

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

COMMONWEALTH EDISON COMPANY)	
)	
)	Docket No. 05-0597
Proposed general increase in rates for delivery service)	
)	

**BRIEF ON EXCEPTIONS OF THE
STAFF OF THE ILLINOIS COMMERCE COMMISSION**

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Table of Contents

	<u>Page</u>
I. INTRODUCTION	1
II. PROCEDURAL HISTORY	2
III. STATEMENT OF UNCONTESTED ISSUES.....	2
A. Issues That No Party Contests	2
1. Elements of Rate Base	2
a. Staff Adjustment Related to ComEd Schedule B-2.1	2
b. Pro Forma Capital Additions and Construction Work In Progress	3
2. Other Issues.....	3
a. Exelon GSA-Reporting Requirements	3
IV. ARGUMENT ON CONTESTED ISSUES.....	4
A. RATE BASE	4
1. General Plant: Functionalization and Amount; Intangible Plant: Functionalization and Amount.....	4
a. ComEd Has Not Explained Why G&I Should Increase by \$304 Million; A General Labor Allocator Should be used to Functionalize G&I	4
b. Staff’s Position Should Include Staff’s Reply Brief Arguments.....	11
2. Pension Asset	13
3. Customer Deposits.....	24
4. Budget Payment Plan	26
5. Materials and Supplies Inventory	27
6. Procurement Case Expenses [Rate Base Effect]; Rate Case Expenses [Rate Base Effect]	28
7. Procurement Case Expenses Recovery Mechanism	33
8. Recovery of Unamortized Balances of Rate and Procurement Case Expenses	33
9. Staff Adjustment Related to ComEd Schedule B-2.1	34
B. OPERATING EXPENSES AND REVENUES	37
1. Administrative & General Expenses.....	37
a. Overall Amount.....	37
2. Incentive Compensation.....	44

3. Uncollectibles Expenses	44
4. Environmental Expenses.....	44
5. Payroll Taxes	47
C. RATE OF RETURN	48
1. Capital Structure	48
2. Cost of Long-Term Debt.....	54
3. Cost of Common Equity	56
4. Approved Rate of Return on Rate Base.....	59
D. RATE DESIGN	60
1. Customer Class Delineations	60
a. Residential	60
2. Environmental Cost Rate Redesign	61
3. Rider ECR	63
4. Rider NS.....	63
a. Rider NS and Elimination of Rider 8	63
(1) PO Incorrectly Describes ComEd’s Position.....	64
(1) ComEd	66
(2) ComEd has not Shown that Terminating Rider 8 is “Just and Reasonable”	67
(3) If ComEd’s Alternative Proposal is Accepted then PO Needs Modification	73
5. Rider POG.....	74
6. Supply Administration Charge.....	77
7. Real Time Pricing Meters and Energy Smart Pricing Plan	79
8. Rider ZSS7.....	84
9. Rate BES-L	84
10. Tariff Implementation Issues	85
V. STAFF REPORTS ON COMED’S PERFORMANCE	88
A. Electric Metering.....	88
VI. CONCLUSION.....	89

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Now comes the Staff of the Illinois Commerce Commission ("Staff"), by and through its undersigned attorneys, and pursuant to Section 200.830 of the Rules of Practice of the Illinois Commerce Commission ("Commission"), 83 Ill. Adm. Code Section 200.830, respectfully submits this Brief on Exceptions to the Administrative Law Judges' ("ALJs") Proposed Order issued on June 8, 2006 ("Proposed Order" or "PO").

I. INTRODUCTION

Commonwealth Edison Company ("ComEd" or the "Company") filed new tariff sheets on August 31, 2005, in which it proposed a general increase in rates for delivery service. Significantly, this case presents the first determination of rates for delivery service to be effective after the end of the mandatory transition period and rate freeze on January 1, 2007. The Proposed Order rejects many of Staff's recommendations, and Staff takes exception to many of the conclusions and rulings set forth in the Proposed Order.

II. PROCEDURAL HISTORY

The PO fails to acknowledge the fact that the Commission entered an interim order on April 5, 2006 granting Staff's Motion for Entry of Interim Order Directing Performance of Original Cost Audit to have the Commission initiate an audit to verify the original cost of ComEd's distribution plant in service at December 31, 2004. Given the importance of the original cost audit, the Commission's final order should acknowledge the interim order.

Recommended Language

Staff recommends the following changes to page 4 of the PO.

* * *

DOE's witness was Dr. Dale E. Swan, Senior Economist and Principal, Exeter Associates, Inc.

On April 5, 2006 the Commission entered an interim order granting Staff's Motion for Entry of Interim Order initiating an audit process to verify the original cost of ComEd's distribution plant in service at December 31, 2004. The details of the audit process are set forth in the interim order.

UNCONTESTED ISSUES

* * *

III. STATEMENT OF UNCONTESTED ISSUES

A. Issues That No Party Contests

1. Elements of Rate Base

a. Staff Adjustment Related to ComEd Schedule B-2.1

See IV.A.9., Staff Adjustment Related to ComEd Schedule B-2.1

b. Pro Forma Capital Additions and Construction Work In Progress

The PO, Appendix A, page 6, column (e) reflects an incorrect amount for the uncontested CWIP adjustment. The correct amount, as reflected in ComEd Ex. 45.0 and Staff's Initial Brief, is (\$12,402,000), and the PO therefore should be corrected.

2. Other Issues

a. Exelon GSA-Reporting Requirements

The PO at page 7 correctly reflects the agreements between Staff and ComEd regarding various reporting requirements, including the schedules ComEd will file as part of its Form 21 in the future. However, these agreements are not mentioned in the PO's Findings and Ordering paragraphs.

Recommended Language

Staff recommends the following changes to page 303 of the PO

(13) ComEd shall comply with the agreement described in this Order regarding when ComEd shall notify the ICC of substantial changes to service company allocations in its Exelon General Services Agreement;

(14) ComEd shall file a copy of its FERC Form 60 with the ICC and provide a copy to the Manager of Accounting on the day it is filed with the FERC;

(15) ComEd shall comply with the agreements described in this Order to file, as part of its ILCC Form 21, a report of BSC corporate governance charges and the additional schedules identified in this Order.

IV. ARGUMENT ON CONTESTED ISSUES

A. RATE BASE

1. General Plant: Functionalization and Amount; Intangible Plant: Functionalization and Amount

Staff has two exceptions to the PO's General and Intangible Plant ("G&I") section. The first and most critical is that the PO failed to properly consider Staff's evidence on the issue and came to an improper conclusion in support of ComEd's position on these costs. Therefore, the Commission Analysis and Conclusion section should be changed to adopt Staff's position. Second, the discussion in the Proposed Order of Staff's position on the G&I plant issue has to be amended, because it does not reflect Staff's arguments in its reply brief.

a. ComEd Has Not Explained Why G&I Should Increase by \$304 Million; A General Labor Allocator Should be used to Functionalize G&I

The Commission Analysis and Conclusion with respect to the functionalization of General and Intangible (G&I) plant is erroneous and needs to be corrected. The PO incorrectly accepts ComEd's proposed 142% increase in G&I plant (from \$446,591,000¹ to \$1,079,579,000). (ICC Staff Exhibit 6.0 Corrected, p. 5, lines 95-99) The PO's rationale for its decision was that

The Commission however, was not provided with any evidence by Staff nor the IIEC to support their proposed adjustments. While Staff highlights the fact that in ComEd's last delivery services rate case the Commission found a reduction to general and intangible plant costs to be appropriate that is not a proper basis upon which the Commission should determine costs in this rate case. The

¹ *Commonwealth Edison Company, Petition for approval of delivery services tariffs and tariff revisions and of residential delivery services implementation plan and for approval of certain other amendments and additions to its rates, terms and conditions*, Ill. C.C. Docket No. 01-0423, Final Order, Appendix A, Schedule 3 (March, 28, 2003) ("01-0423 Order")

Commission is required to look thoroughly at each docket on a case by case basis.

(PO, p. 24). This conclusion has accepted ComEd's tone deaf appreciation for evidence on this issue, stating that Staff has presented no evidence (ComEd IB, pp. 44, 47; ComEd RB, pp. 24, 26, 31), when clearly Staff has done so. In addition, while it is correct for the PO to state that a rate case is to be evaluated on a case by case basis, this basic principal should not be taken so far as to turn a blind eye to previous Commission decisions. As Staff explained in its reply brief, the same issues was before the Commission in Illinois Power's delivery service rate case, and the Commission denied the utilities requested increase.² (Staff RB, pp. 8-10) The Commission should reach the same decision in this case.

The evidence Staff relied upon in forming its adjustment is ComEd's own data request response. (ICC Staff Exhibit 6.0 Corr., pp. 12, 14-15; ICC Staff Exhibit 17.0 Corr., pp. 7-10, 14-15) In that data request response, ComEd admitted that \$405 million³ of the increase in G&I plant is attributed to what the Commission disallowed in the ComEd's last DST rate case. (*Id.*). Mr. Lazare also testified that ComEd diverged from the *01-0423 Order* by allocating costs through direct assignment instead of the general labor allocator. (ICC Staff Ex. 6.0 Corrected pp. 6-8, 12-13, 14-15; ICC Staff Ex. 17.0 Corrected pp. 2-4, 9-10). This change fundamentally altered the allocation of costs and

² Illinois Power Company, *Proposed Revisions to delivery services tariff sheets and other sheets*, Docket No. 01-0432, 2002 Ill. PUC LEXIS 366, *14-*34 (March 28, 2002) ("Final Order 01-0432").

³ Staff reduced the original \$405 million adjustment in gross plant has been reduced by approximately 25% to \$304 million, based on additional evidence presented in ComEd's rebuttal testimony. (ICC Staff Exhibit 17.0 Corr., p. 14)

by itself accounted for nearly a 90%⁴ increase in G&I plant over the level approved in the *01-0423 Order*.

ComEd has to explain the change from the previous order -- explaining why the \$405 million should be moved from production to transmission and distribution. ComEd cannot just rely on what it put forth in the previous delivery services case. Just because they proposed \$813 million for delivery services in Docket No. 01-0423, does not mean they have the ability to recover it in this case. (See ComEd Redirect Ex. #4; Tr., pp. 921-27) In previous cases the Commission has required the utility to explain that it requires such a large increase in G&I relative to the amount that was specifically established by the Commission in the last DST rate case. (*Final Order 01-0432*, p. *31) ComEd has provided testimony and argument on G&I, but it has not shown that it requires this G&I plant that was disallowed in Docket No. 01-0423.

The ComEd witnesses who have addressed G&I stated that the \$405 million adjustment relates to production and that ComEd no longer has production (ComEd Ex. 19.0 Corrected, 19:413-421), that as part of ComEd's divestiture the Company has removed and transferred \$164 million of its G&I to Exelon Generation and Exelon BSC (ComEd Ex. 19.0 Corrected, 21:463 - 22:493 and Schedule 4 and 7; ComEd Ex. 36.0 Corrected, 14:308 – 311; Hill, Tr. at 921:7 - 927:2; ComEd Redirect Ex. 4), and that the Commission approved the journal entries of the transfer in Docket No .01-0423⁵.

⁴ This figure is the \$405 million divided by delivery service revenue requirement set in the *01-0423 Order* of \$446,591,000. (See ICC Staff Ex. 6.0 Corrected, p. 12)

⁵ ComEd has argued that the Commission has already reviewed and gave advance approval of ComEd's January 1, 2001, transfer of its nuclear plant assets to Exelon Generation under Section 16-111(g), and part of ComEd's compliance with the Order was its filing of the journal entries showing the assets to be transferred, including general and intangible plant assets. (ComEd IB, p. 47). No such thing has occurred. The Commission is to independently review the issue in this case. The Commission (continued...)

(ComEd Ex. 36.0 Corrected, 14:311 - 15:324 and Schedule 5) On re-direct examination, ComEd witness Hill also explained the aggregate numbers in Docket No. 01-0423 from which the \$405 million is derived – essentially stating that the \$405 million is the difference between the amount of G&I ComEd proposed be functionalized to delivery services and what the Commission approved. (Tr. at 921:7 - 927:2). Therefore, undoubtedly, ComEd is seeking to change what the Commission has approved in the *01-0423 Order*. However, they have not provided substantive evidence supporting such an increase. Therefore, the Commission should not allow ComEd to increase G&I from what was approved in ComEd’s last DST rate case.

ComEd’s request is similar to what Illinois Power requested in Docket 01-0432, and which the Commission denied. Prior to IP’s rate case, it had divested its generation; similar to ComEd. In its rate case, IP sought to allocate cost to G&I that had been allocated to generation in IP’s previous delivery services rate case. (*Final Order 01-0432*, pp. *16-*17,*31) Similar to what ComEd is arguing in this case, IP argued “that because of divestiture of its generation function all assets that were not sold or transferred remained to support the remaining operations of the Company.” (*Final Order 01-0432*, p. *31) In that case, the Commission refused IP’s request, and correctly so, stating:

The Commission finds such argument to be deficient in that there has been no showing that the remaining operations require such a large increase in G&I relative to the amount established by the Commission in 1999.

(continued from previous page)

addressed the same issue in Docket No. 01-0432 and held that the sale and transfer of assets as permitted under the Illinois Public Utilities Act “does not mean that the Commission has approved the accounting allocations made or that the amount of assets that were transferred are proper.” (*Final Order 01-0432*, pp. *32-*33).

The Commission accepts Staff's contention that based on the 1999 DST Order, IP should be required to allocate a portion of its G&I plant to "generation" even though prior to the test year in this case IP divested all its generation and had essentially no generation facilities, business or labor expense during the 2000 test year.

*(Final Order 01-0432 pp. *31-*32).*

In this case, ComEd, like IP, has not presented testimony showing that the remaining delivery service operations require a \$304 million increase in G&I. Therefore, Staff urges the Commission to be consistent in its rulings, and find in this case as it did in the IP case, and deny \$304 million of the increase in G&I that ComEd is requesting. In addition, the PO incorrectly accepts ComEd's argument that its direct assignment study provides the foundation for a reasonable functionalization of G&I costs. The PO state as follows:

Further, the Commission agrees with ComEd that the use of "direct assignment" of costs is the preferred approach over the general labor allocator approach. Because determining such costs is possible, the Commission is in agreement with ComEd that direct assignment be used in this case. Additionally, the Commission points out that the record evidence supports the fact that were the general labor allocator approach to be used in this case, general and intangible plant costs in rate base would in fact increase.

(PO, p. 24-25)

This conclusion is flawed on two levels. First, it misunderstands the nature of the ComEd direct assignment methodology. For the most important step of the functionalization process, ComEd's direct assignment study plays no role in determining the allocation of costs to the revenue requirement. That is because the Company's direct assignment methodology only functionalizes G&I costs within the regulated transmission and distribution utility. (ComEd Ex. 5.0, pp. 18-22, lines 385-470: ComEd Ex. 5.2, WPB-1, p. 1 of 12) The functionalization of costs between production, which

has been deregulated, and the utility falls outside the scope of the analysis. As the Company states, “there is no need to allocate general and intangible plant between a delivery business and a generation business.” (ComEd IB, p. 43) As explained above, ComEd has arbitrarily functionalized costs to the transmission and distribution (“T&D”) utility without explanation. (ICC Staff Ex. 6.0 Corr. pp. 6-8, 12-13, 14-15; ICC Staff Ex. 17.0 Corrected, pp. 2-4, 9-10). In the course of this arbitrary process, the Company restores to the revenue requirement G&I plant that the Commission had allocated to production in the Company’s last delivery service case, Docket 01-0423.

It is ironic that the PO finds that the general labor allocator would produce an even higher revenue requirement. (PO, p. 25) The increase seen in this case is caused by ComEd refunctionalizing significant levels of G&I plant from the unregulated production subsidiary back to the regulated utility (as discussed *supra*) and it no longer matters greatly what method is used to functionalize between transmission and distribution. Regardless of the method used, ratepayers will incur a significantly higher level of G&I plant costs as the proposed 142% increase attests.

Accordingly, and for all the reasons set forth in Staff’s post-hearing briefs, Staff recommends that the PO be amended to adopt Staff’s position on this matter.

Recommended Language

Staff proposes the following revised language for the “Commission Analysis and Conclusion” on G&I plant costs:

Commission Analysis and Conclusion

At issue here is Staff and IIEC’s proposal to disallow \$304 million or at least \$441 million respectively, of ComEd’s General and Intangible Plant costs in rate base. ComEd’s primary argument in

opposition to these proposed adjustments is that these costs were reasonably incurred and that neither party has presented any evidence to the contrary. In order for the Commission to approve such costs the Commission must find that the costs were prudent and used and useful. The Commission however, was not provided with any substantial evidence by Staff nor the IIEC ComEd to support their its proposal to restore G&I plant to the revenue requirement that the Commission excluded in its last delivery service case. Instead, the Company refunctionalized this plant back to the revenue requirement without providing meaningful support. ed adjustments. ~~While Staff highlights the fact that in ComEd's last delivery services rate case the Commission found a reduction to general and intangible plant costs to be appropriate that is not a proper basis upon which the Commission should determine costs in this rate case.~~ The Commission is required to look thoroughly at each docket on a case by case basis. Nevertheless, the The record established here by ComEd is supported by fails to present convincing evidence that the costs associated with general and intangible plant assets are reasonable. Thus, the Company has failed to establish that the G&I plant identified by Staff should be refunctionalized back to distribution.

Further, the Commission disagrees with ComEd that the use of "direct assignment" of costs is a meaningful issue for functionalizing G&I plant. The Company's direct assignment study only applies to functionalization within the transmission and distribution utility. It plays no role in the Company's proposed functionalization of costs between the unregulated production subsidiary and the regulated utility. Thus, the issue of whether to use direct assignment or a general allocator for G&I plant loses meaning when the functionalization process excludes the production subsidiary. the preferred approach over the general labor allocator approach. Because determining such costs is possible, the Commission is in agreement with ComEd that direct assignment be used in this case. Additionally, the Commission points out that the record evidence supports the fact that were the general labor allocator approach to be used in this case, general and intangible plant costs in rate base would in fact increase.

Moreover, the Commission finds the IIEC's argument for limiting the increase in general and intangible costs in proportion to distribution plant costs to be insufficient and unsupported by the record. Although the IIEC witness advocated such a position he never identified any cogent reason for such a correlation.

Similarly, the Commission finds that the record does not support the proposal by CES to reallocate some of the general and intangible plant to the SAC. CES never established that these costs are production costs. Accordingly, the Commission finds that the ComEd's proposed general and intangible costs are appropriate.

b. Staff's Position Should Include Staff's Reply Brief Arguments

The PO does not include a summary of the arguments in Staff's Reply Brief.

Recommended Language:

Staff proposes the following language be added to Staff Position for the "Commission Analysis and Conclusion" on G&I plant costs:

Staff Reply

Staff emphasizes that ComEd may have explained how it uses its plant for delivery services (ComEd IB, pp. 45-46), but it has not specifically addressed how the \$405 million that was denied in previous delivery services case is reallocated in G&I plant and is used an useful. Because of this deficiency, Staff recommends that ComEd has not supported this large increase, and therefore, \$304 million should be removed from G&I plant.

Staff contends that ComEd overbroadly interprets the Commission's ruling in Docket No. 01-0423. According to ComEd, the Commission stressed that its order for G&I plant in Docket 01-0423 was:

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

(ComEd IB, p. 47) Staff's contends that ComEd is overextending the application of this statement from the 01-0423 Order. Staff argues that this statement was intended to address the method of allocating costs, and the issue of whether to use direct assignment or a general allocator. In Docket No. 01-0423, ComEd proposed the use of a direct allocator (01-0423 Order, pp. 39-40), while Staff proposed the use of a general labor allocator (id, pp. 34-38).

Therefore, this statement was not intended to foreclose Staff from understanding how the divestiture of generation in 2001 impacts the 2004 test year in this case.

Staff also responded to ComEd's argument related to the general labor allocator. The Company argues that "Staff's position also overlooks the support in past Commission orders for use of "direct assignment" of costs where feasible, rather than relying on the general labor allocator approach." (ComEd IB, p. 48) ComEd cites a general statement by the Commission in Docket No. 99-0013 favoring direct assignment. (ComEd IB, p. 48) Staff responds that ComEd has ignored what the Commission had to say specifically about the application of direct assignment to G&I plant:

The Commission disagrees with Edison's direct assignment approach. The very nature of these costs suggests they are not amenable to direct assignment.

(99-0013 Order, p. 11) Staff then asserts that this statement clearly indicates the Commission's position on this matter - that the Commission does not consider direct assignment appropriate for G&I plant.

Staff also relies upon the Commission's decision in Docket No. 01-0432 to support the use of a general labor allocator instead of direct assignment. Staff explained how ComEd was similar to the utility in Docket No. 01-0432, since they both had divested themselves of generation and then attempted to allocate costs to its G&I plant that had been attributed to generation in its previous delivery services rate case(Docket Nos. 99-0120/99-0134). Since the issues in the cases were nearly identical, Staff encouraged the Commission to rule in a manner consistent with that docket.

Staff also responded to ComEd's contention that Staff's position is also inconsistent with Section 16-111(g) of the Public Utilities Act and the Commission's Order in Docket Nos. 00-0369 and 00-0394 [consol.]⁶ in which the Commission approved ComEd's transfer of nuclear plant assets to Exelon Generation and presented "journal entries showing the assets to be transferred,

⁶ Commonwealth Edison, *Request for confidential treatment for portions of the notice of transfer of generating assets and wholesale marketing business and entry into related agreements pursuant to Section 16-111(g) of the Illinois Public Utilities Act*, Docket No. 00-0396, and *ICC v. Commonwealth Edison, Proceeding pursuant to Section 16-111(g) of the Public Utilities Act concerning proposed transfer of generating assets, and wholesale marketing business and entry into related agreements*, Docket No. 00-0394, (Consolidated), (dated Aug. 17, 2000).

including general and intangible plants.” (ComEd IB, pp. 48-49) ComEd argues that the Commission gave ComEd approval in advance to decide what G&I assets may be transferred to distribution and included in the revenue requirement. Staff strongly disagrees with this legal interpretation, and so did the Commission in Docket No. 01-0432. In that docket, the Commission addressed this same issue, and determined that its decision regarding divestiture under Section 16-111(g) does not predetermine how G&I assets may be transferred to distribution and included in the revenue requirement. Moreover, Staff asserts that the Commission’s approval of the transfers does not remove the burden of proof obligation ComEd has under 200 ILCS 5/9-201(c).

In sum, Staff argues that ComEd has failed to provide adequate support to show how costs allocated to generation in the 01-0423 Order are reincorporated into the G&I plant for the 2004 test year, since generation has been divested from ComEd. Therefore, ComEd has failed to show that the reallocated plant is used and useful. Moreover, the Commission has addressed a similar issue in Docket No. 01-0432, in which the Commission denied an increase in G&I plant due to the divestiture and determined that a general labor allocator should be used. Therefore, the Commission should approve Staff’s proposed adjustment of \$304 million in G&I plant as a reasonable alternative to the massive and unsupported increase proposed by ComEd.

2. Pension Asset

Staff urges the Commission to consider the arguments raised by Staff in its Briefs (Staff IB, pp. 21-26; Staff RB, pp. 12-19) that provide appropriate justification for the Commission to reverse the conclusion reached in the PO and not allow the “pension asset” in rate base. The Proposed Order simply disregards Staff’s arguments as being “off the mark”. The reality is that no party has cited to a Commission rate proceeding that included a pension asset in rate base, and to Staff’s knowledge this has never occurred. The evidence in this case does not support the recognition of a pension asset.

Furthermore, the Proposed Order’s rationale for disregarding Staff’s arguments establishes dangerous criteria that parties may attempt to apply in future cases to

support inclusion of an asset in rate base. Thus, Staff submits that reference to the following criteria **must** be deleted from the Proposed Order:

- 1) That an asset should go into rate base as long as the asset is used and useful and acquired at a reasonable and prudent cost;
- 2) That there is no requirement that rate base assets be the result of a non-discretionary creation; and
- 3) That a legal obligation to fund pension obligations is justification for pension prepayments to be included in rate base.

In addition, the PO's statements in the conclusion mischaracterize Staff's position and should be corrected regarding the following:

- 1) Whether Staff's position is based on the cost increases to the revenue requirement; and
- 2) Staff's citations to the NICOR and GTE orders.

Used and useful and acquired at a reasonable and prudent cost

The Proposed Order states that "...as long as the asset is used and useful and acquired at a reasonable and prudent cost, that asset should go into rate base." (PO, p. 37) There are a number of problems with the statement and use of this criterion. First, it disregards the threshold issue of whether an asset exists. As explained in Staff's initial and reply briefs, ComEd has failed to establish that a pension asset exists under Statement of Financial Accounting Standards No. 87. (Staff IB, pp. 23-25; Staff RB, pp. 12-13) Since no pension asset exists, there can be no demonstration that it was prudent and used and useful. Second, the Proposed Order's use of the used and useful criterion seems to ignore that 1) the concept of interperiod equity and 2) the term "used and useful" cannot be applied in the traditional sense to an accounting based pension asset.

First, interperiod or intergenerational equity requires an allocation of costs to those specific periods when the costs actually provide service to ratepayers. In other words, present customers should be required to pay only for costs directly incurred in providing their specific service. It is under this concept that rates are determined. However, under the Proposed Order, the cost associated with the “pension asset” disproportionately increase the cost to current ratepayers for the benefit of future ratepayers. The criteria for determining whether an asset should be eligible for rate base treatment should include that the asset is *required* to provide utility service to current customers. In other words, that it was prudent for the Company to make the investment.

Second, the “pension asset” is not “used and useful” in supplying utility service to current customers in a traditional sense. A funding obligation is not something that can be termed as “used and useful”. Furthermore, nothing in the record supports how the pension funding is used and useful in the provision of utility service to the ratepayers. Rather, as Staff has demonstrated, it was not necessary to make this investment and there certainly has not been a demonstration that this “investment” was in the best interest of ratepayers.

A more textbook definition of a rate base asset is “...investor-supplied plant facilities and other investments required in supplying utility service to customers.”⁷ An asset could be used and useful, but not necessarily “required” to provide utility service to customers. For example, a utility could purchase an extra heavy duty truck that to

⁷ Accounting for Public Utilities 2005, Filed through Release No. 22, October 2005, by Robert L. Hahne, Gregory E. Aliff, and Deloitte and Touche LLP, Matthew Bender, a member of the LexisNexis Group, page 4-2.

support meter reading that, while used and useful in a literal sense if used for meter reading, is not truly necessary to perform that function. Thus, such a purchase would not be a “prudent” purchase even if the price paid is a reasonable and prudent cost for that type of truck. Similarly, the “pension asset” here may be used to fund the Company’s pension obligations, but that does not mean that it was prudent to incur that expense or that it is “used and useful” in such manner as to be necessarily included in rate base.

An asset in rate base is not required to be the result of a non-discretionary creation

The Proposed Order provides that for an asset to be in rate base, it can be the result of a discretionary action. ComEd did not choose to pre-fund its pension obligation, ComEd’s parent, Exelon, at its own discretion, chose to pre-fund the pension obligation. Exelon made a contribution to the pension trust prior to ComEd’s recognition of the corresponding expense on its books.

The Proposed Order establishes criteria that an asset can be included in rate base even if it does not exist but is a product of the manipulation of various accounting entries. As agreed to by ComEd’s own witness Houtsma on cross examination that **the assets are equivalent to the obligation** (Tr., pp. 378-379). **When this happens, there simply can be no prepaid asset for inclusion in rate base.** ComEd Witness Mitchell also confirmed this when he agreed that Exelon’s consolidated financial statements (ICC Staff Cross Exhibit 11) reflect the contributions that were made to reduce the liability related to the pension plan. (Tr., p. 2443) ComEd witness Houtsma testified that the pension asset is merely the “result of the contribution to the fund

amounts in excess of amounts previously recognized in the annual pension expense”. (Tr., p. 377) Ms. Houtsma explains that the “pension asset” is not disclosed on Exelon’s consolidated financial statement since it was offset by a liability that was recorded at Exelon. (Tr., p. 444) Ms. Houtsma further admitted that due to a decision on how to record the pension liability at the Exelon level, ComEd did not record the liability related to the actuarial loss (Tr., pp. 505–511). Therefore, while no “pension asset” exists at the Exelon level where the actual funding occurred, through an accounting entry decided by Exelon, an asset appears on ComEd’s books.

A legal obligation to fund pension obligations is justification for pension prepayments to be included in rate base

This criteria established by the PO encourages a “perverse financial incentive” for utilities to borrow money to fund future obligations and earn a return on those funds through rates that is higher than the cost to borrow. This incentive to borrow and invest money only maximizes rate base to the detriment of ratepayers. The fact that Exelon chose to pre-fund its pension obligation should not automatically result in increased rates to ComEd’s ratepayers.

The funding in March 2005 was not made pursuant to legal requirements. The Company claims that without the equity infusion from Exelon, ComEd would have had to issue additional debt itself resulting in a downgraded credit rating. No evidence in the record supports this claim. The point that is being overlooked in this example is that the funding of the pension plan was not **required** in March 2005. The funding itself was purely at the discretion of Exelon, not ComEd. Exelon had been funding its pension

plan at an increased level since 2002. The decision to fully fund the plan in March 2005 was only based on financial impacts to Exelon. At no point were the impacts to ComEd's ratepayers considered. Neither was the funding in March 2005 made out of necessity for the provision of safe and reliable service to ComEd's ratepayers. Rewarding shareholders for decisions made purely from their own financial standpoint irrespective of the impact on ratepayers is contrary to sound ratemaking practice.

Staff's proposal does allow recovery of pension costs

Staff does not dispute that ComEd is responsible for all of its *legal obligations*. Further, Staff does not dispute that ComEd recover its pension costs. However, there is nothing in the record indicating that ComEd was in arrears in payments to its pension plan as to require such a funding payment at the Exelon level. As indicated by ComEd, Exelon fully funded the pension plan because "it was the right thing to do" (ComEd Exhibit 7.0, p.8) not because there was a legal obligation to do so. Under Staff's proposal, the Company will recover its costs associated with its pension plan to enable it to meet its legal obligation; namely, it will recover periodic costs of the pension plan as determined by its actuary through base rates. Staff's proposal ensures that present customers pay only for costs directly incurred in providing their specific service.

Staff's position is **not** based on the cost increases to the revenue requirement

The PO insinuates that Staff's position is based on the cost increases to the revenue requirement and therefore the "pension asset" should not be allowed for recovery. While Staff never explicitly claimed that the contribution to the pension trust was not prudent, such a conclusion can be reached from Staff's argument regarding the

increased cost to ratepayers. The record demonstrates that the Company's decision to fully fund the pension plan was based solely on financial impacts to Exelon. At no time were the impacts to ratepayers considered. This leads to the imprudence of the contribution in that the impacts to all parties were not considered. The Company dances around the detriment it supposes could befall the Company were the contribution not made, yet does not consider the impacts of the various alternatives on the ratepayers of ComEd. The contribution increased the revenue requirement by \$27.9 million as compared to an increase of only \$8.6 million had the contribution not occurred (Staff IB, p.25). No such measurement of the detriment to ComEd absent the pension contribution is contained in the record.

PO Mischaracterizes Staff's citations to the NICOR and GTE orders

The PO also mischaracterizes Staff's citations to the NICOR and GTE orders (PO, p. 37); the citations were to illustrate the separate ratemaking treatment of pension expense and pension assets (ICC Staff Exhibit 2.0, pp. 13-14, Staff IB, p. 35)), **not** as evidence that pension assets are to be disallowed from rate base. Staff never argued that the shareholders did not fund the pension contribution. Both of the Orders are instructive in how the pension expense should be determined.

Recommended Language

Staff proposes the following language changes to the PO's conclusion on pages 36 – 38:

Commission Analysis and Conclusion

~~The Commission finds that the salient point at issue is that a pension asset does not exist. ComEd Staff argues that the record clearly shows that the pension asset was merely a creation of accounting entries made on ComEd's books to record transactions made at the discretion of its parent, Exelon. The Commission agrees with Staff that on a stand-alone basis, the pension trust was fully-funded rather than over-funded after the contribution was made in March 2005 and thus no pension asset exists. Therefore Staff's adjustment to remove the "pension asset" from rate base as well as Staff's companion adjustment to ADIT are approved. decision to fund ComEd's pension obligations fully was prudent and reasonable. According to them, prior to the \$803 million contribution, the funding status of the pension plan was at the very low end of the spectrum for large companies. After the contribution, it was more in line with those of other companies and ComEd's goals for itself. Moreover, the \$803 million contribution was part of a larger effort by Exelon to fund its pension plan for all employees. The Commission notes that in recent history, major corporations have run into trouble after funding pension plans at minimum levels and then finding themselves in financial distress, unable to meet pension commitments. ComEd points out that employees are well aware of troubles experienced by companies that have not adequately funded pension plans, and are now more aware of the funded status.~~

~~ComEd claims that the The Commission does not want to establish perverse financial incentives by adopting adjustments that would encourage utilities to fund-borrow money to fund future obligations and allow shareholders to earn a return on those funds before they are used in the provision of utility service. The balance between ratepayers and shareholders interests would be totally thrown askew were this situation allowed to occur. -only the minimum requirements for a pension plan and would deny cost recovery when the Company prudently funded more than that level. ComEd argues that it would be unfair and confiscatory if the Commission does not allow shareholders to receive a return on the funds that they have invested in the pension plan prior to collection of these amounts from customers. In addition, without inclusion in rates of both the pension asset and the lower pension expenses made possible by the contribution that created that asset, ComEd rates would not appropriately reflect the cost to provide service to customers.~~

~~ComEd claims it has demonstrated that the \$803 million contribution results in a pension asset on ComEd's books, not only from an accounting perspective (as a contribution related to future pension obligations) but more importantly from a regulatory~~

~~perspective (as funds contributed by shareholders to satisfy future pension obligations above and beyond the amount previously collected from customers through rates). Pension assets are created in multiple ways — not just overfunding, as Staff claims, but as here, where the pension asset represents funds that have been contributed to a pension fund by shareholders and bondholders to satisfy future pension obligations in an amount above and beyond what has previously been collected from customers through rates. The record is clear that ComEd's pension asset was not solely the product of accounting entries, and that the “disappearance” of that asset in the financial consolidation process is simply the result of required consolidation accounting practices under GAAP.~~

~~Staff's citations to prior Commission orders addressing ratepayer-funded pension contributions are instructive in the determination of the appropriate level of pension expense. inapposite and ignore the specific facts of those cases. The record is clear that ComEd's pension asset was funded exclusively from shareholder-supplied funds, and the liability that was funded has not previously been recognized in cost of service. It is undisputed that customers have not provided the source of funds for the pension contribution. Both of the cases cited by Staff, the Nicor Gas ICC Docket 04-0779 Order and the GTE ICC Docket 93-0301/94-0041 (cons.), Order, make clear that the appropriate level of pension expense is determined by an updated actuarial study and is totally separate from the ratemaking treatment of a pension asset was denied because it was funded by ratepayer-supplied funds. Thus, neither both Orders is are precedent for how the pension asset and related expense reduction should be treated determined in this proceeding.~~

~~The Commission is unpersuaded by attempts to disallow the pension asset. The assertion that such asset does not represent funds within ComEd's disposition and in which it has an interest is off the mark in multiple respects. First, federal law requires contributions to the pension trust be used exclusively to provide pension benefits. The Commission has consistently provided recovery to utilities of employee pension benefits, even if these benefits are provided through contributions to pension trust funds that cannot be accessed for general corporate purposes. Finally, the pension trust funds generate investment income that reduces pension expense included in the cost of service. Staff asserts that the Company's obligation is discretionary in nature when it comes to the pension contribution. There is no Commission criterion requiring that rate base assets be the product of a non-discretionary creation; rather, as long as the asset is used and useful and acquired at a reasonable and prudent cost, that asset~~

should go into rate base. The Commission finds that ComEd has a legal obligation to fund its pension obligations.

Staff asserts that the customer impact of including the pension asset outweighs the benefit of the lower pension expense that results from the contribution. The fact that the impacts to all parties affected by the pension contribution were not considered in the ultimate decision to make the contribution calls into question the prudence of the contribution. Rewarding shareholders for decisions made purely from their own financial standpoint is contrary to sound ratemaking practice. In other words the contribution is detrimental to customers and should not be included in rate base. Fundamentally, we do not exclude expenditures from cost of service solely because its inclusion would increase rates. The Commission recognizes that virtually all expenditures have the effect of increasing rates, but if the costs are reasonably and prudently incurred they should be reflected in the rate setting process.

The Commission also rejects Mr. Effron's alternative, fall-back proposal to remove the pension asset from rate base, but to add to jurisdictional operating expense approximately \$27 million, representing the cost of debt financing for the contribution. This alternative simply moves the impact of the pension contribution from a rate base item to an operating statement item and does not change the final revenue requirement. The record shows that the cost of debt financing to which Mr. Effron refers is the cost of debt Exelon incurred to provide the cash contribution to ComEd. The record shows that if ComEd had funded the contribution with its own debt, the Company's credit rating likely would have been downgraded. Maintaining acceptable credit ratings is important, as failure to do so can adversely affect access to capital and the cost of capital. Strong credit ratings will be particularly important as ComEd is entering into a period of competitive procurement of power beginning in January 2007. In addition, the Commission finds that Mr. Effron's proposal trying to impute to ComEd the cost of the debt issued by Exelon to fund the contribution, would violate Sections 16-111(i) and 9-230 of the Act.

In addition, we reject the AG's proposed adjustment to pension expense to recognize a full year's effect of the pension contribution. The record demonstrates that the suggested full-year's effect will not be realized until 2006, when many other factors will also affect pension expense. Accordingly, the Commission finds Mr. Effron's proposal to slice out just one of these factors improper. Finally, the Commission accepts the

~~proposed fair value adjustment to pension and post-retirement health care expenses.~~

~~The record shows that the pension expense based on the updated actuarial study is because the contribution will generate additional pension trust fund earnings, the contribution also decreases jurisdictional pension expense by approximately \$30 \$11.7 million, which has been reflected in both Staff's and ComEd's proposed revenue requirement. The Commission finds ComEd's the proposal to reflect this reduction appropriate. The Commission finds no merit in Staff's dual position of denying the pension asset, yet allowing customers to receive the benefit of the reduction in pension expense that such contribution generated. The Commission rejects this position as contrary to longstanding and widely recognized ratemaking principles that treat costs and benefits consistently. The Commission concludes that none of the Orders cited by Staff here are applicable.~~

If the Commission agrees with ComEd that the "pension asset" should be afforded rate base treatment, the PO paragraph (PO, p. 37) that sets forth the criteria for determining whether an asset can be included in rate base must be changed as follows:

~~The Commission is unpersuaded by attempts to disallow the pension asset and finds that Staff's position should be rejected. The assertion that such asset does not represent funds within ComEd's disposition and in which it has an interest is off the mark in multiple respects. First, federal law requires contributions to the pension trust be used exclusively to provide pension benefits. The Commission has consistently provided recovery to utilities of employee pension benefits, even if these benefits are provided through contributions to pension trust funds that cannot be accessed for general corporate purposes. Finally, the pension trust funds generate investment income that reduces pension expense included in the cost of service. Staff asserts that the Company's obligation is discretionary in nature when it comes to the pension contribution. There is no Commission criterion requiring that rate base assets be the product of a non-discretionary creation; rather, as long as the asset is used and useful and acquired at a reasonable and prudent cost, that asset should go into rate base. The Commission finds that ComEd has a legal obligation to fund its pension obligations.~~

3. Customer Deposits

Staff takes exception with the conclusion in the PO for Customer Deposits that Staff's position is inconsistent and arbitrary (PO, pp. 40-41). This rationale is simply not true. Staff's position is completely consistent with the Commission's practice to treat customer deposits and cash working capital as separate components of rate base. (See for example, *Commission Order, Commonwealth Edison Company Docket No. 01-0423*, App. A, Sch. 3, line 2; *Commission Order, Illinois Power Company Docket No. 01-0432*, App. A, p. 4, lines 8 and 18; *Commission Order, MidAmerican Energy Company Docket No. 01-0444*, App. A, p. 3, lines 6 and 10; *Commission Order, Central Illinois Light Company Docket Nos. 01-0465, 01-530 and 01-0637 (Cons.)*, App. A, Sch. 3, Lines 3 and 12; *Commission Order, MidAmerican Energy Company Docket No. 01-0696*, App. A, p. 3, lines 6 and 18; *Commission Order, Central Illinois Public Service Company and Union Electric Company Docket Nos. 02-0798, 03-0008, and 03-0009 (Cons.)*, Apps, A and B, Sch. 3, lines 8 and 18; *Commission Order Central Illinois Light Company Docket NO. 02-0837*, App. A, Sch. 3, lines 6 and 19; *Commission Order, Illinois Power Company Docket No. 04-0476*, App. p. 4, lines 6 and 19; *Commission Order, Northern Illinois Gas Company Docket No. 04-0779*, App. A, p. 5, line 15)

Staff further takes exception to the conclusion in the PO for customer deposits that Staff is remiss to apply this theory on any other issue which would result in an increase to rate base. Again, this rationale is simply not true. Staff often makes adjustments that increase the revenue requirement. Even in this case, Staff proposed that the real time metering costs be included in operating expense to increase the revenue requirement and Staff proposed an adjustment to increase interest expense to

recognize ComEd's obligation to pay interest on customer deposits in the Company's operating expenses.

ComEd claims that customer deposits are a component of cash working capital and that ComEd has not requested cash working capital in this proceeding. The evidence contradicts ComEd's claim that customer deposits are a component of cash working capital. Ms. Ebrey testified that, in her experience analyzing cash working capital, she has **never** seen a utility include customer deposits as a source of funds in a lead/lag study, which is the most frequently used basis for the derivation of a Cash Working Capital requirement for larger utilities. (ICC Staff Exhibit 13.0, p. 26, lines 528-532) Furthermore, contrary to ComEd's claim, it is the Commission's practice to treat customer deposits and cash working capital as separate components of rate base.

Recommended Language

Staff proposes the following language changes to the PO's conclusion on pages 40 – 41:

Commission Analysis and Conclusion

At issue here is whether customer deposits should be deducted from rate base. ComEd contends that Staff's proposal to reduce rate base by \$31,477,000 lacks merit and is inconsistent and unfair. Staff has proposed an adjustment to the Company's rate base to reflect the December 31, 2004 balance on customer deposits, consistent with prior Commission Orders on this issue. The Commission concurs with Staff's~~ComEd's~~ assessment of this issue. ~~Staff has carefully chosen to include customer deposits in rate base resulting in a rate base reduction on the premise that it is a cost-free source of capital.~~ The Commission finds that this basis for said reduction is ~~both inconsistent and arbitrary with prior Commission treatment of customer deposits.~~ Staff is remiss however, as to apply this theory on any other issue which would result in an increase to rate base. ~~The Commission is not persuaded to accept an adjustment solely because the effect of the particular adjustment would result in a rate reduction.~~ Accordingly,

Staff's ComEd's proposal as to customer deposits and the associated interest expense are is-adopted.

4. Budget Payment Plan

Staff takes exception with the PO's conclusion that the Staff position on budget payment plan balances ("BPPB") selectively signals out specific working capital items that would result in a downward adjustment to the Company's revenue requirement (PO, p. 42). However, in leveling this unjustified criticism, the PO fails to consider that the Commission reflects BPPB as a component of rate base separate from cash working capital regardless of whether BPPB result in an increase or decrease to rate base. (See for example, the following Orders in which the Commission reflected BPPB as a separate addition to rate base: Commission Order Central Illinois Light Company Docket NO. 02-0837, App. A. Sch. 3, line 7; Commission Order, MidAmerican Energy Company Docket No. 01-0696, App. A, p. 3, line 7; Commission Order, Central Illinois Light Company Docket Nos. 01-0465, 01-530 and 01-0637 (Cons.), App. A, Sch. 3, Line 9; and Commission Order, MidAmerican Energy Company Docket No. 01-0444, App. A, p. 3, line 11) In this particular case, BPPB happens to be a decrease.

Recommended Language

The Commission should continue to consistently reflect BPPB as a rate base item regardless of which stakeholders it favors in any particular case and proposes the following language changes to the PO's conclusion on page 42:

Commission Analysis and Conclusion

At issue here is whether Com-Ed's rate base should be reduced for budget payment plans as it represents excessive funds for the Company. As in the aforementioned issue ComEd asserts that Staff's position is inconsistent and unfair. Staff has argued that had the Company requested an allowance for cash working capital in its test year rate base BPPB would have resulted in a reduction

to that allowance. Further, in recent years the Company has over collected on BPPB and has had use of these funds which represent ratepayer funds. The Commission disagrees with ComEd that Staff's position on this issue is inconsistent and unfair.

~~Staff's position rests on the contention that had the Company requested an allowance for cash working capital there would have been a reduction to that allowance based on BPPB. The first obvious problem with this contention is that the Company did not elect to request for allowance for cash working capital in its test year rate base. As with customer deposits, the Commission finds that simply selectively signaling out specific working capital items that would result in a downward adjustment to the Company's revenue requirement would be inappropriate. Staff's argument would perhaps be persuasive had it taken this position on all appropriate issues, including those which would have resulted in a revenue increase. In this particular case, the BPPB represent funds provided by the ratepayers rather than shareholders and thus should decrease the balance on which the Company may earn a return.~~ Accordingly, the Commission accepts ~~rejects~~ the proposal by Staff to reduce ComEd's rate base for budget payment plans.

5. Materials and Supplies Inventory

Staff takes exception to the PO's conclusion that Staff's arguments are defective (PO, p. 43). The PO incorrectly accepts the Company's proposed end of test year materials and supplies figure. Appendix A, page 6 column (c) correctly reflects Staff's adjustment reducing materials and supplies inventory to the most recent 13-month average, adjusted for the average accounts payable associated with materials and supplies for the same period. The PO's conclusion overlooks Staff's rebuttal position which adjusted the accounts payable portion of the materials and supplies inventory balance to an average based on the test year. (ICC Staff Exhibit 13.0, pp. 28-29)

Recommended Language

The Commission's conclusion on page 43 should be revised as follows to reflect the appropriate level of materials and supplies inventory to be included in rate base:

Commission Analysis and Conclusion

ComEd has proposed to include its materials and supplies inventory in rate base as of December 31, 2004, the last day of the test year. Staff has alternatively proposed a decrease to ComEd's materials and supplies inventory based on an average of the most recent thirteen month balances provided by ComEd. At issue here is whether or not the close of the test year is the appropriate measure for ComEd's materials and supplies inventory. The Commission agrees with ComEd Staff and finds that ~~their~~ its proposal is both appropriate and reasonable, as well as consistent with prior Commission decisions. The record in this docket provides that ~~ComEd's Staff's~~ proposed figure more accurately reflects a normal level of materials and supplies inventory, their present inventory management policies and practices. Staff's arguments are convincing as they point out the fluctuating nature of the Company's historic materials and supplies balances over time, rather than basing the appropriate level on a single point in time as the Company proposes. ~~defective as they use different periods by which to calculate the accounts payable offset, they discount the direct assignment for functionalization purposes, and the replacement of an allocator.~~ For the foregoing reasons the Commission concurs with ComEd Staff and accepts its proposed materials and supplies figure.

If, however, the Commission retains the conclusion in the PO, Appendix A would need to be revised to eliminate Staff's adjustment to Materials and Supplies Inventory shown on Appendix A, page 6, Column (c).

6. Procurement Case Expenses [Rate Base Effect]; Rate Case Expenses [Rate Base Effect]

As discussed below, Staff still supports its position regarding the proper recovery mechanism for procurement case expenses but is not offering any alternative language. However, the PO's findings relating to procurement expense and rate case expense must be corrected; therefore, Staff proposes alternative language for those corrections.

The first correction is to delete an inaccurate reference made at page 44 of the PO as well as the text appearing below "Commission Analysis and Conclusion" that is

duplicated on pages 45 and 47 of the PO. The reference and the duplicate Commission Conclusion are unnecessary and confusing.

The second correction is to add a Commission Conclusion to the PO to address the procurement and rate case expense amounts that ComEd could not support as just and reasonable. The procurement expense amount is \$566,667 as reflected on ICC Staff Exhibit 12.0, Schedule 12.11, page 2. A similar adjustment for rate case expense amounts that ComEd could not support as just and reasonable is reflected on page 2, column (f) of the PO's Appendix A. That amount is \$626,000. Therefore, it appears the PO intended to adopt Staff's methodology for determining the appropriate amount of procurement *and* rate cases expenses, putting aside the procurement expense rate recovery mechanism issue.

ComEd in a June 15, 2006 letter to the ALJ's asserts that the inclusion of a \$626,000 rate case expense adjustment in Appendix A was a mistake. Staff disagrees. It adds that the "Proposed Order indicates ComEd's position on the issue of the unamortized balance of procurement case and rate case expense was persuasive." While the PO agrees with ComEd that the unamortized balance of such expenses should be included in rate base, the PO does not state that ComEd fully substantiated those costs. Therefore, there is no basis in the PO for ComEd's statement. As set forth in Staff's briefs, ComEd failed to support all of its rate case expense and procurement expense, and this is reflected in the PO's Appendix A. ComEd is correct that a mistake was made; however, the only mistake made was in the failure to include the procurement expense adjustment of \$566,667 in Appendix A.

Therefore, Staff proposes that Appendix A be corrected to reflect an additional reduction to administrative and general expenses of \$566,667 which represents Ms. Hathhorn's procurement case expense adjustment. Staff also recommends that language be included in a Commission Analysis and Conclusion supporting both of Ms. Hathhorn's adjustments.

Recommended Language

Staff recommends the following changes to pages 44 and 45 of the PO.

PROCUREMENT CASE EXPENSES [RATE BASE EFFECT]; RATE CASE EXPENSE [RATE BASE EFFECT];

ComEd

ComEd seeks to recover its legal fees and expenses associated with the Rate Case and the Procurement Case through inclusion of those costs in the test year rate base. Staff does not disagree with ComEd that such costs are recoverable. Hathhorn, Tr. at 1720:14-18. Nor does Staff object to amortizing Rate Case expenses over a three-year period. Hathhorn, Tr. at 1718:22-1719:2. ComEd and Staff have two principal disagreements: (1) where to recover the Procurement Case expenses (delivery services charges (ComEd) or supply administration charge ("SAC") (Staff)); and (2) if both the Procurement Case expenses and Rate Case expenses are recovered through delivery service charges, whether there should be a return on the unamortized balances of the Rate Case and Procurement Case expenses. Hathhorn, Tr. at 1720:2-18; Hill Sur., ComEd Ex. 36.0 Corr., 26:587-98. Staff and CCC also propose certain rate case expense adjustments. For both of Staff's rate case expense adjustment and procurement case expense adjustment Staff's adjustments were due to ComEd failing to substantiate its expenses as just and reasonable.

Staff

~~See discussion of Procurement Case Expenses [Rate Base Effect] at Section III.B.10.~~

Staff witness Dianna Hathhorn testified that an adjustment was necessary to disallow the Company's request to include its unamortized balance of rate case expense of \$3,693,000 in rate base, in order to insure that there is a fair and equitable allocation

of rate case costs between ratepayers and shareholders. Ms. Hathhorn's adjustment also disallows \$626,000 in rate case expense amounts estimated by ComEd but unsubstantiated. (ICC Staff Exhibit 1.0, Schedule 1.12 and ICC Staff Exhibit 12.0, Schedule 12.12) Ms. Hathhorn proposed a similar adjustment for procurement case expense which were also unsubstantiated by ComEd. These amount to \$566,667 as reflected on ICC Staff Exhibit 12.0, Schedule 12.11, page 2.

Ms. Hathhorn stated that her proposed treatment of rate case expense requires shareholders to bear the capital costs associated with improving their investment through increased rates, while ratepayers bear the average annual cost for the continued provision of safe reliable service. Without this treatment, she testified that there is little to no incentive for the Company to keep its rate case expenses to a minimum. (ICC Staff Exhibit 1.0, p. 22)

Further, Staff witness Hathhorn noted that in recent ICC orders for unamortized rate case treatment where it was a contested issue before the Commission, only one case, ICC Docket No. 99-0117⁸, resulted in the inclusion of the unamortized balance of rate case expense in rate base being approved by the Commission. In that case, she explained that ComEd successfully argued that the proceeding was markedly dissimilar from general rate case dockets in that the proceeding was initiated by law and not by a utility's request for a rate increase. (Docket No. 99-0117, Order dated August 25, 1999, p. 49) However, Ms. Hathhorn testified that this rate case proceeding was initiated by a utility's request for a rate increase and not by law. Therefore, Staff recommended that the Commission follow its customary practice of allowing amortization of rate case expense but not allowing a return on the unamortized balance. (ICC Staff Exhibit 1.0, pp. 22-23)

In responding to ComEd's contention that "the only improvement that the shareholders receive [from a rate case] is the re-setting of fair and reasonable returns on their investment" (ComEd Ex. 19.0 Revised, p. 30), Staff witness Hathhorn noted that in Docket Nos. 94-0065 and 91-0317, the Commission found that Staff's adjustment to recognize the benefits to shareholders resulting from ComEd's rate case process was appropriate. (Docket No. 94-0065, Order dated January 9, 1995, pp. 99-98) (Consumers Illinois Water Company, Docket No. 91-0317, Order dated May 28, 1992, p. 23) (ICC Staff Exhibit 12.0, pp. 21-22)

⁸ Order entered August 25, 1999.

Further, Staff noted in its Initial Brief that CUB-CCSAO-City of Chicago witness McGarry supported Staff's adjustments to disallow unamortized balances in rate base. (CUB-CCSAO-City of Chicago Exhibit 5.0, p. 32)

In summary, Ms. Hathhorn testified that her position is based on the premise that the benefits shareholders receive from a rate case are the increased rates. The rates do carry risk of over-charging ratepayers for the costs of the rate case incurred to achieve the increased rates, yet ComEd expects ratepayers to bear this risk, while requiring no such symmetry from shareholders. Ms. Hathhorn's position that expects the shareholders to share in that risk is reasonable and reflects a common practice of this Commission. (ICC Staff Exhibit 12.0, pp. 20-21)

Staff witness Hathhorn testified that for the same reasons, the unamortized balance of procurement case expenses should be disallowed in rate base. (ICC Staff Exhibit 12.0, pp. 20-22)

CES

* * *

Commission Analysis and Conclusion

~~Putting aside the issue of which recovery mechanism is most appropriate for procurement case expense, the Commission will adjust Administrative and General expense to (1) reduce the rate case expense to be recovered by ComEd by Staff's proposed adjustment to disallow \$626,000 in rate case expense estimated by ComEd but unsubstantiated and (2) reduce the procurement case expense to be recovered by ComEd by Staff's proposed adjustment to disallow \$566,667 in procurement case expense which ComEd did not show to be just and reasonable. At issue is whether or not ComEd should be allowed to recover the costs associated with the procurement case through their delivery service rates. ComEd argues that it should be allowed to recover the costs incurred as a result of the procurement case through delivery service rates as those costs are ultimately a benefit to all customers. Staff is opposed to ComEd's proposal and in the alternative has proposed that ComEd only be allowed to recover its unamortized balance of its procurement case expenses through SAC. Section 16-103(a) of the Act mandates that ComEd be a provider of last resort for supply service to most customers. Thus, the Commission agrees with ComEd that all customers derive a benefit from the procurement case. Additionally, the Commission notes that under Staff's proposal, that said expenses be recovered through SAC,~~

~~residential customers could end up bearing the brunt of this expense. Large industrial customers with other competitive options could choose alternative suppliers during this period while reserving the right to return in the future having had avoided this expense. Thus Staffs proposal would be inappropriate. Therefore, the Commission concurs with ComEd's proposal to recover its procurement case expenses through delivery service rates.~~

7. Procurement Case Expenses Recovery Mechanism

Staff's position regarding the proper rate recovery mechanism for the procurement expenses differs from the PO. While Staff still supports its position and therefore does not agree with the PO on this issue, Staff is not offering alternative language for the Commission to consider.

8. Recovery of Unamortized Balances of Rate and Procurement Case Expenses

The PO reached an incorrect conclusion by focusing only on one aspect of the issue, that being the "concern over ratepayers being overcharged." (PO, p. 49) However, there is more to Staff's proposal that was not considered in the formulation of the conclusion. Staff's proposed treatment of rate case expense requires shareholders to share some of the cost of the rate case. If the costs are not shared, there is little to no incentive for the Company to keep its rate case expenses to a minimum. (ICC Staff Exhibit 1.0, p. 22) ComEd's assertion that shareholders do not benefit from --and therefore should not help pay for--rate cases is transparent and self-serving.

The sole reason stated in the PO's conclusion that ComEd's position is persuasive is that "the amortization period as proposed by ComEd appears reasonable". (PO, p. 49) However, the amortization period was not a contested issue among Staff and ComEd, and therefore cannot be a valid basis supporting the conclusion.

The PO's conclusion fails to consider the evidence that the amortization period alone does not insure a fair and equitable allocation of rate case costs between ratepayers and shareholders. Under the PO's conclusion, ratepayers will bear the full cost of the rate case. The Commission has rejected this scenario repeatedly in the past, not only for other utilities but for ComEd. (Docket Nos. 94-0065 and 91-0317, ICC Staff Exhibit 12.0, pp. 21-22) The PO's conclusion does not address why an opposite outcome with the same fact set is appropriate here.

Recommended Language

Staff recommends the following changes to page 49 of the PO

* * *

Commission Analysis and Conclusion

At issue is the concern over ratepayers being overcharged as a result of unamortized balances being included in rate base. The Commission finds ComEd's position on this issue unpersuasive. The amortization period as proposed by ComEd appears reasonable given the estimated life of these rates, however the amortization period alone does not insure a fair and equitable allocation of rate case costs between ratepayers and shareholders. Staff's proposal recognizes the benefits to shareholders resulting from this rate case, consistent with prior Commission conclusions. Therefore, the Commission accepts ComEd's Staff's proposal.

* * *

9. Staff Adjustment Related to ComEd Schedule B-2.1

The PO's conclusion rejecting Mr. Griffin's adjustment to Schedule B-2.1 should be disregarded given there is no evidence in the record to support the rejection of Mr. Griffin's adjustment. Staff witness Griffin proposed an adjustment to correct the plant balance so that there was agreement with ComEd's workpapers supporting ComEd's

Schedule B-2.1 and ComEd workpapers WPB2.1a and WPB2.1b. (ICC Staff Exhibit 3.0 Corrected, p. 5; Staff IB, p. 4; Staff RB, p. 2)

Without any record evidence to support its position, the PO erroneously concludes that:

ComEd demonstrated that Staff's proposed adjustments inadvertently consist of double-counts with adjustments already made by ComEd, except for an incremental \$8,000 reduction in General Plant in rate base. The Commission finds ComEd's Schedule B-2.1 Errata to be reasonable and therefore accepts it as reflected in ComEd's rate base and revenue requirement computations, except that ComEd is directed to reflect that incremental \$8,000 reduction in General Plant in rate base.

(PO, p. 49) However, as set forth in Staff's reply brief, ComEd never objected to Mr. Griffin's schedule B-2.1 adjustment in its rebuttal or surrebuttal testimony. It was not until ComEd filed its initial brief that ComEd took issue with Mr. Griffin's adjustment and it was not until its reply brief that ComEd set forth any detailed position contradicting Mr. Griffin's adjustment. Yet the PO concludes that ComEd "demonstrated that Staff's proposed adjustment inadvertently consist of double-count with adjustments already made by ComEd," (PO, p. 49) As Staff pointed out in its reply brief and as even ComEd acknowledged in its initial brief, a Commission order must be based upon the evidence in the record. (Staff RB, p. 3) The only evidence in the record on Mr. Griffin's Schedule B-2.1 adjustment is Staff witness Griffin's testimony (ICC Staff Exhibit 3.0 Corrected, p. 5 and ICC Staff Exhibit 14.0, p. 13). The statements made by ComEd in its reply brief that:

ComEd's review in connection with the preparation of its Reply Brief has determined that Staff's proposed corrections inadvertently consist of double-counts with adjustments already made by ComEd, except for an incremental \$8,000 reduction in General Plant in rate base.

are not supported by witness testimony, are not in the evidentiary record yet appear to be the basis for the PO's rationale for rejecting Mr. Griffin's adjustment. Given the fact that there is no evidence in the record to support the rejection of Mr. Griffin's adjustment there should be a downward adjustment to Gross Utility Plan in the amount of \$2,063,000 along with related adjustments to accumulated depreciation, accumulated deferred income tax and depreciation expense. (ICC Staff Exhibit 14.0, Schedule 14.2, page 1 of 2; Staff IB, p. 3)

Recommended Language

Staff recommends the following changes to page 5 of the PO.

* * *

b) Staff Adjustment Related to ComEd Schedule B-2.1

ComEd made detailed adjustments to rate base based on ComEd's *pro forma* adjustments for a certain 2005 plant. No party disputes these corrections. Staff's adjustment related to ComEd Schedule B-2.1 is addressed in the contested Rate Base section of the order.

* * *

Staff recommends the following changes to page 49 of the PO.

STAFF ADJUSTMENT RELATED TO COMED SCHEDULE B-2.1

ComEd filed its Schedule B-2.1 as part of its original Part 285 filing. This Schedule listed detailed adjustments to rate base based on ComEd's *pro forma* adjustments for certain 2005 plant. ComEd's Schedule B-2.1 Errata is included in ComEd Ex. 5.1.

Staff's proposed certain additional adjustments to ComEd Ex. 5.1, Schedule B-2.1 Errata. Given that ComEd never contested Staff's adjustment with testimony of its own witnesses and waited until its reply brief to provide any sort of response to Staff's adjustment the Commission accepts Staff's adjustment. Therefore, there should be a downward adjustment to Gross Utility Plan in the amount of \$2,063,000 along with related adjustments to accumulated

~~depreciation, accumulated deferred income tax and depreciation expense consistent with ICC Staff Exhibit 14.0, Schedule 14.2, page 1 of 2. However, ComEd demonstrated that Staff's proposed adjustments inadvertently consist of double counts with adjustments already made by ComEd, except for an incremental \$8,000 reduction in General Plant in rate base. The Commission finds ComEd's Schedule B-2.1 Errata to be reasonable and therefore accepts it as reflected in ComEd's rate base and revenue requirement computations, except that ComEd is directed to reflect that incremental \$8,000 reduction in General Plant in rate base.~~

B. OPERATING EXPENSES AND REVENUES

1. Administrative & General Expenses

a. Overall Amount

Staff has two exceptions to the PO's Administrative and General Expenses ("A&G") section. First, the PO fails to demonstrate an understanding of Staff's contentions, because its conclusions simply state that Staff's position has no merit without explaining why. Therefore, Staff has briefly recited the arguments in favor of its proposed adjustment, and requests that it be adopted for A&G. Second, Staff's position has to be amended, because it does not reflect Staff's arguments in its reply brief.

The PO's conclusion, in support of ComEd's proposed level of A&G expenses, is deficient. This conclusion should be reversed and Staff's proposed adjustment accepted.

It is difficult to decipher the logic behind the Commission's Analysis and Conclusion on this issue, given the brevity of the discussion. The lack of discussion suggests that the ALJs may not have had a firm foundation for the conclusion they reached. Therefore, Staff will attempt to briefly summarize the main arguments in this issue.

The only reference to the Staff position is in the “Commission Analysis and Conclusion” section for Functionalization. In that section the PO states the following:

Staff’s proposed cap is \$176,684,000, the amount approved for the 2000 test year. However, both ComEd and Staff acknowledge that ComEd is not the same utility that [it] was in 2000 and has not been for over five years. Staff’s proposal to cap A&G expenses is without merit and is rejected. (PO, p. 61)

Acknowledging that ComEd is not the same utility that it was in 2000 does not explain why Staff’s proposal is without merit, and likewise, it does not explain why ComEd’s proposal is meritworthy. If anything, the facts show otherwise. The facts in evidence show that ComEd is proposing a lower level of direct distribution, customer service and customer accounts expenses in this case than the Commission adopted for the 2000 test year in Docket 01-0423.

It should be noted that the PO offers similar conclusions in the introductory section of the A&G expense discussion. The relevant passage is as follows:

Staff’s and intervenors’ remaining proposed adjustments to ComEd’s A&G expenses lack merit and should not be approved. They are not supported by, and instead are contrary to, the evidence. They would deny ComEd recovery of prudent, reasonable, and necessary actual expenses incurred in order to perform the distribution and customer functions. (PO, p. 57)

This conclusion is problematic as well. It is unclear whether this is intended to be an overall roadmap of the findings on this issue, or whether these are intended to be findings. If the latter they fail to explain why Staff and Intervenor’s positions “lack merit” and “are contrary to” the evidence.

A closer look at the evidence reveals that ComEd’s proposed increase in A&G expenses is wholly without merit. The shortcomings, which are more fully presented in testimony (ICC Staff Exhibits 6.0 and 17.0, Corrected) and in Staff’s Initial and Reply Briefs (Staff IB, pp. 36-41; Staff RB, pp. 26-31), include the following:

- ComEd witness Hill argues that the proposed increase is driven by new A&G expenses, such as post 9/11 security costs and Sarbanes-Oxley Act compliance costs, that did not exist in 2000. (ComEd Ex. 19.0 Revised, pp. 38-39). He fails, however, to provide an estimate of the magnitude of these costs. (ICC Staff Exhibit 17.0 Corr., p. 16, lines 387-390)
- Mr. Hill contends that A&G expenses must increase to accommodate approximately 3% per year general wage increases since 2000. (ComEd Ex. 19.0 Revised, p. 40). He fails to mention that overall payroll costs have been decreasing over that same time period. (Staff Ex. 17.0 Corrected, p. 17, lines 402-403).
- ComEd's proposed increase in A&G expenses is out of line with the downward trend in the Company's direct Distribution, Customer Accounts and Customer Service Expenses. ComEd is actually proposing reductions in the sum of these expenses from the levels approved by the Commission in its last DST rate case, ICC Docket No. 01-0423. (ICC Staff Exhibit 6.0 Corrected, p. 26, lines 644-650).
- ComEd claims that the unregulated Business Services Corporation, which accounts for 47% of unadjusted A&G expenses for the test year (ComEd Ex. 5.0, p. 27), is achieving significant cost savings through efficiencies and process improvements. Nevertheless, ComEd ratepayers do not appear to be sharing in these savings based on the significant increase proposed for A&G expenses. (ICC Staff Exhibit 17.0 Corr., p. 25, lines

605-607).

- ComEd's proposed \$260,909,000 in A&G expenses, which represents an increase of \$84,225,000 or 47.7% over current levels, follows upon a \$57,806,000 or 48.6% increase approved in the *01-0423 Interim Order* (March 28, 2003). (ICC Staff Exhibit 6.0 Corr., p. 25, lines 613-615). ComEd fails to explain why such significant increases are needed in two consecutive cases.
- ComEd witness Mr. Hill suggests that ComEd's proposed A&G expenses are reasonable because they actually fall \$123 million below total Company A&G expenses for the year 2000. Mr. Hill's argument is irrelevant, because in 2000 ComEd owned generation and in the 2004 test year it does not. (ICC Staff Exhibit 17.0 Corr., pp. 15-16, lines 371-381)

These arguments, which were not addressed in the PO, provide more than enough reason for the Commission to support Staff's proposed adjustment of A&G expenses. Staff recommends that the PO's conclusion on this issue be reversed, and Staff's position adopted.

Recommended Language:

Staff proposes three separate edits to the A&G Expense section of the PO.

The first revision is as follows to page 57 of the PO:

Staff and intervenors have proposed numerous adjustments to ComEd's A&G expenses. ComEd's figure of \$260,909,000 reflects that ComEd has accepted certain of their proposed adjustments, in some cases to narrow the issues. ~~Staff's and intervenors' remaining proposed adjustments to ComEd's A&G expenses lack merit and should not be approved. They are not supported by, and instead are contrary to, the evidence. They would deny ComEd~~

~~recovery of prudent, reasonable, and necessary actual expenses incurred in order to perform the distribution and customer functions.~~

Second, Staff recommends the following revision to the Commission Analysis and Conclusion in the A&G expense functionalization section:

Commission Analysis and Conclusion

~~ComEd argues that its functionalization of its A&G expenses should be approved. The evidence shows that use of the general labor allocator is appropriate in this case given the available information. There is no dispute that ComEd calculation of the general labor allocator based on the 2004 test year is correct. No party has proposed any other method to functionalize ComEd's A&G expenses or shown any valid reason to reject ComEd functionalization. Staff does not propose any other method of functionalizing ComEd's A&G expenses, but instead rests on its proposal to cap these expenses at the level approved in ICC Docket 01-0423. Staff's proposed cap is \$176,684,000, the amount approved for the 2000 test year. The Commission will address the merits of Staff's proposed cap in the next section of this Order. However, both ComEd and Staff acknowledge that ComEd is not the same utility that was in 2000 and has not been for over five years. Staff's proposal to cap A&G expenses is without merit and is rejected.~~

The Coalition of Energy Suppliers ("CES") requested that, the Commission review ComEd's A&G expenses to determine whether it included any expenses that are not properly allocated to the distribution and customer functions. If the Commission determines that any expenses are more properly allocated to the production function, then CES proposes that those expenses be recovered through a Supply Administration Charge. CES does not specifically address any expenses that it feels should be allocated to the production function. The Commission did not find any expenses that should be recovered through a Supply Administration Charge. ~~No other intervenor provided any grounds for rejecting ComEd's functionalization of its A&G expenses. IIEC's witness did not directly address the subject of functionalization of ComEd's A&G expenses. Therefore, the Commission finds that ComEd's functionalization of its A&G expenses is just and reasonable and is approved.~~

Finally, Staff recommends the Commission Analysis and Conclusion for the Overall Amount on p. 68 of the Proposed Order be removed and substituted with the following:

After weighing the evidence, the Commission accepts Staff's proposal to cap A&G expenses at the currently approved level of \$176,684,000. This results in a downward adjustment of \$84,225,000 to the \$260,909,000 in A&G expenses proposed by ComEd. ComEd has failed to provide any meaningful evidence in support of its proposed increase.

ComEd cites wage increases even though overall payroll costs are declining. It mentions post 9/11 security costs and Sarbanes-Oxley Act compliance costs but provides no estimate of their magnitude. ComEd's proposed increase in A&G expenses is out of line with the downward trend in the Company's direct Distribution, Customer Accounts and Customer Service Expenses. ComEd claims that the unregulated Business Services Corporation achieving significant cost savings, but ComEd ratepayers do not appear to be sharing in the benefits. Furthermore, ComEd's proposed \$260,909,000 in A&G expenses, which represents an increase of \$84,225,000 or 47.7% over current levels, follows upon a \$57,806,000 or 48.6% increase approved in the 01-0423 Interim Order. The Company also fails to provide sufficient evidence explaining why such significant increases are needed in two consecutive cases. ComEd suggests that proposed A&G expenses are reasonable because they actually fall \$123 million below total Company A&G expenses for the year 2000. However, in 2000 ComEd owned generation and in the 2004 test year it does not.

In sum, the Commission agrees with Staff that ComEd has failed to provide any reasonable evidence to support its proposed increase in A&G expenses. Therefore, the Commission supports Staff's proposed adjustment to these costs.

The PO does not include a summary of the arguments in Staff's Reply Brief.

Recommended Language:

Staff proposes the following language be added to Staff Position for the "Commission Analysis and Conclusion" on A&G expenses:

STAFF REPLY

Staff asserts that the evidence ComEd has provided in its initial brief to support their proposal as prudent, reasonable, necessary and useful (ComEd IB, pp. 84, 89-90) is lacking. In addition to arguments Staff addressed in its initial brief, ComEd mentions that it's A&G costs were affected by post-September 11th security and Sarbanes-Oxley costs. (ComEd IB, p. 92). Staff responds that ComEd has not provided any figures to demonstrate the effects of these expenses.

ComEd also attempts to justify its increase, by comparing its request to the 97% increase NIGAS received in its most recent rate case. (ComEd IB, p. 93). Staff responds that such a comparison is hardly worthy of weight, given that ComEd is an electric utility and NIGAS is a gas utility, and there is no evidence in the case demonstrating that the increase in NIGAS' A&G expenses is in any way similar to ComEd's situation.

The Company goes on to argue that Staff proposes to remove \$84,225,000 from A&G expenses, and also characterizes Staff's adjustment as being either allocated to the transmission function or to no function. (ComEd IB, p. 93). Staff points out that ComEd has failed to establish whether any of the numbers identified on page 93 of its Initial Brief are meaningful for the purposes of determining A&G expenses in this case; these numbers are stated but no citation to evidence is provided. Staff states that this top-down approach should be rejected, because it is contrary to the burden of proof established in Section 9-201(c). (220 ILCS 5/9-201(c) (stating that the utility has the burden of proving its requested rate)).

Thus, Staff recommends the Commission find that ComEd has not supported its \$84.225 million increase. Moreover, Staff has established that \$176,684,000 is a just and reasonable level of A&G expense. (Staff IB, pp. 41-47). Finally, Staff points out that this adjustment is separate from what Staff witnesses Hathhorn and Ebrey are proposing for MGP expense, interest on customer deposits, incentive compensation rate case expense, procurement expense, charitable contributions, affiliate allocation and corporate governance costs as part of these adjustments' impact A&G expense. (See Staff IB, Appendix A, Schedule 2, line 11; ICC Staff Exhibit 1.0, p. 7, ICC Staff Exhibit 12.0, pp. 4-5).

2. Incentive Compensation

Staff has no exceptions regarding the PO's conclusion for Incentive Compensation Expense.

3. Uncollectibles Expenses

Staff has no exceptions regarding the PO's conclusion for Uncollectibles Expense.

4. Environmental Expenses

Staff takes exception with the PO's conclusion for environmental expenses because it:

- 1) Overlooks the uncontested issue that internal MGP costs should be added to the revenue requirement,
- 2) Does not fully capture ComEd's proposal, and
- 3) Allows an inappropriate pro forma adjustment.

Internal MGP costs should be added to the revenue requirement

Staff proposed an adjustment to allow recovery of internal Company costs related to MGP sites (ICC Staff Exhibit 2.0, Schedule 2.10 and ICC Staff Exhibit 13.0, Schedule 13.8). While the Company at first misunderstood Staff's adjustment to be a reduction in costs (ComEd Ex. 19.0, p. 59), in rebuttal testimony, Staff explained that the adjustment in fact does add back costs to be recovered through base rates. (ICC Staff Ex. 13.0, p. 29) Since the Company agreed with Staff that internal Company costs would not be recovered under Rider ECR (ComEd Exhibit 23.0, p. 66), Staff's adjustment adding those costs back to the revenue requirement appears to be an

uncontested issue in this case. However, Staff's adjustment was not included in Appendix A.

In its determination of the appropriate amount for recovery of non-MGP related environmental expenses to be included in the revenue requirement, it appears that the PO relied on the adjustment put forth by the Company in the surrebuttal testimony of Company witness Hill (ComEd Ex. 36.0, pp 47-48, lines 1062 – 1080). However, the PO did not fully incorporate ComEd's proposal. The PO neglected to also include the proposed adjustment to remove the \$3,303,599 described previously in Mr. Hill's testimony (ComEd Ex. 36.0, p. 4, lines 81 – 102). To fully incorporate the Company's position with regards to non-MGP environmental costs, the revenue requirement should also reflect the reduction of \$3,303,599.

Allows an inappropriate proforma adjustment

Staff continues to take issue with the recovery of any of the non-MGP costs through the delivery services revenue requirement. (Staff IB, p. 101) However, if the Commission finds that some level of cost for non-MGP environmental expenses should be recovered in the revenue requirement, only pro forma adjustments for known and measurable changes from the historic test year should be allowed. The Company's proposed \$1,466,667 adjustment for non-MGP related environmental costs is based on budgets for 3 – 5 years *beyond* the test year. In addition the average of the annual budgets for 2007 – 2009 is approximately 8.4 times greater than the actual expenditures for the test year.⁹ Since the Company did not provide any explanation for the

⁹ As shown on ComEd Ex. 19.0, Schedule 18, the actual expenditures for 2004 for the Superfund sites (continued...)

tremendous increase in the period it chose for its average over the actual expenditures of the test year, that average cannot be the basis for a pro forma adjustment for a known and measurable change in compliance with 83 Ill Admin Code Section 287.40.

Recommended Language

In order to address those concerns set forth above, Staff proposes the following language changes to the Commission's conclusions in the PO on page 101:

Commission Analysis and Conclusion

Both the Company and Staff agreed that internal Company costs related to MGP remediation should be recovered through base rates rather than through Rider ECR. Therefore, Staff's adjustment to add back those internal costs, \$338,000 removed by the Company, is approved.

Because the Commission amended ComEd's proposed Rider ECR to exclude non-MGP related expenses, \$1,466,667 will be added back into certain adjustments must be made to the test year revenue requirement. The Commission finds the proposal set forth in ComEd's surrebuttal testimony (ComEd Ex. 36.0, p. 47) persuasive. The Commission accepts the reduction in environmental expense of \$3,303,599. However, the addition to environmental expense of \$1,466,667 is not in compliance with 83 Ill Admin Code Section 287.40 for pro forma adjustments. The referenced Section states:

A utility may propose pro forma adjustments (estimated or calculated adjustments made in the same context and format in which the affected information was provided) to the selected historical test year for all known and measurable changes in the operating results of the test year. These adjustments shall reflect changes affecting the ratepayers in plant investment, operating revenues,

(continued from previous page)

and the Leaking Underground Storage Tank Sites total \$155,433. The Company's average of those same costs over the three year period 2007 – 2009 is \$1,466,667. That average is 8.4 times the actual expenditures for the 2004 test year. No explanation for those increased budgeted costs has been provided by the Company.

expenses, and cost of capital where such changes occurred during the selected historical test year or are reasonably certain to occur subsequent to the historical test year within 12 months after the filing date of the tariffs and where the amounts of the changes are determinable. Attrition or inflation factors shall not be substituted for a specific study of individual capital, revenue, and expense components. Any proposed known and measurable adjustment to the test year shall be individually identified and supported in the direct testimony of the utility. Each adjustment shall be submitted according to the standard information requirement schedules prescribed in 83 Ill. Adm. Code 285.

Since the Company's proposed \$1,466,667 is based on budgeted amounts for 2007 – 2009, clearly beyond the 12 months after the filing date of tariffs set forth in Section 287.40 and has not been supported in the Company's testimony, that amount cannot be accepted as a pro forma adjustment. Therefore, non-MGP costs to be added back to the revenue requirement shall be the amount of actual expenditures made in 2004, \$155,433.

The following corresponding language changes should also be made on page 212 of the PO:

In summary, the Commission concludes that Rider ECR will cover only MGP related costs. Since non-MGP related costs are not to be included under this Rider, the Commission concludes that ~~\$1,466,667 will be added back into the test-year revenue requirement~~ shall be adjusted as previously discussed in the Operating Expense Section of this Order.

5. Payroll Taxes

Staff proposes the following technical correction to the PO's conclusion on page 104.:

Commission Analysis and Conclusion

Based on these underlying adjustments to ComEd's revenue requirement, ComEd's approved ~~income~~ payroll tax expenses are shown in the Appendix to this Order.

C. RATE OF RETURN

1. Capital Structure

Although the Proposed Order correctly concludes that ComEd's proposed capital structure 1) is not appropriate for ratemaking purposes, 2) does not accurately reflect the capital supporting the Company's depreciated original cost rate base, and 3) is not just and reasonable (PO, pp. 126-129), the Proposed Order erroneously rejects Staff's proposed capital structure of 62.89% debt and 37.11% equity (PO, pp. 129-130). As will be demonstrated below, the Proposed Order relies on mistaken or erroneous information to reject Staff's proposed capital structure. As a result, Staff disagrees with the Proposed Order's conclusion regarding the proper capital structure for the Company. Specifically, the Proposed Order's decision to impute a capital structure is based on erroneous assertions that Staff's proposal is not comparable to previously approved capital structures for ComEd and that Staff's level of debt may not be sufficient to allow the utility to maintain an A- credit rating. In addition, the Proposed Order erroneously refers to Old Dominion as being in Staff's proxy sample. (PO, p. 130)

First, ComEd's approved common equity component was 38.97%, 39.40%, and 42.86% respectively in its last three rate cases. (Order, Docket 94-0065, p. 95 (January 1, 1999); Order Docket 99-0117, p. 46 (August 26, 1999); Order, Docket No. 01-0423, p. 133 (March 28, 2003); Staff Reply Brief, p. 66) Consequently, Staff's proposal for a capital structure containing 37.11% equity is very comparable to previously approved capital structures for ComEd, and the statement in the Proposed Order to the contrary is erroneous. (See PO, p. 130) Staff also notes that in no event should the Commission impute a capital structure that contains more equity than the capital structure the

Commission determined was sufficient to maintain a reasonable level of financial strength in the last proceeding, since the Company has been able to maintain an investment grade credit rating based on that previously adopted capital structure. Thus, even assuming, *arguendo*, that the Commission's final order continues to reject Staff's proposed capital structure, the imputed capital structure should not contain more than 42.86% equity.

Next, although the Proposed Order states that Staff's proposed capital structure "may not be sufficient to allow the utility to maintain its financial strength or a reasonable A- credit rating" (PO, p. 130), there are no specific reasons set forth for this tentative finding and there is no discussion or analysis of Staff's detailed testimony supporting the reasonableness of its proposed capital structure to determine ComEd's overall rate of return. (See PO, pp. 118-122 (Setting forth summary of testimony and arguments supporting reasonableness of Staff's proposed capital structure.)) Staff explained that Standard & Poor's ("S&P") categorizes debt securities on the basis of the risk that a company will default on its interest or principal payment obligations. The resulting credit rating reflects both the operating and financial risks of a utility. Although no formula exists for determining a credit rating, S&P publishes utility benchmark values, by business profile score, for financial ratios it uses to determine credit ratings. S&P currently assigns ComEd a corporate credit rating of BBB+ and a business profile score of 4. Therefore, Ms. Kight compared the values for those benchmark financial ratios that result from combining Staff's proposed adjusted capital structure with components from Staff's proposed revenue requirement to S&P's benchmarks for utilities with an A or BBB credit rating and a business profile score of 4.

According to S&P, utilities with a business profile score of 4 should have a funds from operation (“FFO”) to interest coverage (“FFOIC”) ratio between 3.5X and 4.2X for an A-rating and 2.5X to 3.5X for a BBB-rating. The benchmark ranges for the FFO to total debt (“FFO/Debt”) coverage ratio is 20%-28% for A-rated utilities and 12%-20% for BBB-rated utilities. Ms. Kight testified that Staff’s proposed adjusted capital structure results in a FFO to interest coverage ratio of 3.78X, which is indicative of an A credit rating, and a FFO to total debt coverage ratio of 18.04%, which is indicative of a BBB credit rating.¹⁰ Thus, Ms. Kight concluded that Staff’s proposed adjusted capital structure is indicative of a level of financial strength that is commensurate with at least a BBB credit rating. (ICC Staff Exhibit 4.0 Corrected, pp. 7-8 (emphasis added)) Ms. Kight further testified that a BBB credit rating is indicative of an adequate degree of financial strength. A credit rating of BBB indicates an adequate capacity to meet financial commitments. A debt issuer with a BBB credit rating has access to debt capital under most, if not all, financial market conditions while taking greater advantage of the tax-deductibility of debt interest than capital structures that support higher credit ratings. (ICC Staff Exhibit 4.0 Corrected, p. 10)

¹⁰ The FFO to interest coverage ratio equals interest divided into the sum of the funds available to shareholders, non-cash items (i.e. depreciation, amortization, deferred taxes and investment tax credits), and interest. The FFO to debt coverage ratio equals the sum of the funds available to shareholders and non-cash items divided by total debt. The coverage ratios developed by Ms. Kight determined each component of the ratio based on its contribution to Staff’s recommended revenue requirement for ComEd. “Funds available to shareholders” equals Staff’s recommended weighted cost of common equity for ComEd (i.e., the product of the cost of common equity and the common equity ratio). Depreciation, amortization, deferred taxes and investment tax credits equal Staff’s recommended amounts for those items divided by Staff’s recommended rate base. The interest component equals Staff’s recommended weighted cost of debt in the capital structure for the Company (i.e., the product of the cost of debt and the debt ratio). Total debt equals Staff’s recommended percentage of debt in ComEd’s capital structure. (ICC Staff Ex. 4.0 Corrected, pp. 9-10)

Further, the Proposed Order does not explain its reasoning or cite any evidence to support why it is necessary for ComEd to have an A- credit rating to maintain a reasonable level of financial strength. Nevertheless, Staff notes that under Staff's proposal ComEd's FFO/Debt ratio falls in the top third of the BBB range and its FFOIC ratio is in the middle third of the A range. Together, the two ratios indicate that Staff's proposed rates are sufficient to support financial strength that is commensurate with a credit rating of "A-" and is therefore consistent with the "A-" credit rating that the Company purports to target. (ICC Staff Exhibit 15.0 2nd Corrected, pp. 2-3) Table 1 presents the coverage ratios for the financial guidelines for the business profile "4" as well as those resulting from Staff's proposed capital structure and capital costs and the Proposed Order's capital structure and capital costs.

Table 1

	AA	A	BBB
Financial Guideline Ratios			
FFOIC	4.2-5X	3.5-4.2X	2.5-3.5X
FFO/Debt	28-35%	20-28%	12-20%
Staff Proposal			
FFOIC		3.78X	
FFO/Debt			18.04%
Proposed Order			
FFOIC	4.22X		
FFO/Debt		20.91%	

Staff submits that Table 1 also illustrates that the capital structure recommended in the Proposed Order results in ratios that are commensurate with an "A/A+" credit rating, instead of the "A-" credit rating it apparently believes will allow ComEd to maintain a reasonable level of financial strength. (PO, p. 130)

Finally, the Proposed Order errs in stating that Staff's proposed capital structure "is an outlier compared to utilities generally and to those in Staff's proxy sample (except for Old Dominion, which ComEd points out is a non-profit and functionally unregulated)." (PO., p. 130) First, Ms. Kight did not present any proxy samples. The only proxy sample used by Staff that has any effect on Staff's capital structure or component cost recommendations is the proxy sample used by Mr. McNally, which did not include Old Dominion. (ICC Staff Exhibit 5.0, Schedule 5.1)

Ms. Kight did present, as part of her workpapers, a comparison of A rated electric utilities (including Old Dominion) and a comparison of utilities with an A- credit rating and a business profile score of 4. (ICC Staff Cross Exhibit 13) The comparison of A- utilities with a business position of 4 served merely to illustrate that two of those six companies had three year average equity balances of less than 40%. In fact, the 3-year average equity balance was 38.61% and 38.48% for AGL Resources, Inc. and Scana Corporation, respectively. The same cross exhibit showed that the equity balance ranged from 32.2% to 66.3% over the past five years for all companies with an A- credit rating and a business profile score of 4. Thus, a common equity balance of 37.11%, although on the low end, clearly would not prohibit ComEd from maintaining an A- credit rating.

Recommended Language

Consistent with the arguments and analysis presented above, the Commission Analysis and Conclusion section should be modified as follows:

Commission Analysis and Conclusion

Starting at Page 130, first full paragraph

In light of the foregoing discussion, the Commission believes that Staff's adjustments have merit, ~~but and~~ the Commission is ~~not~~ satisfied that Staff's capital structure properly reflects ComEd's level of debt. ~~If the levels are not set properly, the Company may experience negative market consequences. A severe error may result in rates that are not just inappropriate, but confiscatory.~~ The Commission also finds that Staff's proposed capital structure is reasonable to use for ratemaking purposes based on the results of Staff's benchmark ratio analysis. As a result of that analysis, Ms. Kight concluded that Staff's proposed adjusted capital structure is indicative of a level of financial strength that is commensurate with at least a BBB credit rating. Ms. Kight further testified that a BBB credit rating is indicative of an adequate degree of financial strength and an adequate capacity to meet financial commitments. CUB-CCSAO-City witness Bodmer and IIEC witness Gorman also found Staff's proposed capital structure to be reasonable for purposes of determining ComEd's overall rate of return. The Commission agrees with the analysis and conclusions proffered by Staff and supported by Intervenors.

The Commission also notes that Staff's proposal is ~~not~~ comparable to previously approved capital structures for ComEd ~~or other financially sound utilities~~, and ~~may not be~~ is sufficient to allow the utility to maintain its financial strength as well as its targeted or a reasonable A- credit rating. ~~It also is an outlier compared to utilities generally and to those in Staff's proxy sample (except for Old Dominion, which ComEd points out is a non-profit and functionally unregulated). Other than Old Dominion, the companies in Staff's sample have at least 41% equity.~~ Accordingly, the Commission ~~declines to~~ adopts a capital structure of 62.89% debt and 37.112% equity.

The Commission observes that Illinois Courts have repeatedly stated that setting rates is a legislative function. (*See, e.g., Bus. & Prof'l People for Pub. Interest v. ICC*, 146 Ill. 2d 175, 196 (1991); *Ill. Cent. R.R. Co. v. ICC*, 387 Ill. 256, 275 (1944); *City of Chicago v. ICC*, 281 Ill. App. 3d 617, 622 (1996); *CUB v. ICC*, 276 Ill. App. 3d 730, 734 (1995).) The Commission therefore concludes that in determining whether a proposed capital structure is when no party proposes a just and reasonable capital structure, it is the duty of the Commission to protect both ratepayers and investors ~~by assigning one that is just and reasonable.~~

Weighing all of the considerations discussed above, the Commission finds that Staff's methodology should be adopted ~~to the extent such~~ that the net adjustments produce a capital structure consisting of 37.1146% equity and 62.8954% debt. The

Commission believes that such structure achieves a balance that both reflects Staff's adjustments to set rates based on original cost and trims ComEd's balloon of goodwill resulting from the plant transfers to unregulated affiliates. ~~At the same time, it avoids sharp swings in the Company's capital structure which could cause financial and credit concerns for the Company.~~

2. Cost of Long-Term Debt

Staff disagrees with the Proposed Order's conclusion regarding the cost of long-term debt in the Company's capital structure. The Proposed Order's decision to accept the Company's ending balances and amortization of unamortized loss on reacquired debt as correct (PO, p. 134) is based on ComEd's books that are in violation of Commission rules regarding the amortization of Unamortized Loss on Reacquired Debt. (See General Instruction 17 of the "Uniform System of Accounts for Electric Utilities", 18 CFR 101 (2003), as adopted by 83 Ill. Adm. Code 415.10, subject to the exceptions set forth in 83 Ill. Adm. Code 415.380; Staff Initial Brief, pp. 75-77; Staff Reply Brief, pp. 69-70). The Proposed Order simply fails to address in any way Staff's position and argument regarding the inconsistency of ComEd's "actual" amounts with the Commission's rules. The Company should not be rewarded for failing to follow Commission rules.

Staff witness Ms. Kight explained why and how she determined that the amounts contained in ComEd's Exhibit 20.5b failed to reflect straight-line amortization and thus violate Commission rules:

To illustrate, the unamortized balances of loss on reacquired debt for the 8.750%, Series 30 as of December 31, 2004, are the same on ICC Staff Exhibit 4.0, Schedule 4.2 and ComEd Ex. 20.5b. However, the June 30, 2005 unamortized balances differ. The annual amortization of Series 30 loss is approximately \$90,900 using straight line amortization. Therefore, the June 30, 2005 balance should equal the December 31, 2004 balance of \$772,849 minus half of the \$90,900 annual amortization, or approximately \$727,400. However, ComEd Ex. 20.5b lists the June 30,

2005 balance as \$647,306. The approximately \$80,000 difference between the two June 30, 2005 balances indicates that ComEd's balance does not reflect straight line amortization.

(ICC Staff Exhibit 15.0 2nd Corrected, p. 6)

Staff notes that the surrebuttal testimony of ComEd witness Mr. Mitchell makes the conclusory assertion that he does not agree with Ms. Kight's position "because the balances and amortization amounts shown on ComEd Exhibit 20.5b are accurate and in accordance with applicable accounting and rate making principles." (ComEd Ex. 37.0 2nd Corrected, p. 24) Staff also notes that ComEd did not offer any analysis or explanation attempting to refute Ms. Kight's specific demonstration that ComEd's balances and amortization amounts do not reflect straight line amortization. Given that General Instruction 17 of the Uniform System of Accounts for Electric Utilities provides for the use of straight line amortization, Staff submits that Ms. Kight's recommended cost of long term debt is the only recommendation supported by the record that is consistent with Part 415.

Recommended Language

Based on the discussion above, Staff recommends that the language in the Proposed Order be amended as follows:

Page 134, first full paragraph

Commission Analysis and Conclusion

The Commission finds that ComEd's use of its actual ending balances and amortization amounts of unamortized loss on reacquired debt as of June 30, 2005, do not reflect the use of straight line amortization and thus are inconsistent with the Commission rules regarding the amortization of Unamortized Loss on Reacquired Debt. (See General Instruction 17 of the "Uniform System of Accounts for Electric Utilities", 18 CFR 101 (2003), as adopted by 83 Ill. Adm. Code 415.10, subject to the exceptions set

~~forth in 83 Ill. Adm. Code 415.380). debt cost is consistent with the filing requirements of 83 Ill. Admin. Code §§ 285.4000 - 4030, which, while not determinative, permit utilities to use an historic measurement period (as ComEd has done here). The Commission further finds that Staff's the correct ending balances and amortization amounts are consistent with the Commission rules and reflect a cost of long-term debt of 6.48% support ComEd's actual debt cost of 6.50%, and thus rejects ComEd's proposed 6.50% cost of debt Staff's suggestion of 6.48%, which is not based on straight line amortization such balances and amounts. The Commission also finds no merit in CCC's suggested hypothetical cost – the record shows, among other things, that such cost is based on a different corporation's debt, improperly includes \$300 million of short-term debt, and is based on debt issued in mid-2005, when interest rates were at an historically low level. Indeed, CCC does not question ComEd's use of June 30, 2005 for an historic measurement period date or its computation of its cost of long-term debt, nor suggest that such cost was imprudent or unreasonable. Accordingly, the Commission concludes that ComEd's use of its actual long-term debt cost is appropriate.~~

3. Cost of Common Equity

Assuming that Staff's proposed capital structure is adopted in the Commission's final order, Staff agrees with the Proposed Order's adoption of Staff's proposed cost of equity. Nevertheless, the Proposed Order's stated reasons for choosing Staff's proposed cost of equity should be modified since, as explained below, the "goodwill" basis stated in the Proposed Order is neither reasonable nor logical. If the Commission's final order continues to impute a capital structure with more than 37.11% equity, then Staff recommends that the Commission adopt IIEC's 9.90% cost of equity, as a downward adjustment to at least 9.90% would be required to reflect the reduced risk from having a capital structure with more than 37.11% equity.

The Proposed Order states "that IIEC's 9.90% proposal may be slightly too low in light of their complete exclusion of goodwill related to the plant transfers . . . and our determination, *supra*, that a portion should be included in the capital structure." (PO, p.

155). First, given the Proposed Order's decision to reject Staff and IIEC's proposed capital structure in favor of a capital structure with a higher equity ratio, it is illogical to choose the higher of Staff's and IIEC's cost of equity estimates. Increasing the amount of equity in the capital structure reduces risk. Therefore, the Proposed Order's conclusion that a higher return on equity must be chosen since risk was reduced, is illogical since the higher return on equity suggests a higher level of risk. Indeed, under the Proposed Order's imputed capital structure, a downward adjustment to Staff witness Mr. McNally's cost of equity recommendation would be necessary, since ratios indicate the capital structure proposed by the ALJs is indicative of a A/A+ credit rating. Mr. McNally's recommended cost of equity is reflective of an A-/BBB+ credit rating, which is consistent with the capital structure proposed by Staff and the intervenors. Second, it is improper for the Proposed Order to add back goodwill, since the ALJs concluded that goodwill should not be included in the capital structure; instead, they determined that an imputed capital structure was just and reasonable. Therefore the ALJ's Proposed Order should be modified to remove the reference regarding the adding back in of goodwill. (PO, p. 155)

Recommended Language

Based upon the discussion above, Staff recommends that the PO be amended as follows if the Commission's final order adopts Staff's proposed capital structure:

Page 155, third full paragraph

Cost of Equity

In light of the determination of the foregoing issues, the Commission finds that the ComEd proposal is excessively high due to its improper application of the GDP growth rates, and the CUB/City/CCSAO proposal is inadequately low due to its application of the latter two issues just rejected. This leaves the

proposals of Staff and IIEC. The Commission notes that the results of the analyses produced by Staff and IIEC are relatively close, and that the amount of argument from either against the other is minimal. ~~The Commission finds, however, that IIEC's 9.90% proposal may be slightly too low in light of their complete exclusion of goodwill related to the plant transfers (see, e.g., IIEC Init. Br. at 17-18) and our determination, supra, that a portion goodwill should be included in the capital structure. Staff showed that its proposed capital structure and capital costs are commensurate with a BBB+/A- credit rating, which is consistent with the average credit rating of the companies in the sample from which Staff derived its cost of equity estimate. (ICC Staff Exhibit 5.0, Schedule 5.2.) Thus, Staff's cost of equity is appropriate for use in conjunction with Staff's capital structure, which we have adopted. In contrast, the Commission finds that IIEC's 9.90% proposal may be too low for use in conjunction with Staff's capital structure. Accordingly, Staff's 10.19% cost of equity is adopted.~~

In the alternative, if the Commission's final order continues to impute a capital structure containing more than 37.11% equity, the PO should be modified as follows:

Page 155, third full paragraph

Cost of Equity

In light of the determination of the foregoing issues, the Commission finds that the ComEd proposal is excessively high due to its improper application of the GDP growth rates, and the CUB/City/CCSAO proposal is inadequately low due to its application of the latter two issues just rejected. This leaves the proposals of Staff and IIEC. The Commission notes that the results of the analyses produced by Staff and IIEC are relatively close, and that the amount of argument from either against the other is minimal. ~~The Commission finds, however, that IIEC's 9.90% proposal may be slightly too low in light of their complete exclusion of goodwill related to the plant transfers (see, e.g., IIEC Init. Br. at 17-18) and our determination, supra, that a portion goodwill should be included in the capital structure. Given our decision to impute a capital structure containing more than 37.11% equity (i.e., Staff's proposed capital structure), we agree that a downward adjustment to Staff's cost of equity recommendation is necessary. The higher equity ratio we have adopted suggests a higher level of risk than that suggested by Staff's 37.11% equity ratio. Since Staff's cost of capital recommendations, including the capital structure, are consistent with Staff's cost of equity, it would be inconsistent and imprudent to retain Staff's cost of equity while rejecting Staff's~~

capital structure for one less risky. Thus, since we have adopted a capital structure indicating a lower risk than Staff's analysis, for consistency, we should also adopt a cost of equity indicating a lower risk than Staff's analysis. Accordingly, IIEC's 9.90% ~~Staff's 10.19%~~ cost of equity is adopted.

4. **Approved Rate of Return on Rate Base**

The following amendments to the PO's Approved Rate of Return on Rate Base are necessary to reflect the proper exclusion of goodwill in ComEd's capital structure and Staff's cost of long-term debt:

Page 155

Approved Rate of Return on Rate Base

Upon incorporation of the conclusions stated above, the Commission finds that ComEd's capital structure and cost of capital, resulting in overall cost of capital of ~~7.868~~20% may be summarized as follows:

<u>Class of Capital</u>	<u>Proportion</u>	<u>Cost</u>	<u>Weighted Cost</u>
Long-term debt	62.89 54.00 %	6.48 6.50 %	4.08 3.51%
Common Equity	37.11 46.00 %	10.19%	3.78 4.69%
TOTAL	100.00%		7.86820%

The Commission finds that this overall cost of capital to be reasonable and should be used for purposes of ComEd's authorized rate of return on rate base in this proceeding.

D. RATE DESIGN

1. Customer Class Delineations

a. Residential

The PO rejects the AG's proposal to modify Staff's mitigation proposal adopted by the Commission in ICC Docket No. 05-0159. However, in rejecting the AG's proposal, the PO makes the statement that "[w]hile utility rate increases are unpleasant, the Commission concludes that the rate design adopted herein along with the rate mitigation plan adopted in Docket 05-0159 will sufficiently mitigate the adverse impacts for most residential customers." (PO, p. 184) As the Commission is well aware, ComEd has filed a petition to establish a residential rate stabilization program ("RRS Program"). (ICC Docket No. 06-0411) According to ComEd, "[t]he RRS program is designed to ease residential customers' transition from current reduced and frozen rates to rates that reflect ComEd's just and reasonable and Commission-approved costs of buying and delivering electricity safely and reliably to its residential customers." (ComEd RRS Petition, p.1) The Order in this docket should not preclude the resolution of issues raised in Docket No. 06-0411. Thus, given the pending ICC Docket No. 06-0411 with the stated intent of the petition to examine the potential for further mitigation of residential rates, the statement made in the PO about rate increases and their impacts on customers should be deleted.

Recommended Language

Staff recommends the following changes to page 184 of the PO.

* * *

Using the revenue requirement approved in this Order and its ECOSS, ComEd is directed to develop residential rates that comply with these findings. Finally, the Commission rejects the AG's

proposal to modify the rate mitigation proposal adopted in Docket 05-0159. ~~While utility rate increases are unpleasant, the Commission concludes that the rate design adopted herein along with the rate mitigation plan adopted in Docket 05-0159 will sufficiently mitigate the adverse rate impacts for most residential customers.~~

* * *

2. Environmental Cost Rate Redesign

The Commission should reverse the PO's rejection of Staff's proposed Environmental Cost Rate Redesign. Staff's proposed rate redesign would change rates in an effort to reduce environmental impact of electricity production. The PO's findings are not supported by the record, and the Staff's proposal creates more benefits than harm.

The rationale for the PO's rejection of Staff's proposal is as follows:

Having reviewed the record in its entirety, the Commission rejects Staff's proposal at this time. While the Commission appreciates and shares Staff's concerns, the Commission believes that a twenty percent shift of revenue from facilities charges is not warranted. Elsewhere in this Order and in other docketed proceedings, the Commission is taking affirmative steps to encourage conservation and off-peak usage of electricity. All things considered, the Commission believes Staff's proposed twenty percent adjustment, as it would apply to ComEd, should be rejected, because it would result in distribution facilities charges deviating too far from costs.

(PO, pp. 203-204).

It appears that the ALJ's reached their conclusion based on two points: the Commission is taking affirmative steps in this and other dockets to encourage conservation and that distribution facilities charges would deviate too far from costs. (PO, p. 204).

The facts underpinning the first point are absent from the record. No party argued that there is a sufficient amount of steps being taken to encourage conservation

of electricity. In addition, the implication of the reasoning in the first point is that the Commission has taken, and is taking, enough affirmative steps to encourage conservation and off-peak usage of electricity, and that also lacks factual support.

The second, and primary, point for rejecting Staff's proposal is that distribution facilities charges would deviate too far from costs. While it is true that shifting twenty percent of customer costs away from facilities charges would create some deviation from the associated cost, the benefit from this shift, in terms of recognizing the important connection between electricity consumption and environmental damage, would far outweigh any negative effects from the Staff proposal. In addition, this deviation should be accorded little weight, since the reduction of facilities charges would be recovered by an equal change increase of usage charges.

Thus, Staff recommends that the PO accept Staff's proposed Environmental Rate Redesign as set forth in its Initial Brief (at pp. 93-98) and Reply Brief (at p. 78-81).

Recommended Language

Staff recommends that the final paragraph of the Commission Analysis and Conclusion section be modified as follows:

~~Having reviewed the record in its entirety, the Commission accepts Staff's proposal. Staff has expert knowledge upon which we rely, therefore the absence of a full-blown study regarding price elasticity is not a concern at this time. In addition, Staff's proposal has a zero-net effect, since the increase in user charges would be balanced by an equal and opposite reduction in facilities charges. rejects Staff's proposal at this time. While the Commission appreciates and shares Staff's concerns, the Commission believes that a twenty percent shift of revenue from facilities charges is not warranted. Elsewhere in this Order and in other docketed proceedings, the Commission is taking affirmative steps to encourage conservation and off-peak usage of electricity. All things considered, the Commission believes Staff's proposed twenty percent adjustment, as it would apply to ComEd, should be~~

~~rejected, because it would result in distribution facilities charges deviating too far from costs.~~

3. Rider ECR

Staff suggests two language changes to clarify the conclusion regarding Rider

ECR:

- 1) The amount of non-MGP costs on page 212 should be corrected to be consistent with the PO's conclusion regarding the level of environmental expenses to be recovered through base rates.
- 2) The conclusion should be supplemented to indicate the specific tariff language which the Commission is approving to avoid any confusion.

Recommended Language

Staff proposes the following language revisions to the PO's conclusions on page

212:

In summary, the Commission concludes that Rider ECR will cover only MGP related costs. Since non-MGP related costs are not to be included under this Rider, the Commission concludes that ~~\$1,466,667 will be added back into the test-year revenue requirement~~ shall be adjusted as previously discussed in the Operating Expense Section of this Order. Therefore, the Commission approves Rider ECR as amended above. Rider ECR tariff language that is filed pursuant to this order should be consistent with the foregoing conclusions and as set forth in ICC Staff Exhibit 13.0, Attachment C.

4. Rider NS

a. Rider NS and Elimination of Rider 8

Staff takes three exceptions to the PO's discussion and findings on this issue. First, the description of ComEd's alternative proposal is incorrect. Staff would normally not request that another party's position be corrected, because we view that to be the responsibility of each party to assure that their position is accurately stated, however, in this situation, the error is transferred into the Commission Analysis and Conclusion

section. Briefly stated, the cause of this confusion arises from position descriptions in ComEd's Proposed Order and Reply Brief that differ from the proposals in ComEd witness Crumrine's testimony. (*See infra*). Staff's second exception is that ComEd has provided no evidence showing that the termination of Rider 8 is just and reasonable. ComEd's reasoning for this change is that it is simply "housecleaning", yet, this cleaning harms those customers who purchased transformers in reliance upon being compensated through Rider 8 credits. ComEd's reason for this change is not just and reasonable when balanced against the harm it causes to nearly 140 Rider 8 customers. Finally, the final paragraph of the Commission Analysis and Conclusion section is internally inconsistent. That paragraph contains language that supports both ComEd's primary and alternative proposals. If the Commission adopts one of ComEd's proposals, it needs to clearly state which proposal is being accepted.

(1) PO Incorrectly Describes ComEd's Position

The alternative position ComEd described in its Proposed Order (ComEd Proposed Order, pp. 136-27) and its Reply Brief (ComEd RB, p. 141), differ from what their witnesses proposed. Consequently, the PO incorrectly describes ComEd's position. The PO should be changed to recognize the positions espoused in ComEd's testimony rather than what was submitted in ComEd's Proposed Order and Reply Brief.

The best way to describe the evolution of ComEd's proposals is to review ComEd witnesses Alongi and McInerney's testimony. ComEd's position in direct testimony was straightforward – "ComEd proposes to discontinue Rider 8." (ComEd Ex. 10.0, p. 36, line 834)

In rebuttal testimony, Messr's Alongi and McInerney changed their initial position and offered an alternative. The change to their initial position ("Original Offer") was to terminate Rider 8 and pay each Rider 8 customer one year worth of credits:

ComEd does not believe a one-time payment for loss of future Rider 8 credits is necessary to discontinue Rider 8 because ComEd's proposal includes the replacement of the Rider 8 credit with an appropriate Rider NS standard transformer allowance. Nevertheless, in order to discontinue Rider 8 customer in an amount that is equivalent to one year of Rider 8 credits based on the customer's average Rider 8 credits received over the most recent three-year period.

(ComEd Ex. 24.0, p. 26, lines 664-670) A few sentences later, Messr's Alongi and McInerney proffered an alternative position ("Alternative Proposal") as follows:

In the event that ComEd's offer to provide a one-time, one year-equivalent transition payment is not approved by the Commission, ComEd requests that the Commission approve limiting the availability of Rider 8 to only those customers served under the rider that own all of the transformers at their premises as of the date the Commission enters into its Order in this proceeding and that continued availability of Rider 8 to such customers be conditioned on the customer continuing to own all transformers at its premises. . . . ComEd will include an appropriate rider in its compliance filing that provides for such credits at the rate currently effective in Rider 8 and also adjust ComEd's rate design spreadsheet to provide an offset for such continued credits in order for ComEd to recover its revenue requirement.

(ComEd. Ex. 24.0, pp. 26-27, lines 674-679, 685-689).

ComEd's surrebuttal testimony initiates the confusion of ComEd's position by incorrectly citing the two proposals described in rebuttal testimony as its "original offer:"

We continue to believe that our original offer is reasonable and that the Commission should approve it as described in our Rebuttal Panel Testimony. (ComEd Ex. 24.0, p. 26, lines 667 to p. 27 line 689). However, if the Commission should disagree, then the Commission should allow ComEd to limit the availability of the rider to those customers taking service under Rider 8 as of the date of the Commission's Order. In that case, ComEd will include an appropriate rider in its compliance filing that provides for such credits at the rate currently effective in Rider 8 and also adjust ComEd's rate design spreadsheet (cite omitted) to provide an offset for such continued credits in order for ComEd to recover its revenue requirement.

(ComEd Ex. 41.0 Corrected, p. 18-19)

To summarize ComEd's testimony, ComEd's Original Offer was set forth in direct and modified in rebuttal testimony, and currently is to terminate Rider 8 and pay a transition fee to Rider 8 customers equal to one year worth of credit. In addition, in rebuttal testimony, ComEd proposed an Alternative Proposal. This proposal was then reiterated in surrebuttal testimony (and is quoted above). To Staff's knowledge, ComEd has not formally stated in brief that it has withdrawn or changed any of its positions from what they were stated in testimony. Furthermore, these were not the positions described in ComEd's Proposed Order (ComEd Proposed Order, pp. 136-27), Reply Brief (p. 141) or in the PO (p. 222).

Thus, Staff recommends that the PO be modified to describe the positions espoused by ComEd witnesses Alongi and McInerney in their rebuttal testimony, and not the position incorrectly stated in ComEd's Proposed Order.

Recommended Language

ComEd's Position should be modified as follows:

(1) ComEd

ComEd proposed that current Rider 8 should be eliminated. As described by ComEd, this seldom-used rider provides a small credit (20.533¢/kW) to approximately 225 current customers (less than 35 have installed their own transformer and utilized Rider 8 over the past 10 years) who have installed their own transformers. ComEd proposed to provide a standard transformer allowance under Rider NS to replace the Rider 8 credit, which ComEd indicated would likely result in lower Rider NS monthly rental charges for many of the current Rider 8 customers.

In response to Staff's recommendation, ComEd stated that it is agreeable to provide a one-time transition payment to each Rider 8 customer in an amount that is equivalent to one year of Rider 8

credits, based on the customer's average Rider 8 credits received over the most recent three year period.

In the event that ComEd's offer to provide a one-time, one year-equivalent transition payment is not approved by the Commission, ComEd requests that the Commission approve limiting the availability of Rider 8 to only those customers served under the rider that own all of the transformers at their premises as of the date the Commission enters into its Order in this proceeding and that continued availability of Rider 8 to such customers be conditioned on the customer continuing to own all transformers at its premises. ComEd will include an appropriate rider in its compliance filing that provides for such credits at the rate currently effective in Rider 8 and also adjust ComEd's rate design spreadsheet to provide an offset for such continued credits in order for ComEd to recover its revenue requirement ("Alternative Proposal").

(2) ComEd has not Shown that Terminating Rider 8 is "Just and Reasonable"

The PO's rejection of Staff's proposal lacks sufficient evidentiary support to show that the elimination of Rider 8 is "just and reasonable." In addition the finding is internally inconsistent. The PO finds that it is best to eliminate Rider 8¹¹ and offer a one time payment to customers that is equal to one year's worth of credit and accepts ComEd's alternative proposal. ComEd's alternative proposal is contradictory to the PO's findings because the alternative proposal continues to offer Rider 8 to current customers taking of Rider 8, but does not allow new customers to take of the rider. Therefore, Staff recommends that its position be adopted. (Staff IB, p. 106)

By rejecting Staff's proposal, the PO is failing to acknowledge the potential financial harm to customers currently relying on the Rider 8 transformer credit to

¹¹ Rider 8 provides a credit to customers who are supplied or delivered electricity at 2,160 volts or more and where the customer furnishes, installs and maintains any an all transformers and other facilities necessary to reduce primary voltage. (Rider 8, as set forth in tariff sheet -- ILL. C.C. No. 4, 31st Revised Sht. No. 70).

compensate them for the outstanding cost of the purchase and maintenance of the transformer. (See Tr., pp. 1300-01, ComEd Witness Alongi stating that the credit compensates the customer for the cost of the purchase and maintenance of the transformer) The PO's decision places a burden on the customer beyond just paying higher electricity rates, it determines that this class of customer (those who purchased a transformer and have not received credits equal to the cost of the transformer) now has to assume the outstanding cost of the transformer they purchased as well as the unrecovered maintenance costs. This PO's decision is unequivocally unfair to those customers.

Beyond the fairness of this decision, ComEd has not shown that terminating Rider 8 is just and reasonable. ComEd justifies the termination of Rider 8 by calling it a housekeeping change (ComEd IB, p. 225), however, as discussed in the preceding paragraph, terminating this compensation imposes a financial harm to ratepayers. (Staff RB, p. 84; Staff IB, pp. 107-08) It is not "just and reasonable" to terminate a compensation because of a "housekeeping change" when there are customers who made a significant capital outlay to purchase a transformer and had an expectation of being compensated through Rider 8. Even ComEd witness Alongi acknowledged that the credit was intended to compensate the customer for their cost of purchasing and maintaining a transformer. (Tr., pp. 1300-01, lines 21-3) ComEd's alternative proposal (to continue paying customer credits under Rider 8 until the customer decides to terminate service or needs a new transformer), in effect, recognizes that there are some Rider 8 customers who rely upon the credits to offset the purchase price of the transformer.

In addition, ComEd should be required to negotiate a termination payment with the Rider 8 customer. (Staff RB, p. 83; Staff IB, pp. 106-108) ComEd proposes to give one year's worth of credit to each Rider 8 customer, however it did not prove that such a credit is adequate compensation for the outstanding cost of the transformers purchased by Rider 8 customers. Thus, the PO's decision to provide Rider 8 customers one year's worth of credits is not adequately supported by the record in this case. In reply brief ComEd complained that there were no parameters on the negotiations. (ComEd RB, p. 141) If that was a concern that influenced the decision stated in the PO, it is easily resolved. Staff witness Linkenback stated that ComEd and the Rider 8 customer reach a mutually agreeable transition payment. (ICC Staff Exhibit 19.0, pp. 7-8) The customer has the best knowledge of what costs and maintenance expenses it incurred and if there are any other extrinsic costs that would factor into an determining an equitable transition payment. After all, there are no parameters on the negotiations of the sale of a home. If a mutually agreed upon price cannot be reached, there is no harm, the customer continues on Rider 8.

The PO (at p. 227) states: "Staff's concern that certain customers may pay more as a result of transitioning from Rider 8 to Rider NS, while legitimate, is an inevitable result of administrative rate making." That is not a fair assessment of the increase that would occur under this proposal. The bottomline impact of ComEd's proposal is that the ability to recover the outstanding cost of the transformers that were purchased will be foreclosed to over 140 of the total 225 Rider 8 customers. (ICC Staff Exhibit 8.0, p. 14 line 318; Tr., p. 1298, lines 5-9, 83 Rider Customers are hybrids, therefore the remaining customers are impacted by the termination of Rider 8). Rider 8 customers

purchased transformers with the opportunity of recovering those costs through the Rider 8 credit. (Staff RB, p. 84; Staff IB, pp. 107-08) Terminating Rider 8 deprives those customers from recovering the cost of the transformer they purchased, while ComEd was able to benefit from not having to purchase a transformer for these customers.

Thus, the PO's findings should be changed, Rider 8 should continue for all existing customers to provide them the benefits they expect when they purchased their transformers. If the Commission, however, decides that ComEd should be allowed to terminate Rider 8, the Commission should reject ComEd's proposed termination payment of a "one-time, one-year equivalent transition payment", and instead require ComEd and the customer to negotiate a payment for termination.

Recommended Language

If the Commission adopts Staff's primary position, Staff recommends the following edits:

ComEd proposes to eliminate Ride 8 and provide a standard transformer allowance under Rider NS to replace the Rider 8 credit. Staff expressed concern that this proposal would raise the cost to some Rider 8 customers and opposes the elimination of Rider 8. Therefore, Staff recommends that Rider 8 not be eliminated, or as an alternative, that Rider 8 customers be allowed to negotiate a termination payment. The termination payment would allow the customer to be able to agree upon an amount that would adequately compensate it for the costs it incurred in having to purchase a transformer. In response, ComEd proposes an alternative to the position it put forth in its direct testimony, proposing to suggest that in conjunction with eliminating Rider 8 it would continue Rider 8 and provide those customers who want to terminate Rider 8 a one-time transition payment to each Rider 8 customer in an amount equivalent to one year of Rider 8 credits. This would be based on the customer's average Rider 8 credits received over the most recent three-year period. Staff argues that any one-time credit should be negotiated between ComEd and each Ride 8 customer, since it is unclear whether such a credit would adequately compensate Rider 8 customers for the

~~outstanding cost of their purchase of a transformer. In the event the one-time credit is not negotiated, Staff recommends that Rider 8 be retained.~~ ComEd objects to negotiating a one-time credit with customers and instead would prefer to allow existing customers to be grandfathered under Rider 8 and allow ComEd to make a corresponding adjustment to its rate design to provide an offset for such continued credits to allow ComEd to recover its revenue requirement.

Having reviewed the record as well as the arguments on this issue, the Commission concludes that it would be best to ~~allow ComEd to eliminate~~ continue Rider 8 without modification. We find that ComEd has not provided sufficient reason for us to find the termination of Rider 8 to be just and reasonable. In addition, we do not see the termination of Rider 8 to be reasonable given that approximately 140 of the 225 customers would no longer recover the money they invested in the purchase of one or more transformers. Rider 8 customers purchased transformers with the expectation that Rider 8 credit would compensate them for their cost of purchase. To leave those customers without adequate compensation causes a harm that is not justified at this time. ~~As discussed elsewhere in this order, determining how many rate classes should exist involves balancing competing interests. Staff's concern that certain customers may pay more as a result of transitioning from Rider 8 to Rider NS, while legitimate, is an inevitable result of administrative rate making. In the Commission's view, it is undesirable to create a new "grandfathered" customer class on Rider 8. The Commission believes that ComEd's proposal to provide a one-time transition payment based on the customer's average Rider 8 credits over the most recent three-year period is a reasonable compromise. ComEd's alternate proposal is therefore adopted.~~

If the Commission adopts Staff's alternative position, Staff recommends the following edits:

ComEd proposes to eliminate Ride 8 and provide a standard transformer allowance under Rider NS to replace the Rider 8 credit. Staff expressed concern that this proposal would raise the cost to some Rider 8 customers and opposes the elimination of Rider 8. Therefore, Staff recommends that Rider 8 not be eliminated, or as an alternative, that Rider 8 customers be allowed to negotiate a termination payment. The termination payment would allow the customer to be able to agree upon an amount that would adequately compensate it for the costs it incurred in having to purchase a transformer. In response, ComEd proposes an

~~alternative to the position it put forth in its direct testimony, proposing to suggest that in conjunction with eliminating Rider 8 it would continue Rider 8 and provide those customers who want to terminate Rider 8 a one-time transition payment to each Rider 8 customer in an amount equivalent to one year of Rider 8 credits. This would be based on the customer's average Rider 8 credits received over the most recent three-year period. Staff argues that any one-time credit should be negotiated between ComEd and each Rider 8 customer, since it is unclear whether such a credit would adequately compensate Rider 8 customers for the outstanding cost of their purchase of a transformer. In the event the one-time credit is not negotiated, Staff recommends that Rider 8 be retained. ComEd objects to negotiating a one-time credit with customers and instead would prefer to allow existing customers to be grandfathered under Rider 8 and allow ComEd to make a corresponding adjustment to its rate design to provide an offset for such continued credits to allow ComEd to recover its revenue requirement.~~

Having reviewed the record as well as the arguments on this issue, the Commission concludes that it would be best to ~~allow ComEd to eliminate continue Rider 8, but close it to new customers, and allow the existing customers to negotiate a termination payment. The record is clear that some customers would be harmed from terminating Rider 8, since the Rider 8 credit provided an offset to their cost of purchasing a transformer. If we were to terminate Rider 8, approximately 140 of the 225 Rider 8 customers would no longer receive credits that compensate them for the cost of purchasing and maintaining their transformer. The loss of the Rider 8 credit is a harm to Rider 8 customers that outweighs the reasons put forth by ComEd. To ensure that Rider 8 customers are adequately compensated for the outstanding purchase and maintenance costs they have incurred, we find it reasonable to require ComEd to enter into negotiations with those Rider 8 customers to determine a mutually agreeable transition payment amount.~~ As discussed elsewhere in this order, determining how many rate classes should exist involves balancing competing interests. Staff's concern that certain customers may pay more as a result of transitioning from Rider 8 to Rider NS, while legitimate, is an inevitable result of administrative rate making. In the Commission's view, it is undesirable to create a new "grandfathered" customer class on Rider 8. The Commission believes that ComEd's proposal to provide a one-time transition payment based on the customer's average Rider 8 credits over the most recent three-year period is a reasonable compromise. ComEdStaff's alternate proposal is therefore adopted.

(3) If ComEd's Alternative Proposal is Accepted then PO Needs Modification

The PO's summary of ComEd's position is incorrect – it does not describe ComEd's alternative proposal. This translates into confusion in the Commission Analysis and Conclusion section because it expressly states “ComEd's alternative proposal is therefore accepted” (PO, p. 227). Therefore, if Staff's proposals are not accepted and it is the intent of the Commission to accept ComEd's alternative proposal, then Staff recommends that the final paragraph clarify that intent. The key distinction between ComEd's primary proposal and its alternative proposal is that Rider 8 is not eliminated (*supra*), but that it is closed to new customers and that rates will be adjusted accordingly.

Recommended Language

If the Commission adopts ComEd's alternative position, Staff recommends the following edits:

ComEd proposes to eliminate Ride 8 and provide a standard transformer allowance under Rider NS to replace the Rider 8 credit. Staff expressed concern that this proposal would raise the cost to some Rider 8 customers and opposes the elimination of Rider 8. Therefore, Staff recommends that Rider 8 not be eliminated, or as an alternative, that Rider 8 customers be allowed to negotiate a termination payment. The termination payment would allow the customer to be able to agree upon an amount that would adequately compensate it for the costs it incurred in having to purchase a transformer. In response, ComEd proposes an alternative to the position it put forth in its direct testimony, proposing to suggest that in conjunction with eliminating Rider 8 it would continue Rider 8 and provide those customers who want to terminate Rider 8 a one-time transition payment to each Rider 8 customer in an amount equivalent to one year of Rider 8 credits. This would be based on the customer's average Rider 8 credits received over the most recent three-year period. Staff argues that any one-time credit should be negotiated between ComEd and each Ride 8 customer, since it is unclear whether such a credit would adequately compensate Rider 8 customers for the

~~outstanding cost of their purchase of a transformer. In the event the one-time credit is not negotiated, Staff recommends that Rider 8 be retained.~~ ComEd objects to negotiating a one-time credit with customers and instead would prefer to allow existing customers to be grandfathered under Rider 8 and allow ComEd to make a corresponding adjustment to its rate design to provide an offset for such continued credits to allow ComEd to recover its revenue requirement.

Having reviewed the record as well as the arguments on this issue, the Commission concludes that it would be best to continue Rider 8, but close it to new customers, and allow the existing customers to receive a transition payment equal to one year's worth of credits. ~~allow ComEd to eliminate Rider 8. As discussed elsewhere in this order, determining how many rate classes should exist involves balancing competing interests. Staff's concern that certain customers may pay more as a result of transitioning from Rider 8 to Rider NS, while legitimate, is an inevitable result of administrative rate making. In the Commission's view, it is undesirable to create a new "grandfathered" customer class on Rider 8.~~ The Commission believes that ComEd's proposal to provide a one-time transition payment based on the customer's average Rider 8 credits over the most recent three-year period is a reasonable compromise. ComEd's alternate proposal is therefore adopted, and that it will adjust its rates accordingly to its testimony.

5. Rider POG

Staff does not object to Rider POG, but proposes it be modified so that it furthers the intent of federal and state law, while still allowing ComEd to offer the PJM spot market prices. The PO seems to rely on two points in denying Staff's recommendation that Rider POG be modified to include an expressly stated level of compensation. The first point relied upon by the PO is that the record does not support a conclusion that a small generation facility would decide to become a qualified facility based on how much money they would be compensated. (PO, p. 232) The second point is that avoided energy costs set forth in Part 430 are "not compatible with the evolving wholesale and retail market in Illinois." (*Id.*). If the Commission, however, approves ComEd's proposed

Rider POG, Staff does not believe such a rider complies with the intent of 18 C.F.R. §292 and Part 430 (83 Illinois Admin. Code Part 430). For Rider POG to further Congress' intent to promote co-generation, Rider POG should also expressly state a compensation level per kW-hr in dollars and cents. (Staff IB, pp. 113-115)

Contrary to the points relied upon by the PO, Staff's briefs and testimony explained support the need for a stated rate of compensation under Rider POG. The compensation described in Rider POG does not inform small generators or co-generators that are, or would want to become, a qualified facility ("QF") how much ComEd would compensate them for their excess generation. (ICC Staff Exhibit 19.0, p. 4) Potential small power producers will likely be discouraged by the absence of a definite rate in proposed Rider POG and decide not to make the investment in generating equipment, which in turn would reduce the number of small power producers who choose to operate in ComEd's service territory. (*Id.*) To further Congress' goal of promoting cogeneration and small power production, QF's and potential QF's need to know what the compensation rates will be so they can determine their potential return and risk. This lack of information increases uncertainty in this area of power generation and deters companies from becoming a co-generator or a small power producer. Therefore, the method of compensation in Rider POG is contrary to the Public Utility Regulatory Policies Act of 1978 ("PURPA"). (Staff IB, pp. 112-13)

For Rider POG to further Congress' intent to promote co-generation, Rider POG should be modified to expressly state a compensation level per kW-hr in dollars and cents. These rates should be stated in Rider POG as an alternative to the Nodal and Zonal Compensations currently in the Rider. (Staff IB, pp.113-115).

Thus Staff recommends that the Commission adopt Staff's position as set forth in its Initial and Reply Briefs.

Recommended Language

If the Commission adopts Staff's position, Staff recommends the following edits to the Commission Analysis and Conclusion section on pages 231-232 of the PO:

Commission Analysis and Conclusion

ComEd proposes to replace Rider 4, Parallel Operation of Customer's Generating Facilities, with Rider POG. Staff avers that the issue is not yet ripe. Staff also objects to Rider POG and, among other things, insists that an annual fixed avoided energy cost rate is needed to promote small power producer production in Illinois. Under Rider POG, ComEd's avoided energy costs would be the PJM spot prices. ComEd argues that this issue was essentially decided in Docket 05-0159 and that requiring an annual fixed avoided energy cost rate would jeopardized ComEd's full cost recovery. However, ComEd has provided no citation that clearly identifies this issue expressly being addressed in that docket, therefore, we reject this argument.

Staff argues that Rider POG, unlike Rider4, does not clearly identify how much a Qualified Facility will be compensated for the excess electricity they generate and sell to ComEd. This lack of information, Staff argues, could cause co-generators or small generators who are QFs to stop selling excess electricity, or influence those that are not yet a QF to not become one. Thus, providing instability in the QF market. Staff further argues that such instability is contrary to federal law, under the Public Utility Regulatory Policy Act of 1978 (PURPA), which promotes the use of QFs. To resolve this problem, Staff recommends that Rider POG provide a expressly state a compensation level per kW-hr in dollars and cents. These rates should be an alternative to the Nodal and Zonal Compensations currently in Rider POG. witness Linkenback states, "I do not think a potential small generator trying to decide if it is reasonable to purchase and install a small generation facility would consider next-day spot market prices as an indication of what their payment might be over a longer term." (Staff Ex. 19.0 at 3) Staff seems to suggest that such investment decisions would be based upon an annual fixed avoided energy cost rate. The Commission does not believe the record supports such a conclusion.

~~The Commission recognizes, as does Section 16-101A of the Act, that long-standing regulatory relationships need to be altered to accommodate the competition that could fundamentally alter the structure of the electric services market. Staff may be correct that Part 430 is not fully compatible with the evolving wholesale and retail market in Illinois. Nevertheless, the fact remains that the electric services market in Illinois has, and is, changed, and it is necessary to adapt with the changing market.~~

~~All things considered, the Commission finds Staff's proposal to be just and reasonable. This decision furthers federal law as stated in PURPA, until it is amended or rescinded, that ComEd's proposed Rider POG as shall be modified to include by the language proposed by Staff, and that Rider POG be updated annually with in the manner it updated Rider 4, contained in ComEd Ex. 49.0, is just and reasonable and should be adopted. If Staff continues to believe that Part 430 requires modification, it should draft an initiating order for the Commission's consideration. However, the Commission does not believe that deferring a decision on this question is in the best interests of customers who own and operate qualifying facilities or is in the public interest.~~

6. Supply Administration Charge

The conclusion reached in the PO concerning the allocation of Supply Administration Charge ("SAC") costs should be reversed. The PO accepts ComEd's proposed allocation of these costs on a customer basis, stating as follows:

The Commission observes that this issue involves the allocation of costs that cannot be directly assigned. As such, no allocation factor will be perfect. In the Commission's view, ComEd's proposed allocation factor is superior to Staff's. The Commission does not agree that supply administration costs are positively correlated with the amount of supply ComEd procures. Nor does the Commission believe that supply administration costs are positively correlated with number of customers. Nevertheless, the Commission finds that ComEd's allocation factor is superior. The Commission finds that the cost to be allocated is largely a fixed cost; therefore ComEd's allocation factor, which incorporates the number of customers, is superior to Staff's usage-based allocation factor.

(PO, pp. 254-255).

Staff takes issue with this conclusion on a number of points. The first problem lies with the statement that SAC costs are not positively correlated with the amount of supply ComEd procures. In fact, Staff has provided evidence in this proceeding to demonstrate that these costs are related to supply. If ComEd's bundled supply were one-tenth the size of its currently projected level, it would be reasonable to expect that SAC costs would decline with a smaller level of demand and fewer suppliers to oversee. (ICC Staff Ex. 6.0 Corr., pp. 49-50). In contrast, ComEd admits that these costs do not vary with the number of customers served, the methodology it proposes. (ComEd Ex. 23.0, p. 49, lines 1044-1045).

The second issue, is the acceptance of ComEd's argument that because SAC costs are fixed and the appropriate method for recovering fixed costs is the number of customers, these costs should be recovered on a customer basis. In fact, as Staff has fully explained, ComEd itself proposes to recover numerous fixed costs, such as distribution lines, poles and transformers, through variable charges such as delivery charges or demand charges. (ICC Staff Exhibit 17.0 Corr., p. 37, lines 916-919).

Third, the PO fails to address the inconsistency in ComEd's argument for a customer-based allocator. ComEd witness Crumrine allocates SAC costs between the Basic Electric Service ("BES") auctions on a usage basis and within the auctions on a customer basis. Using one allocator for the first step and a different allocator for the second step is illogical. Staff's proposal to base SAC charges on usage throughout the allocation process is clearly more consistent than ComEd's proposal. (ICC Staff Exhibit 17.0 Corrected, p. 36, lines 893-897)

Based on the foregoing discussion, Staff recommends that conclusion be amended, and Staff's proposal be accepted – that SAC be based on usage of bundled customers. (ICC Staff Ex. 6.0 Corr. P. 49).

Recommended Language:

Staff recommends the following edits to the Commission Analysis and Conclusion section for Supply and Administration Charge:

~~The Commission observes that this issue involves the allocation of costs that cannot be directly assigned. As such, no allocation factor will be perfect. In the Commission's view, ComEd's proposed allocation factor is superior to Staff's. The Commission agrees ~~does not agree~~ that supply administration costs are positively correlated with the amount of supply ComEd procures but not. Nor does the Commission believe that supply administration costs are positively correlated with number of customers. Therefore~~ Nevertheless, the Commission finds that Staff's ~~ComEd's~~ allocation factor is superior. The Commission rejects the Company's argument that the proper allocation of fixed costs such as the SAC is on a customer basis. Staff has shown that significant fixed costs are allocation on both a usage and demand basis. Furthermore, Staff's proposal is more consistent than the Company approach because it would allocate between auctions and within auctions on the same usage basis. ~~finds that the cost to be allocated is largely a fixed cost; therefore ComEd's allocation factor, which incorporates the number of customers, is superior to Staff's usage-based allocation factor. (Proposed Order, pp. 254-255)~~

7. Real Time Pricing Meters and Energy Smart Pricing Plan

The PO accepts the CUB proposal to levy a charge on all residential customers to fund the availability charges associated with installing Interval Demand Recording meters on the premises of a limited number of residential customers that wish to take real-time pricing. As stated in the PO, the charges are based on the expectation that between 30,000 and 70,000 customers would switch to real time pricing ("RTP") service

over the next three years. (PO, p. 270)¹² However, the only basis for the 30-fold enlargement of the current participation level in the ongoing residential RTP pilot program of approximately 1,500 customers derives from the opinion of the representatives of the Community Energy Cooperative (“CEC”) of the demand for RTP in the ComEd service area, as reported to CUB witness Thomas. (Tr., p. 1135) None of the CEC witnesses testified in this proceeding, and no other evidence of the demand for the proposed program was presented in the record.

Staff in its Initial and Reply briefs discussed pending legislation Senate Bill 1705 (“S.B. 1705”) yet the PO does not acknowledge that if S.B. 1705 becomes law, electric utilities will have to file tariffs with the Commission permitting residential customers to take real-time pricing that can only be approved if the Commission concludes that the potential for demand reductions will result in net economic benefits to all residential customers. S.B. 1705 reads, in part, as follows:

b-5) Each electric utility shall file a tariff or tariffs allowing residential retail customers in the electric utility's service area to elect real-time pricing beginning January 2, 2007. A customer who elects real-time pricing shall remain on such rate for a minimum of 12 months. The Commission may, after notice and hearing, approve the tariff or tariffs, provided that the Commission finds that the potential for demand reductions will result in net economic benefits to all residential customers of the electric utility. In examining economic benefits from demand reductions, the Commission shall, at a minimum, consider the following: improvements to system reliability and power quality, reduction in wholesale market prices and price volatility, electric utility cost avoidance and reductions, market power mitigation, and other benefits of demand reductions, but only to the extent that the effects of reduced demand can be demonstrated to lower the cost of electricity delivered to residential customers.
<http://www.ilga.gov/legislation/fulltext.asp?DocName=&SessionId=50&GA>

¹² Staff notes that the relevant charges, if approved, should be based on ComEd Ex. 40.1, rather than ComEd 23.1. Thus, if the CUB proposal is adopted, as recommended by the PO, the addition to revenue requirement would be \$5,353,526, rather than \$6,067,662.

[=94&DocTypeID=SB&DocNum=1705&GAID=8&LegID=19897&SpecSess=&Session=\)](#)

Staff's understanding is that S.B. 1705 was sent to the Governor on May 5, 2006,¹³ and that Governor Blagojevich must decide within 60 days, or around July 5, 2006, whether to sign the bill into law. Unless the bill is vetoed or not returned to the legislature within 60 days it becomes law. (IL. CONST. art. IV Section 9) Thus, whether the bill becomes law should be known before the Commission issues an order in this proceeding.

Based upon the evidence presented in this proceeding, it is Staff's position that the Commission cannot conclude that the CUB proposal satisfies the requirements of S.B. 1705. There is no evidence in this proceeding that a RTP program would provide net benefits, as defined in S.B. 1705, to ComEd residential customers. The PO correctly notes Staff Witness Schlaf's opinion that the ongoing pilot RTP program does not address the question of net benefits. (PO, pp. 264-265)

Regardless of whether S.B. 1705 becomes law, Staff recommends that the Commission not adopt the CUB proposal and prohibit ComEd from spreading incremental metering fees among all residential customers. Staff also notes that, before the Commission determines that the CUB proposal is in the public interest and should be adopted, the Commission should consider whether the proposal meets the requirements of 83 Illinois Administrative Code Part 452, which generally prohibits utilities from promoting its service offerings.

Recommended Language

¹³

See, <http://www.ilga.gov/legislation/billstatus.asp?DocNum=1705&GAID=8&GA=94&DocTypeID=SB&LegID=19897&SessionID=50#actions>.

Staff proposes the following language changes to the PO's conclusion on pages

262 – 263:

The Commission has reviewed the record and hereby ~~adopts~~ denies the CUB/City proposal to expand existing residential real-time pricing programs for up to 70,000 customers at any given time over three years. While the Commission understands the potential benefits of the CUB/City proposal ~~Staff's concerns~~, it believes ~~the public interest will be best served by expanding the record does not support implementing the~~ real-time pricing program at this time. The Commission cannot approve such a program without a quantification of the potential benefits of the proposal, especially the benefits to the non-participants. ~~The Commission concludes that program costs shall be added to ComEd's revenue requirement for residential customers and reflected in the residential Customer Charge. All residential customers will pay the same Customer Charge, regardless of the tariff under which they take service. Such means of cost recovery reflects the Commission's view that all customers benefit, either directly or indirectly, from this program.~~

~~The Commission finds that it is appropriate for the CUB/City Proposal to be available for RTP programs offered by alternative suppliers, subject to the cap of 70,000 customers described above. The Commission also finds that any RES seeking to provide RTP to residential customers must:~~

~~provide a sworn statement to ComEd that all such customers are, in fact, on an hourly energy pricing program, where the hourly prices directly reflect PJM Interconnection, L.L.C. spot prices;~~

~~provide advance notice to ComEd of when pricing in the customer's contract changes to something other than hourly energy pricing, so that the IDR metering can be exchanged as it would for a Rate BES-H customer;~~

~~agree to submit to a periodic audit conducted by Staff (for which ComEd will reimburse the Commission for its travel and business expenses) of its applicable customer contracts; and~~

~~assume financial responsibility for all charges and fees waived for such customer in the event it is determined that such customers are not or are no longer on a legitimate hourly energy pricing service from the RES.~~

As for ComEd's statement that its support for the Proposal also is predicated on the Commission's rejection of Staff witness Lazare's proposal to shift 20% of the costs reflected in the Customer Charges to the DFCs, the Commission finds it appropriate to decide the two issues independently. The Commission finds ComEd's concern that Staff's proposal has the potential to jeopardize ComEd's cost recovery by 20% to be separate from the instant policy question, and an insufficient reason not to undertake expansion of the RTP program. The Commission's conclusion on Staff's rate redesign proposal is addressed elsewhere in this Order and is independent of the real-time pricing proposal adopted here.

~~———— The Commission rejects CUB/City's suggestion that ComEd should be required to equally share the risk of the program with customers. While the Commission believes the CUB/City proposal has merit, this suggestion would be unfair to utility and is therefore rejected.~~

~~———— Additionally, ComEd is directed to work closely with stakeholders in an effort to actively educate customers about the benefits of RTP programs.~~

~~———— Cost of capital, as well as the question of whether an efficiency factor should be included in the residential real-time meter charges of Rider ML, are issues that CUB/City claim are still in dispute. They are addressed elsewhere in this Order.~~

~~———— As noted above, the Commission rejects the idea that ComEd should be denied recovery of the reasonable incremental costs associated with implementing the approved real-time pricing program. ComEd witness Crumrine essentially left it to the Commission to determine the reasonable cost. (See ComEd Ex. 23.0 at 45-46) For purposes of determining the cost associated with the program that ComEd should be allowed to recover through base rates, the Commission has reviewed ComEd Ex. 23.1. The Commission finds it is appropriate to average the high and low cost estimates shown on the exhibit to determine the incremental impact on ComEd's revenue requirement. Therefore, the Commission concludes that ComEd should be authorized to include an additional \$6,067,662 in its test year operating expenses to reflect the additional costs associated with the real-time pricing program approved herein.~~

8. Rider ZSS7

The Proposed Order omitted Staff's position regarding Rider ZSS7. As Staff stated in its Initial Brief, it does not object to ComEd's proposed Rider ZSS7 -- Zero Standard Service 2007, which would replace existing Rider ZSS -- Zero Standard Service. (Staff IB, p. 11)

Recommended Language

Staff's Position

Staff does not object to ComEd's proposed Rider ZSS7 -- Zero Standard Service 2007, which would replace existing Rider ZSS -- Zero Standard Service. (ICC Staff Exhibit 7.0, p. 10) Rider ZSS7 provides a credit to customers who do not use ComEd's distribution facilities. The credit compensates customers for charges they pay to ComEd for ComEd facilities they do not use. Customers who take from this rider are required to have direct access to PJM markets (i.e., the regional transmission organization that provides wholesale electricity to ComEd's territory).

9. Rate BES-L

The Proposed Order omitted Staff's position regarding Rate BES-L. As Staff stated in its Initial Brief, it does not object to ComEd's proposed Rate BES-L -- Basic Electric Service-Lighting, which would replace two existing special service contracts (i.e., contract with Chicago Park District and City of Chicago) covering service for street lighting. (Staff IB, p. 12)

Recommended Language

Staff's Position

Staff does not object to ComEd's proposed Rate BES-L ("Basic Electric Service-Lighting"), which would replace two existing special service contracts (i.e., contract with Chicago Park District and City of Chicago) covering service for street lighting. (ICC Staff Exhibit 7.0, p. 10) In 2007, ComEd will begin acquiring energy from

third party providers. It is Staff's view that ComEd need not offer special service contracts to selected customers, because the remaining customers would be subsidizing the rates the special service customers pay. Rate BES-L ties the costs of serving the Chicago Park District and City of Chicago to ComEd's delivery services and to its costs under the procurement process. (*Id.*, p. 11) Tying the costs of service to the costs of procurement resolves Staff's concern regarding subsidization through special services contracts.

10. Tariff Implementation Issues

The PO grants ComEd's request for a variance to the tariff sheet numbering requirements contained in 83 Ill. Admin. Code 255.30(c) (PO, p. 269) without addressing the arguments made by Staff for why such a variance should not be granted. As Staff set forth in its reply brief, Staff's concern with ComEd's proposal is that the Chief Clerk's Office receives hundreds of tariff filings from utilities providing electric, gas, water, sewer, telecommunication and pipeline services. In the process of accepting or rejecting thousands of tariff sheets, the Chief Clerk's Office relies on the consistency of the tariff sheet numbering rules in Part 255. By allowing ComEd's request for a variance to Part 255, Staff fears the request would set a precedent for other utilities to address their individual concerns and possibly create overall numbering problems that may be difficult to resolve in the future. (Staff RB, p. 97)

Staff also noted in its reply brief that Staff is aware that the ICC has an on-going development project for an electronic tariff filing system for use by the regulated utilities. The development of this system is based on the tariff numbering rules set forth in Part 255. Staff is concerned that a variance to the tariff numbering rules will jeopardize the development of this system by making the system unable to operate effectively. Specifically, the development of the system is currently not being developed to handle

any variances such as the one ComEd is proposing and if its variance were to be approved, significant programming and development changes would be unnecessarily required. (Staff RB, p. 97)

Finally, while Staff recognizes ComEd's desire to make its tariff book more "user friendly" and supports ComEd's effort to do so, there are other ways to accommodate that need and therefore, Staff is willing to work with ComEd to make its new tariff book as user-friendly as possible while incorporating and maintaining existing rules and the Commission's Chief Clerk's Office needs. (Staff RB, pp. 97-98)

Recommended Language

Staff recommends the following changes to page 269 of the PO.

* * *

TARIFF IMPLEMENTATION ISSUES

ComEd

In light of the magnitude of changes being proposed by various parties in this proceeding, as well as the fact that the final Commission Order is scheduled to be entered several months in advance of the beginning date on which charges under the proposed tariffs would apply (*i.e.*, January 2, 2007), ComEd requested 30 days from the time the final order is entered in which to file its compliance tariffs. Alongi/McInerney Sur., ComEd Ex. 41.0 Corr., 39:901-40:925.

ComEd made two additional housekeeping proposals regarding its proposed rates. See *id.*; Alongi/McInerney Dir., ComEd Ex. 10.0, 9:216-31. First, ComEd proposed that the Commission, in its order in this proceeding, direct ComEd to file a new Schedule of Rates with a new schedule number (*e.g.*, Schedule ILL. C.C. No. "XX") within a reasonably short period of time after the mandatory transition period ends (*e.g.*, within eight months). ComEd indicated that this is necessary because ComEd's current set of rates will remain in ComEd's Schedule of Rates, but will no longer be operational at the end of the mandatory transition period. *Id.*

Second, to facilitate a customer's ability to locate information in the new Schedule of Rates, ComEd requested that the Commission's order in this proceeding provide a variance to the tariff sheet numbering requirements contained in 83 Ill. Admin. Code 255.30(c), and instead allow ComEd to file its new post-2006 Schedule of Rates (*i.e.*, Schedule ILL. C.C. No. "XX") using the proposed tariff sheet numbering structure shown in ComEd Ex. 10.5.

Staff

Staff's concern with ComEd's proposal is that given the voluminous tariff filings the Chief Clerk's Office receives, the Chief Clerk when accepting or rejecting tariff sheets relies on the consistency of the tariff sheet numbering rules contained in part 255. By allowing a variance it may create overall numbering problems that may be difficult to resolve in the future. Staff also noted that given the ICC's on-going development project for an electronic tariff filing system which is based on the tariff numbering rules set forth in Part 255 granting a variance to ComEd is a cause of great concern for Staff. Granting a variance like the one ComEd requests may jeopardize the development of an effective electronic tariff filing system. If other utilities are granted a variance like ComEd requests, significant programming and development changes would be required.

Commission Analysis and Conclusion

The Commission finds that ComEd should be directed to file its compliance tariffs within 30 days from the time the final order is entered in this case. ComEd is hereby directed to file a new Schedule of Rates with a new schedule number (e.g., Schedule ILL. C.C. No. "XX") within eight months after the mandatory transition period ends. The Commission ~~denies~~ also ~~grants~~ ComEd's request for a variance to the tariff sheet numbering requirements contained in 83 Ill. Admin. Code 255.30(c). The Commission agrees with Staff and is authorized to file its new post-2006 Schedule of Rates (*i.e.*, Schedule ILL. C.C. No. "XX") using the proposed tariff sheet numbering structure shown in ComEd Ex. 10.5 that allowing such a request may set a precedent for other utilities which would result in tariff sheet numbering problems for the Chief Clerk's Office that may be prove difficult to resolve in the future and it may jeopardize the development and implementation of and electronic tariff filing system which is already underway. For these reasons, ComEd's request for a variance from the requirements of 83 Ill. Admin. Code 255.30(c) is denied.

V. STAFF REPORTS ON COMED'S PERFORMANCE

A. Electric Metering

In the last sentence of the Commission Analysis and Conclusion section for Electric Metering, the PO may have incorrectly stated that "The Commission plans to address that issue in a separate proceeding." It is unclear whether the Commission intends to open another docket on its own accord, or whether the PO is attempting to acknowledge Staff's position of taking the necessary steps to ensure compliance with Commission rules. To the extent that the PO intends for that statement to mean the latter or that Staff will be initiating a docket to address this matter, the statement is incorrect. At this time, Staff has not definitively decided to initiate an investigation, but is continuing to inspect and monitor ComEd's activities to see if the corrections they make bring them within compliance of Part 410 (83 Illinois Admin. Code Part 410). The evidence Staff has been presented about electric metering was for the purpose of informing the Commission on electric metering at this point in time.

Recommended Language

If the intent of the PO was to acknowledge Staff's statement that it will continue oversight and take action later, then Staff recommends the following edits to the PO on page 297:

The Commission finds Staff's recommendations and ComEd's efforts to address them, including additional expenditures needed for such efforts, prudent and reasonable. ~~The Commission does not, however, the exception to ComEd's response regarding the application of certain installation standards of older meters. The Commission plans to address that issue in a separate proceeding.~~

VI. CONCLUSION

Staff respectfully requests that the Illinois Commerce Commission approve Staff's recommendations in this docket.

Respectfully submitted,

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