

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Commonwealth Edison Company :
: **ICC Docket No. 07-0566**
Proposed General Increase in Rates. :

BRIEF ON EXCEPTIONS
OF
THE COALITION TO
REQUEST EQUITABLE ALLOCATION OF COSTS TOGETHER
REACT

COMPRISED OF:
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¹ This Brief on Exceptions follows the outline format used in the July 10, 2008 Proposed Order.

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**BRIEF ON EXCEPTIONS OF
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The Coalition to Request Equitable Allocation of Costs Together (“REACT”), comprised of A. Finkl & Sons, Co., Alsip Paper Condominium Association, Aux Sable Liquid Products, LP, the City of Chicago, Commerce Energy, Inc., Flint Hills Resources, LLC, Integrys Energy Services, Inc., the Metropolitan Water Reclamation District of Greater Chicago,² PDV Midwest Refining LLC; United Airlines, Inc., and Wells Manufacturing Company. through its attorneys DLA Piper US LLP, pursuant to Section 10-111 of the Public Utilities Act (the “Act”) and Section 200.830 of the Rules of Practice of the Illinois Commerce Commission (“Commission”) (83 Ill. Admin. Code 200.830), hereby submits its Brief on Exceptions to the July 10, 2008 Proposed Order regarding the proposed general increase in rates of Commonwealth Edison Company (“ComEd” or the “Company”).³ A copy of the Proposed Order containing replacement language is attached hereto and made a part hereof as Appendix A.

² The Proposed Order inadvertently omits the Metropolitan Water Reclamation District of Greater Chicago (“MWRD”) from the list of REACT members. (See Proposed Order at 2.) MWRD was permitted to intervene as a member of REACT pursuant to an April 28, 2008 oral ruling of the Administrative Law Judges. (See Tr. at 58: 5-11.)

³ Positions stated herein do not necessarily represent the positions of any particular member of REACT.

I. INTRODUCTION

The Proposed Order represents at least a half step in the right direction. However, several modifications are necessary to ensure appropriate implementation of the proper policy guidance contained in the Proposed Order.

REACT is an *ad hoc* group, with diverse members, including some of ComEd's largest and most prominent commercial, governmental, and industrial delivery services customers, as well as retail electric suppliers ("RESs") that are interested in providing service to residential and small commercial customers. (*See* REACT Init. Br. at 3; REACT Reply Br. at 1.) REACT's members are committed to advocating that the Commission ensure accurate, appropriate, and equitable allocation of ComEd's costs – both among its customer classes and between the supply and delivery services components of its rates. (*See* REACT Initial Br. at 3-4; REACT Reply Br. at 1.)

Given REACT's fundamental concerns about ComEd's proposed massive, disproportionate rate increase for over-10 MW customers and ComEd's misallocation of supply-related Customer Care Costs to delivery services rates, REACT was pleased to see that the Proposed Order reaches several appropriate conclusions on these significant issues. The Proposed Order:

- Properly rejects ComEd's Embedded Cost of Service Study ("ECOSS") as a basis for allocating the rate increase;
- Prudently implements an across-the-board rate increase; and
- Correctly recognizes that ComEd failed to allocate a percentage of Customer Care Costs to supply-related charges.

(*See* Proposed Order at 200, 227-29.) The Proposed Order's conclusions on these points are solidly supported by the record evidence and correctly reflect the fact that ComEd bears the

burden of proof to support its proposals. (*See, e.g.*, REACT Init. Br. at 2-3, 5-8, 10, 25-31, 41-42, 49-60, 68-69; REACT Reply Br. at 2-7, 10-18, 22-23, 25-34, 39-41; Staff Init. Br. at 96-101, 106; Staff Reply Br. at 74-76; 220 ILCS 5/9-201(c).)

However, having reached these important conclusions, the Proposed Order stops a little short in carrying through on several significant points. In particular, on the two most important cost allocation issues:

- **As a matter of fundamental fairness, the Commission should direct ComEd to determine the actual costs of the facilities that are used to serve its 79 largest customers.** Having concluded that ComEd failed to accurately account for the costs associated with serving its largest customers, the Proposed Order nonetheless suggests that performing individualized cost of service studies for the 79 largest customers prior to the next rate case is unduly burdensome. (*See* Proposed Order at 202.) This suggestion is not supported by, and is contrary to, the evidence in the record, and also is contrary to other conclusions in the Proposed Order. Although the 79 over-10 MW customers represent only a tiny fraction of a percent of ComEd's 3 million customers, ComEd proposed that they bear well over 10% of requested the rate increase, an increase of more than \$41.5 million per year. (*See* ComEd Ex. 13.2 at 1, 2.) With the amount of money at stake, and given the disproportionate result of ComEd's proposed cost study, all 79 of ComEd's largest customers deserve to see the actual costs ComEd claims it incurs to provide delivery services to each such customer.
- **The Commission should direct ComEd to reallocate at least \$64.8 million in Customer Care Costs from its delivery services rates to its supply rates.** Although the Proposed Order recognizes that ComEd has failed to properly allocate the Customer Care Costs between its supply function and its delivery services function (*see* Proposed Order at 200), the Proposed Order fails to take the logical and necessary step of specifically excluding the \$64.8 million of misallocated Customer Care Costs from the amount ComEd is entitled to recover under the delivery services rates being approved in this proceeding.

Additionally, on some of the secondary issues, the Commission likewise should follow through in the same direction suggested by the Proposed Order:

- **The Commission should provide further guidance regarding the SMP process to address issues unique to over-10 MW customers and important to the competitive market.** The Proposed Order properly limits the scope of Rider SMP (*see* Proposed Order at 135.), but fails to direct ComEd to take into consideration the competitive market issues and unique circumstances related to over-10 MW customers that already have installed "smart grid" technology at their own expense.

- **The Commission should direct ComEd to retain Rider ACT in its current form, and direct an across-the-board increase in Distribution Loss Factors.** The Proposed Order suggests that the Commission accept ComEd's modified positions on Rider ACT and Distribution Loss Factors even though ComEd has failed to satisfy its burden of proof on these issues. (*See* Proposed Order at 220, 224.)
- **The Commission should further address competitive market issues.** Finally, while the Proposed Order implicitly recognizes that competitive market issues are relevant to the instant proceeding, the Proposed Order fails to specifically address important competitive market issues. (*See* Proposed Order at 225.)

REACT respectfully requests that the Commission modify the Proposed Order to provide guidance regarding the important next steps necessary to ensure appropriate allocation of ComEd's costs, and enter an Order consistent with the arguments outlined herein and in Appendix A.

VII. NEW RIDERS

The Proposed Order recommends that the Commission endorse a very limited version of Rider SMP. (*See* Proposed Order at 135.) Specifically, the Proposed Order recommends directing ComEd to implement Phase 0 of AMI deployment, together with a direction for initiation of a workshop process to begin to examine smart grid issues; subsequently, a Commission docketed proceeding would be initiated to adopt specific goals relating to smart grid issues, at which time ComEd could refile its request for rider recovery related to smart grid investment. (*See id.*) REACT does not object to this limited approval of Rider SMP, provided that the issues relating to prior investment by the over-10 MW customers and potential anti-competitiveness are addressed through the various formal and informal proceedings that the Proposed Order envisions.

B. **Rider SMP**

1. **The Overwhelming Majority of Parties Opposes Rider SMP Outright**

Private, governmental, and public interest stakeholders oppose Rider SMP outright for myriad reasons. (See REACT Init. Br. at 12-18; Staff Init. Br. at 69-81; AG Init. Br. at 1, 23-65; IIEC Init. Br. at 44-50; Metra Init. Br. at 7-12; CTA Init. Br. at 5-13; Commercial Group Init. Br. at 4-5; CUB Init. Br. at 36-46; Kroger Init. Br. at 2-4; AARP Init. Br. at 3-11; Nucor Init. Br. at 1-6; see also REACT Ex. 5.0 at 14-16:281-331; ICC Staff Ex. 21.0 at 1:15-16; AG/CUB Ex. MLB-4.0 at 4:1-10; IIEC Ex. 5.0 at 19:359-70; AARP Ex. 2.0 at 2:15-20.) This broad consensus of opposition is based upon substantial record evidence that would support, without question, the outright rejection of Rider SMP.

2. **Any Future Incarnation of Rider SMP (By That or Any Other Name) Must Address Competitive Issues and Avoid Imposing An Unjustified Burden on Over-10 MW Customers That Already Have Invested in Advanced Technology**

Rider SMP is open-ended, unnecessary, confusing, procedurally inappropriate and burdensome, and potentially anti-competitive. (See REACT Init. Br. at 12-17; REACT Reply Br. at 9.) Additionally, REACT has explained that Rider SMP poses particular issues for over-10 MW customers. (See *id.*) Many over-10 MW customers previously invested their own money in the very type of advanced technology for which ComEd now seeks guaranteed before-the-fact recovery of costs, a point that ComEd has not addressed in any of its discussions of Rider SMP. (See generally ComEd Init. Br. at 66-83; ComEd Reply Br. at 85-93.)

In short, Rider SMP presents the following specific problems with respect to over-10 MW customers:

- **Rider SMP fails to account for prior investment made by ComEd's over-10 MW customers.** (See REACT Init. Br. at 13-15; REACT Reply Br. at 9-10.)

- **Rider SMP provides no credit for the system-wide benefits that all customers have received from the over-10 MW customers' previous investment in advanced meter technology.** (See REACT Init. Br. at 16; REACT Reply Br. at 9-10.)

Additionally, ComEd never addressed concerns that Rider SMP could be implemented in an anti-competitive manner. (See REACT Ex. 5.0 at 16:317-23.)

The Proposed Order should be modified to ensure that any future proceedings relating to, and any future incarnations of, Rider SMP take into account competitive market issues and the particularized concerns of over-10 MW customers, and minimizes procedural burdens of multiple, simultaneous, overlapping Commission informal and formal proceedings.

VIII. COST OF SERVICE AND ALLOCATION ISSUES

A. Overview

1. The Proposed Order Properly Rejects ComEd's ECOSS as a Legitimate Basis for Setting Rates

Numerous parties question ComEd's use of the ECOSS in the instant proceeding. (See REACT Init. Br. at 26-29; REACT Reply Br. at 13; IIEC Init. Br. at 52-70, 79-81; IIEC Reply Br. at 25-26; DOE Init. Br. at 2-12; Metra Init. Br. at 13-24; CTA Init. Br. at 17-25; see also REACT Ex. 2.0 at 12-19:243-393; REACT Ex. 6.0 at 5-6:103-21, 14-17:290-374; Staff Ex. 18.0 at 18:402-03; IIEC Ex. 5.0 at 3-4:24-44, 7-8:122-31; IIEC Ex. 7.0 at 2-3:15-41; City of Chicago Ex. 2.0 at 3:69-73, 5:116-18; DOE Ex. 2.0 at 2-3:21-23, 26-59; Metra/CTA Ex. 3.0 at 4:10-25; BOMA Ex. 5.0 at 4:35-38.) ComEd itself historically has questioned the use of an ECOSS to set rates. (See REACT Init. Br. at 26; REACT Reply Br. at 13.) The Proposed Order properly concludes that ComEd's ECOSS is fundamentally flawed, and cannot be relied upon as a basis to allocate ComEd's proposed rate increase. (See Proposed Order at 198-200, 228-29.)

2. **The Commission Should Direct ComEd to Perform Individualized Cost of Service Studies for its Largest Customers**

The Proposed Order improperly suggests that the Commission reject the recommendation that ComEd be required to perform customer-specific cost-of-service studies for its 79 customers with demands over 10 MW, apparently due to a concern over the practicality of that approach. (See Proposed Order at 202.) Yet, the record evidence demonstrates that **customer-specific cost of service studies are feasible for the over-10 MW customer classes.** (See Tr. at 1646:7-8; Tr. at 1654-55:9-22, 1-3; see also REACT Init. Br. at 23-26, 31-35.) ComEd has presented nothing beyond general and conclusory statements to attempt to support its assertion about complexity and difficulty of performing individualized cost of service studies for these customers.

B. **Embedded Cost-of-Service Study Issues**

1. **REACT Supports the Proposed Order's Rejection of ComEd's ECOSS**

The Proposed Order properly identifies many of the shortcomings of ComEd's ECOSS and rejects the ECOSS as a basis for setting rates in the instant proceeding. (See Proposed Order at 198-200, 228-29.) REACT supports that conclusion, based, *inter alia*, on several fundamental issues, including the following:

- **As a general rule, costs should be paid by the cost causer.** (See REACT Init. Br. at 21-22; REACT Reply Br. at 13.)
- **It is necessary to have an accurate cost study in order to identify any alleged cross-subsidies.** (See REACT Init. Br. at 22-23; REACT Reply Br. at 13; CTA Init. Br. at 17-22; DOE Init. Br. at 3; IIEC Init. Br. at 55, 81.)
- **The Commission has not endorsed the ECOSS as a method for allocating costs to the over-10 MW customers.** (See REACT Init. Br. 25-26; REACT Reply Br. at 13.)

The Proposed Order's rejection of the ECOSS is well grounded in the record evidence in the instant proceeding.

2. **Customer-Specific Cost-of-Service Study Recommendations**

It is fundamentally unfair for ComEd to request that rates for its 79 largest customers increase by well over 120% -- to the tune of \$420,000 to \$3.2 million per year, per customer-- and then for ComEd claim that it does not have the funds or know-how to accurately calculate the actual costs to serve each of those customers. If ComEd really wants to move toward cost, as it professes, it should be willing to undertake the basic analysis necessary to determine the actual cost of serving its 79 largest customers. If ComEd is unwilling to take that step voluntarily, then the Commission should order ComEd to collect that data and present it in its next rate case.

Unfortunately, the Proposed Order suggests that Commission allow ComEd to proceed without collecting the detailed information regarding serving 77 of these 79 customers. (*See* Proposed Order at 202.) The basis for this suggestion is unclear, but it appears to be based upon an unsubstantiated fear that the issues will become more complex and that more customers will intervene in ComEd's next rate case if ComEd presents more detailed data. (*See id.*) According to the Proposed Order:

Given the time constraints inherent in rate making, the Commission finds that requiring ComEd to extend the level of cost study scrutiny to that of individual large customers would be unwise. A granular analysis of costs on a customer by customer basis even for a small class of customers would likely significantly increase the number of issues and the number of litigants in these proceedings. The Commission rejects the individual cost study proposal.

(*Id.*) Respectfully, the Commission should reevaluate the priorities that are reflected in the Proposed Order. That is, it seems that the Proposed Order inappropriately is more concerned about the administrative efficiency associated with the next rate case than the accuracy of the data ComEd will present to justify its next proposed rate increase.

The Commission should be mindful that the rate increases that ComEd proposed for its largest customers are extraordinarily high relative to the rate increases that ComEd proposed for its other customers – the proposed increase for the largest customers was more than more than **five times** the proposed system average increase, which would have resulted in impacts **well in excess of a million dollars *per year*** for many of these customers. However, ComEd failed to provide any response to the question: “What did the over-10 MW customers do to deserve such a disproportionate, massive rate increase?” (REACT Ex. 6.0 at 3:54-55.) Indeed, ComEd’s president admitted that the question went unanswered, and ComEd’s counsel admitted that the largest customers have done “nothing” that would justify such an increase. (*See* Tr. at 1542:3-7.) Individualized cost studies would provide the data that would allow the Commission to determine whether these customers are doing anything to justify a rate increase; and, if particular customers are doing something that would justify an increase, the information would provide accurate price signals to sophisticated customers regarding the steps they can take to reduce those costs.

To be clear, regardless of whether individual cost studies are performed, ComEd admits that it will make assumptions regarding the extent to which each facility is used and the appropriate cost to be assigned for using that facility. (*See* Tr. at 2037:12-2038;18, 2039:8-22.) The question on this point is whether ComEd should be allowed to lump all of its largest customers together in making those assumptions if and when ComEd proposes massive rate increases for those customers.

Although the 79 over-10 MW customers represent only a tiny fraction of a percent of ComEd’s 3 million customers, ComEd proposed that they bear well over 10% of requested the rate increase, an increase of more than \$41.5 million per year. (*See* ComEd Ex. 13.2 at 1, 2.)

With that amount of money at stake, and given the disproportionate result of ComEd's proposed cost study, all 79 of ComEd's largest customers deserve to see the actual costs ComEd claims it incurs to provide delivery services to each such customer.

Significantly, the Proposed Order accepts the argument by the two members of the Railroad Class that an individualized cost-of-service study is appropriate for them: "We direct ComEd to consult with CTA and Metra to conduct a load flow study to determine whether and if so, how much ComEd uses Railroad Class facilities to serve other customers." (Proposed Order at 258.) The Commission should endorse a similar approach for the other 77 over-10 MW customers.

Indeed, the record evidence established (and ComEd argued) that it was the Railroad Class customers that likely have *the most* complex facilities for purposes of performing an individualized cost-of-service study. (*See* ComEd Init. Br. at 96.) As a result, ComEd's "complexity" objection to performing individualized cost-of-service studies for the other over-10 MW customers falls away. That is, just as individualized cost-of-service studies are appropriate (and feasible) for the most complex customers, so too, similar studies are also appropriate (and feasible) for the other over-10 MW customers.

Given the relatively small number of over-10 MW customers, and given that the parties advocating for some form of individualized cost study represent a significant portion of that group of customers, a consensus position in favor of individualized cost studies has been presented in the instant proceeding by the particularly affected customers. (*See, e.g.*, REACT Init. Br. at 31-35; REACT Reply Br. at 16-17; IIEC Init. Br. at 65-67; Metra Init. Br. at 2, 15, 24; CTA Init. Br. at 16, 25-26. *See also* REACT Reply Br. at 14.)

The record contains uncontradicted evidence that:

- The rate level ComEd proposed for its largest customers is well above the rates other utility companies charge their largest customers. (*See* REACT Ex. 6.0 at 22:483-98.)
- Individualized cost studies would be more accurate than ComEd’s proposed ECOSS. (*See* REACT Init. Br. at 33-35.) Indeed, ComEd’s own witness made comments regarding the need to measure actual costs in an embedded cost of service study. (*See* ComEd Ex. 33.0 at 4:66-68.)
- Performing individualized cost-of-service studies for ComEd’s 79 largest customers is feasible. (*See* REACT Init. Br. at 35; REACT Ex. 6.0 at 19-20:417-50; REACT Cr. Ex. 19, ComEd Response to REACT Data Request 4.28.) As noted above, the Proposed Order appears to reach this conclusion with respect to individualized cost-of-service studies for members of the Railroad Class – given the complexity of those customers’ facilities, the feasibility of such studies for other over-10 MW customers should not be considered a dispositive issue.
- Performing individualized cost-of-service studies is consistent with ComEd’s stated desire to “move toward cost.” (*See* REACT Init. Br. at 35; REACT Ex. 6.0 at 17:380-84.)
- Performing individualized cost-of-service studies is consistent with the principle of avoiding cross subsidization. (*See* REACT Ex. 6.0 at 11-13:235-81.)

Thus, the evidentiary record strongly supports the conclusion that the Commission should order individualized cost-of-service studies. Nevertheless, if the Commission determines for whatever reason that it is unwilling to direct ComEd to perform individualized cost studies for its 79 largest customers, the Commission still should direct ComEd to work with these customers

prior to ComEd filing its next rate case to determine the appropriate inputs for its cost study. Cost studies can incorporate differences in the age of equipment used by ratepayers, the relative amount of underground and overhead lines required by different rate classes, differences in the quantity of circuit miles required to serve alternative groups, and many other factors. (*See* REACT Ex. 6.0 at 26:588-91.) If the Commission has as a goal minimizing the number of issues, and potentially the number of intervenors, in the next rate case, it would seem that requiring ComEd to actively engage with its largest customers prior making a Commission filing would be appropriate. The Commission should require ComEd to work with its largest customers on a transparent basis, and explicitly encourage ComEd to be more open-minded and resourceful with respect to the application of whatever cost study it develops.

REACT respectfully requests that the Commission modify the Proposed Order and enter an Order directing ComEd to perform individualized cost of service studies for its 79 largest customers and to work with those customers in developing its cost study prior to its next rate case.

C. **Rate Impact Analysis**

1. **The Proposed Order Appropriately Rejects ComEd's Proposal for a Massive, Disproportionate Enormous Rate Increase for Its Largest Customers**

The Proposed Order properly rejects the structure of ComEd's proposed rate increase, which would have imposed a massive, disproportionate rate hike upon the over-10 MW customers. (*See* Proposed Order at 205.) However, the Proposed Order seems unjustifiably reluctant to conclude that ComEd's proposal would constitute "rate shock" for the over-10 MW customers. The testimony of ComEd's president as well as the evidence presented by REACT and other parties such as DOE leaves no doubt that ComEd's proposal would constitute rate

shock. (See Tr. at 108-12.) The sheer size of the increases faced by over-10 MW customers, as expressed both in percentage increases (140.4% and 129.4%) and in actual dollars (\$420,000 to \$3.2 million per year, per customer), is daunting. (See REACT Init. Br. at 35-37; REACT Reply Br. at 19-20; REACT Ex. 1.0 at 10:230-37; REACT Ex. 5.0 at 2:31-37, 7:132-35.) ComEd did not try to dispute the fact that the increases faced by over-10 MW customers are grossly out of proportion to the much lower increases for other customer classes. (See REACT Init. Br. at 37-38; REACT Ex. 1.0 at 10:230-37; REACT Ex. 5.0 at 7:132-35.) ComEd merely offered the euphemism that its enormous proposed rate increase would be a “measured movement to cost.” (See REACT Reply Br. at 19, *citing* ComEd Init. Br. at 101.)

In any event, in order to move “to cost,” there first must be an accurate measure of the “cost” – and the Proposed Order properly concludes that ComEd has not accurately measured the cost to provide service to its over-10MW customers. REACT agrees with the Proposed Order’s rejection of ComEd’s proposed allocation of its rate increase.

D. **Interclass Allocation Issues**

The Proposed Order fairly and properly determines that an across-the-board rate increase is the only fair and equitable approach to an increase given the record evidence and the circumstances of the instant proceeding. (See Proposed Order at 205.) REACT agrees.

E. **Supply vs. Delivery Services Allocation Issues**

1. **REACT Strongly Supports the Proposed Order’s Recognition that ComEd is Charging Supply-Related Costs in its Delivery Services Rates**

The Proposed Order accurately concludes that ComEd has failed to properly exclude its supply-related costs when calculating its delivery services-related costs. (See Proposed Order at 200.) In particular, the Proposed Order criticizes ComEd’s failure to allocate any Customer Care

Costs to the supply function, and instead to allocate 100% of those Customer Care Costs to delivery services. (*See id.*) REACT strongly supports the Proposed Order’s analysis on this point.

Fundamentally, ComEd cannot escape the fact that it is charging supply-related costs in its delivery services rates. Thus, ComEd cannot square its claim of proper cost allocation with reality. (*See* ComEd Init. Br. at 116; *but see* REACT Init. Br. at 51-53.) In reality:

- **ComEd’s failure to properly allocate supply costs violates the principle that costs generally should be assigned to corresponding cost-causers.** (*See* REACT Init. Br. at 49.)
- **ComEd’s failure to properly allocate supply costs would result in improper cross subsidization.** (*See id.* at 49-51.)
- **ComEd’s failure to properly allocate supply costs is anti-competitive.** (*See id.* at 50-51.)

The Proposed Order accurately notes that REACT is not alone in recognizing ComEd’s misallocation of supply-related costs. (*See* Proposed Order at 200.) Importantly, Staff, RESA, and the Commercial Group also questioned ComEd’s position on this issue, with both RESA and the Commercial Group explicitly endorsing REACT’s proposed adjustment. (*See* Staff Init. Br. at 106; RESA Reply Br. at 4-6; Commercial Group Init. Br. at 12-13.)

2. **REACT Strongly Supports the Proposed Order’s Finding that ComEd’s Position on Customer Care Costs Lacks Credibility**

The Proposed Order properly concludes that ComEd failed to present any evidence to rebut Mr. Merola’s analysis regarding the allocation of Customer Care Costs. (*See* Proposed Order at 200.) ComEd’s suggestion that Mr. Merola’s analysis and resulting 40% allocation factor is “completely arbitrary” is simply false. (ComEd Init. Br. at 117.) Mr. Merola is an *expert* witness, with over 17 years of diversified experience in the energy industry, including substantial experience analyzing competitive energy issues and testifying in a variety of forums –

ComEd did not and cannot question his qualifications. Mr. Merola's expert analysis was conservative and reasonable based on the available data, particularly when keeping in mind that ComEd refused to provide additional data and does not track meaningful statistics relevant to the analysis. Certainly, given that backdrop ComEd should not now be permitted to criticize Mr. Merola's analysis for lack of data.

ComEd does not and cannot deny that Mr. Merola's approach is entirely consistent with the embedded cost approach that ComEd has proposed for other cost allocation issues: examining actual historic costs and making reasonable assumptions regarding usage of specific assets for different customers. (*See generally* REACT Ex. 7.0: at 18-22.)⁴

Further, ComEd does not and cannot deny that Mr. Merola's analysis adopted a conservative approach:

- Mr. Merola explained that one rational means of allocating these costs would be based on the share of revenue associated with supply compared to the share of revenue associated with distribution. Clearly, supply represents a much higher percentage of a customer's bill than does distribution, and under that methodology the allocation factor would likely be in the range of 67%. (*See id.* at 20:436-41.)
- However, instead of applying such a rough allocator for these costs, Mr. Merola adopted a more conservative, analytic approach to determine a reasonable allocation of ComEd's \$162,150,019 Customer Care Cost revenue requirement for fixed-price bundled customers, concluding that 40%, or \$64,860,008, of ComEd's Customer Care Costs should be allocated to the supply function. (*See id.* at 20-21:441-54.)
- As Mr. Merola explained, his analysis was conservative in a number of ways, fully removing costs attributable to meter reading and the establishment of delivery services, and, again in the absence of ComEd providing actual data or meaningful assumptions of its own, making a very reasonable assumption based upon his extensive experience in the industry regarding the percentage of Customer Care Costs that are associated with providing supply. (*See id.* at 20-21:436-48.)

⁴ All citations herein to REACT Exhibits 3.0, 4.0, and 7.0 are to the "Corrected" versions of such exhibits filed on eDocket on May 6, 2008.

- Mr. Merola also confirmed that his methodology captured some costs associated with ComEd’s use of Exelon Business Services Company to support its supply function, but was careful not to double count this expense. (*See id.* at 21-22:465-86.)
- Finally, Mr. Merola investigated how other utilities that are providing service in competitive markets in other states calculate their supply administration costs, and concluded that the allocation of 40% of the Customer Care Cost to a bypassable supply charge would be fully in line with the treatment of this issue by the other similarly-situated utilities. (*See id.* at 23-27:492-580.) He concluded that ComEd’s supply-related charges are “far lower” than the supply administration rates set by the other utilities he examined, confirming his concern that ComEd’s proposed recovery of supply-related administrative costs appears to be “artificially low.” (*Id.* at 26:540-42.)

The Proposed Order accurately notes ComEd’s failure to respond to this evidence. (*See Proposed Order at 200.*) ComEd had the opportunity to develop actual data allocating Customer Care Costs between supply and delivery; ComEd also had the opportunity in its surrebuttal to challenge Mr. Merola’s allocations by providing allocation factors of its own. ComEd did neither. Instead, ComEd chose to stand by its original position that there is **nothing** to allocate. The Proposed Order is obviously observant of the fact that ComEd bears the burden of proof in the instant proceeding. (*See, e.g., Proposed Order at 42; 220 ILCS 5/9-201(c).*) Thus, ComEd’s position that it incurs zero supply-related Customer Care Costs cannot withstand scrutiny – particularly given its own witnesses’ admissions. (*See Tr. 282:6-15; Tr. at 1382-87; REACT Init. Br. at 50-56.*)

Customer Care Costs are related to both supply and delivery services – a concept that REACT has proven, that ComEd eventually admitted, and that the Proposed Order endorses. (*See REACT Reply Br. at 25-30; e.g., Tr. 287-89:15-22, 1-22, 1-6; Tr. 1387-88:14-22, 1-5; Tr. 1389-90:16-22, 1-2; ComEd Init. Br. at 118-19; Tr. 282:6-15; Tr. 1382-87; Proposed Order at 200.*) Contrary to ComEd’s assertions, far from claiming that Customer Care Costs are “solely supply-related,” Mr. Merola testified that **only 40%** of those costs should be allocated to

ComEd's supply rates. (*See* REACT Init. Br. at 53-56.) Thus, contrary to ComEd's false charge, REACT has explained that, based on the current information, 60% of the Customer Care Costs appear to be properly allocated to delivery services.

The Proposed Order properly takes ComEd to task for failing to come forward with any analytical evidence to attempt to rebut Mr. Merola. (*See* Proposed Order at 200.) Independent of its failure to challenge the evidence presented by Mr. Merola, ComEd alone bears the burden to justify its proposal:

[T]he burden of proof to establish the justness and reasonableness of the proposed rates or other charges, classifications, contracts, practices, rules or regulations, in whole and in part, **shall be upon the utility**. No rate or other charge, classification, contract, practice, rule or regulation shall be found just and reasonable unless it is consistent with Sections of this Article.

(220 ILCS 5/9-201(c) (emphasis added).)

Thus, even if REACT, Staff, and the other parties had remained silent, ComEd would have still needed to meet its evidentiary burden concerning cost allocation to justify its proposed delivery services revenue requirement. Clearly, ComEd failed to do so.

3. **The Proposed Order Properly Recognizes that Misallocation is Anti-Competitive**

The Proposed Order recognizes the anti-competitive effect of misallocation of supply-related costs, stating that the proper allocation of Customer Care Costs “could substantially reduce costs assigned to distribution customers.” (Proposed Order at 200.)

The record on this point is very clear. In particular, Mr. Merola's testimony on this point stands unopposed. (*See* REACT Init. Br. at 51.) Competitive market issues are inextricably intertwined with the question of the proper setting of delivery services rates. Misallocating supply costs into delivery services rates affects the price of electricity in the competitive market.

(See generally Tr. at 2231-33; REACT Cr. Ex. 18.) Specifically, artificially increasing delivery services charges means improperly lowering ComEd's supply-related charges to ComEd Rate BES customers. This incorrect allocation would result in an incorrect price signal in both the supply and delivery of energy, and would effectively inhibit development of competition. In other words, the ComEd Rate BES customers would be paying a *lower* supply-related "price" than they would otherwise if the allocation were correct. This will hurt competition because it is the supply-related price that RESs will be attempting to compete against. Why would a customer switch to a RES if the customer is enjoying an artificially low supply-related price by sticking with ComEd? All things being equal, that customer would not switch. Thus, ComEd is inhibiting competition by misallocating supply-related costs.

Further, an incorrect allocation also forces customers that choose a RES to pay twice for the same Customer Care services – once to ComEd for services the customer does not use, and a second time to the RES for services it does use. (See REACT Ex. 7.0 at 4:88-90.)

The Proposed Order's recognition of the anti-competitive effect of misallocation of supply-related costs is well supported by the record evidence.

4. **The Proposed Order Should be Revised to Require Proper Allocation of Customer Care Costs in *This* Proceeding**

Given the uncontradicted record evidence regarding misallocation of supply-related Customer Care Costs, the Proposed Order should take the logical and necessary step of specifically excluding \$64.8 million of misallocated Customer Care Costs from the amount ComEd is entitled to recover through delivered services rates. REACT appreciates that the Proposed Order's general approach to dealing with the deficiencies in the ECOSS is by ordering ComEd to correct those deficiencies in the next rate case filing. However, the evidentiary record and the Proposed Order's conclusion regarding the ECOSS generally both support action in the

instant proceeding. Failure to adjust this allocation now will have immediate negative impacts upon the development of the competitive market for residential and the smallest commercial customers.

First, as recognized in the Proposed Order, the evidentiary record in the instant proceeding overwhelmingly supports the conclusion that ComEd has failed to allocate supply-related Customer Care Costs to its supply rates. (*See Proposed Order at 200.*) The question is not *if* there has been a misallocation, but *how much*. The evidentiary record provides an answer that ComEd has not even attempted to rebut: Mr. Merola's conservative analysis demonstrates a misallocation of at least \$64.8 million. (*See id.*)

Second, inclusion of the \$64.8 million in the delivery services rates would result in an overstatement of its delivery services revenue requirements. The Proposed Order correctly concludes that the continued inclusion of 100% of the Customer Care Costs in ComEd's delivery services rates is not justifiable, and that ComEd presented no figure to contradict the expert analysis presented by REACT that concluded 40% of those costs should be allocated to supply rates. (*See Proposed Order at 200.*) To permit ComEd to continue to recover the \$64.8 million through delivery services rates would be in direct conflict with the conclusion that the allocation is invalid – it would give ComEd a free pass for having failed to meet its evidentiary burden.

The record evidence shows that at least \$64.8 million of supply-related Customer Care Costs have been improperly misallocated to delivery services rates. Therefore, that amount should be excluded from the amount ComEd is permitted to recover through its delivery services rates in the instant proceeding. ComEd would not be precluded from recovering that amount through the appropriate mechanism for recovering supply-related costs. However, only by excluding these costs from ComEd's delivery services rate calculation now, will the Commission

implement an effective measure to avoid the anti-competitive effects that the Commission has in previous rate cases recognized and cautioned against. (*See, e.g.*, ICC Docket No. 01-0423, March 28, 2003 Order at 24-25 (“[A]n effectively competitive and efficient electricity market for residential and non-residential deliver services is an integral policy consideration.”); ICC Docket No. 05-0597, July 26, 2006 Order at 294 (“Now is the time for the Commission to seriously assume the responsibility to promote retail competition. . . . Th[e] Commission needs to take the appropriate steps to encourage more RESs to enter the Illinois market, especially to offer choices to the mass market customers.”).)

5. **The Proposed Order Fails to Recognize ComEd’s Incentive to Inhibit Competition**

The Proposed Order should be revised to recognize that ComEd has incentives to inhibit residential competition. REACT identified two such incentives in its pre-filed testimony, at the live hearings, and in its briefs. First, REACT explained that ComEd has a profit motive because ComEd can increase short-term revenues based upon inaccurate residential switching projections. (*See* REACT Init. Br. at 71-72.) Second, REACT explained that ComEd’s sister company, Exelon Generation, is able to sell more supply to ComEd under the supplier forward contracts if ComEd suppresses competition for its residential and smallest commercial customers. (*See id.* at 72-73.) Based upon the market conditions that existed at the time ComEd had to make policy decisions related to the positions it would take in this proceeding, it appears that Exelon had a corporate incentive to have ComEd retain those customers. (*See id.*) REACT articulated this issue repeatedly in its testimony and at the live hearings. (*See* REACT Ex. 7.0 at 5-7:110-46; Tr. 117:3-10; Tr. 2231-32:21-22, 1-17.)

The Commission repeatedly has recognized that competitive market issues, including ComEd’s misallocation of supply-related costs, are appropriately addressed in ComEd’s delivery

services cases. For example, in ComEd’s inaugural delivery services rate case, ICC Docket No. 99-0117, ComEd itself presented an expert witness who testified about the need for pricing that would **“improve the efficiency of competition”** and the need for new market entrants to have **“correct distribution price signals.”** (ICC Docket No. 99-0117, Aug. 26, 1999 Order at 52 (emphasis added).) In that same proceeding, **Staff explained that allocating any of the supply-related sales and marketing costs to distribution “would undermine the goal of creating a level playing field for providers in the emerging electricity market.”** (*Id.* at 24 (emphasis added).) (*See also* ICC Docket No. 01-0423, March 28, 2003 Order at 24-25; ICC Docket No. 05-0597, July 26, 2006 Order at 272-94.)

Throughout the course of the instant proceeding, ComEd validated many of the positions advanced by REACT regarding ComEd’s ability and potential motives to discourage customer choice for its residential and smallest commercial customers. First, ComEd did not deny that it has the ability to discourage customer choice by improperly allocating supply costs to its delivery services function. (*See* REACT Init. Br. at 6-7.) Second, ComEd remained silent regarding its ability to reap short-term revenues based upon inaccurate residential switching projections. (*See* REACT Init. Br. at 71-72.) Finally, and perhaps most significantly, ComEd admitted that given the right market conditions, **Exelon, its corporate parent, does have an incentive to discourage its residential and smallest commercial customers from exercising choice.** (*See* Tr. 1817-18:6-22,1-12; Tr. 2231-32:1-22, 1-17.) In response, ComEd just maintained that those conditions did not exist at one point during the hearing, but did not and could not deny that such market conditions *did* exist at the time ComEd had to make decisions regarding the policies that it would advocate in this proceeding. (*See* ComEd Reply Br. at 132; REACT Init. Br. at 6-7.) Moreover, regardless of when such market conditions may or may not

exist, the Commission should be extremely mindful of the apparent or actual conflict of interest that this creates for ComEd. ComEd no longer can be viewed as an “unbiased” arbiter regarding cost allocation issues; as long as Exelon Generation supplies electricity under long-term contracts, ComEd has an incentive to place its thumb on the scale. In this instance, REACT has revealed that ComEd improperly allocated at least \$64.8 million to its delivery services function, in an apparent attempt to discourage choice for its residential and smallest commercial customers.

REACT respectfully requests that the Commission revise the Proposed Order to recognize that ComEd and its related companies have both the motive and means to negatively manipulate or block development of a competitive market for residential choice in Illinois.

IX. **Rate Design**

A. **Overview**

REACT reiterates and incorporates herein its support for the Proposed Order’s endorsement of an across-the-board increase rather than the rate increase structure proposed by ComEd. (*See* Proposed Order at 205.) REACT also reiterates and incorporates herein its arguments in favor of requiring ComEd to perform individualized cost-of-service studies for its 79 over-10 MW customers.

D. **Existing Riders**

1. **Rider ACT**

The Proposed Order improperly endorses ComEd’s modified proposal on Rider ACT. (*See* Proposed Order at 220.) REACT respectfully disagrees with that conclusion and requests that the Proposed Order be modified to retain Rider ACT in its current form.

ComEd has failed to justify any proposed revisions to Rider ACT. Basically, ComEd just asserts, without any solid proof or quantification, that this rate is inconvenient. (*See* ComEd Init. Br. at 110-12.) Even if true, ComEd’s naked assertion about inconvenience is an insufficient reason for the Commission to allow ComEd to abandon or phase out this rate -- especially when ComEd apparently admits that Rider ACT better reflects the cost of serving the Rider ACT customers that have unique needs. (*See* 220 ILCS 5/8-508; ComEd Ex. 45.0 at 21:414; REACT Init. Br. at 37, 62-64.) ComEd has not satisfied its burden of proof. (*See* 220 ILCS 5/9-201(c).) As a matter of law and policy, the Commission should make it clear that ComEd must clear a much higher bar before it will be allowed to make such a fundamental change in a rate.

Accordingly, REACT respectfully requests that the Proposed Order be modified to direct ComEd to retain Rider ACT in its current form.

E. **Distribution Loss Factors**

The Proposed Order accepts ComEd’s proposal regarding ComEd’s proposed increase in the Distribution Loss Factors (“DLF”). (*See* Proposed Order at 224.) However, for over-10 MW high voltage customers, ComEd’s DLF proposal would impose a clearly disproportionate increase as compared to the proposed increase for other customer classes: DLF increases to the over-10 MW high voltage customers would increase by 36% versus the proposed increases to the “Large” (9%); “Very Large” (15%); and “Extra Large” non-high voltage (15%) customer classes. (*See* REACT Ex. 5.0 at 23-24:486-98; REACT Reply Br. at 37-39.)

ComEd makes this proposal while admitting that over-10 MW customers have not done anything unique to justify a disproportionate DLF increase (*see* Tr. 546-47:21-22, 1-3) and that within the over-10 MW customer classes there are very widely ranging DLFs. (*See* Tr. 541-42:21-22, 1-22; REACT Reply Br. at 38.) As with its cost of service study generally, ComEd

opposes performing a particularized DLF analysis for over-10 MW customers, even though ComEd witness Mr. Donnelly specifically stated that:

In general if a customer is responsible for a cost or involved in that costs, they should pay a portion of that cost.

(Tr. 540:7-9.)

ComEd has proposed an enormous percentage increase in the DLFs for over-10 MW high voltage customers, due to a change in ComEd's proposed methodology for calculating DLFs, not anything that those customers have done that would justify the increase. (*See* REACT Reply Br. at 38; Tr. 546-47:21-22, 1-3.) Further, because ComEd's proposed new methodology does not calculate individual DLFs, the amount ComEd has proposed be charged to the class definitely exceeds the particular distribution loss that many of the particular customers cause. (*See* REACT Reply Br. at 38.) Yet, ComEd has refused to perform particularized DLF analyses – obviously, ComEd's position on this issue undercuts its purported desire to implement accurate cost causation systems in an effort to “move toward cost.” (*See* REACT Reply Br. at 38.)

Consistent with the Proposed Order's conclusion that the rate increase in the instant proceeding should be implemented on a across-the-board basis, REACT respectfully requests the Commission modify the Proposed Order to direct ComEd to implement an across-the-board increase of the DLF in the instant proceeding, and to order ComEd to perform an individualized study of DLF as it relates to each over-10 MW customer prior to its next rate case.

F. **Recovery of Supply-Related Costs**

REACT addresses the issues associated with ComEd's improper allocation of supply-related costs in its arguments in Section VIII.F of its Initial and Reply Briefs and Section VIII.E of the instant Brief on Exceptions. Those arguments/positions are incorporated herein.

G. **Competitive Retail Market Development Issues**

1. **The Proposed Order Largely Accepts ComEd's Assertion That Competitive Market Issues Have Nothing to Do With this Case**

The Proposed Order improperly includes a general endorsement of ComEd's view that competitive market issues have nothing to do with this case. (*See* Proposed Order at 224-25.) In fact, the Proposed Order's correct conclusion regarding the misallocation of supply-related Customer Care Costs and the resulting inflated prices paid by distribution customers demonstrates that competitive market issues are interconnected with the rate issues presented in the instant proceeding. (*See id.* at 200.)

ComEd's attempt to completely duck these issues is surprising, given that competitive retail market development issues are not new to ComEd's delivery services rate cases. As noted above, since the very first ComEd delivery services rate, competitive retail market issues have been central to the proceeding. (*See* ICC Docket No. 99-0117, Aug. 26, 1999 Order at 24, 52; ICC Docket No. 01-0423, March 28, 2003 Order at 24-25; ICC Docket No. 05-0597, July 26, 2006 Order at 272-94.) While ComEd may not want to engage on these issues, given the role it has played in suppressing competition, the fact is that competitive market issues must be considered in the context of the question of delivery services rates presented in the instant proceeding. (*See* REACT Reply Br. at 42.)

2. **Resolution of Competitive Market Issues Is Necessary For the Commission to Satisfy Its Statutory Obligation to Promote Customer Choice**

As discussed herein, matters such as the proper allocation of Customer Care Costs have an effect not only on the proper setting of delivery services rates but also on the development of the competitive market for electricity. The Commission is charged with the implementation of that competitive market for all Illinois consumers. (*See* 220 ILCS 5/16-101A(d).) ComEd,

perhaps not surprisingly, advocates a compartmentalized view that would restrict the Commission from examining the interplay between rate design issues and the effects of those rate design issues on the competitive market. That approach elevates form over substance in a manner that would, for example, tie the Commission's hands even where, as here, a rate proposal implicates an anti-competitive result. Neither the letter nor the spirit of the Act so constrains the Commission.

REACT has introduced evidence that raises substantial questions about why, years after the statutory implementation of customer choice for all customers including residential customers (*see* 220 ILCS 5/16-104(a)(4)), the competitive retail electric market for residential customers does not exist, and remains a relatively distant prospect according to ComEd. (*See, e.g.,* REACT Cross Ex. 7; Tr. 1317:13.) REACT has demonstrated that ComEd and its related companies have both the means and the potential motive to undermine the development of residential competitive. (*See, e.g.,* REACT Ex. 7.0 at 5-6:110-22.) ComEd has also presented conflicting and contradictory information about when and whether it forecasts the development of residential competition. (*See* REACT Cross Exs. 7, 20; *see also* REACT Cross Ex. 10.) The Commission should not allow ComEd's attempt to sweep this record evidence away under the theory that this case is about something else. The Act requires the Commission to do more and certainly does not constrain the Commission's ability to follow the evidence where it leads.

Accordingly, REACT respectfully requests that the Proposed Order be revised to conclude that competitive market issues are squarely and fully before the Commission in the instant proceeding, and that ComEd should address these issues in its next rate case. The Commission has a statutory duty to consider the impact of ComEd's proposals upon the continued development of the Illinois retail electric market.

XII. CONCLUSION

The Proposed Order correctly decides some important issues in a manner that endorses the general themes of equitable allocation of costs that REACT has articulated throughout the instant proceeding. In particular, the Proposed Order reaches some important specific conclusions, including:

- Rejecting ComEd's faulty embedded cost-of-service study data;
- Rejecting the proposed massive and disproportionate rate increases for the over-10 MW customers; and
- Recognizing that ComEd misallocated supply-related Customer Care Costs.

In these respects, the Proposed Order represents a move in a direction consistent with sound ratemaking policies and the pro-competitive mandates of the Act previously embraced by the Commission.

However, the Proposed Order, in its current form, also misses some significant opportunities to advance these policies. Particularly given the rich evidentiary record presented in the instant proceeding, the Commission should take a *full step* toward implementing real and specific equitable cost allocation and pro-competitive positions. Specifically, on the primary issues addressed by REACT, the Commission should

- Require individualized cost-of-service studies for all of the over-10 MW customers; and
- Require ComEd to exclude \$64.8 million of Customer Care Costs from the delivery services rates that ComEd proposes.

Additionally, regarding the other issues addressed by REACT, the Commission should:

- Recognize that Rider SMP should take into account unique circumstances related to the over-10 MW customers and potential impacts upon competitive services;
- Require ComEd to maintain Rider ACT in its current form; and
- Order an across-the-board increase in the DLF.

WHEREFORE, REACT respectfully requests that the Commission modify the Proposed Order and enter an Order in the instant proceeding consistent with the arguments herein, in Appendix A and the previously-filed briefs and testimony of REACT.

Respectfully submitted,

**THE COALITION TO REQUEST EQUITABLE
ALLOCATION OF COSTS TOGETHER**

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