STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY	**:**	
	:	**Dkt. 05-0597**
Proposed general increase in rates for delivery service.	**:**	

REPLY BRIEF OF THE ILLINOIS INDUSTRIAL ENERGY CONSUMERS

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IIEC REPLY BRIEF

I. INTRODUCTION

The Illinois Industrial Energy Consumers ("IIEC") present this Reply Brief in response to certain issues raised and arguments made by Commonwealth Edison Company ("ComEd" or "Company"), the Illinois Commerce Commission Staff ("Staff"), Citizens Utility Board/Cook County States Attorney/City of Chicago ("CUB/CCSAO/City") in their Initial Briefs in this proceeding. IIEC's failure to respond to a brief or argument of any party should not be considered as acceptance of, or agreement with that Brief or argument unless specifically stated otherwise herein. IIEC will refer to the Initial Briefs of the parties as "Brief" throughout its Reply Brief. IIEC's failure to raise any issue in its Reply Brief that was raised in its Initial Brief should not be considered as abandonment of that issue, unless specifically stated otherwise herein.

III. ARGUMENT ON CONTESTED ISSUES

A. Total Revenue Requirement and Base Rate Revenue Increase

ComEd argues that setting the correct revenue requirement is critical for ComEd and its customers. IIEC agrees that setting the correct revenue requirement is critical from a customer point of view. ComEd claims it has a current revenue deficiency of $317,295,000. (ComEd Br. at 30). This means ComEd is asking for an increase in its current delivery service rates of $317,295,000. Staff and Intervenors argue ComEd has no revenue deficiency on the basis of evidence presented in this case. Indeed, the Staff of the Illinois Commerce Commission argues ComEd's current delivery service rates should actually be decreased by approximately $30 million. (Clark Tr. 220). The Commission has previously approved substantial rate reductions and refunds for ComEd without impairing its ability to provide adequate, safe and reliable service. Specifically, the Commission has approved rate reductions and refunds of $1.2 billion for ComEd in the context of a Commission approved settlement and ComEd was able to provide adequate, safe and reliable service thereafter. (Clark Tr. 220-221).

The Commission should not be concerned if the evidence in this proceeding justifies a reduction in ComEd's requested revenue requirement, such that there is no demonstrable revenue deficiency. That is, if ComEd could continue to supply safe, reliable and adequate service in the face of a $1.2 billion rate decrease and refund, it can certainly do so in the face of a $30 million decrease in this case.

ComEd also argues it proved its revenue requirement of $1,862,185,000. (ComEd Br. at 30-31). ComEd points to the testimony and exhibits offered by its witnesses in support of its requested revenue requirement. However, Staff and Intervenors have presented over 50 direct and rebuttal witnesses, many of whom have offered extensive testimony and evidence demonstrating that ComEd has not, in fact, proven a revenue requirement of $1,862,185,000. It is, of course, for the Commission to determine whether or not ComEd has proven its revenue requirement, in light of the evidence presented by all the parties, not just ComEd.

ComEd states it " . . . 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 Br. at 35). With all due respect to ComEd, it is the Commission that must review ComEd's testimony and that of Staff and Intervenors and arrive at the appropriate revenue requirement for ComEd. IIEC has presented evidence relating to the appropriate level of A&G expense, G&I plant, and cost of capital the Commission may rely on in determining the appropriate revenue requirement for ComEd in this case. The Commission should, and must, consider the evidence presented by IIEC, Staff and other Intervenors as well in arriving at its final conclusion.

ComEd also argues it has proven its revenue deficiency (the needed base rate increase) (ComEd Br. at 35). Specifically, ComEd says there does not appear to be any contested issue as to the calculation of the revenue deficiency. (Id.). IIEC agrees there is no dispute as to the arithmetical calculation of the deficiency identified by ComEd. The dispute is whether or not there is, in fact, a revenue deficiency at all, and if there is, whether it is something substantially less than the revenue deficiency calculated by ComEd.

ComEd also argues that Staff's and Intervenors' proposed revenue requirements are unsupported by the evidence. (ComEd Br. at 36). IIEC respectfully disagrees. Its proposed adjustments and revenue requirement recommendations are supported by evidence. IIEC will demonstrate below the valid and lawful basis for each of its revenue requirement recommendations.

B. Rate Base

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

In support of its requested level of G&I plant, ComEd argues this case is different from past ComEd delivery service cases. ComEd reasons that in those cases, the issue before the Commission was how to separate G&I plant associated with the delivery service business from G&I plant associated with ComEd's transmission and generation/production businesses. (ComEd Br. at 43). ComEd says there is no need to so separate G&I plant in this case because ComEd is no longer in the generation or production business. (Id.). ComEd implies the issue now before the Commission is whether the requested level of G&I plant is reasonable. (*See* ComEd Br. at 43-44). IIEC says it is not reasonable.

a. IIEC's Position On and Approach to Determining the Appropriate Level of G&I is Supported by Substantial Evidence

ComEd argues that IIEC's recommendation on the appropriate level of G&I plant is not supported by substantial evidence in the record. (ComEd Br. at 50). ComEd argues that IIEC's position is based on the fiction that ComEd is still in the generation business. (ComEd Br. at 44).

IIEC witness Chalfant also recognized the present delivery service case was different from past delivery service cases. Mr. Chalfant testified that in those cases, the issue before the Commission on G&I plant related to the separation of G&I plant among the various business functions of ComEd (distribution, transmission and generation). (Chalfant Tr. 1696-1697). Therefore, he noted the issue in this case was the reasonable level of G&I plant for ComEd now that it is a delivery service company only. (Chalfant Tr.1697-1698). He testified the best way to judge the reasonableness of G&I plant in this case was to compare the level of G&I plant the Commission found reasonable in ComEd's last delivery service case to the level ComEd had requested in this case. (Chalfant Tr. 1698). Using methods approved by the Commission in Illinois Power Docket 01-0432, in a Commission Order sustained on appeal, Mr. Chalfant looked at the relationship between G&I plant and other distribution costs. (Chalfant Tr. 1698-1699). He concluded there had been a substantial increase in G&I plant compared to the last case. (Chalfant IIEC Ex. 2.0 at 6:110-117). He specifically noted that while ComEd has presented evidence demonstrating what was in each of the relevant accounts for G&I plant, it had not explained the large increase in the level of G&I plant from the level approved in the last case. (Chalfant IIEC Ex. 2.0 at 7:118-122). In arriving at his conclusion, Mr. Chalfant relied on ComEd's responses to Staff data requests on this issue. (Chalfant Tr. 1672-1673). He also relied on his detailed review of the testimony of ComEd witnesses Hill and Costello and a more limited review of the testimony of ComEd witness Mr. DeCampli. (Chalfant Tr. 1662-1663).

Therefore, IIEC's proposal is supported by substantial evidence in the record and based on fact, not fiction.

b. IIEC's Proposal is Lawful

ComEd argues that IIEC's position on, and its approach to determining the appropriate level of G&I plant is not lawful. (ComEd Br. at 49). As noted above, IIEC's position on and its approach to determining the reasonable level of G&I plant for ComEd in this proceeding are fully consistent with prior Commission determinations for other Illinois delivery service companies. Those determinations have been sustained on appeal. Therefore, IIEC's position on and approach to determining the reasonable level of G&I plant for ComEd in this proceeding are, indeed, lawful.

In the Illinois Power case, the Commission concluded it would accept the IIEC and Staff arguments that the relative relationship between G&I plant and distribution plant rate base, established in IP's prior delivery service case, should be maintained in the then current IP case. (Illinois Power Company, Dkt. 01-0432, Order, March 28, 2002 at 17).

In addition, the Commission rejected several of the arguments ComEd now makes in this case against adoption of IIEC's position.

In the Illinois Power case, the utility argued no party had identified any G&I plant that was imprudent or unreasonable. (Id. at 11). ComEd makes similar arguments in this proceeding. (*See* ComEd Br. at 10). In adopting the IIEC and Staff position in the Illinois Power case, the Commission rejected this argument.

The Commission also rejected arguments made by IP that the only basis for limiting the level of G&I plant recommended by Staff and IIEC was that IP should allocate G&I plant to its generating business and that IP no longer owned any generation. ((Illinois Power Company, Dkt. 01-0432, Order, March 28, 2002 at 11). ComEd makes a similar argument here. (*See* ComEd Br. at 44). In adopting the IIEC and Staff position in the IP case, the Commission rejected this argument as well.

The Commission's decision was affirmed on appeal by the Appellate Court for the Fifth Appellate District in a decision rendered on May 22, 2003 where the Court said in pertinent part:

> The general principle that guided the allocation is that changes in G&I plant and A&G account levels should be proportional to changes in the associated direct accounts over time from the 1999 DST order to the instant case. For example, the increase in G&I plant is commensurate with the increase in other distribution-plant accounts. Similarly, any change in A&G expenses is consistent with changes in direct O&M expenses.
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> * * * *
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> The record discloses the Commission considered various allocation methodologies and reasonable determined that the methodology proposed by Staff and IIEC should be adopted.
> (Illinois Power Company v. Illinois Commerce Commission, et al., Petition for Review of an Order of the Illinois Commerce Commission, Appellate Court Dkt. No. 5-02-0406, May 22, 2003 at 13-14 (available on the Commission's e-docket RE: Illinois Power Dkt. No. 01-0432)).

The IIEC approach to determining the appropriate level of G&I plant has been followed by the Commission in past utility delivery service cases and the Commission's approach has been affirmed on appeal. Thus, IIEC's proposal is lawful.

C. Operating Expenses

3. Administrative and General Expense

a & b. Functionalization and Overall Amounts

ComEd argues its requested level of A&G expense is just and reasonable and should be approved. (ComEd Br. at 83). It argues A&G represents corporate support and overhead costs ("overhead"). (*See* ComEd Br. at. 83). It says that proposals to adjust ComEd's overhead costs, other than those proposals specifically determined by ComEd to be appropriate, should be rejected since they are unsupported by, and contrary to, the evidence in this case. (ComEd Br. at 84).

(I) ComEd's Rebuttal Testimony Does Not Refute IIEC's Position

ComEd argues it presented rebuttal testimony, which refuted IIEC's position on A&G and that, "tellingly," IIEC did not attempt to rebut same when it had the opportunity to do so. (ComEd Br. at 49). ComEd presented the rebuttal testimony of Mr. Hill in response to IIEC's position on A&G. IIEC (and the Staff) have criticized ComEd for its failure to offer a detailed explanation of the increase in overhead expense over levels authorized in ComEd's last delivery service rate case. (*See* Chalfant IIEC Ex. 2.0 at 2-6:35-109; and Lazare Staff Ex. 6.0 (Corrected) at 19-20:465-481). Mr. Hill, in attempting to explain the difference in this rebuttal, claimed that some overhead expenses present in 2004 were not present in 2000, but he had not attempted an exhaustive study.

(Hill ComEd Ex. 19.0 Rev. at 40-41 850-853). Mr. Hill also apparently compared 2004 FERC Form 1 A&G costs to ComEd's proposed (not Commission approved) A&G in the last case. (*See* Hill ComEd. Ex. 19.0 Sch. 12 Fn. 1 and Col F. Fn. 2 referring to the 2004 FERC Form 1 and Mr. Hill's workpapers from the last case.) However, if there were expenses that existed in 2004 that did not exist in 2000, it is probably equally true there were expenses that existed in 2000 that may not have existed in 2004. However, because Mr. Hill did not do an exhaustive study, neither ComEd nor the Commission can determine the exact reasons for the difference in the level of A&G authorized as just and reasonable by the Commission in the last case and the level requested by ComEd in this case.

Furthermore, ComEd's limited attempts to "explain" the differences goes to the difference between the level of A&G expense ComEd has requested in this case and the level it requested in the last case. Thus, the analysis does not explain the difference between the level of just and reasonable A&G expense determined in the last case and the level requested in this case.

ComEd also argues that Mr. Hill's rebuttal testimony shows ComEd's actual total 2004 AG expense was 26% lower than its actual 2000 A&G expense. (ComEd Br. at 91-92). Again, ComEd's analysis here and elsewhere in its brief appear to be based on comparisons between ComEd's requested A&G in this case and its requested A&G in the last case. The appropriate comparison is the A&G level authorized as just and reasonable in the last case and the level requested in this case. Furthermore, ComEd fails to explain why "actual" A&G levels in 2004 are 26% less than actual A&G levels in 2000, but ComEd seeks approval of A&G expense that is 55%

higher than the level the Commission determined just and reasonable in the last case.[1] (*See* Chalfant IIEC Ex. 2.0, Table 1).

Thus, there has been no need to rebut Mr. Hill because his rebuttal testimony does nothing to explain the substantial increase in ComEd's A&G over the level approved as just and reasonable by the Commission in ComEd's last case. ComEd has not offered a detailed explanation for the difference – indeed, ComEd has failed to offer a valid explanation of any kind for the difference.

(ii) IIEC's Position on an Approach to Determining the Appropriate Level of A&G is Supported by Substantial Evidence

ComEd argues IIEC's recommendation and the appropriate level of A&G is not supported by substantial evidence in the record. (ComEd Br. at 50). Mr. Chalfant used a methodology adopted by the Commission in determining the appropriate level of A&G expense for Illinois Power Company. (<u>Illinois Power Company</u>, Dkt. 01-0432, Order, March 28, 2003, at 48 accepting Staff and IIEC's arguments that the relationship between A&G expenses and distribution labor expense should be maintained.) In his testimony, Mr. Chalfant pointed out that A&G expenses are primarily related to corporate level activities of the utilities such as salaries of corporate officials, pensions and benefits, injuries and damages, office supplies and miscellaneous expenses sometimes referred to as "overhead." (Chalfant IIEC Ex. 2.0 at 4:66-70). ComEd has provided a similar description of these expenses in its brief. (ComEd Br. at 11). Mr. Chalfant determined the level of A&G

[1] In other delivery service cases, the Commission has been skeptical of utility arguments claiming a reduction in electric A&G expenses during the relevant time periods and the utility's failure to reconcile such a claim with the fact that it had requested to recover from distribution customers a significant increase in the level of A&G expenses. (*See* <u>Illinois Power Company</u>, Dkt. 01-0432, Order, March 28, 2002 at 45).

expense requested by ComEd in this case and noted it had increased by 55% over the levels found just and reasonable in ComEd's last case. (Chalfant IIEC Ex. 2.0 at 4). Mr. Chalfant testified that the appropriate standard for ratemaking purposes in this case was to compare the levels of A&G the Commission found just and reasonable in the last case with the level of A&G the company requested in this case. (See Chalfant Tr. 1690). Mr. Chalfant is supported in his position by the Commission itself, which has stated in reviewing the requested A&G expense levels of Illinois Power Company, another delivery service utility in Illinois, " . . . the Commission cannot find that IP has adequately explained the significant increase in electric distribution A&G expenses relative to the level approved in 1999." (Illinois Power Company, ICC Dkt. 01-0432, Order, March 28, 2002 at 48).

Mr. Chalfant testified that ComEd was requesting an additional $97 million over the level of A&G previously authorized by the Commission without explaining the significant increase. (Chalfant IIEC Ex. 2.0 at 5:78-83). He further noted the request amounted to one-fourth of ComEd's total requested increase. He noted that under ComEd's proposal, ComEd would add 63.2 cents to every dollar of O&M expense (excluding A&G) required for delivery service as compared to 35.8 cents in the last case. (Chalfant IIEC Ex. 2.0 at 5:85-91). He noted ComEd had not explained this difference in its direct case. Furthermore, as noted above, ComEd has not really explained this difference in its rebuttal case. Under the circumstances, he proposed that ComEd's A&G expense should be increased or decreased in proportion to the increase or decrease in O&M expense determined to be adequate for the provision of delivery service. This approach would maintain the relationship between A&G and O&M other than A&G adopted in the last case. (Chalfant IIEC Ex. 2.0 at 5-6:75-109).

Mr. Chalfant essentially testified ComEd's A&G expenses were unreasonable in the aggregate. (Chalfant Tr. 1693). He further testified that even though ComEd's overall O&M expense, including A&G had increased only about 5.6% (Chalfant Tr. 1695; ComEd Cross Ex. 13), it was inappropriate to determine the level of A&G expenses to be allowed for ratemaking purposes by relating it to a set of costs that include A&G expense as a component. He considered this to be circular reasoning. In addition, he noted his evidence demonstrated that while A&G expenses increased by about $97 million, since the 2000 test year for ComEd, O&M expense had, in fact, decreased by $60 million. He suggested this really demonstrated that to the extent A&G expenses were effective in lowering O&M costs, it required a $100 million increase in A&G costs to achieve the $60 million reduction in O&M costs. (Chalfant Tr. 1700-1701).

Mr. Chalfant also testified that in reaching his conclusions, he had reviewed the testimonies of ComEd witnesses Hill and Costello and conducted a limited review of the testimony of ComEd witness DeCampli while relying on ComEd data responses to Staff witness Lazare which provided him with sufficient information to make his analysis. (Chalfant Tr. 1662-1663 and 1672-1673).

In sum, IIEC's position is supported by substantial evidence. It has not been adequately refuted or rebutted by ComEd. It is consistent with approaches approved by the Commission for other delivery service utilities in Illinois. IIEC's position should be adopted.

(iii) IIEC's Proposal is Lawful

ComEd argues that IIEC's position on, and its approach to determining appropriate levels of A&G expense in this case, which is based in part on the levels of A&G approved in Docket 01-0423 are not lawful. (*See* ComEd Br. at 95). As noted in Section III.C.3.a&b.(ii) above, IIEC's position on and its approach to determining A&G plant, is fully consistent with prior Commission determinations for other Illinois delivery service companies. Those determinations have been sustained on appeal. (*See* Illinois Power Company, Dkt. 01-0432, Order, March 28, 2002, at 48; Illinois Power Company v. Illinois Commerce Commission et al., Petition for Review of an Order of the Illinois Commerce Commission, App. Ct. Dkt. No. 5-02-4460, May 22, 2003 (available on the Commission's e-docket Re: Illinois Power Company, Dkt. No. 01-0432). (*See also* III.B.2& 3.b).

Therefore, IIEC's proposal for determination of a reasonable level of A&G expense, contra to ComEd's argument, is not unlawful in and of itself.

E. Rate of Return

In its Brief, ComEd urges the Commission to focus on the utility's "actual costs" and its "full recovery" of those costs. (ComEd Br. at 151-152, 155). However,"actual costs" and unqualified "full recovery" are not compatible with either the Commission's regulatory responsibilities or governing law. Regulated utility rates do not automatically recover every utility cost -- whatever its magnitude, purpose or derivation. The Commission can approve rates that achieve "full recovery" of "actual costs" only when those costs are, in addition, reasonable and prudently incurred. *See* 220 ILCS 5/9-211.

In particular, the reasonable costs of capital that ComEd may recover through delivery services rates are a reasonable return, as defined in *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) and *Bluefield Waterworks v. Public Service Comm'n*, 262 U.S. 679

(1923),[2] only on "such investment which is both prudently incurred and used and useful in providing service to public utility customers."[3] 220 ILCS 5/9-211. The metric for compliance with those standards is not a dollar amount, like ComEd's alleged capital costs of $552 million (ComEd Br. at 151), but an authorized return level that provides financial integrity and is commensurate with returns on other investments of similar risk.

ComEd acknowledges that its management decisions on capital structure and the costs those decisions produce are not sacrosanct: "It is the Commission's task to review those decisions for prudence and reasonableness . . . ." (ComEd Br. at 153 (citations omitted)).[4] ComEd cites the appellate opinion in *Hartigan v. ICC*, 214 Ill. App. 3d 222 (1991) as support for its position that ComEd need not use the lowest cost financing, but concedes that these capital costs must (as IIEC argues) be reasonable and prudent. ComEd Br. at 153. ComEd also presumptuously admonishes the Commission not to "second guess" ComEd or the capital markets in making that assessment. (ComEd Br. at 153). However, these alleged limitations on the Commission's role do not preclude the searching inquiry that the PUA mandates.

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[2]These decisions identify the general standards to be considered in establishing the cost of common equity for a public utility. Those general standards are that the authorized return should: (1) be sufficient to maintain financial integrity; (2) attract capital under reasonable terms; and (3) be commensurate with returns investors could earn by investing in other enterprises of comparable risk. (IIEC Ex. 3.0 at 20:454-458).

[3]The authorized overall rate of return determined in this case will be applied to ComEd's rate base – the assets dedicated to its provision of regulated delivery services.

[4]ComEd's management decisions must also be lawful. Delivery services rate recovery of costs associated with assets that are not used and useful in the provision of delivery services is not lawful.

The Act's Section 9-201 (220 ILCS 5/9-201) directs the Commission to approve the "rates or other charges, . . . proposed, in whole or part, or others in lieu thereof, which it shall find to be just and reasonable" (*emphasis added*). In *Hartigan v. ICC*, 148 Ill. 2d 348 (1991), the Illinois Supreme Court's review of the decision ComEd cites, the Court said the following about the depth of the Commission's inquiry into costs proposed for rate recovery: "The determination of whether a cost is includable in or disallowable from the utility's rate base is the essence of the Commission's ratemaking duties." (Id. at 368).

In the testimony of Mr. Michael Gorman and in its Initial Brief, IIEC has shown that the capital structure and return on equity elements of ComEd's proposed overall rate of return are unreasonable and unjustified. Staff and CUB/CCSAO/City[5] also oppose ComEd's cost of capital proposal. Though their specific recommendations are different, IIEC, Staff and CUB/CCSAO/City all agree that ComEd's return on equity (ROE) and equity ratio proposals are excessive. Staff and CUB/CCSAO/City also oppose ComEd's proposed cost of debt.

An objective assessment of the record evidence under the governing criteria confirms that ComEd's rate of return proposals are not reasonable and must be rejected.

1. Capital Structure

ComEd

ComEd makes few new arguments in its Initial Brief's treatment of capital structure issues. ComEd continues its apparent strategy of confusing, rather than clarifying, the process of

[5]The AG also adopts the overall return recommendation of CUB/CCSAO/City witness Mr. Edward Bodmer. (AG Br. at 2).

determining a reasonable capital structure that reflects the ComEd debt and equity costs actually supporting its provision of delivery services.

While ComEd agrees that it should not "earn a return on anything more than its rate base" (ComEd Br. at 171), ComEd simultaneously seeks to boost its profits on that rate base by inflating both the cost and the amount of equity in its capital structure. Inflating the size of the higher-priced equity component of its capital structure leads to a higher overall cost of capital. That, in turn, boosts ComEd's calculated revenue requirement and the resulting rates.[6]

This section of IIEC's Reply Brief responds mainly to ComEd's arguments defending the inflated equity ratio it proposed -- a ratio every other expert in the case found unreasonably high.

a. ComEd's Actions and Words Contradict Its Arguments Purporting to Support the Use of ComEd's "Actual" Capital Structure

ComEd argues that any capital structure other than its actual capital structure constitutes "an express denial of cost recovery." (ComEd Br. at 155). That position is so untenable that, inevitably, ComEd contradicts itself.

First, and most important, ComEd's actions contradict its argument. "In this case, ComEd proposes to use its actual capital structure, after a *pro forma* adjustment . . . ." (*See* ComEd Br. at 155). ComEd, Staff, CUB/CCSAO/City and IIEC each concluded that there is common equity in ComEd's actual capital structure that is not appropriately used for ratemaking purposes; each made an adjustment to the capital structure. ComEd refers to its own adjustment as "a pro forma

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[6]Overall Cost of Capital = (% Equity * ROE) + (% Debt * Cost of Debt)
Revenue Requirement = Overall Cost of Capital * Rate Base

adjustment" and its modified capital structure proposal as “actual adjusted” or “actual”, while criticizing other parties’ substantively identical recommended capital structure adjustments. (*See* ComEd Br. at 155-156). This is transparent sophistry that does not change the common basis for all the intervenors’ recommendations -- that ComEd’s “actual” capital structure is inappropriate for ratemaking purposes. The arguments respecting the adjustments are discussed below.

Second, the utility’s own words contradict its argument. In the same section of its brief, ComEd refers to circumstances where “a <u>hypothetical</u> capital structure is <u>properly</u> <u>used</u> <u>in</u> <u>lieu</u> <u>of</u> the <u>actual</u> capital structure” -- acknowledging that capital structures other than that shown by ComEd’s books are neither unusual nor *per se* improper. (ComEd Br. at 155). Similarly, ComEd concedes that "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." (ComEd Br. at 161). That is precisely what IIEC, Staff and CUB/CCSAO/City have recommended.

b. ComEd’s Capital Structure Must Reflect the Capital Actually Supporting Its Provision of Regulated Delivery Services

At page 156 of its Brief, ComEd presents a table of all the capital structure recommendations made at any point in this case. However, only two of those shown are supported by experts in the case. After reviewing the evidence of record, including the analysis of Staff witness Ms. Sheena Kight, Mr. Gorman concluded that a 50-50 structure (as well as ComEd’s) fails to reflect the capital actually supporting ComEd’s regulated services, and is not a reasonable capital structure to employ in setting rates. Staff’s capital structure, which all intervenors, including IIEC, support, is reasonable.[7]

Despite its purported devotion to actual costs, ComEd avoids any discussion of whether its inflated common equity component represents costs that <u>actually</u> support its provision of delivery services. ComEd never even avers that the equity in excess of its rate base (largely goodwill) is <u>actually</u> used in providing delivery services. Indeed, ComEd has conceded that "Goodwill could not be ascribed to any particular assets," including distribution assets. (Houtsma Tr. 410, *also* 412). Recovery of costs associated with assets not used and useful in the provision of regulated delivery services is neither reasonable nor lawful.[8]

In an Illinois Power delivery services case, the Commission addressed an analogous utility proposal to recover costs admittedly not attributable to delivery services. There the Commission expressly rejected the utility's contention that post-divestiture costs, of whatever description or use, must be deemed allowable costs for its remaining regulated services.

> IP has argued that because of divestiture of its generation function all assets that were not sold or transferred remain to support the remaining operations of the Company. The Commission finds such argument to be deficient in that there has been no showing that the remaining [delivery services] operations require such a large increase . . . .

(Order, Dkt. 01-0432, issued Mar 28, 2002 at 17). The Commission held that capital costs

[7]Since Mr. Gorman expressly adopted Staff's capital structure over the 50-50 structure because it better represented the capital supporting delivery services, there was no need for him to further "disavow or repudiate" the reasonableness of a 50-50 capital structure <u>for</u> <u>ComEd</u> <u>on</u> <u>this</u> <u>record</u>. (*See* ComEd Br. at 159).)

[8]The phrases "supporting delivery service assets" and "supporting the provision of delivery services" (and minor variations) both refer to the regulatory requirements for approval as allowable investments or costs for delivery services rates.

previously attributed to since-divested generation operations cannot automatically be deemed costs of providing its remaining delivery services. There must be a showing through record evidence that the costs are employed in the provision of the regulated services, even where the costs cannot readily be avoided. (Id.). Compare ComEd's analogous position. ComEd argues for inclusion of its non-rate base equity (mainly goodwill) in its capital structure, though ComEd acknowledges that it is attributable to the ongoing business of the corporation (Houtsma Tr. 410); "The facts are clear: ComEd's entire capital structure – including all of its equity and debt -- supports its utility business" (ComEd Br. at 171 (*emphasis added*)). Whether these costs support Illinois delivery services ComEd never says.

c. ComEd's Focus on Accounting Cannot Support Its Inadequate Goodwill Adjustment or Its Proposed Capital Structure

In its Initial Brief, ComEd falsely attributes to opponents of its proposed capital structure the focus on accounting ComEd offered to support its proposal. (ComEd Br. at 162-170; ComEd Ex. 7.0 at 7:117 *et seq*.) ComEd claims that those opponents were unable to prove that the utility's proposal is unreasonable,[9] leading them to argue that Staff's capital structure "is required by the need to undo the effect of 'purchase accounting' . . . as it relates not to the merger but the value of nuclear assets subsequently transferred to an affiliate in early 2001." (ComEd Br. at 162). ComEd

[9] Under the PUA, ComEd has the express and unequivocal burden of proving that its proposal is reasonable. Its failure to do so must result in a finding against the utility. (220 ILCS 5/9-201(c)). Even if one accepts, *arguendo*, ComEd's erroneous claim that its proposed structure must be proven unreasonable (ComEd Br. at 157) this record does show that ComEd's proposed structure is unreasonable, because it includes capital not used or useful for regulated delivery services.

is wrong.

Contrary to ComEd's argument, Staff's recommended capital structure is supported by several parties, with distinct supporting analyses. Each of those analyses is an adequate foundation for Commission approval of Staff's recommended capital structure. IIEC's analysis, in particular, does not rely on purchase accounting.

As Mr. Gorman explained, defining an appropriate capital structure is part of determining the utility's cost of providing regulated delivery services. (Gorman Tr. 2055). The Commission must identify, separately, the utility's reasonable asset and operating costs incurred to provide delivery services. Those amounts -- which exclude imprudent, unreasonable, and not used or useful costs -- are the bases for calculating a delivery services revenue requirement that provides ComEd a return on its delivery services rate base and recovery of its delivery services operating expenses.

ComEd's mechanical accounting approach cannot properly determine the utility's allowable costs. Simplistic accounting may sweep up imprudent or not used and useful investments or other unreasonable expenditures that are recorded on the utility's books. Commission disallowances regularly reject the use of such accounting entries for ratemaking purposes. (*See, e.g.*,Order, Illinois Power, Dkt. 01-0432, issued Mar 28, 2002). Logically, assets excluded from rate base should not be employed in other aspects of ratemaking. But, blind acceptance of ComEd's accounting computations gives a false picture of the appropriate ratemaking capital structure by inappropriately incorporating such non-rate base assets. ComEd's argument does not establish a sound basis for its proposed capital structure.

ComEd's brief displays the utility's inability to refute Mr. Gorman's testimony explaining clearly how his capital structure analysis differed from, but complemented, Ms. Kight's and why ComEd's proposed capital structure is unlawful and unreasonable. (Gorman Tr. 2051-2053) Instead, ComEd resorts to confusion.

First, for rhetorical purposes, ComEd groups all critics of its ill-conceived capital structure under a single label and incorrectly attributes the same arguments to all parties. (ComEd Br. at 7-8, 159). ComEd's references to "advocates" or "proponents" of Ms. Kight's capital structure (Id. at 159, 167) ignore the clear distinction between (a) the accounting arguments ComEd criticizes and (b) the clear disconnect between ComEd's proposed capital structure and the capital actually supporting its delivery service assets -- the basis for Mr. Gorman's support of Staff's recommendation. In their brief, CUB/CCSAO/City-CCSAO-City explain that their analysis, like Staff's and IIEC's, shared the objective of identifying the equity that actually supports ComEd's delivery services. (CUB/CCSAO/City Br.at 23-24).

Second, ComEd's brief repeats the mantra of ComEd witnesses Kathryn Houtsma and Barry Mitchell that ComEd's equity was only affected by $2.92B when it recorded goodwill. (ComEd Br. at 162; *See* Mitchell Tr. 2473:4-8 and Houtsma Tr. 484:4-8, 13-16). ComEd asserts further that only the utility's revalued asset balance and the merger purchase price are relevant to this capital structure issue, with the difference between the two amounts defining the appropriate equity adjustment. (ComEd Br. at 162; Houtsma Tr. 514). ComEd purposefully ignores the fact (confirmed by the utility's own evidence) that at the time of the merger, ComEd's equity was directly affected by its revaluation of generation assets to a greater extent than ComEd's calculation suggests. ComEd Ex. 7.0 at 7:140 is reproduced immediately below, with emphasis added.

A. The following changes to ComEd's equity were made upon the application of purchase accounting at the merger date ($millions):

Plant Writedowns	($4 ,791)
Deferred Taxes and ITC's	2,157
Pension, OPEB and severance	144
Other assets, liabilities and L ong term debt	77
Goodwill (net of amortization)	4,705
Net increase in Equity	$2,292

ComEd's subtraction exercise(ComEd Redirect Ex.1) conflates the intermediate accounting steps that reveal the other changes in ComEd's equity. It is undeniable that the generation asset revaluation significantly reduced the net change in ComEd equity that otherwise would have been made at the merger. The generation asset revaluation did not affect ComEd's delivery services asset accounts ((Houtsma Tr. 410, 513), and it should not be allowed to distort the equity component of the delivery services capital structure.

Mr. Gorman sponsored an illustrative exhibit (IIEC Redirect Ex. 1 (Fig. 1, *infra*)) to explain why equity not supporting delivery services is properly excluded from the utility's delivery services capital structure, regardless of purchase accounting or the treatment of ComEd's goodwill.

COMMONWEALTH EDISON COMPANY

Capital Supporting T&D Rate Base

Line	Test Year	Amount (000)	Source
1	Total Unadjusted Capital (1)	$11,874,770	ComEd Ex. 7.1, Schedule D-1 and WPD-1
2	T&D Rate Base	6,189,171	Schedule A-2
3	Incremental Capital Above Rate Base	5,685,599	Line 1, less Line 2
4	Good Will/Other Intangibles	4,926,000	ComEd Ex. 7.0 at 7
5	Incremental Capital Excluding Good Will	759,599	Line 3, less Line 4

(1) Total Capital $9,582,770, add book common equity adjustment of $2,292,000 made on WPD-1.

Figure 1

Line 1 of the exhibit shows ComEd's total test year common equity of $11.874 billion, including the $2.292 billion of common equity Mr. Mitchell removed to produce the Company's proposed capital structure. (ComEd Ex. 7.0 at 7:135-137). The $5.685 billion difference between ComEd's total outstanding capital and its test year rate base of $6.189 billion clearly is not used to support delivery services assets. That difference is accounted for mostly by equity supporting ComEd's goodwill asset, for which its books show a balance of $4.926 billion. Since even ComEd admits its goodwill asset should be excluded from ComEd's delivery services rate base, it is important to remove the common equity supporting that goodwill from the capital structure.

Otherwise, the structure is not skewed by equity not actually used to provide delivery services. (*See* IIEC Redirect Ex. 1; (Gorman) Tr. 2056-2058).

Third, ComEd's Initial Brief attempts to tie other parties' opposition to ComEd's capital structure to its nuclear plants transfer, since it believes (incorrectly) it has stronger arguments there. (ComEd Br. at 8, 160, 162, 164). ComEd alleges that those parties' capital structure recommendation is based on the accounting for nuclear assets transferred to an affiliate in 2001. (ComEd Br. at 162). ComEd contends that its transfer accounting was reviewed and approved by the Commission, and that pursuant to PUA Section 16-111(g) the Commission irrevocably "established the proper post-merger and post-transfer capital structure for ComEd."[10] (ComEd Br. at 163-164, 8; 220 ILCS 5/16-111(g)).

The Commission considered -- and rejected -- this accounting approval argument in an Illinois Power rate delivery services case. (Order, Illinois Power, Dkt. 01-0432, issued Mar 28, 2002). There the Commission held that its approval of accounting for generation transfers does not pre-determine its ratemaking decisions, noting that its regulatory review under Section 16-111(g) of the Act is limited to questions of the utility's ability to provide safe and adequate service and an increased likelihood of a rate increase request. (220 ILCS 5/ 16-111(g)).

Although IP has sold its generation assets and exited the generation business,

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[10]ComEd includes in this section of its brief a chart purporting to show that Staff is proposing an equity balance of approximately $3 billion. (ComEd Br. at 168). The chart actually plots a hypothetical balance that ComEd alleges would have resulted from a transfer under certain assumed accounting restrictions that have no foundation in the record. This is not the only instance in which ComEd presents novel information without the record support and citations called for by the Commission's rules. (*See* 83 Ill. Adm. Code 200.830(e)). ComEd's unsupported argument should be summarily rejected.

> as permitted under the Act, the Commission's approval in and of itself does not mean that the Commission has approved the accounting allocations made or that the amount of assets that were transferred are proper. The role of the Commission in divestiture of generation is limited by 16-111 (g).

(Id. at 17-18). ComEd offers no reason why the Commission's decision should be different here.

As to the capital structure approved in ComEd's last rate case, as ComEd knows, the Commission's quasi-legislative decisions (including ratemaking determinations) are not *res judicata*, and each subsequent decision must be based on the record then before it. (*City of Chicago v. ICC*, 133 Ill. App. 3d 435 (1st Dist 1985) at 440 *(citing Mississippi River Fuels Corp. v. ICC* 1 Ill 2d 509 (1953)); 220 ILCS 5/10-201(e)(iv)(A)).[11] The circumstances and evidence of record in this case are significantly different from those in Dkt. 01-0423. During the transition period of the earlier case, unusual financial transactions were permitted to ease the effects of "stranded" generation costs and the utility's transition. Here, the determination of ComEd's cost of capital relates solely to post-transition delivery services. Moreover, the Dkt. 01-0423 record lacked the evidence that warrants rejection of ComEd's proposed capital structure in this case.

ComEd, Staff, CUB/CCSAO/City-CCSAO-City, and IIEC all agree that the equity component of ComEd's actual capital structure is not appropriate for ratemaking. (ComEd Ex. 7.0 at 6:118-121; IIEC Ex. 7.0 at 6:119; CUB/CCSAO/City Ex. 1.0 at 21:607). Each party (including ComEd) supports removal of some amount of common equity. The main difference between the ComEd position and other parties' common position is simply the magnitude of the common equity

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[11] Indeed, that accepted principle of regulatory law has been invoked selectively by ComEd in this proceeding. (*See, e.g.*, ComEd's proposal to eliminate previously determined cost-based class definitions, contrary to the Commission's 01-0423 decision).

adjustment needed. ComEd's accounting adjustment does not remove all costs that do not support regulated delivery services.

c. ComEd's Capital Structure Comparisons Lack Evidentiary Foundations and Do Not Support Its Position

ComEd argues that Staff's recommended capital structure, which is supported by all intervening parties, will not produce credit metrics sufficient to maintain its targeted "A-" bond rating and, therefore, is not appropriate for setting rates in this proceeding. That argument rests on comparisons of Staff's capital structure equity component to those of various groups of utilities and the structure approved in Dkt. 01-0423 are both legally inadequate and unpersuasive.

ComEd's comparisons of capital structure percentages put the cart before the horse. In ratemaking, the Commission first determines what assets have been proved to support ComEd's delivery services. The relative amounts of equity and debt used to support those assets define the capital structure appropriate for setting rates. Indeed, that is precisely the approach ComEd purports to have taken in this case -- adjusting its capital structure to remove goodwill not attributable to delivery service assets. (ComEd Br. at 155-156). ComEd thereby rejected its own specious argument that the Commission's determination of allowable costs should be displaced by comparisons of capital structures with other utilities, in other states, that likely do not have comparable capital structures. Indeed, no utilities have been shown on this record to have equity-to-rate base disparities of billions of dollars or hundreds of millions in goodwill.

The comparison to the capital structure approved in Dkt. 01-0423, aside from *res judicata* problems, also is unpersuasive. ComEd asserts that "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." (ComEd Br. at 164). The 42.86% common equity ratio approved in Docket No. 01-0423 is significantly lower than the common equity ratio proposed by ComEd in this proceeding, 54.20%. The Commission's Dkt. 01-0423 determination, which ComEd purports to rely upon, actually is more in line with Staff's recommended common equity ratio of 37.11%, which also is supported by IIEC and CUB/CCSAO/City. If there is any precedential value in the Commission's 01-0423 decision, it supports Staff/IIEC's proposed common equity ratio and capital structure – not ComEd's.

ComEd also objected to the Staff's capital structure recommendation because it allegedly reflected greater amounts of debt leverage than a proxy group of companies used in determining a cost of equity recommendation. Because the principal thrust of ComEd's argument on this point appears to be a plea for another upward adjustment in ComEd's ROE, the argument (including its capital structure implications) will be addressed in the following Section III.E.3.

d. ComEd's Numerous Alternative Capital Structure Explanations Should Be Rejected

ComEd's preferred criteria for allowable costs dismiss the fundamental regulatory requirement that allowed costs must be attributable to used and useful assets and also be reasonable and prudent. Instead, ComEd would defer to utility management or to dubious comparisons with respect to capital structure. (*See* ComEd Br. at 158). Although ComEd does not dispute that its goodwill is not a delivery services asset or that the cost of goodwill should be excluded from its rate base,[12] ComEd nonetheless wishes to include equity supporting that goodwill asset in the capital structure that will be used to determine its revenue requirement and its rates.

As Mr. Gorman observed during his oral testimony, a utility's capital structure does not normally balance precisely with its rate base, but it is usually close. (Gorman Tr. 2052-2053). In this case, however, there is a significant difference between ComEd's common equity and its rate base. That difference, largely the equity supporting ComEd’s goodwill asset, represents equity that is not supporting assets used and useful in providing ComEd’s regulated services. (Id; IIEC Redirect Ex. 1). ComEd’s extended arguments to the contrary are totally unsupported by any citation to record evidence. (*See* ComEd Br. at 170).

ComEd also asserts that capital structure is a historical accident. From this bare assertion, ComEd argues that it is “senseless” to look for any tie between total equity and the equity supporting delivery services assets or to conclude that capital excluded from rate base does not support undefined “utility activities.” (ComEd Br. at 170-171). At the same time, ComEd inconsistently contends that its capital structure is the result of deliberate financing decisions by ComEd management to which the Commission should defer. (ComEd Br. at 153).

Extending its rejection of applicable *res judicata* law, ComEd claims that “CCC, IIEC, and Staff are simply trying to retroactively eliminate more than $2.6 billion of equity that the Commission has expressly approved.” (ComEd Br. at 166). "Moreover, if equity ‘supports' good will as Mr. Gorman suggests, it does so only in the most trivial sense that if good will is impaired,

[12]ComEd argues that it has removed all goodwill from its rate base. (ComEd Br. at 171, n. 54).

equity is reduced." These assertions, however, are directly contradicted by ComEd's own statements.

For example, IIEC Ex. 7.1 (ComEd's response to IIEC DR 4.04) shows clearly that $4.926 billion of common equity was created and recorded on ComEd's balance sheet solely because a goodwill asset of $4.926 billion was created in connection with the Unicom-PECO merger.[13] (*See also* Houtsma Tr. 396-397 (confirming the DR response)). Thus, that common equity does not represent equity sold to the public or earnings retained by the Company to invest in delivery services plant. It is a "residual accounting entry" (ComEd Br. at 171, n. 54) that relates solely to the merger. Costs attributable to that equity are not a proper element of the utility's cost of regulated service -- whether from inclusion in rate base or as part of the capital structure.

Ultimately, ComEd asks the Commission to approve a capital structure that ignores reality and the law, to ComEd's advantage. The reality is that the amount of equity included in its proposed capital structure exceeds the amount actually devoted to providing ComEd's delivery services. In its entire 20-page discussion of this issue, ComEd has never denied that fact. Nor has ComEd affirmatively averred that the equity at issue actually does support its delivery services rate base, as

[13]In the DR that is IIEC Ex. 7.1, ComEd states:

After the common equity balance was reduced by $2.634 billion to recognize the fair value, the balance of common equity was then compared to the value of the consideration paid by the acquiring company. The difference, which in this case was $4.926 billion, was recorded as an increase in goodwill and a corresponding increase in common equity. The end result of these two steps, both recorded as of the merger date, was an increase in common equity resulting from purchase accounting of $2.292 billion. (*emphasis added)* opposed to some undefined "utility activities."[14] Without openly declaring that it seeks delivery services rates that recover costs not incurred in the provision of its regulated delivery services, ComEd's proposed capital structure would achieve precisely that result.

Staff and CUB/CCSAO/City

Parties other than ComEd agree that the capital structure recommended by Staff is a reasonable structure that accurately reflects the capital actually supporting ComEd's provision of the delivery services regulated by the Commission. (CUB/CCSAO/City Br. at 20-21). ComEd, in contrast, strains to avoid any acknowledgment that such a connection is necessary or appropriate. Although the respective analyses of Staff, IIEC, and CUB/CCSAO/City differ, each agrees that ComEd's proposal would overload the capital structure with excess expensive equity that would unjustly increase customer rates.

Staff argues that "ComEd's transfer of its generation assets distorted the relationship between its actual capital structure and the capital supporting its depreciated original cost rate base." (Staff Br. at 67). According to Staff, ComEd's former generating assets were not transferred at their book value, but at a lower revalued amount, and the generation related goodwill remained with ComEd. Staff concluded that, as a result, ComEd's capital structure does not accurately reflect the original cost book value of the assets and liabilities transferred, or of the remaining assets that support its delivery services. Because of this anomalous separation of original generation cost components, ComEd's reversal of the purchase accounting adjustments does not entirely correct the distortion.

[14]This is not the same as ComEd's assertion that the costs support its corporate business. (ComEd Br. at 170-171). And, the legal implications are significantly different. (*See* Section III.E, *supra*; Order, Dkt. 01-0432, issue March 28, 2002).

Accordingly, Staff proposed a further adjustment.

In its Initial Brief, CUB/CCSAO/City praises the clarity and correctness of Mr. Gorman's analysis. Equally important, that brief points out that the witnesses for Staff, IIEC, and CUB/CCSAO/City each "demonstrated the artifice of ComEd's position" when each testified that the costs approved in this proceeding must be shown to support assets needed for ComEd's provision of delivery services, and that the costs attributable to ComEd's inflated capital structure do not. (CUB/CCSAO/City Br. at 21).

3. Cost of Common Equity

The principal points of divergence between the analyses of Mr. Gorman and Dr. Hadaway are two specific inputs to their DCF and Risk Premium ("RP") models and Dr. Hadaway's result-oriented screening of inputs. In IIEC's view, Dr. Hadaway's DCF growth rates subordinate observable current conditions to his more subjective projections of the future or extrapolations of the past. Repeatedly, Dr. Hadaway's preferred inputs are those that do not yield results he subjectively deems too low. (*See, e.g.*, Gorman IIEC Ex. 3.0, 41-42 (DCF growth rates); ComEd Ex. 8.0 at 36:837 (RP interest rates) ComEd Ex. 21.0 at :37; IIEC Br. at 24). IIEC also responds in this section to other ComEd claims.

a. GDP Growth Rate

ComEd says Dr. Hadaway's projected Discounted Cash Flow ("DCF") growth rates "allow [him] to look beyond the present low inflation environment." (ComEd Br. at 178). Dr. Hadaway's presumption that expected growth rates for the period the rates determined in this case will be in effect are less important than problematic, long-term projections or historical trends of growth rates is unsupported and should be rejected along with his result-oriented screening of data inputs.

In Dr. Hadaway's view, the DCF model requires a very long-term growth rate for future years -- "technically to infinity." ComEd Ex. 38.0 at 10:216-217. However, as Dr. Hadaway acknowledges:

> Since the mid-1980s, dividend growth expectations for many electric utilities have fluctuated widely. . . . Under these circumstances, long-term growth rate estimates have become highly uncertain, and estimating a reliable "constant" growth rate for some companies is virtually impossible.

(ComEd Ex. 8.0 at 18-19:394-401).

To address this problem, Dr. Hadaway reaches far into the past for a historical data trend that he freezes and applies to most future years -- notwithstanding his recognition of (a) significant changes in the historical growth pattern and (b) current long-term growth projections that are distinct from historical patterns. On an unsupported assumption that history will resume after a brief pause, Dr. Hadaway's 2-stage DCF model dilutes all significant effect of current long-term projections by using current growth estimates for only 5 years, then using his preferred higher growth rate in a second 150-year stage.[15] (ComEd Ex. 8.0 at 27:588-593; ComEd Ex. 8.6 at 5 (Cols. 12, 30)).

Staff agrees that Dr. Hadaway's DCF growth estimate is inappropriate -- for reasons distinct from (but complementary to) Mr. Gorman's. Staff observed that his estimate is economy-wide, not

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[15]This is not the only instance of result-oriented input screening by Dr. Hadaway. For example, he summarily rejected the results of his constant growth DCF model -- "Because this result falls 100 basis points or more below my risk premium checks of reasonableness, it is excluded from my final DCF range." ComEd Ex. 8.0 at 32:743-744. Despite his expert opinion that "a combination of DCF and risk premium methods provides the most reliable approach," Dr. Hadaway rejects the lower result, when he could just as easily have rejected the higher one – with a result that would approximate Mr. Gorman's equity cost estimate.

company-specific. Moreover, his subjective model components have the apparent objective -- and actual effect -- of boosting ComEd's proposed ROE far above the level justified by a transparent application of the models. (*See* Staff Br. at 85). Staff concludes that "the Company effectively overstates ComEd's cost of equity by combining the higher dividend yield resulting from the lower actual current retention rate with the higher growth rate associated with a higher assumed future retention rate. (ICC Staff Exhibit 16.0, pp. 10-11)." (Staff Br. at 86).

d. Other

(i) ComEd's RP Analysis Is Distorted By Questionable Assumptions and Obsolete Data Trends

In its Brief, ComEd states "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 . . . returns." (ComEd Br. at 176). This bare-bones description of ComEd's analysis obscures a myriad of questionable inputs Dr. Hadaway employed in his RP analysis.

ComEd's risk premium study used only long-term projections of "A" bond yields. Those projection inputs are significantly increased over current observable "A" rated utility bond yields and are not likely reflective of investors' cost of capital demands. (IIEC Ex. 3.0 at 3:40-51). As with his DCF growth rates, Dr. Hadaway selects inputs that deny customers any benefit of the current low capital costs.

Dr. Hadaway's interest rate growth inputs for the risk premium model continue that consistent pattern. Dr. Hadaway relied entirely on "highly problematic" interest rate projections in his risk premium analysis. (IIEC Ex. 3.0 at 12:291-292). His model denies ComEd's customers any benefit from the reality of today's low cost capital markets, keeping rates artificially high. (IIEC Ex. 3.0 at 13:309-310). "[R]eflecting current observable utility bond yields of approximately 6.0% in Dr. Hadaway's risk premium analysis would lower his risk premium study from 10.8% down to 10.4%." (IIEC Ex. 7.0 at 23:540-542).

In addition, Dr. Hadaway increased his proxy group risk premium analysis results by over 40% (from 3.08% to 4.38%) to recognize an alleged inverse relationship between interest rates and risk premiums. (IIEC. Ex. 3.0 at 43:938-942). Mr. Gorman rejected that adjustment, criticizing it on several grounds. First, the data Dr. Hadaway used in his regression analysis is not capable of providing the precision he purports to have found. As Mr. Gorman explained:

> Dr. Hadaway has unreasonably attempted to create a forward-looking specific point risk premium estimate using this historical data. This is not reasonable because the data and model are not this precise.

(IIEC Ex. 3.0 at 43:944-946). The data used in Dr. Hadaway's analysis is not representative of current or future outlooks for interest rate volatility or inflation. (IIEC Ex. 3.0 at 43:946-953). Second, the academic literature on which Dr. Hadaway's adjustment is based rests on data from the 1980s and very early 1990s -- an anomalous period from which extrapolations of current relationships are dubious. "During the 1980s and very early 1990s, an inverse relationship did exist, but that was not the case prior to 1980 and has not been shown to be the case since the early 1990s." (IIEC Ex. 7.0 at 19:443-445).[16]

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[16] Indeed, the academics examining this question found a positive relationship between interest rates and equity risk premiums before 1980 and an inverse relationship from 1980-1984. (IIEC Ex. 7.0 at 20:461-464). Moreover, whatever relationship existed was not tied solely to changes in nominal interest rates and could "change materially over time." (IIEC Ex. 7.0 at 19:439-441). Dr. Hadaway's simplistic, unsupported adjustment "inappropriately increases

Finally, and most important, the relevant, comparative empirical data confirm Mr. Gorman's conclusions.

> [U]tility bond yield spreads over Treasury yields currently are below average, relative to the last 25 years. This indicates that the market's assessment of investment risk for the utility industry is not higher now than it has been over the last 25 years. Hence, utility equity risk premiums today should conservatively be comparable to the average equity risk premiums experienced over the last 25 years, not higher, as Dr. Hadaway asserts.

(IIEC Ex. 3.0 at 47:1051-1056).

(ii) ComEd's Comparison of Commission Awards Is Not a Lawful Basis for Rejection of IIEC's Recommended ROE

ComEd's principal objection to the ROE recommendations of other parties is that "Fundamentally, each of these [other parties'] proposals is significantly below the COEs approved in recent years for electric utilities in the United States." (ComEd Br. at 176). This wrong-headed analysis is the crux of ComEd's argument in brief. (Id). But, it is a legally inadequate basis for a Commission decision.

Decisions of other regulatory commissions, in other states, for other utilities, on different evidence, and without any showing of relevant similarities are neither the proper nor a lawful basis for setting rates in Illinois. The Commission's decision here must be based on the record evidence respecting the specific costs of providing ComEd's delivery services. (220 ILCS 5/10-201(e)(iv)(A)). Were the standard as ComEd suggests, the Commission could dispense with evidentiary hearings and simply conduct polls.

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equity risk premiums for no other reason than a reduction in nominal interest rates." (IIEC Ex. 7.0 at 21:492-494).

The PUA requires more -- an evidentiary foundation establishing the cost of equity <u>for ComEd</u>. However, ComEd's Initial Brief offers only a chart of legally irrelevant data and a sweeping conclusion that its proposed 11.00% ROE subjectively "makes sense" because of various risks it supposedly faces. (ComEd Br. at 177). If there is evidence of record that associates other commissions' awards with these specific ComEd risks, ComEd does not cite it. In fact, the evidence in this record questions the post-transition significance of some of the major risks ComEd claims to face, especially in comparison to the level of risk faced by other utilities. *(See, e.g.,* IIEC Ex. 1.0 at 4-5:90-102 (commenting on ComEd's reduced risks of regulatory disallowances and provider of last resort procurement risks under its auction process); IIEC Ex. 3.0 at 10:238-249; and CUB/CCSAO/City Ex. 1.0 at 14-15:418-426). ROEs awarded to companies selected simply by the dates of their rate orders -- companies not likely to have the same characteristics or costs as ComEd -- have no probative value.

IIEC's recommended 9.9% ROE stands on Mr. Gorman's multi-faceted analysis. ComEd's brief relies mainly on a legally irrelevant comparison to other commissions' decisions and a subjective claim that other parties' recommendations are "below the mainstream." (ComEd Br. at 176). ComEd's 11.0% proposed ROE should be rejected.

(iii) ComEd's Analysis of Debt-Equity Ratios Does Not Support An Upward Adjustment in Its Return on Equity

ComEd asserts that the irrelevant contrast between other parties' ROE recommendations (for ComEd) and various commissions' ROE decisions (for other utilities) "is even more stark when ComEd's capital structure is considered." (ComEd Br. at 177). ComEd alleges that other parties in this case "have failed to consider what the cost of equity of such a hypothetical highly leveraged company would be" (ComEd Br. at 178) and contends that Staff's capital structure, which is supported by all other parties, warrants a boost in its ROE. IIEC disagrees.

No risk-based adjustment to ComEd's return on common equity is warranted or appropriate. ComEd purported to mimic the financial ratio analysis employed in financial markets to assess its risk in the eyes of investors. (ComEd Ex. 20.0 at 3-5:49-97). But, ComEd's analysis does not accurately replicate the market's assessment of ComEd's risk.[17] In computing the financial ratios on which its argument depends, ComEd refuses to exclude transitional funding instruments ("TFIs") from the capital structure. (ComEd Br. at 172). TFIs should not be included -- and indeed are not included -- in the capital structure used by the financial markets to assess ComEd's financial risk. (IIEC Ex. 7.0 at 12:256-258 and 14-15:323-332).

The appropriateness of excluding TFIs should not be in dispute, as ComEd itself has assured the Commission that TFIs will be considered off-balance sheet debt by the financial markets and will not negatively affect its financial risk. In arguing the opposite here, ComEd effectively repudiates its firm representations to this Commission concerning TFIs.

> [B]ecause the Notes will be non-recourse to ComEd, the transaction will be analyzed as an off-balance sheet transaction for purposes of ComEd's credit rating (i.e., not viewed as leverage for credit rating purposes). This means that . . . any increase in ComEd's leverage for accounting purposes (i.e.,

[17]Mr. Gorman testified that ComEd is considered more risky because of its ties to its parent company's unregulated operations. (Gorman Tr. 1969; *see also* ComEd Ex. 7.8, Sched D-8; ComEd Ex. 20.6 at 3-4). Illinois law requires that only the regulated activities of a utility be considered in setting rates. (220 ILCS 5/9-230). Eliminating this prohibited effect on ComEd's cost of capital (and derivatively its rates) could require a lower return than ComEd's credit rating argument might suggest.

> including the Notes) would be disregarded for purposes of ComEd's general credit rating. . . . [I]nvestors are likely to view the Notes as beneficial to ComEd and to decrease, not increase, ComEd's risks and, therefore, its cost of capital.

(IIEC Ex. 7.0 at 13:272-302 (*quoting* testimony of ComEd V.P. and Treasurer Ruth Gillis in Dkt. 98-0319)). Another ComEd witness in that same proceeding, where the Commission authorized ComEd's TFIs, was even more definitive. Mr. William Abrahams, who was presented as an expert on utilities' credit standing and financial risk, stated:

> The notes are non-recourse to ComEd. These securities will be treated as off-balance sheet financing by the credit rating agencies. Therefore, it will not be counted by the agencies in evaluating ComEd's financial risk.

(IIEC Ex. 7.0 at 13;272-302 (*quoting* testimony of ComEd witness W. Abrahams in Dkt. 98-0319)).

More important, credit rating agencies have confirmed that TFIs are, in fact, excluded from their assessments of ComEd's financial risk. (IIEC Ex. 7.0 at 14-15:323-332). IIEC witness Gorman reviewed ComEd's credit rating reports and showed that Standard & Poor's and Moody's both removed the effects of TFIs in constructing credit rating financial metrics. (Id. at 14:323-329). Therefore, consistent with ComEd's assurances to the Commission, TFIs should not be included in ComEd's capital structure when comparing its calculated financial risk indicators to the financial risk ratios of credit rating guidelines or of other companies.

Despite ComEd's assurances to the Commission that TFIs would not affect its financial risk and despite the fact that the market actually does exclude ComEd's TFIs from its financial risk analyses, the utility argues an inconsistent contrary position in this case:

> 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.

(ComEd Br. at 172). But, removing TFI revenues as ComEd proposes is not the simple matter it suggests, and the record contains no evidence that market risk assessments would change. If TFI revenues are to be removed from the ratemaking calculus, the starting point would have to be the consolidated credit metric calculations performed on Exelon's consolidated operations, not just ComEd's regulated utility operations. As shown in the Standard & Poor's report attached to Mr. Mitchell's testimony, S&P assessed the relevant credit metrics on a consolidated Exelon basis. (*See, e.g.,* ComEd Ex. 7.8, Sched D-8; ComEd Ex. 20.6 at 4 ("The corporate credit rating on Exelon incorporates the consolidated business and financial profiles of the company's regulated and nonregulated businesses" and listing securitized debt paid through rates as a point of note regarding the company's liquidity). ComEd's speculative review of TFIs' effect on ComEd's credit rating would require a complete review of Exelon's credit standing -- not simply ComEd's. No party in this case advocated such an analysis, and is clearly inappropriate to do so. The objective in this case is to establish a fair and reasonable rate of return on ComEd's delivery services rate base.

The record does show that the result of excluding ComEd's TFIs from its capital structure and recomputing the financial risk indicators. Those results confirm that ComEd's financial risk is comparable to that of IIEC's and Staff's proxy company groups. (IIEC Ex. 7.0 at 12:262-268). ComEd's common equity ratio excluding TFIs is 45%, which is comparable to the 48.8% common equity ratio ComEd estimated for Staff's proxy group of companies and the 46% common equity ratio associated with IIEC's proxy group of electric companies. (Id.). Because these common equity ratio risk indicators -- when properly computed -- show that ComEd's financial risk is comparable to the Staff and IIEC proxy groups' risk, there is no need to adjust ComEd's return on common equity as the utility proposes.[18]

4. Overall Cost of Capital

ComEd suggests that its proposal is superior because it is "derived from its actual capital structure, actual embedded cost of debt, and the most reasonable estimate of its cost of equity." (ComEd Br. at 182). ComEd's assertion is false.

The "actual" capital structure to which ComEd refers is, in fact, a hypothetical structure created by ComEd's goodwill adjustment to its test year capital structure. Other than the inadequacy of ComEd's adjustment, ComEd's capital structure is no different in that respect from the capital structure supported by other parties. (*See* Section III.E.1.a *supra*).

IIEC has not contested ComEd's cost of debt proposal, accepting ComEd 6.5% cost of debt. However, as IIEC witness Mr. Gorman pointed out, it is a "<u>conservative</u> estimate of ComEd's current incremental cost of debt," generous enough to include sometimes controversial issuance expenses. (IIEC Ex. 3.0 at 19:443-446 (*emphasis added*)). Other parties identified specific elements of the conservative (*i.e.*, higher) 6.5% debt cost that they contest. Staff disagreed with ComEd's proposed cost of debt because it incorporated numbers that did not reflect straight line amortization. (Staff Br. at 76). CUB/CCSAO/City point out that some of the debt issues underlying ComEd's

[18]Moreover, the sample of firm ratings in Mr. Bodmer's rebuttal testimony, the equity ratio guidelines for ratings that ComEd relies on are not determinative. CUB/CCSAO/City Ex. 4.0 at 18:539-540. Companies with equity ratios lower than those recommended by Mr. Gorman, which ComEd criticizes as inadequate to preserve investment grade ratings, actually can have ratings above investment grade. See (<u>Id</u>.); CUB/CCSAO/City Ex. 4.0 at 18:510-523.

6.5% cost will expire before or shortly after the rates being determined become effective. Each of those parties recommends a lower cost of debt be used in calculating ComEd's overall cost of capital.

Finally, Mr. Gorman and Staff's Mr. McNally identified significant flaws in ComEd's cost of equity estimates. (*See* Gorman IIEC Ex. 3.0 at 37-51:840-1134 and McNally Staff Ex. 5.0 at 18-28:348-560; *See also* CUB/CCSAO/City Ex. 1.0). ComEd's ROE estimate is not "the most reasonable estimate of its cost of equity;" the evidence of record shows that it is not a reasonable estimate at all. (Flaws that make ComEd's ROE estimate unreasonable are discussed in Section III.E.3 of this brief.)

The chart immediately below shows the overall cost of capital recommendations of the parties in this case.

	CAPITAL STRUCTURE	**RETURN ON EQUITY**	**COST OF DEBT**	**OVERALL RETURN**
COMED	54.20% - 45.80%	11.00%	6.50%	8.94%
STAFF	37.11% - 62.89%	10.19%	6.48%	7.86%
IIEC	37.11% - 62.89%	9.90%	6.50%	7.75%
CUB/CCSAO/CITY	37.11% - 62.89%	7.75%	6.23%	6.79%
AG	----	----	----	6.79%

Interestingly, given ComEd's frequent complaint that some other party's recommendation is outside the mainstream, ComEd's proposed cost of capital appears to be the outlier. It is further from the mainstream position than the recommendation of any non-utility party. Given the identified defects and upward bias in ComEd's estimates of the factors -- capital structure, ROE and cost of debt -- used to derive an overall cost of capital, ComEd's above the mainstream result is neither surprising nor appropriate.

F. Cost of Service Issues

1. Embedded Cost of Service Study

ComEd describes its embedded cost of service study. It reserves its right to propose the use of a marginal cost of service study in future proceedings. It states its proposed ECOSS is consistent with the ECOSS filed and approved by the Commission in prior dockets, and that Staff has not proposed any adjustment to the study in this proceeding. Therefore, ComEd argues the record demonstrates its ECOSS is reasonable and should be approved. (ComEd Br. at 183-184).

First, IIEC notes ComEd's ECOSS was rejected by the Commission for the purpose of intraclass rate design in ComEd's last case based on substantial evidence in the record. (ComEd Dkt. 01-0423, Order, March 28, 2003 at 137-139). Therefore, it would not be appropriate to adopt the study for that purpose in this case on the assumption that the study in this case is consistent with the study in the last case.

IIEC addressed the Company's ECOSS in its Initial Brief. (IIEC Br. at 28). It suggested the study was consistent with principles of cost of service, with one important exception. The study failed to adequately identify the customer component of the distribution system in that it failed to incorporate the minimum distribution concept (MDS) quantified using either the zero intercept or minimum size method. (Id.). IIEC also pointed out the study presented by ComEd failed to provide the justification for the combination of the four non-residential rates consisting of customers 1 MW to 3 MW, over 3 MW to 6 MW, over 6 MW to 10 MW and over 10 MW because it does not identify the cost of serving each of the four classes. (Id.). On the basis of the differences in the cost to serve, IIEC recommended that a separate class for 10 MW and over customers be retained and the proposed rate class for 69 kV and higher customers be adopted, and the rates for those classes be established in proportion to the overall rate increase or rate decrease approved by ComEd by adjusting the rates upward or downward in proportion to the overall increase or decrease. (IIEC Br. at 34-40). IIEC will address the Company's failure to use the minimum distribution system concept in Section III.F.2. below. It will address the combination of rate classes and rate issues relating to the 10 MW and over class in Section III.H.1.b.(2) below.

2. Minimum Distribution System

ComEd takes the position that the minimum distribution concept had been rejected by the Commission in past cases and that IIEC (and other proponents of the minimum distribution system concept such as BOMA) had provided no new information that would lead the Commission to change its prior conclusions and therefore, the Commission should deny IIEC's request to require ComEd to incorporate the minimum distribution system in the next case. (ComEd Br. at 184-185).

Staff also takes the position that IIEC's proposal to require ComEd to either incorporate the minimum distribution system concept or present parties with a study quantifying the concept in its next case should be rejected because the Commission has not previously adopted the concept. (Staff Br. at 90-92). Staff also argues the minimum distribution system concept is "flawed" and therefore, should be ignored by the Commission for regulatory eternity. (Staff Br. at 92).

The issue addressed in the application of the minimum distribution system concept, is how much of the distribution system is customer related. Its use for that purpose has been accepted by the National Association of Regulatory Commissioners. (McClanahan Direct BOMA Ex. 2.0 at 13:280-299). It is true the Commission has not previously adopted this method. Contrary to Staff's position, IIEC does not believe it would be good public policy for the Commission to rule out a study. Such action would preclude an informed exploration of the concept in any future regulatory proceeding.

Given the majority view in this case that distribution costs are demand and customer related, it would be appropriate for ComEd to incorporate the MDS concept in its next cost study. This would more accurately reflect the impact on customer classes by properly recognizing the customer component of much of the distribution system on a going forward basis. In the alternative, ComEd should at least present a study in its next case, which would allow the Commission and customers to better determine how much of the system is actually customer related.

3. Proper Allocation of Distribution Costs

CUB/CCSAO/City argue that ComEd's ECOSS improperly fails to take into account peak and average demand. (CUB/CCSAO/City Br. at 41). ComEd suggests that its study uses class NCP and CP demands to allocate distribution costs in a manner consistent with past embedded cost studies and the past practice of the Commission. (ComEd Br. at 205). IIEC agrees with ComEd. The allocation method proposed by CUB/CCSAO witness Ruback is essentially a 50/50 allocation method which would allocate 50% of the distribution system on the basis of energy usage and 50% on the basis of demand. This witness admitted in cross-examination that his recommendation is really an attempt to base rates on something other than cost of service. (Ruback Tr. 1193). In essence, he proposes to allocate the cost of the distribution system on his subjective judgment of what is fair and equitable, by allocating 50% of the system on energy and 50% on demand. This proposal should be rejected. First, it has been the Commission's long-standing policy to attempt to base rates on cost of service. (*See* Illinois Power Company, ICC Dkt. 03-0183, Order, April 6, 1995 at 88; Central Illinois Light Company, ICC Dkt. 04-0040, Order, December 12, 1994, 1994 Ill. PUC Lexis 557*158; and Northern Illinois Gas Company, ICC Dkt. 95-0219, Order, April 3, 1996 at 45, 45 and 49).

Second, abandoning the principle that rates should be based on an objective definition of "fairness" and "equity," i.e., cost causation in favor of a subjective standard of "fairness" and "equity" exposes all customers, residential and non-residential, to cost allocations and rate designs which bear no relationship to economic reality and which are structured to meet a purely subjective and forever changing standard of fairness or equity. CUB/CCSAO/City would not appreciate a future Commission which would decide that regardless of cost causation, it would be "fair" and "equitable" to assign 80% of the cost of the distribution system to the residential customers because the residential class represents more than 80% of the total number of customers on the ComEd system. The Commission would indeed be headed down an extremely dangerous path if it were to adopt the CUB/CCSAO/City recommendation in this proceeding.

Third, as noted above, it has been the Commission's policy to move rates toward cost of service for many years. Allocating the distribution system 50% on energy and 50% on demand based on one party's whimsical and extremely subjective standard of fairness and equity would violate that philosophy. While the Commission has certainty considered customer impact in making revenue allocations in past cases, it has usually tried to make incremental movement to cost based rates while at the same time minimizing, when appropriate, customer impact. (Id.).

To the best of IIEC's knowledge, the Commission has never determined that the allocation of any portion of utility plant (production, transmission or distribution) should be allowed on the basis of subjective judgments "what is fair or equitable" at the expense of cost causation. Abandoning these principles, as CUB/CCSAO/City propose, would be a fundamental and profound change in Commission policy. It would also violate one of the declared goals and objectives of the Public Utilities Act, which is to ensure "efficiency" which has been defined in relevant part to be the provision of reliable electric service at the least possible cost to the citizens of the state; in a manner that: ". . . . (iv) tariff rates for the sale of various public utility services are authorized such that they accurately reflect the cost of delivering those services . . . .; (v) variation in cost by customer class and time of use it taken into consideration in authorizing rates for each class." (220 ILCS 5/1-102(a)(iv)(v)).

Also, it violates the goal and objective of "equity" as set out in the PUA as the "(d) . . . fair treatment of consumers and investors in order that . . . (iii) the cost of supplying public utility services is allocated to those who cause the cost to be incurred." (220 ILCS 5/1-102(d)(iii)). The CUB/CCSAO/City proposal is not efficient in that, according to the testimony of their own witness, does not really result in rates that actually reflect the cost of delivering electricity. It does not consider the variation in costs by customer class. It does not consider "equity" in that it does not ensure that the cost of supplying electric delivery service is allocated to those who cause the costs to be incurred. In fact, the proposal, according to Mr. Ruback, is not based on principles of cost causation, but "non-cost causation" principles. (*See* Ruback CUB/CCSAO Ex. 3.0 at 28:568-571).

Fourth, the Commission has never used the 50/50 allocation method in electric cases, nor has it been adopted where proposed in electric cases in other jurisdictions in the experience of IIEC witness Chalfant, who has participated in over 400 cases, at lest 300 electric cases. (Chalfant IIEC Ex. 6.0 at 6-9:150-162; Chalfant Tr. 1686). The Commission has rejected similar proposals in the past to simply allocate costs on a 50/50 basis. (*See*, for example, Central Illinois Public Service Company, ICC Dkt. 90-0072, 1990 Ill. PUC Lexis 625*74-75; Northern Illinois Gas Company, ICC Dkt. 95-0219, Ill. PUC Lexis 204*107, 109).

Fifth, CUB/CCSAO/City do not explain, nor can they explain, why it would be appropriate to adjust the allocation of the cost of the distribution system on the basis of non-cost causation principles in order to mitigate rate impacts to residential customers, who will see a class increase of 16% (CUB/CCSAO/City Br. at 42) when, in fact, the record here demonstrates there are large customer groups which will see increases ranging from 109% to 160% under ComEd's proposal. (Stephens IIEC Ex. 1.0 at 7-8:Tables 1 and 2; Swan DOE Ex. 1.0 at 4-5:86-89). The CUB/CCSAO/City recommendation can only exacerbate the adverse impact of the ComEd proposal on larger customers.

Sixth, to the extent the Commission wishes to mitigate rate impacts on residential customers, it should do so through the adoption of appropriate rate mitigation plans, not through the violation of cost causation principles in the allocation of cost responsibility for ComEd's distribution system.

Seventh, CUB/CCSAO/City's proposal to abandon cost causation principles in establishing ComEd's rates because ComEd is now a distribution company, ignores the fact that this is ComEd's third delivery service case since the adoption of the Customer Choice and Rate Relief Act of 1997. (220 ILCS 5/16-101 et seq.).

Eighth, CUB/CCSAO/City argue there is economic justification for allocating ComEd's distribution costs partly on energy use. (CUB/CCSAO/City Br. at 39). The "economic justification" referred to by CUB is that it is appropriate to allocate 50% of the distribution system on demand and 50% on energy because one-third of ComEd's revenue is derived from a per kWh charge (CUB/CCSAO/City Br. at 39) ignores the fact that this fraction of ComEd revenues is primarily a function of ComEd's rate design and the lack of demand metering systems for residential customers. (*See* Crumrine ComEd Ex. 23.0 at 39:831-844 testifying that the type of metering used for residentials tends to focus on a volumetric basis rather than demand.) It also ignores the fact that where ComEd has been able to install demand metering for non-residential customers, ComEd's rates contain no per kWh charge. Non-residential charges consist primarily of a distribution facilities charge/demand charge, customer charge and metering charge. If CUB/CCSAO/City were correct in their arguments, then presumably, these non-residential rates will contain a per kWh charge. In fact, if CUB/CCSAO/City witness Ruback was right in suggesting that "without kilowatt hour charges the distribution system would not be economically justified." (Ruback CUB/CCSAO/City Ex. 6.0 at 6:116-117) that portion of the system used to serve non-residential customers would not be built. Of course, Mr. Ruback and CUB/CCSAO/City are wrong. The design and construction of the system is not a function of whether there are kilowatthour charges in the utility's rates and make no economic sense to suggest otherwise. Therefore, CUB/CCSAO/City are incorrect.

CUB/CCSAO/City argue, through their witness Mr. Ruback, it is unfair for customers with the same demands to pay the same demand costs if one customer uses more energy than another. This ignores the fact that the system is designed to accommodate each customer's demand (not energy usage) and the fact that the utility incurs the same cost to serve each customer's demand regardless of the total energy usage of the other customer. IIEC questions whether it is fair to charge the customer who makes the most efficient use of the utility facilities more for those facilities than the customer who makes less efficient use of them. IIEC believes it is patently unfair. Yet, under the CUB/CCSAO/City witness Ruback's approach, the more efficient customer would be charged more, even though both customers impose the exact same cost on the utility. For example, if two neighbors each installed a concrete driveway of the same length, width and thickness, but one neighbor had one car and the other neighbor had two cars, would it be logical or "fair" to charge the neighbor with two cars more for his driveway than the neighbor with one car? The answer is obviously no. It makes no economic sense to do so and it would be unfair to do so. The approach recommended by CUB/CCSAO/City also ignores the reality that the utility has the obligation to serve the customers in its service territory. (*See* 220 ILCS 5/8-401 requiring utilities to provide service and facilities that are adequate, efficient and reliable.) Therefore, assuming both customers have the same demands, the utility would be required to install the same facilities for each customer regardless of their energy usage. Arguing that it is appropriate to allocate the distribution system 50% on demand and 50% on energy based on the assumption that the utility would not install these facilities, absent the greater level of energy usage by one of the customers, ignores this fundamental reality. The utility would have to install these facilities under its obligation to serve regardless of the level of energy usage of either of the two customers.

For all these reasons, the CUB/CCSAO/City proposal to allocate 50% of the distribution system on demand and 50% on energy should be rejected.

G. Revenue Allocation

2. Class Risk Differentials

CUB/CCSAO/City argue again that "fairness" requires an adjustment to the allocation of the revenue requirement to the residential class. (CUB/CCSAO/City Br. at 41). They suggest that even though the Commission set just and reasonable rates in two previous ComEd delivery service cases, it must now consider an alternative approach to revenue allocation, because residential customers will now actually pay delivery service rates. (Id. at 41-42). They further suggest that because the residential revenue requirement will increase by 16% under ComEd's proposal in this case, there is a need to consider their one-of-a-kind and purely speculative revenue allocation proposal in order to mitigate the impact on residential customers. (Id. at 42). Therefore, they propose that Mr. Ruback's target rate of return of 97.5% for the residential class be adopted in this proceeding for revenue allocation purposes. They are wrong in their position for several reasons.

First, they ignore the fact that ComEd most likely will not receive the level of relief it has requested in this case and therefore, it is unlikely the residential rate class will see the level of revenue increase that apparently is the genesis of the CUB/CCSAO/City proposal.[19]

Second, the residential class increase of 16%, assuming ComEd's full rate request, compares

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[19]One could argue that the best mitigation for the residential class and for all classes in this case, is for the Commission to mitigate the overall revenue increase to ComEd by adopting the revenue requirement positions of the parties in this proceeding. Presumably if there were a rate decrease, there would be no need to mitigate the increase to the residential class.

well to the overall revenue increase proposed by ComEd of approximately 20.5%,[20] suggesting that the ComEd revenue increase has already been mitigated in some respects for the residential class. Therefore, there is no need for further mitigation.

Third, there are already proposals being made to mitigate the entire electric bill for residential customers. These proposals can be considered and adopted as appropriate without unnecessarily increasing the cost burden of other customer classes in this proceeding, as the CUB/CCSAO/City proposal would most certainly do. (*See* ComEd Br. at 187-188).

Fourth, the CUB/CCSAO/City proposal to allocate revenue responsibility on the basis of class risk has no demonstrated relationship to economic reality. (*See* ComEd Br. at 188). Furthermore, the record in this proceeding does not justify the adoption of a 97.5% target rate of return for the residential class because it was pulled out of thin air. According to IIEC witness Mr. Chalfant, Mr. Ruback's proposal was deficient on several grounds. It ignores the fact that it is not even possible to evaluate customer risk in the same fashion, as one evaluates risk in determining the utility's required return on equity, (Chalfant IIEC Ex. 6.0 at 9:173-177) even though this is the fundamental basis for Mr. Ruback's proposal. Furthermore, in suggesting the 97.5% target rate of return for the residential class, CUB/CCSAO/City witness Ruback presented no evidence which quantifies the alleged differences in risk between the residential class and other classes. (Chalfant IIEC Ex. 2.0 at 10:178-186). He provided no linkage between any quantification of the class risk for any class and the development of the proposed 97.5% multiplier. (Chalfant IIEC Ex. 2.0 at

[20]ComEd's requested revenue requirement is $1.862 billion. (ComEd Br. at 5). ComEd's requested rate increase is $317.295 million. (ComEd Br. at 30). $1.862 billion less $317.295 million = $1,544,741,000. The percentage increase would be roughly 20.5%.

10:187-188). The multiplier he did propose is entirely without support in the record. Therefore, even if every other argument made by CUB/CCSAO/City on this issue were valid (which they are not), there is no reasonable basis for adopting a 97.5% multiplier versus a 99.9% multiplier in the record. Thus, there is no basis for the Commission to adopt a multiplier as proposed by CUB/CCSAO/City.

CUB/CCSAO/City argue that suggestions by ComEd and IIEC that residential customers may be riskier to serve, ignores the fact ComEd's weather normalization of billing determinants blunts the effect of weather on ComEd's ability to recover cost of service. (CUB/CCSAO/City Br. at 43). This argument proves too much. One, it suggests that the residential class may in fact be riskier to serve than other classes under certain circumstances. Two, it ignores the fact that weather normalization applies in some respect to the billing determinants for all classes, not just the residential class. Therefore, any favorable impact on alleged customer class risk would apply to all customer classes. Thus, all else equal, it appears the residential class may in fact be more risky to serve for the other reasons identified by IIEC witness Chalfant and ComEd witness Crumrine. (Chalfant IIEC Ex. 6.0 at 10:191-201; Crumrine ComEd Ex. 23.0 at 39:832-844).

In addition, the CUB/CCSAO/City argument that because ComEd may experience a greater economic loss, on a per customer basis, when a large customer leaves the system, than when a residential customer leaves the system, begs the issue as framed by their witness Mr. Ruback. Mr. Ruback has framed the issue as a difference in "class risk," not individual customer risk. (*See* CUB/CCSAO/City Ex. 3.0 at 8:143-147; 11:208-210 and 28:571). Therefore, the suggestion that if a single large customer leaves the system, it has a greater economic impact on ComEd than the loss of a single residential customer, does not support the idea that the residential class, as a whole, is less risky to serve than other customer classes. In fact, the record in this case shows that the residential class, as a whole, is actually more risky in terms of utility cash flow than other classes. (Crumrine ComEd Ex. 23.0 at 39:831-844).[21]

Finally, IIEC would note that the parties to this proceeding have presented numerous witnesses and extensive testimony relating to the differences in risk between ComEd and other utilities. They have identified various means and methods for determining the difference in the level of risk, including use of financial industry publications and various criteria from bond rating agencies. (*See* for example, Janous IIEC Ex. 4.0; Hadaway ComEd Ex. 8.0 at 2-3:34-37; Bodmer CUB/CCSAO Ex. 1.0 at 28:845-857). Mr. Ruback and CUB/CCSAO/City have failed to identify a single industry accepted means, method or standard for determining the difference in risk between customer classes. Therefore, the Commission should reject the analogy between determining utility risk and customer class risk posed by Mr. Ruback and the sponsors of his testimony. There is no analogy between the two situations.

In sum, the CUB/CCSAO/City approach should be rejected by the Commission in this proceeding. It has no foundation in the record. It bears no relationship to economic or regulatory reality. It is a recommendation based on pure speculation, not demonstrable fact.

[21]IIEC would like to point out to the Commission that it has not recommended a revenue allocation be based on the assumption that the residential class is more risky to serve than the other rate classes in this proceeding. IIEC disagrees with such approaches as a matter of principle. IIEC believes revenue allocations should be associated with the cost of serving the various classes.

H. Rate Design

1. Customer Class Delineations

ComEd argues that for ratemaking purposes, customers are grouped into classes on the basis of the cost characteristics of these classes (ComEd Br. at 189). ComEd claims its proposed customer classes are broad enough to encompass customers with the same cost pattern and narrow enough to ensure that customers with different cost patterns are not grouped together. (Id.). ComEd says that proper customer classes will avoid the creation of intraclass subsidies. (Id.). However, the net effect of ComEd's proposal to combine the existing non-residential classes made up of customers with demands of over 1 MW to several hundred MW into a single class is a reduction in granularity. ComEd witness Crumrine essentially agreed that when you reduce granularity, you by definition, increase the possibility of intraclass subsidies. (*See* Crumrine Tr. 2551-2552).

ComEd reasons that its proposed rate classes reflect its new status as a wires-only company. (ComEd Br. at 189). ComEd's existing customer classes for delivery service were developed in ComEd's first delivery service case after the adoption of the Customer Choice and Rate Relief Law of 1997. (220 ILCS 5/16-101 et seq.). In the first delivery service case, ComEd argued that its proposed rate classes (the current rate classes) facilitated assignment of costs in accordance with cost causation, customer understanding and implementation of open access (i.e., delivery service) and were just and reasonable. (Commonwealth Edison Company, ICC Dkt. 99-0117, 1999 Ill. PUC Lexis 647*107-108).

ComEd retained these classes in its next delivery service case in Docket 01-0423. By this time, ComEd had divested itself of its generation and acknowledged that its risk of owning and operating generation had been removed. (Commonwealth Edison Company, ICC Dkt. 01-0423, Order, March 28, 2003 at 26). Indeed, ComEd argued, in the context of that case, it had already been split into a wires only company. (*See* Id. at 33-34). Yet, ComEd proposed no change in its rate classes, presumably because they continued to reflect the principles of cost causation, customer understanding, and continued to facilitate the implementation of open access in spite of the fact that ComEd had becomes a wires-only company.

Thus, ComEd's current customer class delineations already reflect ComEd's new role as a distribution company and, if one is to accept ComEd's representation in the first two cases as accurate, are just and reasonable as so determined by the Commission.

b. Non-Residential

ComEd argues that the underlying cost of service for the customer groupings of 1 MW to 3 MW customers, over 3 MW to 6 MW customers, over 6 MW customers to 10 MW customers, and over 10 MW customers is sufficiently close to justify combining these now separate rate classes into a single class. (ComEd Br. at 195). ComEd's argument at this point in its brief is based upon the direct testimony of its witness, Mr. Paul Crumrine. (Id.). However, Mr. Crumrine did not actually demonstrate that the "costs" of serving any customer class was close for any purpose in his direct testimony. He actually recommended a combination of the classes on the assumption that "charges" for these four customer classes were similar and on the assumption that the elimination of the CTC reduced the need for the current rate classifications. (Crumrine ComEd Ex. 9.0 at 38:814-816; Stephens IIEC Ex. 1.0 at 11-12:183-225). IIEC witness Stephens demonstrated that the "charges" applicable to the current rate classes were, in fact, substantially different. (Stephens IIEC Ex. 1.0

at 7-8:Tables 1 and 2, 11:196-201). He further demonstrated that the current rate classes were not impacted by the CTC. (Stephens IIEC Ex. 1.0 at 12:206-225). Therefore, ComEd is quite simply mistaken in arguing that Mr. Crumrine's direct testimony supports a combination of the rate classes because it demonstrates the underlying cost of serving these classes are similar.

Nor does ComEd's embedded cost of service study in the last case support ComEd's proposal to combine these four rate classes in this case. That study included 69 kV customers in each of the then four current rate classes. (Chalfant IIEC Ex. 2.0 at 9-10:179-182). Furthermore, it was rejected for intraclass revenue allocation purposes by the Commission in ComEd's last case. (*See* Commonwealth Edison Company, Dkt. 01-0423, March 28, 2003 Order at 137).

ComEd's original study in this case as adjusted by IIEC witness Chalfant shows that the over 10 MW class has a lower per kW cost then the other three classes below 10 MW. (Chalfant IIEC Ex. 2.0 at 12:234-240; IIEC Ex. 2.2).

Nor does ComEd's embedded cost of service study, presented in rebuttal, justify combination of the rate classes. It has been demonstrated that this study actually shows a difference in the cost of service between the 10 MW and over customer class and the other three customer classes. (Chalfant IIEC Ex. 6.0 at 14:Tale 1).

Thus, ComEd has not adequately demonstrated a sufficient similarity in costs between the 10 MW and over customer class and the other three classes so as to justify their combination in this case.

2) Very Large Load Customers

(i) The Over 10 MW Customer Class Should Be Retained

ComEd incorrectly argues the over 10 MW customer class should be eliminated. (ComEd Br. at 197). ComEd argues that it has presented extensive factual evidence in direct and rebuttal supporting the conclusion that the underlying cost of service for the four largest non-residential customer classes was sufficiently close to justify combining these classes. (Id.). However, as noted above, ComEd provided no evidence in its direct case establishing the underlying cost of serving the four largest rate classes. Indeed, IIEC witnesses noted that ComEd had failed to present any study which separately identified the cost of serving these four classes. (Stephens IIEC Ex. 1.0 at 15:276-284; Chalfant IIEC Ex. 2.0 at 9:164-171, 10:182-185). IIEC also presented testimony demonstrating the flaw in the two rationales offered by ComEd, in its direct testimony, for combining the rate classes. IIEC demonstrated that contrary to ComEd Crumrine's position, the similarity in "charges" for the rate classes did not justify combining the classes because there was no similarity in the charges applicable to those rate classes. They were, in fact, very different. (Stephens IIEC Ex. 1.0 at 7-8:Tables 1 and 2). The over 10 MW distribution facilities charge is about one-half the distribution facilities charge (DCF") for the other rate classes. (Id. at 11:198-199). IIEC also demonstrated that contrary to Mr. Crumrine's position on direct, elimination of the CTC did not justify combining these rate classes. (Id. At 12:206-225). In fact, since the charges applicable to the rate classes were actually different, application of ComEd's logic in its direct case would dictate against the combination of these rate classes.

IIEC also presented evidence that the cost of serving the over 10 MW customers was different than the other classes. This evidence demonstrated that the cost of serving the over 10 MW class on a per kW basis was different from the other three classes. (Chalfant IIEC Ex. 2.0 at 11-12:206-241).

ComEd's reliance on the cost of service study that it presented in its last case (ICC Dkt. 01-0423) is also misplaced. (*See* ComEd Br. at 197-198). The study is not relevant to the issue at hand. As discussed above in Section III.H.1.b., the study was not accepted by the Commission for the purpose of intraclass revenue allocation in that case. It also was based on non-residential rate classes that included 69 kV and over customers (which ComEd has placed into a separate rate class in this case). (Chalfant IIEC Ex. 2.0 at 9-10:179-182). Therefore, by definition, it reflects the cost of serving 1 to 3 MW customers, over 3 MW customers to 6 MW customers, over 6 MW customers to 10 MW customers, and over 10 MW customers, including the 69 kV customers in those classes. The appropriate measure is the cost of serving those classes, absent the 69kV customers, which are now to be in a separate HVDS class under ComEd's proposal in this case. (*See* ComEd Br. at 203).

Finally, ComEd's reliance on the new cost of service study presented in rebuttal, is misplaced. It has been demonstrated that when properly viewed, it shows a significant cost differential associated with serving the 10 MW and over customer group. ($5.12/kW for over 10 MW, $6.41 for the 1 MW to 10,000 kW classes.) (Chalfant IIEC Ex. 6.0 at 4:Table 1, 5:78-82). Thus, even evidence presented by ComEd demonstrates that over 10 MW customers impose costs on the system that are different from those of the other three rate classes ComEd proposes to combine into the Very Large Load Class.

As noted above, IIEC witness Chalfant testified the Company's rebutal study showed it was 25% less costly to serve the over 10 MW class on a per kW basis than it was to serve the other customers in the Very Large Load Class (1 to 10 MW). (Chalfant IIEC Ex. 6.0 at 3:54-57). His analysis was illustrated in Table 1 of his rebuttal testimony. (Chalfant IIEC Ex. 6.0 at 4:Table 1). ComEd criticized this analysis, suggesting that Mr. Chalfant had used "inappropriate" billing determinants. (Alongi/McInerney ComEd. Ex. 41.0 at 37:863-866). However, the record shows that even if ComEd were correct in its criticism of Mr. Chalfant's use of "inappropriate" billing units, there would still be a 20% difference in the cost of serving the over 10 MW class versus the 1 to 10 MW customers. (McInerney Tr. 1360-1361). Therefore, IIEC's fundamental position that there is a significant difference between cost of serving the over 10 MW class and the 1 to 10 MW customers is still correct.

Furthermore, ComEd's criticism of Mr. Chalfant's analysis is misplaced. Mr. Chalfant used the same billing determinants that ComEd witnesses Alongi and McInerney provided to ComEd's cost of service witness Mr. Heintz in the context of its direct case. (McInerney Tr. 1356). Mr. McInerney testified that in providing the billing determinants they intended to provide "accurate" information. (Tr. 1356-1357). The billing units used by Mr. Chalfant reflected the current definition of MKD and the billing units used and the Company's criticism of Mr. Chalfant reflected the Company's proposed definition of MKD. In addition, Mr. Chalfant did exclude the Pumping class billing units from his analysis. However, the pumping class represents less than 1% of the Very Large Load Class on a per kWh basis. (McInerney Tr. 1354-1355). In any event, Mr. Chalfant calculated a 25% difference between the kW cost of serving over 10 MW customers and the per kW cost of serving 1 to 10 MW customers, even if he had used the numbers ComEd deems appropriate, he difference would still have been 20% as noted above.

ComEd's position in this case is also believed by the positions taken by ComEd witness Crumrine in the original delivery service case. In that case, Mr. Crumrine rejected proposals to combine six of ComEd's rate classes into a single rate class stating:

> The inescapable mathematical result of that process would be to systematically lower the rates for those at the smaller end of the spectrum and increase rates for customers at the higher end of the spectrum. I do not believe this level of revenue shifting and cost shifting is appropriate. (*See* Stephens IIEC Ex. 1.0 at 14:243-271 quoting from Mr. Crumrine's testimony in Dkt. 99-0117).

The principle is the same in this case. The inescapable mathematical result of combining the four largest non-residential rate classes would be to systematically lower rates for those at the smaller end of the spectrum and increase rates for customers at the higher end of the spectrum. Mr. Crumrine, and hence ComEd, should have rejected the concept for combining these classes for the same reasons it rejected such a concept in Docket 99-0117. The Commission apparently agreed with ComEd in Docket 99-0117 because it did not combine the rate classes which were the subject of Mr. Crumrine's testimony in that case. (*See* Commonwealth Edison Company, 1999 Ill. PUC Lexis 647*115-117).

In sum, substantial evidence presented by IIEC demonstrates there is no similarity between the cost to serve over 10 MW customers and the cost to serve the other three non-residential rate classes ComEd proposes to combine. ComEd's own evidence demonstrates there is no similarity, there is a substantial difference. Therefore, a separate class for over 10 MW customers should be retained.

b. ComEd's Alternate Proposal

ComEd has offered an alternative proposal if the Commission concludes the over 10 MW customer class should be retained. Under this proposal, ComEd would phase in the distribution facility charge (DFC) between this case and the next case for these customers. ComEd indicates that if the Commission chooses "this approach," it is critical that the 24-hour MKD be approved because it alleges the two issues are linked. (ComEd Br. at 199). IIEC is not altogether clear on whether ComEd is suggesting that the 24-hour MKD approval is linked to its proposal to phase in the DFC charge for 10 MW and over customers, or the retention of a separate class for 10 MW and over customers. Because this proposal was presented in surrebuttal, IIEC did not have the opportunity to respond.

ComEd argues that under current rates a non-residential customer is assigned to a customer class based on the highest 30-minute demand during the demand peak period. (i.e., 9:00 a.m. to 6:00 p.m. Monday through Friday, excluding holidays) in the preceding twelve months. (ComEd Br. at 199). ComEd also notes that under current rates charges to the over 10 MW delivery service class are lower than they are for the three delivery service classes with loads of over 1 MW and up to 10 MW. ComEd also states that ComEd measures the customer's MKD (to which the DFC applies) only during the demand peak periods in the current billing month. (ComEd Br. at 199). All of these factors together, according to ComEd, give customers with very large and highly flexible loads, the incentive 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 charges, to which over 10 MW customers are currently entitled. (ComEd Br. at 199). ComEd's "perverse incentive" argument is without merit.

First, ComEd's brief ignores the fact that to the extent such an incentive may exist (and IIEC does not agree that it necessarily will), it exists regardless of whether or not the definition of MKD is changed. ComEd witness Crumrine admitted as much (*See* Crumrine Tr. 2279) agreeing that customers will still have incentive to game the system as alleged by ComEd even if the MKD definition is changed. Therefore, there is no linkage between MKD and the retention of the over 10 MW class or the level of the DCF.

Second, to the extent such an incentive allegedly exists, it also exists under the current rate structure, ComEd has failed to present a scintilla of evidence that large customers with highly flexible loads have actually gamed the system, in the manner described by ComEd, under the current class rate structure and/or the current definition of MKD. Indeed, ComEd has presented not one whit of evidence to suggest that any customer under the current rate classes has "gamed" the system as described by ComEd, much less very large customers with highly flexible loads.

Third, ComEd's argument is deficient in logic because it would seem that it would be the smaller customers with less flexible load who would have the greatest incentive to act in the manner described by ComEd (shifting load from off-peak to an on-peak period one 30-minute period per year) in order to qualify as a member of a larger demand class in order to secure the benefit of lower charges.

Fourth, ComEd's new definition of MKD does not alter the fact that customers would still have the opportunity to set their demand at any 30-minute period during the year in order to establish eligibility for the over 10 MW class.[22] Indeed, ComEd's rate structure would allow, in theory, customers to set their demand for any 30-minute period during the year in order to become eligible for ComEd's proposed new rate class of 1 MW and over customers. Thus, the potential for gaming, as described by ComEd, will exist regardless of whether ComEd changes the definition of MKD. ComEd's argument is obviously a red herring and should be rejected by the Commission.

With respect to maintaining the over 10 MW class, ComEd claims that IIEC proposes some form of an "across-the-board" increase. (ComEd Br. at 200). ComEd also alleges that such proposals would maintain a subsidy that it claims currently exists for the over 10 MW class. IIEC's proposal is not an across-the-board increase. Under IIEC's proposal, the over 10 MW class would receive an increase larger than the average increase for the other three classes that ComEd proposes to combine.[23] Thus, ComEd's alleged subsidy, assuming one exists, would be reduced under IIEC's approach.

However, the evidence in the record shows that it is actually less costly to serve the over 10 MW customer group than it is the other three rate classes which ComEd proposes to combine. (Chalfant IIEC Ex. 2.0 at 11-12:206-241; Chalfant IIEC Ex. 6.0 at 4:Table 1). Therefore, there is no subsidy as alleged by ComEd.

Next, ComEd argues that complaints about percentage increases ranging from 106% to 160%

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[22]ComEd has not proposed to change this provision in its tariffs. (*See* ComEd Ex. 10.1, Sheet No. 365).

[23]As shown on Tables 1 and 2 of IIEC Ex. 1, at pages 7-8, under ComEd's proposal, the rate changes for the 1-3 MW, 3-6MW and 6-10 MW classes range from a 35% <u>decrease</u> to a 22% increase. In contrast, IIEC's proposal would increase over 10 MW customers' rates by 25.7%. (See IIEC Br. at 7 as corrected by May 1, 2006 Errata.)

in the delivery service rates for the proposed over 10 MW class do not "tell the whole story." (ComEd Br. at 201). ComEd then points to testimony offered by ComEd witness Crumrine to the effect that the proposed Very Large Load Delivery Class and the proposed HVDS delivery class would pay less on a cents per kWh basis than the residential class and the watt-hour non-residential class. (ComEd Br. at 201). ComEd's argument is misleading. First, the impact of ComEd's proposed delivery service rates for large customers are demand based, not energy based. (Stephens IIEC Ex. 5.0 at 18:420-425). Therefore, they should be judged on a demand basis, not an energy basis. (Id.). It defies common sense to suggest that increases in delivery service charges of 106% to 160% are not serious because customers are paying only pennies per kWh. ComEd is well aware (or perhaps given its argument it is not aware), that larger customers purchase huge quantities of energy, and relatively small changes in the cost, even on a per kWh basis, can have significant impact on these customers. To the extent that ComEd is not aware of this circumstance, this may explain some of its unreasonable, and from the large customers point of view, costly proposals for rate design in this case.

Furthermore, ComEd's implication that comparison of the costs of very large load customers, some of whom take service at 138,000 volts, with the cost of residential customers who take service at 120/240 volts is irrelevant. (Stephens IIEC Ex. 5.0 at 19:426-431). Therefore, suggesting or implying that the Commission should ignore the impact of ComEd's rate design proposals on larger customers such as 138,000 volt customers, because that customer is already paying a lower rate than a residential customer served at 120/240 volts is irrelevant and meaningless to the decision making process in this case. The Commission should ignore ComEd's argument.

Finally, in sum, ComEd's attempt to link the 24-hour MKD issue with its improper consolidation of customer classes should be rejected. There is no link between the changing of the definition of the MKD and the proposal to combine customer classes, ComEd's arguments to the contrary not withstanding.

3. Environmental Cost Rate Design

The Staff argues that its environmental cost rate design is appropriate because ComEd's delivery service rates fails to account for environmental production costs. (Staff Br. at 93). It goes on to argue that the costs in question are quite difficult to quantify. It states that under its proposal there would be minimal impact on customer energy usage. (Staff Br. at 97). It further notes that some customers' bills will go up and some will go down. (Staff Br. at 98). The costs in question are not part of ComEd's revenue requirement. (Staff Br. at 96). It also implies that these issues are being address or will be addressed in the context of the sustainable energy plan. (Staff Br. at 95-96). Yet, Staff argues that its approach will send "accurate price signals" to customers and provide environmental benefits. While IIEC agrees these are laudable goals, it respectfully suggests there has been no demonstration the Staff's proposal will actually achieve either of them. In fact, under the circumstance described in Staff's brief, it is difficult to see how they could be achieved or how the Commission can determine whether or not they are being achieved. The price signal being sent cannot be quantified. It will have minimal impact on energy usage and will increase some customers' bills while decreasing other customers' bills, thereby encouraging or discouraging additional energy use as the case may be.

Furthermore, Staff's suggestion that environmental costs are already reflected in delivery service rates through the nuclear decommissioning rider, (Id. at 96) overlooks the fundamantal fact that the nuclear decommissioning rider is creature of statute. (Lazare Tr. 587). In addition, there apparently is no other provision in the Act which would allow the recovery of environmental production costs that are not part of the utility revenue requirement. (Lazare Tr. 587-588). The nuclear decommissioning rider is set to expire at the end of 2006. (Lazare Tr. 588).

The Staff's concerns are better addressed in a different forum and/or context. For the reasons stated above, Staff's proposal should not be adopted in this case.

4. Rider ECR

ComEd states: "The main issue between the parties in testimony was how ComEd's environmental costs were to be recovered." (ComEd Br. at 204). However, the issues raised by ComEd's proposed Rider ECR begin before one contemplates what cost recovery process should be used. Specifically, there are serious unanswered questions about the scope and definition of the costs ComEd proposes to recover.

a. Rider ECR's Definition of Recoverable Costs Is Unlawfully Vague

ComEd's Initial Brief does little to reduce the vagueness of the costs encompassed by the over-broad language of the proposed rider. (*See* IIEC Br. at 42-43). The broad scope and the imprecision of Rider ECR's definition of recoverable costs are sufficient reasons to reject the rider. Yet, ComEd's initial brief does not address cost definition issues at all.

Instead, from the Commission's prior approval of MGP cost recovery riders for other utilities, ComEd leaps to the conclusion that the matter is already settled for its full range of environmental costs. ComEd characterizes MGP and non-MGP costs as "virtually identical," with "no reasonable distinction" between them. (ComEd Br. at 211). Neither conclusion is supported by the evidence or the authority of the decisions ComEd cites.

ComEd observes that IIEC has not challenged the Commission's policy position on the recovery of MGP costs.[24] But, ComEd seeks Commission approval of a specific tariff rider, not a policy. The proposed rider contains provisions that use specific, consequential language that has never been considered or approved by the Commission. And, ComEd has cited no similarly broad Commission policy of rider recovery for all non-MGP environmental costs.

As IIEC emphasized in its Initial brief, the Commission should not approve automatic, dollar-for-dollar, rider recovery of costs as poorly defined as those encompassed by the language of the proposed rider.

> The precise scope of those terms, indeed whether they have any bounds at all, remains uncertain. Indeed, on its face, Rider ECR is broad enough to authorize recovery of nuclear plant clean-up costs at sites formerly owned by ComEd.

(IIEC Br. at 43 (note omitted)). The scope and nature of ComEd's non-MGP costs are especially problematic. The proposed rider's inclusion of litigation expenses would compromise ComEd's economic incentive to protect itself and its customers from avoidable litigation or excessive legal fees and costs. (IIEC Ex. 3.0 at 52-53:1172-1179).

Especially troubling are the rider provisions that purport to define the rider's boundaries, yet

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[24]IIEC notes that the Commission established that policy during the period when Illinois utilities integrated their transmission and distribution functions with generation, which is the source of many of the environmental costs at issue. (*See* ComEd Br. at 213, n. 68 and cases cited therein).

explicitly reject any limitation, and ComEd's refusal to narrow the definitions or even to address cost definition issues. Identification of recoverable costs under Rider ECR requires interpretation of the rider's interwoven definitions of "Environmental Activities" and "Incremental Costs."

> "**Environmental Activities**" mean activities performed by or for the Company that include, but are not limited to, the investigation, sampling, monitoring, testing, removal and response measures, disposal, storage, remediation, or other treatment of environmental contamination, including the operation and maintenance of remediation and treatment measures, which environmental contamination is subject to applicable federal, state, or local laws and regulations. Environmental Activities include, but are not limited to, such activities conducted or implemented to address contamination at, or associated with, former manufactured gas plant sites.

The rider's separately stated definition of Incremental Costs also disavows any limitation suggested by its equally lengthy list of specific, included items.

> "**Incremental Costs** mean costs incurred by the Company in association with Environmental Activities and include, but are not limited to . . .")).

These definitions are essentially unbounded, using language so sweeping that through Rider ECR approval, the Commission might inadvertently open a door to recovery of nuclear clean-up expenses at sites ComEd no longer owns.[25]

Examples of how these expansive definitions may operate in the future are presented in the City's Initial Brief. ComEd claims the right to recover -- in addition to costs of legally mandated remediation -- costs it incurs to prepare property for sale. Such sales need not benefit customers. (*See* City Br. at 4). Also, ComEd lists numerous statutes as sources of the environmental costs it

[25] Under certain environmental statutes, prior ownership of a site can support possible liability for certain environmental costs. ComEd could easily narrow the rider definitions, but declined any such change in its revised proposed rider . (*See* ComEd Ex. 23.3).

wishes to recover. However, even though ComEd concedes that it is not subject to some of the statutes it listed, the rider's language does not limit recovery to legally required costs in any case. (*See* City Br. at 3).

ComEd argues that "neither Mr. Gorman nor any other witness challenged ComEd's figures that show the volatile and fluctuating nature of environmental remediation costs." (ComEd Br. at 214). IIEC questions whether the demonstrated cost variability, which exists for many costs recovered through base rates, justifies special tariff treatment, not the accuracy of ComEd's limited data. (*See* IIEC Br. at 45-46).[26] ComEd's information is only a small subset of the costs encompassed by the rider's language. In any case, the nature of costs that may be recoverable under the rider's broad language actually is impossible to determine, precisely because those costs are so poorly defined.

ComEd's Initial Brief presents nothing to diminish the gravity of the scope and nature objections raised in IIEC's Initial Brief. (IIEC Br. at 42-47). The precision of recovery and ratepayer protection ComEd promises cannot be achieved with such vague definitions. Commission approval of special, automatic recovery for such vague and expansively defined costs is not just and reasonable

[26]ComEd also resurrects testimony from a case almost 15 years old to support its claim of cost volatility. Apparently ComEd expects Mr. Gorman to hold fast to an outdated position without consideration of how circumstances have changed in the interim. Changes in relevant factors like the connection to regulated services, the effect on utility earnings and how costs being assessed are defined make ComEd's self-serving presumption that Mr. Gorman's position in this case should be the same wholly unrealistic and unreasonable.

b. ComEd's Threshold for Rider Recovery Is Unlawfully Low

Riders are exceptional recovery vehicles in Illinois ratemaking. They are departures from the Commission's established regulatory rate case model (*see, e.g.,* 83 Ill. Adm. Code Parts 285, 287), which recognizes that as some costs increase and others decrease, ratepayers should be burdened only with the net revenue requirement.[27] Riders have been deemed appropriate only where costs are "unexpected, volatile, or fluctuating expenses which [the utility] cannot control." (*Finkl & Sons v. ICC*, 250 Ill. App. 3d 317 (1993) ("*Finkl*") at 327; *also CUB v. ICC*,166 Ill. 2d 111 (1995) ("*CUB*") at 138). However, such recovery has not been automatic. Costs with those characteristics that also were "not significant" in magnitude and "recoverable through the usual base rate mechanism" have been rejected as unlawful. (*Finkl* at 327). The Finkl court also validated concerns about an imprecise definition of the costs to be recovered through a rider. (Id. at 333) noting a Commissioner's concern that the utility had been given "essentially a blank check for these vague . . . expenses"). In this case, each of those factors is implicated by ComEd's overly broad and poorly-defined environmental cost recovery proposal.

ComEd has prepared remediation programs for many sites and categorized budgets more than ten years into the future. Thus, the costs at issue are clearly not "unexpected" or entirely unpredictable. These are costs that "reveal no greater potential for unexpected, volatile or fluctuating expenses which Edison cannot control, than costs incurred in estimating base ratemaking." (Id. at 327). As Mr. Gorman's testimony, the Act and relevant case law suggest, any

[27] Accordingly, courts have held that ratemaking costs should not be treated in isolation -- the prohibition on single-issue ratemaking. *(See generally CUB and Finkl).*

reasonable exercise of the Commission's discretion should consider the magnitude of the costs, the clarity of the cost specification, the effect of a rider on management behavior, and the impact on rate predictability and continuity, in addition to threshold cost characteristics. Against these more reasonable detailed criteria, ComEd's Rider ECR proposal falls short.

ComEd's assertion of an entitlement as to all environmental costs is unsupported. ComEd has identified no authority that <u>mandates</u> rider approval upon a minimalist showing of volatile, unexpected or fluctuating" costs (CUB at 138) -- irrespective of cost magnitude, susceptibility of the costs to base rate recovery, or rider tariff terms. This exceptional mechanism remains a matter of Commission discretion.

c. ComEd's Revenue Requirement Arguments Are Unsupported

ComEd's brief suggests that only a rider can assure absolute precision in environmental cost recovery. (ComEd Br. at 209). That has never been the standard for utility ratemaking. Such precision is not required, even for the larger cost amounts recovered through base rates. As Mr. Gorman testified, utility rates should be set to provide an opportunity to earn authorized returns.

ComEd is less concerned with the accuracy of cost recovery when adjusting for rejection of the rider. If the rider is rejected, ComEd proposes a method of cost recovery that allegedly allows recovery of more expenses than shown on ComEd's books. (Hill Tr. 885). ComEd asserts that the Commission permitted such recovery in Dkt. 01-0423. (ComEd Br. at 211). However, ComEd provides no citation to the record or the Dkt. 01-0423 order where this methodology is explained or adopted. IIEC urges the Commission to reject any such over-recovery in this case, even if the Commission previously permitted it.

d. ComEd Still Has Not Shown That Its Non-MGP Costs Are Delivery Services Costs Or Prudently Incurred

ComEd sweepingly asserts (without citation) that "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." (ComEd Br. at 211). More accurately, IIEC questions whether certain non-MGP environmental costs that appear related to ComEd's transferred or sold generation assets are prudently incurred.

ComEd has provided no evidence that its non-MGP site costs are related to the provision of delivery services. As discussed above, ComEd does not limit its rider recovery to remediation tasks or other legally required costs. Even where a company is legally required to incur certain costs as to stay in business (*See CUB*), recovery of those costs through regulated delivery service rates nonetheless requires that they be reasonable and prudently incurred.[28] 220 ILCS 5/9-201. ComEd's brief does not address these issues of the prudence and reasonableness of the (ill-defined) costs at issue.

There is an obvious connection between many of the sites and ComEd's previous generation assets and activities. The costs ComEd seeks to recover through a rider remain in the delivery service company only because ComEd (perhaps imprudently) failed to protect its ratepayers from such generation related potential costs. ComEd presented no evidence to explain its decisions to retain such generation sites, without obtaining indemnification agreements or other protection

[28]To the extent that ComEd is relying again on an argument that all costs remaining after generation assets were divested can properly be assigned to delivery services, the Commission has rejected such attempts at automatic inclusion in regulated costs of service. (*See* Order, Dkt. 01-0432, issued Mar 28, 2002 and Section III.E.1, *supra*).

against generation related environmental expenses. ComEd's failure to protect ratepayers calls into question the prudence of the resulting costs.

ComEd's proposed Rider ECR , which covers much more than the MGP costs recovered by other utilities, (1) fails to meet the applicable requirements for the exceptional mechanism of cost recovery through a rider and (2) is so vague as to amount to a blank check drawn on ComEd ratepayers. It must be rejected. In testimony, ComEd had argued that because the average common equity ratio it calculated for Staff's proxy group was higher than Staff's proposed common equity ratio for ComEd, Staff's capital structure increased ComEd's financial risk above that of the proxy group. ComEd then suggested that its return on equity should, therefore, be higher than the Staff recommendation developed using that proxy group. This ROE argument is addressed further in Section III.E.3, *infra*.

17. Rider RESALE

ComEd, CES, BOMA and IIEC support the modification to proposed Rider RESALE recommended by ComEd in its rebuttal testimony in this proceeding. (*See* CES Br. at 20; IIEC Br. at 47-48; BOMA Br. at 17-18).

The Staff, in its Initial Brief, takes the position that the Staff does not object to modifications to Rider RESALE as set forth in the surrebuttal testimony of ComEd witnesses. (Staff Br. at 121). IIEC does note that one of Staff's concerns was that the eligibility provisions of the Rider have been expanded. IIEC notes that ComEd witness Alongi testified that proposed Rider RESALE and current Rider 12 both limit the eligibility to those retail customers who have been reselling electricity since 1957. (Alongi Tr. 1293). Staff was concerned this was not the case. (Staff Br. at

120).

Because no party opposes modification of Rider RESALE as proposed by ComEd in its rebuttal testimony, the Commission should adopt same.

22. Proposed Change in Definition of Maximum Kilowatts Delivered

ComEd argues that its proposal to change the way usage for "certain large customers" is defined for billing purposes is one of the most "misunderstood" issues in the case. (ComEd Br. at 243). If the issue is misunderstood, then part of the reason for the misunderstanding is in ComEd's suggestion that this issue affects only "certain large customers." ComEd's proposal applies to all customers in the current demand rate classes from the smallest (0-25 kW) to the largest (over 10 MW). (*See* ComEd Ex. 10.1, Sheet Nos. 364-365, 368, 369 showing the applicability of the MKD). Any misunderstanding is also associated with ComEd's own misleading assertions and arguments regarding the linkage between this issue and the retention of the 10 MW and over class and/or the phase-in of the DCF charges for over 10 MW customers when there is no such linkage. IIEC demonstrated **CONFIDENTIAL MATERIAL BEGINS** xxxx xxxxxxxxx xxxx xxxx xxxxxx xxxxx xxxx xx xxxxxxxxx xxxxxxxx xx xxxxxxx xxxxxxxx,xxxxxxxxxx xxxxxxxxx xx xxxxx xx xxxxx xx xxx xxxxxxx xxxxx. **END OF CONFIDENTIAL MATERIAL**. (Stephens IIEC Ex. 8.0 (Confidential) at 12:246-249).

ComEd also implies that maintenance of the current definition of MKD would somehow prevent a determination of the delivery classes applicable to customers; the determination of standard distribution facilities provided customers; and the determination of charges applicable to customers for those standard distribution facilities. (ComEd Br. at 244-245). This argument overlooks the fact ComEd and the Commission have apparently been able to determine the delivery classes applicable to customers under the current definition of MKD, in every delivery service rate case filed by ComEd, since the adoption of the Customer Choice and Rate Relief Law of 1997. It also overlooks the fact that ComEd and the Commission have apparently been able to determine the standard distribution facilities provided to customers in each of those cases. Finally, it overlooks the fact that ComEd and the Commission have apparently been able to determine the charges applicable to customers in each of those cases as well. In each instance, the current definition of MKD was obviously applicable. Therefore, none of those determinations appear to be dependent on the Commission's adoption of ComEd's proposed definition of MKD in this case.[29]

ComEd also suggests that its proposed 24-hour MKD is consistent with the approach to classifying supply groups on a 24-hour demand basis in the recent ComEd power procurement case. (ComEd Br. at 245). This ComEd argument appears to be in direct conflict with the testimony of ComEd witness Crumrine in this case. He testified that evidence that ComEd's proposed delivery service rate classes did not conform to the customer classes proposed in the power procurement cases and would not assist the Commission in understanding ComEd's proposal to combine the rate classes. (Crumrine ComEd Ex. 23.0 at 23:544-555). He stated because:

> ComEd has not suggested that its delivery service rate customer classes should be aligned directly with the procurement supply groups. (Crumrine ComEd Ex. 23.0 at 26:547-548).

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[29]IIEC notes that this faulty ComEd assertion was first suggested by ComEd in its surrebuttal testimony, and therefore, no party had an opportunity to respond to this position in the context of their testimony. (*See* ComEd Br. at 199 citing to ComEd witness Crumrine's surrebuttal testimony. (ComEd. Ex. 40.0 Corrected).

Mr. Crumrine went on to state that:

> . . . the whole concept of aligning supply groups with delivery service customer classes is suspect. (Id. at 548-549).

ComEd now appears to have changed its mind in making this argument that it is desirable to have consistency between the customer supply groupings from the power procurement case and the customer groupings for delivery service. The Commission should not accept the argument, since ComEd's own witness has testified that it is "suspect."

ComEd also argues that the vast majority of its customers would not be affected by this proposal. (ComEd Br. at 245). ComEd conveniently overlooks the fact that all customers billed on a demand basis would be affected. (*See* Stephens Ex. 8.0 (Confidential) at 11-12:237-254; Stephens Ex. 8.1 (Confidential)). Therefore, the "vast majority" of customers would be affected.

ComEd argues that because of the size of the demand of its largest customers, it must install facilities that are sized to meet the customer's maximum demand. Therefore, shifting load from peak to off-peak cannot have an effect on the manner in which ComEd sizes its distribution facilities to serve these customers. (ComEd Br. at 245). However, ComEd ignores the fact that the distribution facilities in question are "dedicated facilities only". ComEd has not suggested, and cannot suggest, that there are not other portions of the distribution system which are installed to meet on-peak demands. Indeed, ComEd's own cost of service study recognizes this fact. (*See* ComEd Br. at 205).

Next, ComEd argues that customers who use the distribution system outside of the demand peak period receive a free ride under the current MKD definition. (ComEd Br. at 246). ComEd appears to assume that these customers provide absolutely no benefits to the distribution system in their decision to operate off-peak or that they pay nothing toward the cost of facilities to serve them. However, ComEd's position ignores the fact that much of the distribution system is shared or "system" facilities. Its position appears to be based exclusively on "dedicated facilities." ComEd fails to acknowledge the benefits of ComEd's operation of lower coincident demands due to customers operating primarily during off-peak periods. ComEd also ignores the beneficial impacts to the cost of shared distribution facilities resulting from lower coincident demands due to off peak operations. (*See* Stephens IIEC Ex. 8.0 (Public) at 4; *see also*, Lazare Staff Ex. 23.0 (Corrected) at 2-4:36-96). Even ComEd witness Crumrine agreed ComEd would have a zero capacity obligation with PJM for customers who do not contribute to the system peak. (Crumrine Tr. 2287). Also, ComEd ignores the fact that many of these customers, to the extent they use non-standard facilities, pay for those facilities through current Rider 6. Therefore, they cannot, by definition, be receiving a free ride. They will continue to do so under ComEd's proposed Rider NS if approved by the Commission in this case. (Crumrine/Alongi ComEd Ex. 46.0 at 27:565-573).

a. ComEd's Proposed MKD Definition Actually Ignores the Reality of Distribution System Design

ComEd argues that parties have created confusion over how the proposed MKD relates to what investments ComEd must incur to serve its customers. (ComEd Br. at 246). In particular, ComEd suggests that Staff witness Peter Lazare is confused in failing to take account of facilities that are dedicated (or largely dedicated) for the use of a single customer. (ComEd Br. at 248). However, it is ComEd's approach that fails to take into account network facilities that are used to serve large numbers of customers, the cost of which can be favorably impacted by the diversity of customer demand. Next, ComEd, relying upon data presented to illustrate how one large customer, the CTA, influences the sitings of feeders to a certain power substation, suggests that no party has disputed this data or the implications of the data despite "four" opportunities to do so. (ComEd Br. at 248). IIEC respectfully points out that ComEd presented this data in its surrebuttal testimony and, therefore, parties actually had zero, not four, opportunities to address the data and its implications.

ComEd attempts to refute a hypothetical example that IIEC provided to demonstrate that while non-standard distribution facilities dedicated to individual customers have their costs driven by the highest demand of a single customer at any hour of the year, facilities that are used to provide service to many customers have their costs driven by the highest level of combined demand of those customers who are served by the shared facility. (Stephens IIEC Ex. 9.0 at 3). IIEC points out that this is not the same as the sum of the highest individual demands of all customers served by those facilities, which ComEd has asked the Commission to approve for billing purposes. (Id.). ComEd's proposal diverges from cost causation and results in higher bills to the very customers, that through their diversity, contribute directly to lowering distribution costs for ComEd and its other customers. (Id.). IIEC presented an example in support of its contention. (Id. at 3-4). ComEd claims that under the IIEC example, it would have to install 30 MW of dedicated facilities. However, ComEd ignores the fact that it would only have to size its network facilities under this scenario to meet 25 MW of load. The costs ComEd proposes to recover in this case are primarily costs of network facilities. ComEd has agreed it has other mechanisms to recoup costs of non-standard dedicated facilities through Rider 6 or Rider NS. (Crumrine/Alongi ComEd Ex. 46.0 at 27:565-573).

In sum, the Commission should not look at only part of the system cost in resolving this issue. The distribution system consists of more than the dedicated facilities, which ComEd continues to exclusively refer to in its argument. The Commission should also consider the benefits to ComEd's electrical system and other customers which accrue through the use of electric power and energy in off-peak periods. Indeed, ComEd, in its Brief cites to the plethora of testimony that supports the existence of these diversity benefits. (*See* ComEd Br. at 250 citing testimony of Staff, IIEC, IAWC and CTA). ComEd suggests the claims of these parties are based on a faulty understanding of the types of customers the 24-hour MKD proposal would affect. IIEC respectfully suggests that it is exactly those types of customers who are providing or have the potential to provide diversity benefits to the system as a whole and ComEd's other customers. Provision of this diversity should be encouraged, not discouraged, as proposed by ComEd.

Therefore, the current definition of MKD should be retained.

b. ComEd's Proposed MKD Definition and Alleged Intraclass Subsidies

ComEd argues the current MKD definition results in an intraclass subsidy. IIEC witness Mr. Stephens looked at this issue. He noted that IIEC had asked for workpapers and supporting analysis for the subsidy in discovery. ComEd had provided a one-page document which summarized the alleged subsidy for each of the existing demand rate classes from the smallest to the largest. He, therefore, concluded that ComEd was not able or willing to provide the backup data to verify the accuracy of its calculation of the dollar value of the alleged subsidy. (The exact response is attached to IIEC Ex. 8.0 (Confidential) as IIEC Ex. 8.1 (Confidential)). Indeed, it appears that the "large customers," ComEd is purportedly concerned about, actually account for less than a third of the alleged subsidy. In addition, a review of these exhibits will demonstrate ComEd has apparently made the calculation of the alleged subsidy on the basis of its proposed rates and rate design which are the subject of this litigation and may be determined differently than ComEd has proposed. ComEd cites to the Table 1 in the rebuttal testimony of ComEd witness Crumrine in support of its argument. (Crumrine ComEd Ex. 40.0 at 6:Table 1). On its face this Table demonstrates that the alleged MKD subsidy is overstated since some amount (ComEd says small) will actually be received from customers who operate in the off-peak periods. (Id., Fn. 6). Therefore, this calculation should not be relied upon for any purpose in this proceeding.

Finally, ComEd again argues that its proposal would affect only a relatively small number of customers. IIEC has demonstrated this is not the case. (*See* III.H.22 above). For all these reasons, ComEd's subsidy argument should be ignored.

c. Off-Peak Demands and Distribution Prices

ComEd discusses a portion of its response to certain questions raised by Commissioners Ford and Lieberman and present the results of a survey of other utility rates and their method for determining maximum billing demand. (ComEd Br. at 252). IIEC notes that approximately two-thirds of the utilities surveyed appear to recognize the need to reflect the benefits of off-peak demand in their delivery service rate design by recognizing on-peak demand for billing purposes. (*See* Crumrine/Alongi ComEd Ex. 47.1). Only about one-third take the 24-hour clock approach recommended by ComEd. The table in the ComEd brief is not an exact replica of the table in Mr. Crumrine's testimony. A review of that table shows that roughly 68% of the utilities surveyed apparently give some recognition to on-peak demands in designing their delivery service rates. The ComEd position in this case, therefore, appears to be a minority position.

In its discussions, ComEd's refers to a "demand ratchet." ComEd's discussion only leads to further "misunderstanding" with the MKD issue. Use of such a ratchet really has nothing to do with the distinction between on and off-peak periods. In fact, the utilities surveyed by ComEd and using a demand ratchet are using the demand ratchet to actually measure on-peak demand. The ratchet, therefore, has nothing to do with the distinction between on and off-peak periods. (*See* ComEd Br. Table at 252 Crumrine/Alongi ComEd Ex. 47.1).

In any event, the Commission should determine this issue based on the evidence presented in this case. The evidence presented in this case justifies retention of the MKD definition.

30. Rider ZSS7

ComEd implies there is no remaining disagreement on Rider ZSS7. (ComEd Br. at 30). Therefore, it does not discuss any of the issues raised by IIEC with regard to this Rider. IIEC's position is described in its Initial Brief. (*See* IIEC Br. at 53). IIEC will rely on the arguments made and the position taken in that Brief.

III. Conclusion

For the reasons stated herein, IIEC's position on the issues described should be adopted by the Commission.

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Respectfully submitted,

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