

Commonwealth Edison Company

ICC Docket: 05-0597

Corrected Page

REPLY BRIEF

Staff Init. Br. at 28 – 29. Staff argues that that decision should be disregarded as “inconsistent with the Commission’s long-standing practice,” citing three other Commission Orders, but Staff does not state whether this issue was raised in those cases. *Id.* More importantly, in all three of the cases, the utility sought and was allowed cash working capital.<sup>33</sup> The same reasons that prompted the ruling in Docket 01-0423 have been proved in this case. ComEd Init. Br. at 72. Staff’s proposed adjustment should be rejected.

## **8. Materials and Supply Inventory**

ComEd has included in its proposed rate base its inventory of materials and supplies as of December 31, 2004, the last day of the test year. ComEd Init. Br. at 72. Staff proposes that a 13-month average of ComEd’s materials and supplies inventory, less a figure for accounts payable associated with the materials and supplies inventory, be used instead, resulting in a proposed net deduction from rate base of \$1,609,000. Staff Init. Br. at 30.

Staff’s suggestion that materials and supplies balances are highly volatile, and thus should be averaged (Staff Init. Br. at 30), is not borne out by the evidence. Staff initially used a 13-month average for materials and supply inventory and a four-year period for associated accounts payable. Staff noted that, in response to ComEd’s criticism about the use of mismatched time periods for the proposed adjustment, Staff switched to the use of a 13-month average for accounts payable in its rebuttal. *Id.* Notably, had Staff used the four-year average methodology for both parts of its proposed adjustment, then the result would be a \$5,268,000 increase in the inventory (before functionalization and the accounts payable offset), and had Staff used the average of the 13-month averages for the last four years, then the result would be a

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<sup>33</sup> *Consumers Illinois Water Co.*, Docket 03-0403, p. 4 (Order April 13, 2004); *Central Illinois Public Service Co. (AmerenCIPS), et al.*, Docket 02-0798 Cons., p. 18 (Order October 22, 2003); *Illinois Power Co.*, Docket 01-0432, pp. 8-9 (Order March 28, 2002).

goals will occur even if the “financial” goals are not met. *Id.* at 13:281-84. In ComEd’s most recent delivery services rate case, the Commission found proper recovery of incentive compensation based on “*reduced operating expenses and ... greater efficiency.*” *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2003), at 121 (emphasis added). Indeed, the Commission has regularly recognized that incentive compensation programs that reward employees for lowering operating costs benefit customers. *See, Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2002); *Consumers Illinois Water Co.*, ICC Docket 03-0403 (Order, April 13, 2004); at 14 – 15; *Northern Illinois Gas Co.*, ICC Docket 95-0219 (Order, April 3, 1996), at 27. Accordingly, ComEd’s plan has provided incentives to its workers to improve ComEd’s performance on those measures that directly benefit customers, and those incentives have worked, as ComEd’s performance on each measure has improved. Thus, the Commission’s test is undisputedly met as to the “operational” measures.

Furthermore, the customer satisfaction aspect of ComEd’s plan is an “overlay” that affects the payout under the entire plan – both the operational and financial aspects. As Mr. Costello described:

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

Costello Sur., ComEd Ex. 30.0, 10:202-11. Both Staff and the AG ignore this salient fact.

The tangible customer benefits described above distinguish ComEd’s incentive compensation plan from the plan at issue in the Nicor Gas Co. rate case, ICC Docket 04-0779, cited by the AG. In that case, the Commission disallowed recovery because it “conclude[d] that the majority of the incentive compensation is based on financial goals,” in large part because

testimony is inconsistent with the fact that “the Company admitted that it had not made any specific incremental change to any other component of its total compensation package as a direct result of the Commission’s disallowing \$24 million of incentive compensation expense” in the prior DST case. *Id.* Staff ignores, however, that the Commission’s Order in that DST case *approved* recovery of more than \$33 million of incentive compensation based on operational measures. *Commonwealth Edison Co.*, ICC Docket 01-0423 (Order, March 28, 2003), at 122. In addition, ComEd did not increase any other aspect of compensation because of that partial disallowance for incentive compensation because ComEd continued to pay the full amount of requested incentive compensation despite the disallowance; therefore, ComEd did not need to increase any other aspect of compensation to make up for the partial incentive compensation disallowance. In any event, the fact that ComEd continued to pay incentive compensation despite not recovering for all of it does *not* represent a valid basis for denying recovery here.

Staff also highlights Mr. Costello’s testimony that a reduction in costs brought about by incentive compensation would generate “lower rates in the next [rate] case.” Staff Init. Br. at 55. Staff then claims that “Mr. Costello refuted his own claims by stating that in his 36 years at Commonwealth Edison, he is not aware of any time that the Company has filed for a rate decrease as a result of these alleged lower costs.” *Id.* Staff cannot seriously contend that they interpreted Mr. Costello’s testimony regarding reduced rates to mean that ComEd would, after a number of years of inflation and increased demand for service, request an overall decrease in rates. Mr. Costello was simply making the obvious point that, if operating costs are lower than they otherwise would have been due to incentive compensation, then rates in future rate cases will be lower *than they otherwise would have been* had incentive compensation not kept costs

more costs to the CTA than the sole use of CP does. *Id.* This self-serving proposal is without merit and should be rejected.<sup>67</sup>

## **2. Minimum Distribution System**

BOMA and the IIEC assert that ComEd's ECOSS should incorporate the minimum distribution system ("MDS") concept for accounts 364-368, although they generally recommend that the Commission direct ComEd to make this change in its next distribution rate case. BOMA Init. Br. at 6 – 7; IIEC Init. Br. at 28 – 30. As ComEd and Staff both pointed out in their Initial Briefs, the MDS is a flawed concept that the Commission has repeatedly rejected in past cases: *MidAmerica*, ICC Docket 01-0444, (Order Mar. 27, 2002), at 19; *Central Ill. Pub. Serv. Co.*, ICC Docket 00-0802 (Order, Dec. 11, 2001), at 41 – 42; *CIPS*, ICC Docket 99-0121, 1999 Ill. PUC Lexis 646, at \*163-164 (Order, Aug. 25, 1999); ComEd Init. Br. at 185; Staff Init. Br. at 91 – 92. As Staff explains in its initial brief, because the costs to connect different customers vary, the MDS would improperly shift costs. Staff Init. Br. At 90-91 The MDS should not be used in this or any future rate case proceedings. *Id.* BOMA and IIEC have provided no reasoned basis for the Commission to depart from its prior decisions on this point.

## **3. Marginal Cost Of Service Issues/Considerations**

ComEd continues to reserve its right to propose the use of a marginal cost study in future proceedings.

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<sup>67</sup> ComEd addresses the social policy arguments the CTA advances to lower its rate below cost in Section III.H.18, Rate RDS (CTA).

reasonable. CTA and METRA have not provided the Commission any reasonable alternative. Thus, the only options in the record are ComEd's original proposal or its compromise proposals. There is no evidence in the record for any alternative treatment for METRA and CTA.

c) **Retention Of The Railroad Customer Contracts**

The CTA and METRA each take the position that their respective contracts trump the Commission's authority. *See, e.g.*, CTA Init Br. at 24; METRA Init. Br. at 9. The CTA goes as far as to say that “[u]sing this proceeding to impose a new charge on the CTA would be contrary to the contract and such action would exceed the Commission's authority.” CTA Init. Br. at 24. Even further, the CTA states that Commission interference with those contracts would violate the Illinois and United States Constitutions. *Id.* at 28. This argument is meritless.

First, these parties seem to forget that the contracts themselves recognize the Commission's authority over them. Each of the contracts specifically provides that the contract is subject to Commission approval and modification. *See* ComEd Init. Br. at 238 – 239; CTA Ex. 3.2; METRA Cross Ex. 1.0. The argument that these contracts somehow bind the Commission—even though they require Commission approval—defies logic. The argument is a non-starter and should be ignored. Moreover, the Commission has the authority to modify any contracts it deems, in its discretion, to contain unjust or unreasonable rates. *See* 220 ILCS 5/9-102.1(d); *see also* *Citizens Utility Bd. v. Illinois Commerce Comm'n.*, 275 Ill. App. 3d 329, 655 N.E.2d 961 (1<sup>st</sup> Dist. 1995) (holding that contracts allowing a utility and its customers to negotiate rates without Commission and public input were invalid).

Indeed, Staff took the position that the Commission should eliminate the tariff contracts for CTA and METRA and replace them with Rate BES-RR. *See* Hanson Dir., Staff Ex. 7.0, 11:242 – 12:262. Staff is correct with respect to the Commission's authority. That is, the Commission has the authority to terminate these contracts. However, ComEd is not advocating