sur., ComEd Ex. 43.0, at 3:47-51. Fourth, a customer can take advantage of services available in the marketplace, such as energy consulting, without appointing vendors offering such services as the customer's agent. Meehan Reb., ComEd Ex. 26.0, 8:161-9:184; Meehan Sur., ComEd Ex. 43.0, at 3:55-7.

The issues raised by CES are complex IT and business process issues that have statewide implications, and are more appropriate for a workshop forum than for a decision in this rate case. Crumrine Reb., ComEd Ex. 23.0, at 80:1721-32; Crumrine Sur., ComEd Ex. 40.0, at 83:1871-1908; Meehan Sur., ComEd Ex. 43.0, at 4:74-93. Notably, Staff agrees. Schlaf Reb., Staff Ex. 20, 13:291-14:307. The CES proposals with regard to agency should be rejected.

C. Electronic Data Interchange

Electronic Data Interchange ("EDI") is a standardized system that allows the computers of different companies – in this case ComEd and participating RESs – to communicate. Through this process, ComEd and RESs can exchange information and data relating to a RES's supply of electric power and energy to customers, including enrollments, drops, billing information, usage data, and changes to customer information. (Meehan Reb., ComEd Ex. 26.0 11:237-12:242).

CES recommends that ComEd make significant alterations to its operations regarding EDI – customer enrollment on ComEd products via EDI, listing of all active meters on an account at the time of sign-up, real-time drop notifications, additional account information, and alteration of the time in which a customer’s bundled balance is checked for purposes of Rider SBO - Single Bill Option (“SBO”). There is no demonstrable need for such information. Meehan Reb., ComEd Ex. 26.0, 12:255-20:426. Additionally, CES’ recommendations would grant GAAs access to the same Electronic Data Interchanges (“EDI”) that are currently reserved for RESs. Meehan Reb., ComEd Ex. 26.0, 12:255-20:426. That this request is coming from the CES, one or more of whose members have employed agency to enroll customers on ComEd supply services to varying degrees in the past, begs larger policy questions regarding the appropriate roles of both RESs and agents in a competitive marketplace and consumer protection, just to name a few. Crumrine Reb., ComEd Ex. 23.0, 77:1673-79:1720.

As was the case with regard to the issues relating to agency, the issues raised by CES are not appropriate for discussion and decision in this rate case. If the Commission wishes to address these issues, it should initiate a workshop during which all interested parties can participate, providing the time needed to explore the business issues being raised and determine what, if any, process modifications would be appropriate throughout the state. Meehan Reb., ComEd Ex. 26.0, at 12:243-54; Meehan Sur., ComEd Ex. 43.0, at 5:105-6:128; Crumrine Reb., ComEd Ex. 23.0 at 80:1721-1732. Staff concurs with ComEd’s position. Schlaf Reb., Staff Ex. 20.0, 13:291-14:307.

D. Data Exchange for PowerPath

ComEd provides RESs with access to usage data necessary for scheduling and/or billing purposes, and provides interval data reports and meter summary reports in a form that allows the

variety of RESs operating in ComEd's service territory to analyze such data as they desire for each of their customers. CES' contention that RESs be allowed direct access to smart meters, which would grant RESs access to confidential usage data throughout ComEd's system, should once again be rejected, as it was in the Commission's Order in ICC Docket No. 99-0013 (Order, October 4, 2000 at 68-74. Meehan Reb., ComEd Ex. 26.0, 21:465-22:79; Meehan Sur., ComEd Ex. 43.0, 6:130-7:153. CES' recommendation that ComEd be required to customize reports at the whim of a RES for a given customer, and that ComEd total particular columns of reports that are provided to RESs as spreadsheets in excel format, are unnecessary and should be rejected. ComEd provides relevant information to all RESs in same format – one that permits a RES to easily sort the relevant data, in order to analyze the report to serve the RES' purpose with regard to a particular customer. Meehan Reb., ComEd Ex. 26.0, 22:480-23:502; Meehan Sur., ComEd Ex. 43.0, 7:154-8:175.

E. Improved Electronic Communication with Customers/RESs

ComEd established its business processes to provide clear, consistent information to customers and RESs. ComEd segments its CSRs between business and non-business customers. The business CSRs are fully trained to address the issues raised by commercial and industrial customers and by RESs, and ensures that a CSR familiar with the concerns of business customers is always available. Additionally, ComEd's Electric Supplier Services Department ("ESSD") includes account managers, each of whom are assigned to particular large commercial and industrial customers and/or RESs, and can assist customers and/or RESs in resolving conflicts or clearing up any confusion that they may be experiencing. Meehan Reb., ComEd Ex. 26.0, 24:518-25:535.

F. Utility Consolidated Billing with Purchase of Receivables

It does not make sense for ComEd to offer the consolidated billing service proposed by CES at this time. ComEd's current business processes and IT applications do not support utility consolidated billing, with or without a purchase of receivables option. Meehan Reb., ComEd Ex. 26.0, 25:538-26:574; Meehan Sur., ComEd Ex. 43.0, 8:177-9:190. Furthermore, ComEd currently is not in the third-party billing or "bad debt" collection or insurance businesses, nor is it currently interested in pursuing such businesses. Crumrine Reb., ComEd Ex. 23.0, 80:1734-81:1757; Meehan Reb., ComEd Ex. 26.0, 26:575-78; Meehan Sur., ComEd Ex. 43.0 at 9:191-203. CES failed to demonstrate that UCB/POR would improve competition, and failed to acknowledge that potential statewide ramifications would need to be considered and thoroughly addressed before any UCB/POR proposal could be implemented. Crumrine Reb., ComEd Ex. 23.0, 81:1758-82:1783; Crumrine Sur., ComEd Ex. 40.0, Corr. 84:1910-86:1945. Finally, UCB service would constitute a new service under Section 16-103(e) of the Act, 220 ILCS 5/16-103(e), which ComEd cannot be compelled to offer. Crumrine Reb., ComEd Ex. 26.0, 81:1741-44. Staff agrees that UCB/POR would represent a new service that ComEd cannot be compelled to offer and suggests that the propriety of any UCB/POR proposal should be discussed in a workshop setting. Schlaf Reb., Staff Ex. 20.0, 10:216-12:261.

V. STAFF REPORTS ON COMED'S PERFORMANCE

In December 2005, Staff presented its Reliability Report and Reliability Performance for 2004 (the "Reliability Assessment"), a report on ComEd's efforts to improve and maintain reliability. The report is prepared each year in accordance with 83 Ill. Adm. Code § 411.140. The Reliability Assessment identifies and discusses many of ComEd's efforts to improve system performance and reliability, the costs of which are included in rate base for those efforts that

occurred during the 2004 test year. The Reliability Assessment, offered and introduced through Staff testimony, demonstrates that ComEd is clearly doing more and spending more to meet customers' needs, and that no critical inquiry into ComEd's activities suggests that ComEd should cut back its activities or its service to customers. To the contrary, since the 2004 test year, at Staff's recommendation ComEd has made certain modifications to its business processes that will increase ComEd's costs during the time frame in which the proposed rates will be in effect.

In addition to its Reliability Assessment, Staff also performed a November 14-16, 2005 electric meter shop inspection. Staff set forth its conclusions from that inspection in a December 6, 2005 letter to ComEd, as discussed in the testimony of Staff witness Rockrohr (Staff Ex. 11.0) (the "Meter Shop Inspection Report").

A. Tree Trimming

Staff witness Spencer prepared a September 27, 2005 report on vegetation management, which was attached as Exhibit A to the Reliability Assessment. This portion of the Reliability Assessment noted, among other things, significant improvement in ComEd's tree trimming program, while also identifying areas for improvement and certain areas requiring additional attention. Mr. Spencer recommended that ComEd (1) investigate certain problem areas regarding compliance with National Electric Safety Code Rule 218 ("Rule 218") and consistency in tree trimming, (2) resolve certain identified tree clearance problems as soon as possible; and (3) assure that it meets the requirements of Rule 218 throughout its service area. Staff Ex. 9.1, at 10. The report also recommended that Staff perform additional random tree condition inspections in 2006. *Id.* ComEd has taken several steps to address these recommendations already, and has planned several more. For instance, ComEd has already addressed or developed

a plan to address the vegetation issues at each of the 140 individual locations that Mr. Spencer identified as needing attention. Costello Reb., ComEd Ex. 13.0 Corr. 38:861-65. More generally, ComEd has been following a four-year tree-trimming cycle, with mid-cycle trims, and has undertaken various efforts to continue bettering its vegetation management performance. *Id.*

B. Reliability Performance

Staff's Reliability Assessment recognizes, among other things, significant improvements and the strong overall trend in ComEd's reliability and service. Examples cited include substantial improvements in customer surveys, fewer complaints, significant numbers of customers experiencing no interruptions, and new corrective maintenance efforts. Staff Ex. 10.1, *see* Stutsman, Tr. 1763:2. Although the Reliability Assessment suggests further improvements and notes certain deficiencies, Staff has recognized the improvements that ComEd has made so far in several areas. The Reliability Assessment recommends that ComEd (a) continue focusing on improving customer service, (b) continue improving its vegetation management program and address Staff's concerns, and (c) inspect and modify where needed insulating oil levels of substation equipment. Staff Ex. 10.1.

ComEd agrees with these recommendations, and has already addressed or begun to address each of Staff's recommendations. ComEd has been working to improve customer service in many ways. Among other things, ComEd has promoted a "customer-centric" culture, training its employees on guidelines for interacting with customers in positive ways and focusing on the importance of customer satisfaction. ComEd has also been continuing its efforts to better respond to storms, and has been working to improve its worst-performing circuits. ComEd plans to continue focusing on customer service in the future, as customer satisfaction will continue to be one of ComEd's strategic focus areas.

C. Electric Metering

Staff's Meter Shop Inspection Report concluded that ComEd's metering practices conform with the metering requirements of 83 Ill. Adm. Code Part 410, but that ComEd had not demonstrated compliance in four areas – namely: 1) certifying that all meter installations meet Section 4.7 of ANSI C12.1-1995 standards; 2) meeting post-installation inspection requirements; 3) when performing meter tests more than 30 days after a customer request, showing that the customer agreed to the delay; and 4) calculating properly billing adjustments for meters found to be inaccurate. Rockrohr Dir., Staff Ex. 11.0, Sched. 11.1. Staff recommended that ComEd 1) develop more accurate descriptions of the reasons for each meter test; 2) identify whether meter tests are for sample testing, periodic testing, or testing at customer request; 3) adopt a method to demonstrate more readily that it is meeting periodic testing requirements; 4) ensure that employees involved in billing adjustments understand and can respond to meter creep; and 5) refine its self-audit process to verify consistency of billing adjustments. Rockrohr Dir., Staff Ex. 11.0, Sched. 11.1.

ComEd agrees with – and has acted on – Staff's observations on compliance, except regarding the application of certain installation standards to certain older meters (for which ComEd is planning to file with the Commission a petition seeking a clarification or exemption). In addition, ComEd is already taking steps to implement Staff's recommendations. At hearing, Staff witness Rockrohr agreed that the steps to which ComEd agreed are "reasonable and appropriate in complying with Part 410," (Rockrohr, Tr. at 1642:4-8), and that these activities "would resolve the issues that Staff found," Rockrohr, Tr. at 1642:11-13. Mr. Rockrohr also acknowledged that these were not activities that ComEd had in place at the time of the Meter Shop Inspection Report (Rockrohr, Tr. at 1642:14-17), and that, to the extent the recommendations require work not previously performed, ComEd will require additional

resources (Rockrohr, Tr. 1643:9-17), for which there may be additional costs. Rockrohr, Tr. at 1645:13 – 1646:1.

VI. Response to Commissioner Questions Relating to Demand Response

On March 16, 2006 Commissioners Lieberman and Ford issued a set of questions relating to the potential for additional demand response initiatives. Some of the issues raised by this set of questions have been fully discussed in previous sections of this Brief. These include the use of the highest 30-minute demand for electric power and energy established during the monthly billing period (*i.e.* a 24-hour demand) for certain demand-based tariff charges (*see* discussion *supra* at Section III.H.22), meter costs applicable to residential RTP (*see* discussion *supra* at Section III.H.27), and the residential RTP program proposed by CUB (*see* discussion *supra* at Section III.H.27). Those discussions are not repeated here.

There are, however, several additional points worth mentioning from the responses that were filed to the Commissioners' questions. First, demand response has not been ignored in Illinois or by ComEd. In fact, Illinois has been a national leader in mandating forms of RTP for all customers. *See* Crumrine Alongi Sup., ComEd Ex. 46.0, at 16:329-33. Second, the Commission's approval of an hourly energy pricing default service for the largest customers in the procurement rider proceeding was consistent with the recommendations of the Department of Energy ("DOE") issued in response to the 2005 amendments to the Energy Policy Act of 2005 ("EPAAct"). *See id.*, at 9:180-93; U.S. Department of Energy, *Benefits of Demand Response in Electricity Markets and Recommendations for Achieving Them* (Feb. 2006) ("*DOE Report*"). Third, ComEd has, in this proceeding, offered three tariffs that incorporate demand response (Riders AC7, VLR7 and CLR7). These tariffs are continuations of programs with which ComEd has had much experience, and the existing data demonstrates that these programs provide

benefits to both the system and customers. As such, the tariffs are just and reasonable and should be approved. *Crumrine Alongi Sup.*, ComEd Ex. 46.0, at 4:72-84. And fourth, all of the commenting parties agree that although demand response is important to a well-functioning market, further investigation is needed to determine the benefits and costs of implementing additional programs.

ComEd further notes that despite general agreement that demand response could provide net benefits to customers and to the system, no party was able to quantify the benefits associated with any specific new demand response program, and all agreed that the methodologies that would be used to evaluate such benefits were not sufficiently defined. CUB, which was joined by the City and the AG, also succinctly summarized another area of agreement among the commenting parties. Referencing Dr. Schlaf's testimony on residential RTP programs, CUB/City witness Mr. Thomas noted, "I share his desire to ensure that the benefits of residential RTP are carefully monitored and recorded." *Thomas Suppl. Dir.*, CUB/City Ex. 3.0, at 5:89-91. How such benefits are defined, how they should be monitored, and how the resulting data is to be evaluated, are all areas that require additional analysis and discussion among interested entities.

The conclusion that further investigation is needed before additional full-scale programs are implemented is further confirmed by the *DOE Report*. Indeed, the DOE found:

- "Based on the findings of this study, DOE has determined that it is not appropriate to develop recommendations on achieving specific levels of demand response benefits by January 1, 2007. The eleven months between submission of this report and January 2007 do not allow time for meaningful recommendations to be successfully implemented. Instead, DOE offers a set of recommendations for consideration by state, regional and federal agencies, electric utilities and consumers to enhance demand response in a manner consistent with state and regional conditions." *DOE Report*, at 51.
- The results of the studies that DOE reviewed "point out important inconsistencies in how demand response is currently measured, *id.*, at vi, show that "[t]o date

there is little consistency in demand response quantification,” *id.*, and led to the conclusion that “without accepted analytical methods, DOE finds that it is not possible to quantify the national benefits of demand response,” *id.*, at vii.

- In evaluating demand response programs, “regional differences in market design, operation, and response balance are important and must be taken into account.” *Id.*, at vii.

Given the complexity of these issues and the need to explore further the potential for demand response on both a statewide and regional basis, ComEd has recommended that these and other issues be explored in the rulemaking proceedings that were ordered in the procurement rider docket and that will occur pursuant to the amendments made by the EPAct to the Public Utility Regulatory Policies Act (PURPA). *See* 16 U.S.C. §§ 2621 & 2625 (2006).

VII. OTHER ISSUES

Not applicable.

VIII. TABLE OF PROPOSED ADJUSTMENTS

ComEd presented its original (corrected) proposed revenue requirement in Mr. Hill’s direct testimony and the attachments thereto. Hill Dir., ComEd Ex. 5.0 Corr.; ComEd Ex. 5.1; ComEd Ex. 5.2

Over the course of the case, ComEd agreed to and made a number of adjustments that reduced its revenue requirement, as discussed in Section III.A, *supra*.

ComEd’s final revised proposed revenue requirement, reflecting all of those adjustments, may be found in Schedule 1 Revised to Mr. Hill’s surrebuttal testimony. Hill Sur., ComEd Ex. 36.0 at Sch. 1 Revised. A copy of this Schedule is attached as Appendix A.

IX. ACRONYMS AND TERMS

A list defines acronyms and terms that ComEd has used or expects may be used in the Initial and Reply Post-Hearing Briefs in this matter is attached hereto as Appendix B.

Dated: April 25, 2006

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Appendix A

Table of Proposed Adjustments and Final Revenue Requirement

Appendix B

Table of Acronyms and Terms

¢/kWh Cents Per Kilowatt-Hour
A & G Administrative and General
AAF Accuracy Assurance Factor
ABB Asea Brown Boveri
ABO Accumulated Benefit Obligation
AC Residential Air Conditioner Load Cycling Program
ACSI American Customer Satisfaction Index Proxy
ADIT Accumulated Deferred Income Taxes
AFUDC Adjustment for Funds Used During Construction
AG Attorney General of the State of Illinois
AICPA American Institute of Certified Public Accountants
AIMR Association for Investment Management and Research
AIP Annual Incentive Plan
ALM Active Load Management
APS Arizona Public Service Company
APT Arbitrage Pricing Theory
ARES Alternative Retail Electric Supplier
ATO Automatic Throw Over
BAI Brubaker & Associates, Inc.
BES Bundled Electric Service
BES-H Basic Electric Service-Hourly
BES-L Basic Electric Service-Lighting

BES-NRA Basic Electric Service-Nonresidential (Annual)
BES-NRB Basic Electric Service-Nonresidential (Blended)
BES-R Basic Electric Service-Residential
BES-RR Basic Electric Service-Railroad
BG&E Baltimore Gas & Electric Company
BOMA Building Owners and Managers Association, an intervening party
BPPB Budget Payment Plan Balances
BUP New Jersey Board of Public Utilities
BWMQ Brown, Williams, Moorhead & Quinn
C&I Commercial and Industrial
CADOPS ComEd's Operations Control Center
CAIDI Customer Average Interruption Duration Index
CAMS Control Area Management System
CAPM Capital Asset Pricing Model
CCC Citizens Utilities Board, Cook County State's Attorney's Office & City of Chicago
CCSAO Cook County State's Attorney's Office
CEC Community Energy Cooperative
CES Coalition of Energy Suppliers, an intervening party
CILCO Central Illinois Light Company
CIMS Customer Information Management System
City City of Chicago
Capacity-Based Load Response and System Reliability Program
CML Capital Market Line
CNE Constellation New Energy, an intervening party

CO Capacity Obligation
ComEd Commonwealth Edison Company
ComEd 2001 Rate Case <i>Commonwealth Edison Company: Proposed General Increase in Delivery Service Tariffs Rates, Illinois Commerce Commission, Docket No. 01-0423</i>
Commission or ICC Illinois Commerce Commission
ConEd Consolidated Edison Company
Cons. Consolidated (with respect to two or more dockets pending before the Illinois Commerce Commission)
CPA Certified Public Accountant
CPCN Certificate of Public Convenience and Necessity
CPD Chicago Park District
CPI Consumer Price Index
CPP Competitive Procurement Process
CPWG Communications Protocol Working Group
CS Contract Service
CSL City of Chicago Street Lighting
CSR Customer Service Representative
CTA Chicago Transit Authority
CTC Customer Transition Charge
CUB Citizens Utility Board
CWIP Construction Work in Progress
DASR Direct Access Service Request
DCF Discounted Cash Flow

DCS Distributed Control System
DE Distribution System Extensions
DFC Distribution Facilities Charge
DGAA Designation of General Account Agency
Direct Direct Energy Services
DLF Distribution Loss Factors
DLR Direct Load Control
DOE Department of Energy
DST Delivery Services Tariffs
E2I Electricity Innovation Institute
ECOSS Embedded Cost of Service Study
ECR Environmental Cost Recovery Adjustment
EDI Electronic Data Interchange
EDSS Energy Delivery Shared Services
EED Exelon Energy Delivery LLC
EEl Edison Electric Institute
EGS Electric Generation Supplier
EIA Energy Information Administration
ElAS Exelon Internal Audit Services
EMCS Energy Management Control System
EPAct Energy Policy Act of 2005
EPEC Equal Percentage of Embedded Cost
EPIS Electric Plant in Service
EPRI Electric Power Research Institute

ERISA Employee Retirement Income Security Act
ERT Estimated Restoration Times
ESC Energy Service Companies
ESIF Energy Savings Income Fund
ESPP Energy Smart Pricing Plan
ESSD Electric Supplier Services Department
Ex. Exhibit
Exelon BSC Exelon Business Services Company
FAQ Frequently Asked Questions
FAS Financial Accounting Standard
FCA Franchise Cost Additions
FERC Federal Energy Regulatory Commission
FFO Funds From Operation
FPC Federal Power Commission
GAA General Account Agency
GAAP Generally Accepted Accounting Principles
GCB Governmental Consolidated Billing
GDP Gross Domestic Product
GIS Geographical Information System
GRCF Gross Revenue Conversion Factor
GSA General Services Agreement
H&M Harris and Marston
HASC Hourly Auction Supply Charge
HVDS High Voltage Delivery Service

IAPA The Illinois Administrative Procedure Act, 5 ILCS 100/1 et seq.
IAWA Illinois Association of Wastewater Agencies, an intervening party
IDC Integrated Distribution Company
IDR Interval Demand Recording
IEDT Illinois Electricity Distribution Tax
IEEE Institute of Electrical and Electronics Engineers
IEPA Illinois Environmental Protection Agency
IFC Instrument Funding Charge
IIEC Illinois Industrial Energy Consumers, an intervening party
IPL Indianapolis Power & Light Company
IPO Initial Public Offering
IRV Interactive Voice Response
ISO Independent System Operators
ISS Interim Supply Service
IT Information Technology
ITC Investment Tax Credits
JBC John Buck Company
KPI Key Performance Indicators
kW Kilowatt
kWh Kilowatt-hour
LDC local distribution company
LGC Local Government Compliance Adjustment
LIHEAP Low Income Home Energy Assistance Program
LMP Locational Marginal Prices

LTIP Long Term Incentive Plan
MDS Mobile Data System
METRA Metropolitan Rail (see NIRCRC)
MGP Manufactured Gas Plant
MI Market Index
MIS Management Information Systems
MKD Maximum Kilowatts Delivered
ML Meter-Related Facilities Lease
MMF Modified Massachusetts Formula
Moody's Moody's Investors Service
MoPSC Missouri Public Service Commission
MOU Memorandum of Understanding
MSP Metering Service Provider
MSPS Metering Service Provider Service
MTP Mandatory Transitory Period
MVM Market Value Methodology
MWG Midwest Generation, an intervening party.
MWh Megawatt-hour
NARUC National Association of Regulatory Commissioners
NCP Non-Coincident Peak
NERA National Economic Research Associates, Inc.
NESC National Electrical Safety Code
NGPL Natural Gas Pipeline Company of America
NIGAS Northern Illinois Gas Company d/b/a Nicor Gas Company

NIPSCO Northern Indiana Public Service Company
NIRCRC Northeast Illinois Regional Commuter Railroad Corporation d/b/a METRA
NOPR Notice of Proposed Rulemaking
NRC Nuclear Regulatory Commission
NS Non-standard Services and Facilities
NYSEG New York State Electric and Gas
O&M Operating and Maintenance
OATT Open Access Transmission Tariff
OMS Outage Management System
OPEB Postretirement Benefits Other Than Pensions
P&A Peak and Average
PAPUC Pennsylvania Public Utility Commission
PECO PECO Energy Company
PES Peoples Energy Services Corporation, an intervening party
PG&E Pacific Gas & Electric Company
PJM PJM Interconnection, L.L.C.
PM Primary Metering Adjustment
POG Parallel Operation of Retail Customer Generating Facilities
POR Purchase of Receivables
PPO Power Purchase Option
PRP Potentially Responsible Party
PSEG Public Service Enterprise Group
P-T-D-C Production, Transmission, Distribution, and Customer-related
PUHCA Public Utility Holding Company Act of 1935

PURPA Public Utilities Regulatory Policies Act of 1978
PWC PricewaterhouseCooper
QF Qualified Facilities
QIP Quarterly Incentive Program
QSW Qualified Solid Waste Energy Facility Purchases
RCA Retail Customer Assessments
RCDS Retail Customer Delivery Service
RDS Retail Delivery Service
RES Retail Electric Supplier
RESALE Allowance for Resale or Redistribution of Electricity
Restructuring Law Illinois Public Utilities Act and the Electric Service Customer Choice and Rate Relief Law of 1997
RHEP Residential Hourly Energy Pricing, ComEd's experimental tariff
ROE Return on Equity
ROR Rate of Return
RP Risk Premium
RTC Round-the-clock
RTO Regional Transmission Organization
RTP Real Time Pricing
RTU Remote Terminal Unit
RWG Rates Working Group
S&P Standard & Poor's
SAC Supply Administration Charge
SAIFI System Average Interruption Frequency Index
SBO Single Bill Option

SCADA Supervisory Control and Data Acquisition
SDG&E San Diego Gas & Electric Company
SEC Securities and Exchange Commission
SFAS Statement of Financial Accounting Standards
SLA Service Level Arrangement
T&D Transmission and Distribution
TAX Municipal and State Tax Additions
TDC Transmission Distribution Center
TOI Taxes Other than Income
TOU Time-of-Use
TS Transmission Services
TSD Task Scope Documents
TSS Transmission Substation
TXPUC Texas Public Utilities Commission
UAF Uncollectibles Adjustment Factor
UCB Utility Consolidated Billing
USEPA U.S. Environmental Protection Agency
USESC U.S. Energy Savings Corporation
USOA Uniform System of Accounts
UT Austin University of Texas at Austin
Value Line Value Line Investors Service
VLR Voluntary Load Response and System Reliability Program
W&S Wages and Salaries
WMS Work Management System

WP Workpapers
Zacks Zacks Investment Research
ZSS Zero Standard Service

CERTIFICATE OF SERVICE

I, Cynthia A. Fonner do hereby certify that a copy of the foregoing Commonwealth Edison Company Initial Brief served upon all parties on the attached Service List by the method so indicated this 25th day of April, 2006.

A handwritten signature in black ink that reads "Cynthia A. Fonner". The signature is written in a cursive style with a long horizontal flourish at the end.

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