STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Commonwealth Edison Company, Proposal to establish Rider PORCB (Purchase of Receivables with Consolidated Billing) and to revise other related tariffs.	))))	Docket No. 10-0138

Surrebuttal Testimony of

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On Behalf of
Commonwealth Edison Company

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I. <u>Introduction and Purpose</u>

Q. What is your name and for whom do you work?

A. My name is Susan D. Abbott and I am the Principal of Susan Abbott Consulting, LLC. I am an independent consultant to companies in the regulated water, gas and electric utilities sector, providing advice surrounding questions relative to credit ratings, credit worthiness, and rating agency relationships.

Q. What are your qualifications?

A. I have worked in the financial services industry focusing primarily on the electric, gas and water utilities sectors since 1977. I have worked as an institutional investor, a rating agency analyst and Managing Director, and most recently as an investment banker. The vast majority of my career, however, was spent at Moody's Investors Service ("Moody's"), one of the three principal U.S. based global rating agencies. For a total of 13 of the 20 years I was employed by Moody's, I was either a member, or the Managing Director of the Power and Project Finance Group, and was responsible for ratings of electric utility, electric and gas combination utility, water utility, and project finance ratings. Since leaving Moody's, I have been involved in rating agency advisory work with clients, chaired many rating agency panels for the jointly sponsored "Dialogue with Wall Street," (produced by Edison Electric Institute ("EEI")), and Gee Strategies, the consulting firm formed by Robert Gee, a former Assistant Secretary at the Department of Energy, a former Commissioner with the Texas Railroad Commission, and a former staff attorney at the Federal Energy Regulatory Commission), which is a forum for discussion between financial market participants and regulators.

I have a Bachelor's Degree in Literature from Syracuse University, and an M.B.A. in Finance from The University of Connecticut. I sit on the Board of Directors of the Student Managed Funds for the University of Connecticut, and am a member of the UConn Business School Hall of Fame. I have lectured at The Business School of the University of Connecticut, and Wharton Business School at the University of Pennsylvania, and was a faculty member at the University of Idaho's Public Utility Executive Course for 10 years. My CV is attached as ComEd Ex 9.1.

I have testified in a number of rate proceedings. A list of testimony is provided in ComEd Ex. 9.2.

Q. What is the purpose of your testimony?

A. I am replying to concerns raised by the testimony of Rochelle Phipps of the Staff of the Illinois Commerce Commission ("Staff") and Mr. Christopher C. Thomas of the Citizens Utility Board ("CUB"). In Ms. Phipps' case, I am addressing in particular her recommendation that a lower return on equity than that generally authorized for Commonwealth Edison Company ("ComEd") be applied to the Purchase of Receivables with Consolidated Billing ("PORCB") program. I merely acknowledge that Mr. Thomas has submitted testimony in support of that point of view. Additionally, I briefly address the implications of the testimony of Staff witness Ms. Theresa Ebrey in which she questions ComEd's ability to recover certain costs and deferred expenses related to the implementation of PORCB, calling into question ComEd's ability to earn whatever return is allowed before the program even starts.

Q. Please summarize your testimony.

A. Ms. Phipps' recommendation that a return on equity related to the PORCB program be the mid-point between the yield on AAA utility transition bonds and ComEd allowed return on equity indicates a lack of understanding of the risks investors will perceive and be concerned about. To equate AAA-rated utility transition bonds with the cost recovery incidental to the PORCB program shows a misunderstanding of why transition bonds are rated AAA and how the risks investors will evaluate in the PORCB program materially differ from those of transition bonds. Ms. Phipps also mistakenly equates the "assuredness" of recovery of costs of the PORCB program with the security of the flow of funds servicing the transition bonds.

Q. In brief, what is your conclusion?

A. ComEd has taken on a new risk through the PORCB program. While Ms. Phipps and Mr. Thomas argue that there are adjustments that neutralize the risk of the program, it is important to point out that the investing community does not necessarily ascribe an absence of risk, or even a lowering of risk, to assets subject to adjustment clauses. Investors generally perceive that the relationship between these mechanisms and return on equity is a complicated one that requires the evaluation of the specifics of the mechanism in question. Ms. Phipps' general assumption that the adjustment clause associated with the PORCB program neutralizes risk is overreaching and overly simplistic. Ms. Ebrey's challenge to costs that are reasonable and rational before the program even starts further emphasizes my point that regulatory risk is real and present in this situation, and that ComEd should be entitled to its generally allowed return on equity to reflect this real and present risk that is clearly demonstrated by Staff's own recommendations.

II. Response to Ms. Phipps' Testimony Relative to Risk and Return on Equity

Q. Can you explain why Ms. Phipps' assumption is overreaching?

A. Yes. First, Ms. Phipps actually makes a very important point that highlights the unwarranted nature of her assumption, without acknowledging it. On page 9, lines 175 through 177 of her Rebuttal Testimony, Ms. Phipps makes the statement that "there is virtually *no* risk that ComEd will recover less than 100% of the *prudent costs* it incurs to implement the PORCB program." (ICC Staff Ex. 8.0, 9:175-177 (emphasis added).) Ms. Phipps leaves the impression that ComEd is at no risk whatsoever of having costs denied. However, when an investor sees that a prudency review of any costs is contemplated, he or she assumes that some of those costs are at risk of disallowance. That is not any different from the assumptions investors make about all other utility costs that are dealt with in the course of traditional ratemaking activity. Each and every one of them is subject to review by the Illinois Commerce Commission ("Commission" or "ICC"), and therefore subject to non-recovery.

A whole spectrum of costs associated with the PORCB program, from the discount rate to uncollected receivables, is subject to approval by the ICC. Even though there are provisions that eventually "true up" ComEd's various costs under PORCB, the ICC still has to approve those costs. The ICC is ranked a "Below Average 2" by Regulatory Research Associates, the regulatory framework in Illinois is rated Ba by Moody's, and cost recovery provisions rated Baa by Moody's. These assessments indicate that regulatory risk is fairly high in Illinois, and therefore investors are going to be more cautious of investments in Illinois utilities than they would be for a utility in a jurisdiction with a better ranking.

In addition, the very fact that the PORCB program is being instituted to encourage switching by retail customers adds an additional dimension to the uncertainty inherent in the utility business. As Mr. Fruehe points out in his Rebuttal Testimony (ComEd Ex. 5.0), there are serious uncertainties about how the program will work out. There is risk that customers will not be convinced to switch and that the costs ComEd incurs will not be recovered for a number of years. Furthermore, the program may change dramatically as a result of unexpected outcomes of introducing it. As a result of these factors (and possibly others as well) - - none of which Ms. Phipps has considered - - it is my opinion that investors will not view the risk of the PORCB program as being much different from the risks of the traditional utility business.

Q. Why isn't PORCB like utility transition bonds?

A. Utility transition bonds were created in order to protect utilities in states that were transitioning to a competitive model from financial ruin. They were constructed in order to meet the requirements for a AAA rating. Those requirements are quite strict and were fashioned in order that investors would be comfortable that there was infinitesimal risk that principal and interest would not be paid on time and in the precise amounts expected.

Q. What provisions of the transition bonds accomplish that?

A. Transition bonds are first and foremost designed to provide a guaranteed stream of revenues that is separate and apart from the revenues of the utility. This is a critical feature that investors look for when examining the opportunity to invest in transition bonds. That guarantee required an irrevocable pledge by the state involved that funds would be recovered as expected and that the terms and conditions of the bonds would not be changed in any way. PORCB not only does not have these features, there are expectations that the program will change over time as more experience with it is gained.

Q. Are there other issues with Ms. Phipps' explanation of the similarities between transition bonds and PORCB that you disagree with?

A. Yes. On page 2, lines 43 through 44, Ms. Phipps states that "items 4 and 5 do not affect the riskiness of recovery of the cost of the underlying costs." (ICC Staff Ex. 8.0, 2:43-44.) She is referring to Mr. Fruehe's recitation of the 5 conditions that made transition bonds eligible for a AAA rating. Items 4 and 5 to which she refers relate to the segregation of funds and the bankruptcy remote trust that would protect that stream of revenues from the consequences of a bankruptcy of the utility to which they were formerly attached. Both of these provisions are critical to AAA ratings of the transition bonds. While they may not strictly affect "cost recovery" per se, they are critical to the AAA rating, and therefore lower cost, of transition bonds. The segregation of funds assures investors that funds flowing from the transition charge will not be comingled with, and therefore potentially misappropriated by, the utility. The bankruptcy-remote status of the trust ensures that should the utility declare bankruptcy, the flow of funds from the transition charge would continue to flow to the benefit of the transition bondholders and not creditors of the utility. To dismiss these two provisions, without which no transition bonds would have attained a AAA rating, as seemingly irrelevant indicates a lack of understanding of the structure of the transition bonds and why that structure is critical to investors. The PORCB program does not have these provisions. While I am not a lawyer, most investors aren't either. However, my 35 years of experience do not lead me to read the statute implementing the PORCB program as forming an irrevocable pledge for the recovery of assets, segregation of funds, or a bankruptcy remote trust structure that protects investors from the bankruptcy of the utility.

Q. Please state your conclusion.

A. Generally, before an investor will conclude that a cost recovery mechanism like that incidental to the PORCB program will reduce the risk of cost recovery, the specifics of the program need to be analyzed and evaluated. In reaching her conclusion that the PORCB cost recovery mechanism will so reduce ComEd's risks that a vastly lower return on equity is appropriate for PORCB investments, Ms. Phipps has failed to address or identify, much less consider, those specifics. As a result, she has not established any credible basis upon which the Commission can conclude that return on the investments in the PORCB program should be any different from ComEd's overall return. My own independent analysis of the specific risks I have identified leads to that same conclusion.

III. Response to Ms. Ebrey's Testimony

Q. What concerns do you have about Ms. Ebrey's testimony?

A. Ms. Ebrey's testimony challenges or contemplates re-categorization of a number of costs ComEd has identified. In doing so, she is demonstrating why my concerns about the level of risk inherent in this program, despite the adjustment clauses, is justified.

Q. Please explain.

A. For instance, Ms. Ebrey recommends that language be deleted from the proposed tariff that permits recovery of costs related to operation of employee training and procedures, operating and maintenance, and communication and education. While I am not familiar with the intricacies of the specific costs recited by Ms. Ebrey, they appear to be straightforward costs that any prudent utility would expend to make a new program efficient and successful. To recommend that language be deleted from the tariff that provides for the recovery of costs ComEd must spend to implement the program creates exactly the kind of risk levels inherent in traditional ratemaking activities which require a return on equity similar to that generally allowed ComEd.

Other examples of risk introduced by Ms. Ebrey include her challenge to ComEd's ability to recover $2.5 million of deferred expenses related to the PORCB project and speculation regarding whether all of the costs ComEd has identified are properly recoverable through the Rider PORCB, which she does not propose to resolve in this docket.

Q. What is your conclusion relative to Ms. Ebrey's testimony?

A. Ms. Ebrey has demonstrated exactly what I am concerned about, and why ComEd should be allowed a similar return on equity for the PORCB program as they are allowed for their general return on equity. The risk of disallowance is very real, as demonstrated by Ms. Ebrey's recommendations. ComEd is being given the *opportunity* but not a guarantee to earn the allowed return on the PORCB program. Therefore, the return on equity allowed should reflect that risk and be set at a level similar to the generally allowed return on equity for ComEd.

Q. Does that conclude your surrebuttal testimony?

A. Yes.