STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY	:	
	:	No. 10-0467
Proposed general increase in electric rates	:	

COMMONWEALTH EDISON COMPANY'S
INITIAL POST-TRIAL BRIEF

PUBLIC VERSION

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I. INTRODUCTION / STATEMENT OF THE CASE

A. ComEd Needs Rate Relief Because its Rates Cannot Recover its Costs.

Commonwealth Edison Company ("ComEd") filed this case on June 30, 2010, because its revenues from existing rates are some hundreds of millions of dollars less than it needs to meet its costs. The cost recovery shortfall as of surrebuttal is $326 million.[1] ComEd is concerned that, without the rate relief it is seeking, it will be unable over time to provide adequate and reliable delivery service at the lowest reasonable cost, as required by the Public Utilities Act.

ComEd's revenue and cost recovery shortfall is caused by several factors. In the main, its costs have risen, largely due to economic forces beyond its control, while use of its system has not grown to keep up. In particular:

- ComEd has invested nearly $2 billion in meeting the investment needs of customers and modernizing the distribution system;
- The costs of pension and medical benefits for ComEd's employees and retirees has grown rapidly and sizably; and
- Load, and thus, revenues have not kept up, due to poor economic conditions and ComEd's own investment in energy efficiency.

Guerra Direct Testimony ("Dir."), ComEd. Ex. 1.0 2nd Rev., 3:59-4:83.

The long-established standards under which ComEd's capital costs should be evaluated are whether those costs are "prudently incurred," "reasonable," and "used and useful" in serving customers. Yet, with the exception of a single capital project amounting to less than 0.25% of

[1] *See* Houtsma Surrebuttal ("Sur."), ComEd Exhibit ("Ex.") 55.0 2nd Revised ("2nd Rev"), 2:31-32. The precise shortfall has changed somewhat due to later changes in tax law, the effect of which can be determined from record evidence sponsored by ComEd and Staff. This value remains illustrative of the shortfall.

ComEd's requested revenue increase, no witness challenges that ComEd has invested and spent prudently or denies that the assets ComEd invests in are used and useful to customers. ComEd's investments in iron-in-the-ground unquestionably serve customers. ComEd's operating expenses also are prudent and reasonable, and those operations resulted in record reliability and safety. ComEd's investments in its employees' medical care and its retirees' pensions and benefits meet a critical public interest.

Yet, Illinois Commerce Commission (the "Commission" or "ICC") Staff ("Staff") propose that the Commission disallow over $200 million of ComEd's revenue (cost recovery) shortfall. The Illinois Attorney's General's office (the "AG") and Citizens Utility Board ("CUB") propose nearly $400 million in disallowances. These efforts are not based on any reasonable challenge to the reality of ComEd's costs, their prudence, or their importance to serving customers well. Rather, the lion's share is arguments and mathematical artifice tactically chosen to push costs out of the test year period or to invite the Commission simply to ignore them. Their effect is to artificially foreclose recovery of real costs of investments in ComEd's system and of real expenses that ComEd has, or will, incur to serve customers. The upshot is simple. If the Commission can be made to accept these individual "adjustments," then regardless of the actual and growing costs of providing delivery service, ComEd will not recover them. As the former Chair of the Commission, Dr. Philip O'Connor observed:

> [T]he ultimate test of a proposed disallowance is whether it brings the utility's revenue request more in line with its prudent and reasonable costs, not whether a reason can be contrived to exclude costs from rates. If the setting of inadequate rates results from disallowances of investments that the Commission most certainly expects will be made or expenses that it expects will be incurred, then the rates are artificial and fundamentally in conflict with the real level of company operations expected by the Commission.

O'Connor Reb., ComEd Ex. 26.0 Rev., 1:22-2:28.

Although Staff, the AG, CUB, and other intervenors offer many individual "adjustments," in the main, they: propose to apply unrealistic and unlawful standards to *pro forma* expenses; ignore or minimize real and rapidly growing costs of caring for employees and retirees; seek to disallow costs previously approved by the Commission and, in some cases, the courts as well; and pretend that ComEd can continue to invest and operate well when its rates do not recover a cost of capital commensurate with what investors actually expect to earn, or even what the Commission approved in ComEd's last case. For example:

- Staff recommends disallowing every dollar ComEd will incur (some of which is already spent) between January 1 and June 30, 2011 for corrective maintenance, apparently because it cannot be "known and measurable" unless ComEd can specify in advance precisely which wires will fall and where cables will fault during storms, after accidents, and through freezes and thaws. Ebrey Tr. 780-86. That is not just contrary law, it is wholly unrealistic. Everyone knows that tens of millions of dollars of corrective maintenance <u>will</u> be required, and it was forecast predictably and confidently. Claiming otherwise requires turning one's back on the mountain of evidence, and years of experience, that demonstrates with far more than "reasonable certainty" what activity is required to keep the lights on.

- AG/CUB argues that ComEd should recover <u>no</u> costs for investments made between April 1 and June 30, 2011, claiming that the particular forecasts must "rely upon judgment and estimates" and "[t]he further into the future the forecasts extend, the less reliable they are." Effron Dir., AG/CUB Ex. 2.0, 4:87-5:104; Effron Reb., AG/CUB Ex. 8.0, 4:80-5:102. The AG/CUB witness, however, discusses <u>no</u> particular projects, even those already far along, and ignores both the tens of thousands of pages of documentation supporting those projections and the sworn testimony and explanations of the experienced executives.

- Staff argues that ComEd should be allowed a return on equity of no more than 10% and as low as 9.68%, depending on the rate design. Staff's recommendation is out of line with the return that the capital markets actually demand. As demonstrated at the hearing, it is also the direct product of the biased use and unrepresentative input data, including anomalous spot data like that so recently criticized by the Commission in Peoples Gas' last rate case. Others, including AG/CUB, argue for still lower returns, but rely on models that ignore what investors themselves demand and have never accepted by this Commission.

- Another proposed disallowance would reduce the cost of pension contributions, a cost that has been twice been approved by the Commission and recently affirmed by the Appellate Court. Efforts to slash its recovery by some 25% are both

> inconsistent with these decisions, and are based on unfounded assumptions and results-oriented calculations.

Moreover, the legal bases for many of these challenges are not grounded in the Act, in case law, or in past Commission decisions. The costs at issue are not new to the Commission, Staff, or intervenors. They are, for the most part, the day-in, day-out customary costs that all utilities incur to provide safe and reliable service. They are the same costs that Ameren, Mid-American, and other utilities across the nation routinely incur. They are the same types of costs that have been litigated and approved by the Commission in ComEd's three most recent rate cases and in numerous cases involving the other utilities. In fact, many of the assertions that costs should be disallowed were first articulated long after ComEd either spent or committed to spend the money. They are, therefore, patently unfair. No business, let alone a regulated utility, can adequately or predictably manage its limited resources with confidence in such a volatile environment. Dr. O'Connor observed:

> To best serve the public, ComEd in upcoming years must wrestle both with the dual challenges of a growing need to replace or rebuild assets that were installed decades ago and the need to transform its delivery system with smart technology …. [T]he most important factor will be whether ComEd – and the investors who must support it – can have confidence that ComEd will have the financial capacity for such an undertaking.
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> * * * * *
>
> Consistent, steady and predictable regulation in policy and implementation is an essential condition for the billions of dollars in long term investments required for realizing the transformation of the network.

O'Connor Reb., ComEd Ex. 26.0 Rev., 8:180 - 9:185 & 2:37-39.

B. <u>ComEd Provides Reliable Service at a Reasonable Cost</u>

Even with the full increase that ComEd seeks and factoring in changes in supply rates, the impact on customers will be modest, about a $3 increase on the average monthly residential bill. Guerra Reb., ComEd Ex. 25.0, 9:190-191. A customer could *fully* offset that increase by taking advantage of existing ComEd energy efficiency programs. *Id*., 9:192-193. Nor are ComEd's rates, even with the full increase, high. ComEd's average residential rate is less than half New York City's and below rates in other major metropolitan areas such as Los Angeles, Houston, Washington, San Francisco, Dallas, Boston and Detroit. *Id*., 9:198 – 10:201. ComEd has also provided solid service to its customers for those rates. Compared to its peers, ComEd achieved top quartile reliability (*Id*., 7:153-154) – results surpassing that of other Illinois electric utilities. ComEd's level of safety have been in the top decile of the industry.

While ComEd understands that some have expressed concern about the affordability of electric rates, ComEd has worked hard to avoid and minimize the need for rate increases. In 2009, ComEd cut $85 million in operating and maintenance ("O&M") expenses (Guerra Dir., ComEd Ex. 1.0 2nd Rev, 3:53-56) and was thereby able to postpone seeking a rate increase at the time. Because 2009 is the test year in this case, that $85 million in savings results in a dollar for dollar reduction in rates that will be set in this proceeding. Indeed, even with the requested rate relief, ComEd's inflation-adjusted rates will be over 15% *lower* than they were in 1997. Guerra Dir., ComEd Ex. 1.0, 2nd Rev., 10:186.

Moreover, holding rates below costs in the belief that it will help consumers would be inefficient and unsustainable. Income decline and income disparity should not be addressed by artificially decreasing delivery rates. *E.g.*, O'Connor Sur., ComEd Ex. 53.0, 7:147-153. Moreover, as ComEd witness Dr. Hewings testifies, the electric infrastructure plays an important role in the economy of northern Illinois. *E.g.*, Hewings Sur., ComEd Ex. 69.0, 2:24-32. By continuing to maintain and improve its delivery system, ComEd can make a valuable contribution to reviving the regional economy through both job creation and by attracting new businesses to the state and region. *E.g.*, Hewings Sur., ComEd Ex. 69.0, 6:115-123; Guerra Sur., ComEd Ex. 52.0, 6:114-116.

ComEd recognizes that many of the same economic forces that are affecting its ability to recover its costs are also affecting its customers. It has reduced its request throughout this case in response to tax law changes, updated its cost of capital models, and voluntarily accepted valid adjustments. However, at the end of the day, all customers benefit from use of a reliable and well-run delivery system and infrastructure, and ComEd must be given a fair opportunity to recover its costs. ComEd spends well over $130 million in *toto* per month to operate and maintain an aging distribution system. Without adequate cost recovery to support these operations and investments, it is difficult to imagine that its investors will be eager to continue to finance that work, let alone the coming transformation of the grid with technologically advanced infrastructure.

II. OVERALL REVENUE REQUIREMENT AND REVENUE DEFICIENCY

ComEd's overall revenue requirement is $2.267 billion and its revenue deficiency is $326.3 million. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 6:112-13.

III. TEST YEAR

ComEd's revenue requirement is based on its historical 2009 test year with *pro forma* adjustments. Houtsma Dir., ComEd Ex. 6.0 Rev., 4:70-71.

IV. RATE BASE

A. Overview

ComEd's rate base is $7,349,227,000. ComEd Ex. 55.1, Schedule ("Sched.") A-4-Rev.

B. Potentially Uncontested Issues

1. Plant

a. AMI Pilot Costs (including AMI Meter Redeployment)

ComEd's rate base includes $51,888,000 (gross plant) for AMI pilot costs. Marquez Dir., ComEd Ex. 10.0, 18:334-19:357; McMahan Dir., ComEd Ex. 9.0 Rev. 15:308-311; ComEd Ex. 9.1 Schedule F-4. No party contests including these assets in rate base, or their costs. Staff initially proposed a $1.6 million disallowance to reduce ComEd's regulatory asset for 51,203 meters that were allegedly placed back in service, but, in rebuttal testimony, accepted ComEd's explanation that the vast majority of the 51,203 meters were retired and will not be reused. Rockrohr Reb., Staff Ex. 21.0, 22:475-23:496. Staff's rebuttal testimony includes no rate base disallowance for this item. Ebrey Reb., Staff Ex. 16.0, Sched. 16.04.

b. Other

ComEd agreed to the proposal of AG/CUB witness Brosch to adjust ComEd's rate base for a $5.27 million customer advance that has been determined to be related to a distribution project. Houtsma Reb., ComEd Ex. 29.0, 38:807-14.

2. General and Intangible Plant

3. Functionalization

C. Potentially Contested Issues

1. Post-Test Year Adjustments

a. Pro Forma Capital Additions

ComEd seeks to include in rate base $1.017 billion of investment in plant that has or will be made between the end of the 2009 test year and June 30, 2011. Donnelly Sur., ComEd Ex. 58.0 Rev., 67:1408-68:1428. The record shows, based on data available for inclusion in surrebuttal testimony, that ComEd had already placed into service $555.8 million of the $656.6

million in additional plant expected to be placed in service by December 31, 2010, and that the additional amounts to be placed into service during the first and second quarters of 2011 are $177.8 million and $182.8, respectively. *Id*., 66:1410-1411, 67:1423–68:1426. Although Staff and AG/CUB challenge a portion of the $1.017 billion investment, each accepts every dollar of investment that ComEd projected to place in service through December 31, 2010. Ebrey Reb., Staff Ex. 16.0, 5:82-8; Staff Ex. 16.08; Effron Dir., AG/CUB Ex. 2.0, 4:87-5:94; Effron Reb., AG/CUB Ex. 8.0, 2:37-43. In fact, AG/CUB witness Effron goes one step further and would allow the $177.8 million of first quarter 2011 investments[2] by limiting his proposed time-based disallowance to *pro forma* plant additions planned for the second quarter of 2011. Effron Dir., AG/CUB Ex. 2.0, 4:87-5:94; Effron Reb., AG/CUB Ex. 8.0, 2:37-43.

Staff witness Ebrey, on the other hand, would only accept 28 specific projects planned to be placed in service during the first and second quarters of 2011, and those specific projects only account for $57.3 million of the $360.6 million planned to be placed into service during the first and second quarters of 2011. Ebrey Reb, Staff Ex. 16.0, Sch. 16.08, p. 3; Donnelly Sur, ComEd Ex. 58.0 Rev., 68:1438-45. She recommends that the Commission disallow approximately 84% of ComEd's planned investment during the first and second quarters of 2011, more than $303 million, because she believes that work is either not "known" or not "measurable" under the Commission's rules.

[2] Mr. Effron also reduces ComEd's planned investment in general and intangible plant through March 31, 2011 by an additional $32.8 million by limiting the investment in those categories from November 2010 through March 2011 to 5 times the average monthly rate of spending on such plant through the first ten months of 2010 (subject to a "true up" to the actual balance of such plant as of March 31, 2011). Effron Reb., AG/CUB Ex. 8.0, 4:80-5:102. ComEd's *pro forma* amounts are based on actual planned investments which do vary from month to month, and there is no basis for adopting Mr. Effron's proposal to limit planned investment amounts for November 2010 through March 2011 to the average monthly investment over the prior 10 months. See Donnelly Sur., ComEd Ex. 58.0 Rev., 4:85-5:95.

AG/CUB witness Effron's comparatively more modest adjustment would disallow the $182.8 million of plant additions planned for the second quarter of 2011, arguing that those additions cannot be characterized as "known" and "measurable" with any reasonable degree of certainty because forecasts must "rely on judgment and estimates" and "the further into the future the forecasts extend, the less reliable they are." Effron Dir., AG/CUB Ex. 2.0, 4:87-5:104; Effron Reb., AG/CUB Ex. 8.0, 4:80-5:102.

As explained below, Staff's and the AG/CUB's proposed disallowances are based on a radical departure from the Commission's rules and practice, are contrary to the evidence, and should be rejected.

(i) ComEd's Evidence Satisfies the Commission's Pro Forma Rule

The Commission's *Pro Forma* adjustments rule states in relevant part:

> 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 operating results of the test year. These adjustments shall reflect changes affecting the ratepayers in plant investment, operating revenues, expenses, and cost of capital where such changes occurred during the selected 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…. Any proposed known and measurable adjustment to the test year shall be individually identified and supported in the direct testimony of the utility.

83 Ill. Admin. Code, § 287.40 (emphasis added). In other words, ComEd is allowed to include in rate base those investments that are "known" and "measurable" and "reasonably certain to occur" by June 30, 2011; and, as explained below, ComEd has done just that by providing tens of thousands of pages of well-organized and easily accessible documentation supporting the projected work to be done in each of ComEd's five key work categories.

Importantly, no witness contests or presents evidence disputing:

- The justification, cost or prudence of any actual or scheduled plant addition;
- The planning, design or engineering of any proposed plant addition;
- The need for any pending plant addition to be completed on schedule;
- ComEd's commitment of all resources required to complete the plant additions on schedule; or
- The workplan or construction schedule for any planned plant addition.

Donnelly Reb., ComEd Ex. 32.0 Rev., 14:258-69.

No one disputes that ComEd has a legal obligation to provide electrical service to all customers who request service (*see* 83 Ill. Admin. Code §§ 410.330 and 410.410; Tr. 778:16-19), and ComEd plans and executes this work through the New Business work category. It also goes without saying that ComEd must "keep the lights on" by fixing equipment after it fails, and much of this work is managed through its Corrective Maintenance work category. The other three major work categories are equally obvious and necessary to providing basic electric service. They include: 1) Capacity Expansion, through which distribution engineers forecast load on system equipment and plan and construct upgrades to avoid electrical overloads which lead to costly equipment failures; 2) Facility Relocation, when ComEd must relocate facilities to accommodate state and local governmental expansion plans; and 3) System Performance, which involves projects to enhance reliability. Donnelly Reb., ComEd Ex. 32.0 Rev., 24:491-25:503, 27:546-54, 33:680-34-687, 37:761-38-779, 44:924-45:933, 49:1033-36.

To support the projected investments in each of these five work categories, ComEd provided every conceivable, available form of evidence to demonstrate that, with more than reasonable certainty, it will place into service $360.6 million in plant additions, primarily in these categories, between January 1 and June 30, 2011. Specifically, ComEd's most senior operating officer, Executive Vice President, Terence Donnelly, testified in unprecedented detail about the nature and types of work that will be performed. He provided more than 41,000 pages of well-organized, supporting documentation and explained how the work is planned using a "bottom-up" approach. Donnelly Reb., ComEd Ex. 32.0 Rev., 8:147-51, 15:279-16:314; ComEd Ex. 32.2. Importantly, based upon decades of operational experience, ComEd knows with reasonable certainty what will be required of it to serve customers and keep the lights on during that six month period. Donnelly Reb., ComEd Ex. 32.0 Rev., 5:72-80; *see generally*, Donnelly Reb., ComEd Ex. 32.0 Rev., pp. 9-69. That much of this evidence remains unrefuted is not surprising given that Ms. Ebrey, who is an accountant, is admittedly not an expert regarding the construction, operation or maintenance of electric distribution systems.

At the hearing, Ms. Ebrey testified as follows:

> **Q**. You know that ComEd must invest in its system over the next six months, right?
>
> **A.** As an accountant, I don't know that I know what the Company must do over the next six months.
>
> **Q**. Right. As an accountant, you don't pretend to understand what ComEd has to do to meet its obligation to serve, right?
>
> **A**. That's beyond the scope of my testimony and beyond my expertise.

Ebrey, Tr. 795:6-15.

While projections regarding plant additions may be beyond the scope of Ms. Ebrey's testimony and expertise, they fall squarely within the expertise of Mr. Robert W. Donohue, an independent outside expert with more than 42 years of utility operating experience, whose previous work experience included operational oversight of New York City's entire electrical distribution system. Donohue Reb., ComEd Ex. 35.0 Rev., 1:3-11, 3:58-5:98. Specifically, he provided extensive testimony regarding ComEd's investment plans and completed a thorough analysis of ComEd's evaluative techniques and its planning and workplan development methodologies. He also analyzed numerous specific projects in each work category, many of which are in flight and will be in service by June 30, 2011. *Id*. at 7:142-8:157.[3] Based upon his experience and the official and field reviews he conducted, he concluded that ComEd knows, plans and manages it work in a prudent and efficient manner that compares favorably with industry practices and that it is reasonably certain that ComEd will make the additional investments it plans to make between January 2010 and June 30, 2011. *Id*. at 9:87-12:260.

Furthermore, Mr. Donohue performed an analysis of the five most recent 18- month *pro forma* periods (2005 through 2009), evaluating the same 18-month period at issue here, January 1 of year one through June 30 of year two. That analysis showed that ComEd has a strong track record of forecasting plant additions with precision – ComEd's actual spend on plant additions was, on average, within 2.6% of its projected spend for these periods. Donohue Reb., ComEd Ex. 35.0 Rev., 20:437-23:483. If the results for the exogenous and unusual January 2008 – June 2009 18-month period subject to the Global Credit Crisis and strong downturn in new business are removed from Mr. Donohue's analysis, ComEd's actual spend on plant additions was, on average within 1.9% of its projected spend. *Id*. at 24:485-506.

The evidence proffered by ComEd was comprehensive and voluminous. As to all five of its major work categories, ComEd provided the following information.

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[3] Mr. Donohue summarized the scope of his analysis (ComEd Ex. 59.0, 4:52-64):

> As explained in my rebuttal testimony, in addition to the review described above I interviewed personnel, reviewed numerous documents and reviewed specific unique and specific blanket projects to support my conclusion that ComEd will invest consistent with its overall pro forma. ComEd Ex. 35.5 lists the names of 21 key personnel I interviewed who are accountable for the planning and implementation of projects and programs contained in the pro forma. ComEd Ex. 35.4 lists 81 different types of documents I reviewed regarding planning and forecasting as well as the implementation of specific unique and specific blanket projects. ComEd Ex. 35.6 and 35.7 list over 100 specific project ITNs and specific blanket project Work Orders I reviewed. The interviews, documents, and project reviews all support my conclusion that ComEd not only has properly planned the projects, but will implement these plans and make the investments in distribution plant during the pro forma period consistent with its obligation to serve.

- For every individual project that is expected to cost more than $100,000, ComEd provided project authorization documents indicating that the project had been specifically identified and internally challenged and approved (Donnelly Reb., ComEd Ex. 32.0 Rev., 17:337-38);
- work orders and/or project engineering documents for each unique project expected to exceed $1 million (Donnelly Reb., ComEd Ex. 32.0 Rev., 17:339-41);
- four, six-inch binders containing hard copies of contract requisition documents for all work involving third party contractors organized by the five major work categories (Staff Group Cross Ex. 1, pp. 185-196 (Response to TEE 14.03)).

By way of further example, a summary of the evidence ComEd provided to support its plant additions from January – June 2011 for New Business and Corrective Maintenance follows:

New Business ($64.5 million Jan-June, 2011)

The work in the new business category is primarily comprised of 97 unique projects in flight and individually identified and two blanket projects through which smaller dollar customer connections are managed: 1) Outside Chicago baseline (ITN no. 5972); and 2) Inside Chicago baseline (ITN no. 5968). Donnelly Reb., ComEd Ex. 32.0 Rev., 46:954-71. The additional evidence provided by ComEd in support of its New Business projects includes the following:

- For unique projects in excess of $500,000, Mr. Donnelly explained the project specifically, why it was necessary, the equipment to be installed, the cost and when it was expected to be placed in service. Donnelly Sur., ComEd Ex. 58.0 Rev., 33:729- 36:790.
- For each of the blanket programs, ComEd provided comprehensive documentation explaining the repetitive nature of this work, why it is necessary, how costs are derived,

approved and managed, and how much ComEd has spent in recent years. This information was provided in the form of reports prepared by an outside engineering expert, PDR&C. Donohue Sur., ComEd Ex. 59.0, 5:92-6:108, 9:176-10:190; ComEd Ex. 59.2; *see also* Donnelly Sur., ComEd Ex. 58.0 Rev., 32:711-33:722, 36:791-798.

- ComEd's workplans are informed by its recent experience. Outside Chicago New Connections: During the periods January 1, 2009 through June 30, 2009 and January 1, 2010 through June 30, 2010, ComEd connected 5,998 and 4,950 new customers, respectively. Donnelly Sur., ComEd Ex. 58.0 Rev., 33:718-20. ComEd plans to install 5,286 services under this program by June 30, 2011. Donnelly Sur., ComEd Ex. 58.0 Rev, 33:722.
- Inside Chicago New Connections: During the periods January 1, 2009 through June 30, 2009 and January 1, 2010 through June 30, 2010, ComEd connected 2,734 and 2,332 new customers, respectively. Donnelly Sur., ComEd Ex. 58.0 Rev., 33;720-22. ComEd plans to install 2,375 new services between January and June 2011. Donnelly Sur., ComEd Ex. 58.0 Rev., 33:721.
- ComEd has 13,000 work orders open under New Business and at least 3,500 pending requests for new service. Donnelly Reb., ComEd Ex. 32.0 Rev., 47:991-94.

Corrective Maintenance ($89.6 million Jan – June 2011)

The most significant work that ComEd plans for in the corrective maintenance category are cable faults and overhead defect repairs. This work is managed through four blanket projects: 1) Emergency Cable Fault Replacements (ITN no. 20543); Emergency Cable Fault Repairs (ITN no. 10623); 3) Overhead Distribution Defect Repairs (ITN 10622); and 4) Storm Restoration (ITN no. 10628). Donnelly Reb., ComEd Ex. 32.0 Rev., 34:688-37:758; Donnelly Sur., ComEd

Ex. 58.0 Rev., 28:629 – 29:637. The additional evidence that supports these planned investments, include:

- ComEd cable faults are consistent year over year and inform ComEd's plans for the period in dispute. Between January 1 and June 30 of 2007, 2008 and 2009, ComEd repaired 6,416, 6,486 and 6,467 cable faults, respectively (Donnelly Sur., ComEd Ex. 58.0 Rev., 27:589-91);
- A list of specific work orders and contract requisitions (Donnelly Sur., ComEd Ex. 58.1);
- The contract between ComEd and the third party contractor that assists with cable fault repairs, Trench-It, Inc., dated September 23, 2008 (Staff Group Cross Ex. 1, pp. 185-95 (Response to TEE 14.03, Attachment 3, Vol. 4 of 4));
- ComEd experienced at least 600,000 customer interruptions in each of 2008, 2009 and 2010 as a result of storms (Donnelly Sur., ComEd Ex. 58.0 Rev., 29:631-37); and
- ComEd's historical overhead distribution defect repairs from January 1 through June 30 of 2008, 2009, and 2010 were 8,649, 9,402, and 9,038, respectively (Donnelly Sur., ComEd 58.0 Rev., 28:610-11).

(ii) <u>Staff's and Intervenors' Interpretation of Whether an Investment is "Known" Is Unduly Restrictive and Unworkable</u>

Staff witness Ms. Ebrey advances an improper and unrealistic interpretation of the *pro forma* rule in order to justify disallowing 100% of ComEd's planned investment in Corrective Maintenance and 98% of planned New Business investment. ComEd Cross Ex. 4. Relying upon the American Heritage Dictionary definition of "emergent", Ms. Ebrey concludes that all emergent work "comes unexpectedly into existence" and therefore cannot be "known" under the *pro forma* rule. Staff Group Cross Ex. 1, p. 280 (Staff's Data Request response to ComEd-Staff

2.12). While she acknowledges, as she must, that ComEd must fix a cable fault when it occurs, she interprets the *pro forma* rule to mean that every single project must be specifically identified. Because the location of each particular cable fault cannot be identified "in advance", she claims that the costs to address such cable faults can never meet the "known and measurable" standard. Ebrey, Tr. 781:3-16.

Similarly, Ms. Ebrey claims that "If the work is indeed unexpected, it cannot, by definition, be 'individually identified and supported in direct testimony.' Therefore, it cannot be known and measurable when the rate case is filed." Staff Group Cross Ex. 1, p. 280. This is apparently intended to explain why Ms. Ebrey disallows 100% of all costs ComEd plans to spend for Corrective Maintenance between January 1 and June 30, 2011.[4]

Staff's position is based on an incorrect and unreasonable reading of the *pro forma* rule. The *pro forma* rule does state that "[a]ny proposed known and measurable <u>adjustment</u> to the test year shall be individually identified and supported in the direct testimony of the utility." 83 Ill. Admin. Code § 287.40 (emphasis added). Contrary to Staff's position that individual projects must be identified and supported, the rule limits this obligation to the proposed *pro forma* "adjustment" and not every single one of its component parts or projects. Indeed, Staff recommendation to accept all planned *pro forma* investments for November and December of 2010, including investments for emergent work under blanket programs, does not raise this concern or apply this standard. The data and information that supports investments based on emergent work for the first and second quarters of 2011 is not distinguishable from the data and

[4] That Ms. Ebrey's new dictionary definition is wholly unworkable is evidenced by her own inconsistent application of the standard to "emergent" work. At the time of her rebuttal testimony on December 23, 2010, all New Business and Corrective Maintenance work for November and December was based on ComEd's forecast of the work to be performed. Although ComEd had provided no information regarding actual work placed in service for those months at that time, Ms. Ebrey nevertheless recommended that all of the forecasted work for those months be approved. Ebrey Reb., Staff Ex. 16.0, 5:82-88 and Schedule 16.08; *see also* Tr. 773:16-774:2.

information that supports such investments for November and December of 2010. All of this investment has been supported and should be approved. Moreover, the Commission's rules specifically provide that the "standard information requirements do not bind the Commission to a decision based solely on data provided pursuant to this Part …." 83 Ill. Admin. Code 285.110(b).

Staff's position that emergent work is "unexpected" and, therefore, cannot be "known" is also contrary to the record. The evidence is both clear and uncontested that ComEd as well as all electric utilities expect and plan for various types of emergent work. As Mr. Donnelly testified, "blanket programs capture investments in routine core activities that ComEd must complete, and must complete when or shortly after the need arises. For emergent work, claiming that blankets cannot be reasonably certain to proceed at appropriate levels throughout the year is not credible. It amounts to claiming that ComEd cannot be certain that it will, for example, have to repair burned out transformers, replace fallen wire, or replace shorted-out underground cable." Donnelly Reb., ComEd Ex. 32.0 Rev., 21:420-25; *see also Id.* at 26:527-27:539. Similarly, Mr. Donohue explained "emergent" work as follows:

> The need for some of the relatively small, short duration jobs may be identified on the day in which the addition is placed into service or during the preceding few days. That type of work can be reasonably planned. It is work such as repairing or replacing damaged or failed underground or overhead equipment that is needed to restore reliable electric service to customers.
>
> The quantity of emergent work can be reasonably planned while the exact location may not be known in advance. The quantity of that work is driven by the needs of the electric distribution system size, design, age, exposure, and other factors that do not materially change year to year. With the aid of trend analyses and reviews of internal and external factors that may affect those trends, ComEd is able to plan for this small and short duration type of work and costs with reasonable certainty. Of course, particularly in categories where the work is comprised of hundreds of small jobs and dominated by emergent tasks or tasks driven by relatively immediate events or customers' requests, the specific work cannot be completely identified.

> ComEd cannot predict exactly where or when a storm will strike or when a particular transformer or cable will fail. But, it is routine and required for prudent management of the distribution infrastructure to plan for such work. ComEd also has a service obligation to plan resources for that work. ComEd knows with a high degree of certainty that emergent work will occur, and can plan for both the scope and costs of that work with reasonable certainty.

Donohue Reb., ComEd Ex. 35.0 Rev., 17:357-18:376.

Although Ms. Ebrey admits that it would be unreasonable to conclude that ComEd will not connect any new customers between January 1 and June 30, 2011 (Tr. 771), she nevertheless recommends disallowance of 98% of all planned New Business investment during that time period, allowing only a single unique New Business project. ComEd Cross Ex. 4; Ebrey Reb., Staff Ex. 16.0, 15:286-16:298. As regards new business managed through blanket ITNs, Ms. Ebrey would apparently deny this investment because ComEd did not (and cannot) identify in advance every single new connection that will be made. The *pro forma* rule does not impose such a restriction. Staff's position is also contrary to prior Commission rulings allowing *pro forma* adjustments for routine work managed on a blanket basis. *See Central Ill. Light Co., et al.*, ICC Dkt. Nos. 09-0306 - 09-0311 (*cons.*), Final Order (April 29, 2010) at 11-12. ("Staff accepted pro forma plant additions related to both specific and blanket projects that will occur through February 2010 since AIU provided documentation that the projects were known and measurable.") Indeed, Staff's testimony in the Ameren Illinois Utilities rate case made clear that Staff relied on and accepted testimony evidence regarding the recurring nature of blanket project work and its consistent occurrence throughout the year to approve same – similar to portions of ComEd's detailed testimony in the instant case. *See* Mary Everson Rebuttal, Staff Ex. 16.0, ICC Dkt. Nos. 09-0306 - 09-0311 (*cons.*) at 3:59-61 (Filed on e-Docket on Nov. 20, 2009, 3:49 PM) ("Mr. Pate also discussed the type of projects that are included in the blanket work orders and demonstrated that this type of work occurs consistently throughout the year.") Further, while new business work emerges based on customer requests, that work is expected and known as explained above.

To the extent that Staff is arguing that it cannot conduct a used and useful or prudence analysis of blanket investments without specifically identified poles, transformers, or customers, its argument lacks merit. ComEd has included extensive testimony on the work that is performed under each blanket program, including the need for that work, how ComEd has determined the extent of work that is needed and will be performed, information regarding the costs of that investment, and the specific circumstances and situations under which this work will be performed. *See* Donnelly Reb., ComEd Ex. 32.0 Rev., 2:29-35, 13:253-14:257, 15:279-86, 26:527-27:539, 28:561-29:584, 31:631-36, 33:678-37:758, 38:781-39:816, 43:886-44:921, 44:923-48:1002, 50:1045-62:1240, 63:1265-64:1284, 66:1334-69:1378; Donnelly Sur., ComEd Ex. 58.0 Rev., 2:41-3:44, 4:66-71, 10:215-11:228, 18:374-19:394, 20:425-25:540, 25:552-31:676, 31:689-33:728, 36:792-38:836, 39:862-42:938, 43:960-58:1214, 61:1271-62:1310, 63:1326-64:1354, 65:1373-66:1383; ComEd Exs. 58.1 and 58.5; Donohue Reb., ComEd Ex. 35.0 Rev., 2:32-7, .10:229-34, 28:588-97, 34:681-35:701, 40:805-41:833; ComEd Ex. 35.8; Donohue Sur., ComEd Ex. 59.0, 4:65-8:158, 10:196-13:263; ComEd Exs. 59.1 through 59.7. This information clearly establishes that such investment is or will be prudent as well as used and useful, and allows for an informed and substantive analysis of whether such investment is or will be prudently incurred and used and useful.

An argument that prospective investments under blanket programs cannot be reviewed for prudence or used and usefulness would also appear to be a red herring. Ms. Ebrey acknowledges that she "has not conducted a prudency review of the ITNs contained in ComEd 32.1" and that "[a]pplication of the 'used and useful' criterion is beyond the scope of [her] testimony." Staff Group Cross Ex. 1, pp. 304, 306 (Staff's Data Request Responses to ComEd-Staff 7.10 and 7.11). Moreover, Staff did not raise prudence or used and useful concerns for the same type of costs under the same ITNs for investment planned during November and December of 2010. See e.g., Tr. 784:21-785:11. Similarly, Staff witness Mr. Rockrohr acknowledges ComEd's extensive use of blanket programs for recurrent and relatively low individual cost tasks. He did not express any concerns regarding whether ComEd's investments under blanket programs were prudent or used and useful, and apparently did not find it necessary to review investments under blanket programs because they are not tracked on a project location basis and each program involves a common type of work (such as installation of underground and overhead services) that takes place at a multitude of locations. Rockrohr Dir., Staff Ex. 6.0, 10:217-11:238.

Ms. Ebrey then relies upon a single statement in Mr. Donnelly's testimony to the effect that past experience indicates that some New Business projects "may get pushed beyond June 2011" or even "cancelled" by customers to justify disallowance of all but one of the 97 unique new business projects. She cites this testimony to support her conclusion that only one of the unique new business projects are reasonably certain to be placed in service by June 30, 2011, but then ignores pages and pages of Mr. Donnelly's testimony explaining why those projects are reasonably certain to be placed in service by June 30, 2011. As to 97 specific customer connection projects that Mr. Donnelly describes in detail in his rebuttal testimony (Donnelly Reb, ComEd Ex. 32.0 Rev., 44:922-49:1030; ComEd Ex. 32.2; *see also* Donnelly Sur, ComEd Ex. 58.0 Rev., 31:688-36:805), Ms. Ebrey acknowledges that she conducted no analysis regarding when those projects will be placed in service, but they are proposed for disallowance, nonetheless. Ebrey, Tr. 776:10-16.

Staff's position is not only contrary to the facts established in this record, but it is also inconsistent with the law. As noted above, ComEd has a legal obligation to make new customer connections when requested. Work planned to meet ComEd's legal obligations to connect new customers is, by definition, known and reasonably certain to occur as planned. ComEd cannot be simultaneously obligated to perform new business work but unable to recover its costs on a theory that its obligation to perform that work is uncertain. While ComEd was very frank in acknowledging that its experience in the current economic situation suggests that some customers may change their plans, that does not change the fact that ComEd is obligated to move forward on customer requests submitted in compliance with the Commission's rules. Work that ComEd is legally required to perform cannot be deemed to fail the known and measurable standard just because a few customers may take future actions that would change or possibly eliminate the basis for a new customer connection. That work is known and reasonably certain to occur.

If the Commission accepts Ms. Ebrey's dictionary-based interpretation of emergent work, then whole categories of the most basic costs that must be incurred to provide reliable electric service would, by definition, be excluded from the *pro forma* rule. The Commission has never supported such a restrictive interpretation, and ComEd respectfully submits that to do so would represent an unwarranted and unsupported sea change. This simply cannot be what the Commission intended when it adopted the *pro forma* rule.

(iii) Staff's and Intervenors' Interpretation of Whether an Investment is "Measurable" Is Incorrect.

As is customary in historical test year rate cases, the utility initially files *pro forma* adjustments that include estimates or projections of costs for additional planned investments expected to be placed in service during the post-test year *pro forma* period. As the case progresses, data on additional plant actually placed into service during the *pro forma* period becomes available and the proposed adjustment is updated to reflect actual costs and any refinements to the remaining estimated or projected costs – which are then closer in time. When it filed this case in June, 2010, ComEd's *pro forma* plant additions reflected ComEd's estimates or projections of expected investment costs at the beginning of the *pro forma* period and the total anticipated investment was $1.038 billion. Donnelly Dir., ComEd Ex. 8.2; Donnelly Sur., ComEd Ex. 58.0 Rev., 14:302-7. ComEd has since updated its *pro forma* additions data twice in testimony. In November, 2010, ComEd provided an update to include actual plant additions through October 31, 2010 and updated figures for the rest of the *pro forma* period – at that point, the total *pro forma* investment was $1.030 billion. In early January, 2011, ComEd provided actual plant placed in service through November 30, 2010 and updated figures for the rest of the *pro forma* period – resulting in an updated total *pro forma* investment of $1.017 billion.

As explained repeatedly in testimony, ComEd operates in a dynamic environment that occasionally results in adjustments to its work plans. Donnelly Reb., ComEd Ex. 32.0 Rev., 2:29-3:42; Donnelly Sur., ComEd Ex. 58.0 Rev., 13:270-79; Donohue Reb., ComEd Ex. 35.0 Rev., 33:664-34:670. The standard is reasonable certainty, not absolute certainty. As Mr. Donnelly explained, "any true variability would have been due to ComEd adapting to changing customer needs or new system requirements. As a result, the currently planned pro forma investments would be more rather than less "certain" because the current plan already recognizes and accounts for the root causes of any such variability. Indeed, since there are only 6 months left in the 18 month pro forma period, actual investments will have effectively "cured" or "remedied" any actual variability." Donnelly Sur., ComEd Ex. 58.0 Rev., 14:296-301. Moreover, ComEd's projected *pro forma* investment is within approximately 2% of ComEd's original cost estimates, consistent with prior results for ComEd as testified by Mr. Donohue. Such variance does not make the *pro forma* adjustment unmeasurable.

In sum, ComEd provided detailed, competent evidence that demonstrates that it will place an additional $360.6 million of plant in service between January 1 and June 30, 2011. That evidence includes both a huge volume of detailed project- and blanket-specific records and nearly two hundred pages of highly detailed sworn testimony. *See Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 322 Ill.App.3d 846 (2nd Dist. 2001) (testimony, evidence must be considered as evidence, not just other forms of documentation). In contrast, Staff's and the AG/CUB's interpretation of the pro forma rule is unprecedented, unduly restrictive and not competent. Indeed, adoption of such an approach would signal an alarming new policy that discourages utility investments in maintaining a safe and reliable electric system.

b. Accumulated Provisions for Depreciation and Amortization Related Provisions for Accumulated Depreciation

Staff witness Ebrey, AG/CUB witness Effron, and IIEC witness Gorman recommend adjustments to roll forward through the *pro forma* capital additions period the depreciation reserve and accumulated deferred income tax ("ADIT") liabilities related to embedded (end of test year) plant. The Commission rejected similar proposals in ComEd's last rate case, ICC Docket No. 07-0566, and instead followed what had been its consistent practice since at least ICC Docket No. 01-0423, which was to deny the "roll forward" where the utility's plant investment was continuing to increase. *Commonwealth Edison Co.*, ICC Docket No. 05-0597, pp.12-15 (Order July 26, 2006); *Commonwealth Edison Co.,* ICC Docket No. 01-0423, pp.41-44 (Interim Order April 1, 2002) (carried forward to final Order of March 28, 2003); *see also North Shore Gas Co., et al.*, ICC Docket Nos. 07-0241/07-0242, pp. 16-17 (Order Feb. 5, 2008).

The facts in this case that are relevant to this issue even more strongly support rejecting these "roll forward" proposals. Specifically, ComEd witness Kathryn Houtsma rebutted the testimony of Staff witness Ebrey that the roll forward is necessary to ensure that ComEd's revenue requirement is not overstated. When all elements of the revenue requirement are considered, the revenue requirement proposed by ComEd in this case – based on a 2009 test year with no roll forward – approximates cost levels in 2011 when the rates set in this case will take effect.[5] Likewise, the roll forward is not needed to ensure that the rate base is not overstated because ComEd will continue to make significant capital investments during the period when rates set here will be in effect, in amounts that will exceed the continuing accrual of depreciation. Houtsma Reb., ComEd 29.0, 8:142-57; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 11:224-12:237. Ms. Houtsma also noted that in each of the last three years, ComEd's actual earned return on equity ("ROE") has significantly lagged the ROE authorized by the Commission, even though rates set in those cases did not provide for a roll forward of depreciation on embedded plant. Houtsma Reb., ComEd Ex. 29.0, 8:158-9:165; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 8:152-9:168. In short, a roll forward of the depreciation and ADIT reserves is not necessary to protect customers from excessive rates.

It is true that on September 30, 2010, the Illinois Appellate Court issued an opinion in the appeal of the Order in ICC Docket No. 07-0566 that addresses this issue. On January 25, 2011, ComEd filed a Petition for Leave to Appeal the Appellate Court's Ruling to the Illinois Supreme Court. The mandate of the Appellate Court has not yet been issued, and will not issue until such

[5] In the 2003 Ameren rate cases Order, which AG/CUB and IIEC previously have cited many times in support of the "roll forward", (*see e.g.*, Order at pp. 22, 25, Docket No. 05-0597) the Order stated in part in relation to this issue: "The regulatory basis for adopting a test year is to ensure that the rates established are reflective of costs and revenues that may be expected **for the period during which such rates are in place**." *Central Ill. Pub. Serv. Co., et al.*, ICC Docket Nos. 02-0798, 03-0008/03-0009, p. 10 (Order Oct. 22, 2003) (emphasis added).

time as ComEd's Petition before the Supreme Court is acted upon and the appeal finally decided. Ms. Houtsma explained that, given the status of the appeal and the factors discussed in her direct and rebuttal testimony, ComEd continues to believe that a *pro forma* adjustment to roll forward the depreciation reserve and ADIT is not warranted. Houtsma Dir., ComEd Ex. 6.0 Rev., 10:209-15:302; Houtsma Reb., ComEd Ex. 29.0, 7:131-11:210; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 7:125-12:237.

c. Accumulated Deferred Income Taxes (ADIT)

See Section IV C 1 b.

2. Construction Work in Progress

ComEd seeks to include $12.6 million in construction work in progress ("CWIP") on short-term investments not eligible for AFUDC in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev., 26:526-27:528; ComEd Ex. 6.1, Sched. B-7, l. 3, col. B. AG/CUB witness Brosch proposes to disallow this entire amount. Brosch Dir., AG/CUB Ex. 1.0, 17:377-80. Mr. Brosch's objection is two-fold: first, he claims that the projects on which CWIP is included are not in service and thus cannot be considered used and useful; and second, he asserts that ComEd is "likely" to have little or no actual cash investment in these projects that requires any return from investors. *Id.*, 17:381-18:404. Mr. Brosch concedes that in the last ComEd rate case the proposed level of CWIP not accruing AFUDC was allowed into rate base, on an uncontested basis. *Id.*, 20:437-41.[6] Finally, Mr. Brosch suggests that if this investment is not included as

[6] CWIP not accruing AFUDC has been approved in rate base in all of ComEd's delivery services rate cases (2007, 2005, 2001, and 1999). *Commonwealth Edison Co*., ICC Dkt. No. 07-0566, Appendix to Final Order, (Sept. 10, 2008) at 4; *Commonwealth Edison Co*., ICC Dkt. No. 05-0597, Appendix A to Final Order, (July 26, 2006) at 5; *Commonwealth Edison Co*., ICC Dkt. No. 01-0423, Appendix A, Sched. 3 to Final Order, (March 28, 2003); *Commonwealth Edison Co*., ICC Dkt. No. 99-0117, Appendix A, Sched. 3 to Final Order (Aug. 26, 1999). In ComEd's 2005 rate case, CUB initially objected to inclusion of CWIP not accruing AFUDC but later withdrew that objection and supported an agreed amount. *Commonwealth Edison Co*., ICC Docket No. 05-0597, p. 5 (Order July 26, 2006).

CWIP, ComEd could revise its AFUDC calculations to include these CWIP amounts. *Id.*, 20:453-21:466.

Mr. Brosch's CWIP proposal rests on an incorrect legal premise and is otherwise wrong and not likely to benefit customers. First, the "used and useful" objection is not applicable to this CWIP investment. *See, e.g., Citizens for a Better Env't v. Ill. Commerce Comm'n,* 103 Ill. App. 3d 133, 430 N.E.2d 684 (4th Dist. 1981) (affirming inclusion in rate base as CWIP of $97 million of investment in unfinished generating station over objection that the unfinished station was not used and useful). Ms. Houtsma pointed out that Section 9-214(e) of the Illinois Public Utilities Act, 220 ILCS 5/9-214(e), is specifically applicable to CWIP, and provides that "the Commission may include in the rate base of a public utility an amount for CWIP for a public utility's investment which is scheduled to be placed in service with[in] 12 months of the date of the rate determination" without any necessity that the short-term CWIP be shown to be used and useful. Houtsma Reb., ComEd Ex. 29.0, 42:904-43:909. In any event, these short-term CWIP investments will be providing service and be used and useful within weeks of the time the rates set in this case take effect. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:704-11. Furthermore, no one contends that the 12-month limitation in Section 9-214(e) is not met by the CWIP in question.

Mr. Brosch's second objection is also not well taken, because any "vendor financing" will finance the investment for a period of weeks at most, until the invoices are paid. Being a very short term interim source of funds, accounts payable cannot be considered a long term permanent source of financing this investment. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:714-17. ComEd's rate base already accounts for the effects of vendor financing through its cash working capital position. Moreover, Staff witness McNally has proposed reductions to

ComEd's long-term debt and equity balances to account for any third-party CWIP financing. Houtsma Reb., ComEd Ex. 29.0, 43:910-18; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:700-34:723.

As to Mr. Brosch's suggestion that the CWIP could be excluded from rate base and continue to accrue AFUDC, Ms. Houtsma pointed out that this would increase the overall cost of the projects and over time would have the same impact as the current practice. Houtsma Reb., ComEd Ex. 29.0, 43:916-26. Therefore, customers should be economically indifferent as between the two alternatives. *Id.*

For the foregoing reasons, the AG/CUB proposal to disallow the CWIP investment should be overruled.

3. <u>Specific Plant Investments</u>

a. <u>West Loop project repair disallowances</u>

This proposed $4.1 million rate base disallowance, advocated solely by Staff witness Greg Rockrohr, concerns the repair of a 138kV high voltage distribution cable. That work is also referred to as Project ITN 37977. No one contests the necessity of the repair, the manner in which it was carried out, or its costs. Rockrohr, Tr. 857-58. Rather, the theory behind this disallowance is that the cable only failed because of imprudence on the part of ComEd management and, thus, the costs of even a flawless repair should be disallowed. The evidence not only fails to support this claim; it flatly disproves it. The failure of the cable was caused by human error, error of a type that was unprecedented and could not have been anticipated. The evidence shows that human error occurred notwithstanding that ComEd properly selected its contractors, properly supervised the job site, and had policies and practices in place that, had they been followed, would likely have prevented the failure.

The law applicable to this circumstance is clear. Management acts prudently when it makes decisions exercising a

> standard of care which a reasonable person would be expected to exercise under the circumstances encountered by utility management at the time decisions had to be made. In determining whether or not a judgment was prudently made, only those facts available at the time the judgment was exercised can be considered. Hindsight review is impermissible. Imprudence cannot be sustained by substituting one's judgment for that of another. The prudence standard recognizes that reasonable persons can have honest differences of opinion without one or the other necessarily being 'imprudent'.

Illinois Commerce Comm'n v. Commonwealth Edison Co., ICC Docket No. 84-0395 (Final Order, Oct. 7, 1987), at 17. There is no doubt or difference of opinion about this standard. *See, e.g., Illinois Power Co. v. Illinois Commerce Comm'n*, 339 Ill.App.3d 425 (5th Dist. 2003). This same standard is quoted by Staff witness Rockrohr in his testimony and, on the stand, Mr. Rockrohr affirmed the importance of each of its tenets, including that management's conduct need only be within the bounds of reasonability and that management's conduct cannot be judged in hindsight. Rockrohr, Tr. 863:10-865:14.

Moreover, both the Commission and Illinois courts have determined that a utility can act prudently notwithstanding that costs are incurred as a result of "human error." In *Business and Professional People for the Public Interest v. Illinois Commerce Commission,* 279 Ill.App.3d 824, 828, 665 N.E.2d 553, 558 (1st Dist. 1996) ("*BPI")* parties contended that fuel costs resulting from unplanned outages at two of ComEd's nuclear plants were not prudently incurred. The unplanned outages in BPI resulted from human errors, including: (1) a technician who caused a two-day outage by deenergizing the wrong circuit breaker, (2) an employee or contractor who improperly installed a screw, causing a leak that resulted in a 19-day shutdown, and (3) an employee or contractor who installed a defective turbine test switch that caused a two-day outage …." *Id*. In BPI the Commission focused on the propriety of ComEd's hiring and training practices, determined that ComEd had not acted imprudently with respect to the unplanned outages, and explained that it "has consistently maintained that [a utility] cannot be faulted for the human error of its employees unless the evidence shows that [it] failed to adequately hire and train the proper employees." *Id.* at 829. The Appellate Court upheld the Commission's ruling, providing the following reasoning:

> When determining employee management practices, the most efficient management of resources will minimize the sum of (1) the costs of human error, and (2) the costs of preventing human error. The latter includes extra salary to hire more qualified employees, increased training for employees, and additional management personnel for greater oversight. When the sum of costs in (1) and (2) is minimized, the utility will be able to provide its service for the least possible cost to consumers. Thus, a utility at maximum efficiency will still encounter costs from human error.

Id. at 831. The court concluded that "reasonable operating costs should include employee errors which management cannot reasonably prevent," and that one "cannot justify punishing Edison for any mistakes where management has directed matters responsibly." *Id.* at 832.

In short, some human error, even egregious error, is unavoidable. *See* McMahan Reb., ComEd Ex. 33.0, 14:303-4; McMahan Sur., ComEd Ex. 60.0, 7:143-5; Rockrohr, Tr. 858:2-18; BPI, 279 Ill. App. 3d at 833. Mr. Rockrohr would establish a standard of perfection that is untenable. Under the law, however, so long as ComEd's management directed matters responsibly, given what management knew at the time, there is no basis for a disallowance.

What does the evidence show concerning the events that made this repair necessary? The evidence shows that:

- [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

The conclusion from this evidence is clear: "The initial event that sparked this cable failure resulted from human error. The contractors involved were properly qualified and selected, and ComEd had proper procedures and practices in place for constructing and operating such cable. There was no fault in ComEd's practices or in its management. Nothing ComEd did was imprudent." McMahan Reb., ComEd Ex. 33.0, 1:18-22. This conclusion, affirmed by Michael McMahan, ComEd's then Vice President of Engineering and Project Management, is the only possible conclusion that can be drawn from these facts.

Indeed, Mr. Rockrohr did not identify any specific manner in which ComEd managed the installation and activation of the line unreasonably. For example, [redacted]

[redacted] he agrees that differences of professional engineering judgment do not indicate imprudence. Tr. 864:16-865:6. There is no evidence that ComEd did not "direct matters responsibly" and, therefore, no basis for disallowing this repair based upon the cause of the failure. McMahan Rev., ComEd Ex. 33.0, 13-14: 295-302; McMahan Sur., ComEd Ex. 60.0, 3:43-57.

Mr. Rockrohr also contends that, apart from the failure, [redacted]

The evidence is clear:

- [redacted]
- [redacted]
- [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

Under the applicable standard, ComEd's management acted prudently and responsibly. [redacted] Mr. Rockrohr provided no contrary evidence.

For the same reason, Mr. Rockrohr's subjective view [redacted] We <u>only</u> know about this eventuality through hindsight. What is more, Mr. Rockrohr's own suggestions involve additional costs. Yet, there is no evidence that his suggestions are cost effective given that they would need to be deployed universally to prevent a failure that has occurred only once in history. Furthermore, a design like ComEd's is used confidently by numerous specialist engineers across the nation with countless years of experience with just these types of lines. By contrast, Mr. Rockrohr is not a specialist and has *never* been responsible for the design, operation, or maintenance of cables such as the one involved here. Rockrohr, Tr. 850:9-17. His subjective opinion, at best, reflects exactly the kind of "differences of opinion" that cannot sustain a finding of imprudence.

b. <u>Plymouth Court Feeders</u>

ComEd seeks to include $8.96 million in distribution plant investment associated with the Plymouth Court Feeders Project in its revenue requirement. McMahan Dir., ComEd Ex. 9.0 Rev., 15:308-11. 29:539-40, Although Staff witness Elsaid initially questioned the prudence and used and usefulness of the Plymouth Court Feeders Project, following provision of additional detail and explanation in ComEd's rebuttal testimony, Ms. Elsaid concluded that the project was prudent and is used and useful. Elsaid Reb., Staff Ex. 22.0: 3:50-4:82. Thus, this issue appears to be no longer contested.

c. <u>Underground Cable</u>

AG/CUB witness Effron and Staff witness Ebrey propose to reduce ComEd's net rate base by $15.2 million ($18.7 million, gross plant in service) – the entire difference between the 2005-2006 costs incurred and the average unit costs in the 2001-2004 period – because a Staff witness in ICC Docket No. 07-0566 contended that the average unit costs for certain underground cable investments exceeded comparable costs in prior years and that ComEd was unable to provide a satisfactory explanation for that increase. Ebrey Dir., Staff Ex. 1.0, 16:335-

40; Ebrey Reb., Staff Ex. 16.0, 26:534-44; Effron Dir., AG/CUB Ex. 2.0, 9:189-10:215; Effron Reb., AG/CUB Ex. 8.0, 5:105-6:121. Neither Mr. Effron nor Ms. Ebrey contend that the $18.7 million of underground cable costs were imprudently incurred or unreasonable or that the assets are not used and useful in providing service. *Id.* Instead, they seem to premise their arguments on their perception that the Commission intended, in the 07-0566 Order, to make the adjustment permanent.

However, nothing in the Final Order in ICC Docket No. 07-0566 supports the conclusion otherwise escalating costs could never be recovered. Nor could it. ComEd witness Houtsma explained that ComEd disagreed with the adjustment in ICC Docket No. 07-0566 and presented evidence showing that it was unwarranted, but, as part of a stipulation with Staff supported by evidence, agreed not to oppose the adjustment for purposes of that proceeding only. In its Final Order in ICC Docket No. 07-0566, the Commission acknowledged ComEd's factual showing, concluding that "the Company provided justification for the increase in costs". *Commonwealth Edison Co.*, ICC Dkt. No. 07-0566, Final Order (Sept. 10, 2008) at 46. Nothing in the Final Order in Docket No. 07-0566 provided or suggested that the $18.7 million of underground cable costs would be excluded from ComEd's rate base in future proceedings. The adjustment was premised entirely on arguments about the sufficiency of the evidentiary showing in that case. *See also* Houtsma Reb., ComEd Ex 29.0, 11:211-12-251; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 32:680-99.

The new evidence here shows that the $18.7 million – the difference between the 2005-2006 costs incurred and the average unit costs in the 2001-2004 period – is fully attributable to a change in capitalization policy with respect to underground cable fault repairs. This change, which occurred in 2004, resulted in the capitalization of certain costs to Account 366 that had been recorded as expense in the prior years. This accounting change accounts for the seeming "increase" in capitalized underground cable costs. Houtsma Reb., ComEd Ex. 29.0, 12:232-51. As shown on ComEd Ex. 29.4, absent the effect of the change in capitalization policy, the 2005-2006 average unit costs are *lower* than the 2001-2004 inflation adjusted costs. In other words, costs did not increase at all, much less in an unexplained way. Because no cost increase actually occurred, and because the alleged "failure" to explain such increase was the sole basis for the argument in ICC Docket No. 07-0566 that an adjustment to rate base was appropriate, no basis exists for any disallowance in this proceeding of the admittedly prudent investment in unquestionably used and useful assets. Houtsma Reb., ComEd Ex. 29.0, 11:211-12-251; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 32:680-99.

The propriety of this change in capitalization policy was being reviewed by the Commission in Docket No. 08-0312 at the time the Commission entered its Order in Docket No. 07-0566. Houtsma Reb., ComEd Ex. 29.0, 12:245-47. The Commission's conclusions concerning that accounting change was not known at the time of the September 2008 Order in Docket No. 07-0566, and thus could not have been considered in that case. However, the Commission's final Order in Docket No. 08-0312, was issued January 12, 2010, and it that case contained no criticism whatsoever of the relevant change in ComEd's accounting policy. That Commission order should be considered and given full effect in this case. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 32:688-94. The only proper outcome would be for the Commission to permit ComEd to restore the disputed $18.7 million of ComEd's gross plant in service.

Finally, ComEd underscores the importance of this issue to ComEd as compared to the more modest significance to customers. As noted by all parties, the revenue and rate significance of this disallowance is small – about $2 million. But, persisting is denying ComEd all right to recover this costs will require a continued write-off by ComEd of these nearly $19 million in assets. This fact simply underscores the unjust nature of making permanent a disallowance that always was based on nothing more than *questions* about assets that have now been amply answered.

d. **PORCB Costs**

ComEd joins ICEA and Dominion Retail in requesting that the Commission determine in this docket the appropriate allocation of costs related to ComEd's implementation of its purchase of receivables with consolidated billing ("PORCB") project between this case and ComEd's Rider PORCB.

By way of background, at the time ComEd filed this case on June 30, 2010, the approval of ComEd's Rider PORCB was pending in ICC Docket No. 10-0138. Because Rider PORCB was not yet approved, ComEd included the costs associated with implementing PORCB in both this case and in the Rider PORCB docket, and supported the prudence and reasonableness of the costs and the used and useful status in this case. ComEd explained that if the Commission approved the proposed Rider PORCB and permitted ComEd to recover its costs through the rider, ComEd would remove the PORCB amounts from rate base for purposes of determining the revenue requirement in this proceeding. During the course of the PORCB docket, however, certain parties raised questions about whether the PORCB amounts were solely related to the PORCB program or whether a certain portion of those amounts should be allocated to base rates. As Staff witness Ebrey explained, the allocation issue "was never fully vetted due to the time constraints in [the PORCB] case." Ebrey Reb., Staff Ex. 16.0, 31:653-57.

Because the same parties who raised these questions in the PORCB docket are also intervenors in this docket, the pendency of this case provided them with ample time to undertake extensive discovery regarding the PORCB costs and their appropriate allocation. Consistent with the PORCB statute's requirement that the discount rate applicable to the purchased receivables include "any reasonable start-up costs and administrative costs associated with the electric utility's purchase of receivables" (220 ILCS 5/16-118(c)), ComEd's position during the PORCB docket and this case has been that the costs in question would not have been incurred absent the PORCB program, and are therefore appropriately allocated to PORCB as "costs associated with [the] purchase of receivables."

However, as ComEd witness Mr. Fidel Marquez notes, "[t]he appropriate allocation of these costs to some extent is a matter of perspective, where reasonable people may have reasonable differences of opinion …." Marquez Sur., ComEd Ex. 61.0 Rev., 7:154-56. Mr. Marquez explains that the most obvious examples of this difference of opinion are the PORCB Customer Data Warehouse ("CDW") and Retail Office (market settlement system) costs, which total approximately $6.8 million out of the $14.0 million of jurisdictional capital costs (see ComEd Ex. 56.7 for specific figures):

> These costs represent costs largely required to accommodate the higher level of customer switching and shopping that can be expected in a market with PORCB service available. That is, while these enhanced functions are not required as such to effectuate the purchase of receivables and place associated RES supply charges on customers' bills, they are a result of the obligation to provide PORCB service and they are required as a practical matter to achieve the customer choice objectives of the mandate of PORCB service.

Marquez Sur., ComEd Ex. 61.0 Rev., 9:192-98. Because the most appropriate allocation of these costs is, admittedly, not beyond dispute, Mr. Marquez testifies that, in an effort to narrow the issues in this case, ComEd could largely accept ICEA witness Mr. Fein's position – it would not be inconsistent with ComEd's prior treatment of costs incurred for the provision of customer choice to recover the PORCB CDW and Retail Office costs through base rates, while recovering the remainder of the costs through the PORCB cost recovery mechanism. *Id.*, 7:163 – 8:187.

Indeed, the decision of how best to allocate the costs to replace existing systems to accommodate the anticipated increased switching caused by PORCB will hinge on how broadly or narrowly the Commission interprets the phrase "associated with" in Section 16-118(c).

To the extent the Commission finds certain of these costs should be recovered through base rates, ComEd witness Mr. Marquez demonstrates that the PORCB project, which was mandated by Section 16-118 of the Act, is prudent, its costs are reasonable, and it is used and useful. Marquez Dir., ComEd Ex. 10.0, 3:59-60, 27:543 – 29:583; Marquez Reb., ComEd Ex. 26.0 Rev., 2:39-41, 18:408 – 20:454; Marquez Sur., ComEd Ex. 61.0, 2:31-32, 3:61 – 6:139. With the exception of Dominion Retail, whose arguments were rejected by the Commission in the PORCB docket, as noted below no Staff or intervenor witness challenged the prudence or reasonableness of the PORCB project costs. Indeed, even Dominion witness Mr. Crist admits that "[t]he tasks described should have been undertaken regardless of POR implementation." Crist Reb., Dominion Ex. 3.0, 7:95, 102-03, 109-110, 8:115-16.

With respect to Dominion's claims to socialize all costs and cap cost recovery at $2 million, the Commission has already rejected these arguments in the PORCB Order. The Commission should again do so here. Commonwealth Edison Co., ICC Dkt. No. 10-0138, Final Order (Dec. 15, 2010), at 27, 29 ("PORCB Order") ("[W]e find Dominion's arguments to be without merit and decline to require 'socialization' of PORCB costs." "[W]e decline to require ComEd to explain why its costs exceed those of PECO. PECO is a different company with different expenditures in a different service territory.") Because Dominion has proffered no new evidence in support of these arguments, the Commission should, consistent with its recent PORCB Order, reject these arguments.

Staff alone proposes that the allocation issue not be decided here. All other interested parties, including ComEd, hold the position that the allocation issue should be decided in this docket so that ComEd, RESs and retail customers have certainty that the costs being flowed through Rider PORCB during the three-year First Application Period are properly allocable to PORCB. Only Staff proposes that the Commission delay a decision on this issue until the first Rider PORCB reconciliation proceeding, which will not even begin until 2014. ComEd joins ICEA's and Dominion's opposition to Staff's proposed delay because it would create uncertainty regarding both the rates RESs and retail customers pay during this first three-year period and ComEd's ability to recover any costs later deemed to have been improperly allocated to PORCB. Marquez Reb., ComEd Ex. 36.0 Rev., 5:114-16; Marquez Sur., ComEd Ex. 61.0, 10:224-28. The Commission should determine the appropriate allocation of PORCB costs in this docket, all of which were shown to be prudently incurred, reasonable in amount, and used and useful. If the alternative proposal advanced by Mr. Marquez is approved, then the CDW and Retail Office costs should be included in rate base.

e. **<u>Allocation of G & I Plant</u>**

The Commission should approve the inclusion in rate base of $1,419,780,000 of General and Intangible ("G&I Plant") that supports the delivery services (distribution and customer service) ("DST") functions. ComEd Ex. 55.1, Sched. B-1, p. 1, line 3 (gross plant amount, consisting of $1,280,718,000 of test year plant, and $139,106,000 of pro forma capital additions. G&I plant includes costs that are diverse in nature and support one or more business functions, including telecommunications equipment, land and office buildings, office furniture, transportation equipment, and computer systems. Houtsma Dir., ComEd Ex. 6.0 Rev., 21:430-432, 23:472-24:485. The Uniform System of Accounts does not record G&I Plant costs by function, so they must be functionalized. The Commission should approve ComEd's functionalization of its G&I plant both for purposes of calculating ComEd's rate base and of determining rate design (discussed in Section VII.C.1.f, infra).

ComEd has included in rate base the costs recorded in G&I Plant Accounts that support the provision of distribution and customer service. Houtsma Dir., ComEd Ex. 6.0 Rev., 21:430-435, 22:447-458, 23:461-465; ComEd Ex. 6.1, Sched. B-1, p. 1, lines 3, 7, and p. 2, lines 3, 7. ComEd's direct case provided detailed information regarding how G&I Plant had been functionalized between the DST and non-DST functions. Houtsma Dir., ComEd Ex. 6.0 Rev., 23:470 – 26:509; ComEd Ex. 6.1, Sched. A-5; ComEd Ex. 6.2, WPA-5 and WPB-1. ComEd directly assigned the largest G&I Plant Account, Account 397 – Communication Equipment, using the same direct assignment study methodology that was approved for this Account in ComEd's 2007 rate case. Houtsma Dir., ComEd Ex. 6.0 Rev., 24:486-489. ComEd functionalized the remaining G&I Plant Accounts using the general labor allocator (also called the "GLA" or the "Wages & Salaries" or "W&S" allocator), rather than using the mix of the general labor allocator and other methods approved in its 2007 rate case, because that simplified approach results in better alignment with ComEd's Transmission Formula Rate, thereby avoiding over- or under-recovery of G&I plant costs. Houtsma Dir., ComEd Ex. 6.0 Rev., 24:486-500. Staff and intervenors, in their "revenue requirement" direct testimony, did not contest ComEd's functionalization of G&I plant.

However, Staff's "rate design" direct testimony addressing ComEd's Embedded Cost of Service Study questioned the use of the general labor allocator to functionalize the Accounts for which it was not used in ComEd's 2007 rate case. Further, Staff stated that its "revenue requirement" rebuttal testimony would propose a related adjustment to rate base. Rukosuev Dir., Staff Ex. 12.0, 8:166 – 18:400. Staff's subsequent testimony did so, proposing a $15,693,000 reduction in gross plant. Ebrey Reb., Staff Ex. 16.0, 33:710-714, Sched. 16.04, p. 1, line 1, column (f), and Sched. 16.12, line 3, column (b); *see also* Rukosuev Dir., Staff Ex. 28.0, Att. A.

Staff witness Mr. Rukosuev asserts that ComEd failed to present any compelling reason ComEd should not continue to use the same methodologies previously used to allocate certain G&I plant. Rukosuev Dir., Staff Ex. 12.0, 11:230-233. Mr. Rukosuev's position lacks merit.

First, Mr. Rukosuev dismisses out of hand Ms. Houtsma's testimony about how use of a general labor allocator better aligns the allocation of costs between FERC and the ICC on the basis that "the objective for cost allocation should be cost causation principles, not achieving consistency with the functionalization of transmission costs." Rukosuev Dir., Staff Ex. 12.0, 10:216-218. Mr. Rukosuev simply disregards Ms. Houtsma's testimony that by this change "ComEd will not over (or under) recover its associated General and Intangible Plant costs in either jurisdiction." This is a statement about consistently identifying cost causation between the two jurisdictions, not simply a statement about "overlaps or gaps", as Mr. Rukosuev implies. *See* Rukosuev Dir., Staff Ex. 12.0, 10:214-11:226.

Second, ComEd's use of the general labor allocator to allocate the costs in G&I Plant Accounts other than Account 397 has caused the costs to be recovered through ComEd's distribution rates to be approximately the same overall as under the prior methodologies used by ComEd. As shown on Staff's Revised Response to ComEd's Data Request ComEd-Staff 15.01 (ComEd Cross Ex. 14); *see also* Rukosuev Dir., Staff Ex. 28.0, Att. A), if the previous methods for functionalizing General and Intangible plant had been used, then jurisdictional test year General and Intangible plant would have been only about 1.2% lower than the $1,280,718,000 (gross plant amount) requested in this proceeding. Thus, the simplified methodology is not biased towards assigning more costs to distribution service in this case. This is hardly surprising because, as Mr. Rukosuev acknowledges, in most instances the change that was made was from the use of one general allocator (e.g., a plant related general allocation factor) to another general allocation factor – the general labor allocator. Rukosuev, Staff Ex. 12.0, 15:339-343.

Accordingly, the Commission should approve ComEd's allocation of G&I Plant, both for purposes of revenue requirement and rate design.

4. Cash Working Capital

ComEd's cash working capital ("CWC") requirement at the surrebuttal stage is $67,741,000 (ComEd Ex. 55.1, Sched. B-1 Revised, p. 1, line 9; Subbakrishna Sur., ComEd Ex. 57.0, 2:26-29) and should be approved for inclusion in rate base by the Commission. Cash working capital represents the funds required to finance the day-to-day operations of the utility business and, as contemplated by the ICC's rules (Ill. Admin. Code 285.2070), may be included in rate base. Subbakrishna Dir., ComEd Ex. 7.0 Rev., 3:53-56. These funds are included in rate base because they are a capital cost incurred by the utility in order to provide service to customers. *Id.*, 3:57-58.

The lead/lag study that supports this amount was prepared by, and is amply supported by the testimony of, independent expert Nagendra Subbakrishna (ComEd Exs. 7.0 Rev., 7.1, 31.0, 31.1, 31.2, 31.3, 31.4, 57.0, 57.1, 57.2, 57.3). ComEd's CWC figure of $67,741,000 correctly reflects the rebuttal and surrebuttal updates by ComEd witnesses Houtsma and Martin Fruehe to test-year revenue and expense amounts, and reflects, in order to narrow the issues, Staff's proposed collections lag of 36.32 days rather than ComEd's originally filed figure of 39.16 days. Subbakrishna Reb., ComEd Ex. 31.0, 2:36-40, Subbakrishna Sur., ComEd Ex. 57.0, 2:29-33, 3:63-4:70, 8:156-59.

Staff also advances other changes in ComEd's lead/lag study and, in its rebuttal testimony, proposed a CWC amount of $75,774,000. Ebrey Reb., Staff Ex. 16.0, Sched. 16.03, line 10. (Staff's figure does not reflect ComEd's surrebuttal updates.) AG/CUB proposes zero CWC (AG/CUB Ex. 7.1, Sched. B, p. 1, line 6), but that position is arbitrary, inconsistent, and lacks any valid basis, as discussed below.

Staff's witness on this subject, Ms. Bonita Pearce, advocates changes in two other areas of ComEd's lead/lag study (Pearce Reb., Staff Ex. 18.0, 27:640-36:846), but these proposed changes are incorrect and should not be approved. Her proposal to reduce the expense lead for inter-company billings is arbitrary and does not match the reality of when ComEd pays these expenses, as reflected in ComEd's lead/lag study. Subbakrishna Sur., ComEd Ex. 57.0, 2:40 – 3:54, 13:252 – 14:276; Subbakrishna Reb., ComEd Ex. 31.0, 3:59-65, 13:279 – 15:316. Her proposal to change the revenue lags and expense leads for certain taxes also does not match the reality of when these amounts are required to be and are paid by ComEd to the taxing authorities versus when they are collected from customers, also reflected in ComEd's lead/lag study. Subbakrishna Sur., ComEd Ex. 57.0, 3:55-62, 14:279 – 17:341; Subbakrishna Reb., ComEd Ex. 31.0, 3:66-73, 15:319 – 20:411

AG/CUB witness Mr. Brosch proposes that ComEd be allowed zero CWC in rate base (e.g., Brosch Reb., AG/CUB Ex. 7.0, 12:275 – 13:280; Brosch Tr., 1525:11-17), but his position is arbitrary, inconsistent, and lacks any valid basis. He has never prepared a lead/lag study. *Id.* at 1526:8-18. His criticism of ComEd's calculation of its revenue collections lag theorizes that using the mid-point of groups of accounts receivables is unreliable, and that very old receivables should not be used (e.g., Brosch Reb., AG/CUB Ex. 7.0, 11:254-15:336, 19:424-20:439). However, he did not analyze the collections lag or cash working capital results of the 2009 North

Shore and Peoples Gas rate cases, the 2009 Ameren Illinois rate case, or the 2008 Nicor Gas rate case. Brosch Tr. at 1526:19 – 1527:10. In each of those cases, the Commission approved a collections lag methodology using midpoints similar to those in ComEd's presentation. Subbakrishna Reb., ComEd Ex. 31.0, 2:30-34, 3:52-58, 8:169-9:179 and fn. 1; Subbakrishna Sur., ComEd Ex. 57.0, 6:131-137 and fn. 10, 7:145-8:154. Mr. Brosch did quote the final Order in the 2009 Ameren rate case, mentioning in a footnote the Order on Rehearing, but he omitted the fact that the Order on Rehearing approved a cash working capital amount for Ameren that was, in part, the result of use of the mid-point methodology to calculate the revenue lag. *See* Brosch Reb., AG/CUB Ex. 7.0, 16:342-363 and fn. 12; Subbakrishna Tr., 1148:14 – 1150:11. Mr. Brosch also omitted the fact that the lead lag study applies a midpoint methodology to expenses as well as revenues. Subbakrishna Reb., ComEd Ex. 31.0, 9:179-185.

Mr. Subbakrishna's testimony explained in detail that Mr. Brosch's criticisms of ComEd's lead/lag study on the collections lag and other components, including pensions/OPEB and severance lags and leads, were arbitrary, inconsistent and incorrect, and that most of the assumptions in the study that Mr. Brosch criticized were "conservative" in the sense that they reduced, not increased, ComEd's CWC calculation. Subbakrishna Sur., ComEd Ex. 57.0, 4:71 – 5:103, 8:164 – 11:216; Subbakrishna Reb., ComEd Ex. 31.0, 3:52-58, 4:78-88, 8:156 – 13:277, 21:424 – 25:520.

Finally, and further illustrating the misleading nature of Mr. Brosch's criticisms, Mr. Subbakrishna presented a revenue collections lag calculation that did not use the mid-point methodology or any of the other collections lag assumptions criticized by Mr. Brosch. This calculation resulted in a large increase in the revenue collections lag figure. Subbakrishna Sur., ComEd Ex. 57.0, 8-164 – 9:181; ComEd Ex. 57.2. To address Mr. Brosch's criticism of inclusion of aged receivables in the collections lag, Mr. Subbakrishna also presented a calculation of the collections lag which recognized the fact that, if the aged receivables become uncollectible, then they should be assigned an even longer collection lag. Subbakrishna Sur., ComEd Ex. 57.0, 11:217-12:233. Again, the result would be a very large increase in the collections lag figure, and the resulting CWC allowance.

ComEd's cash working capital figure of $67,741,000 is amply supported by the record and should be approved.

5. <u>2009 Pension Trust Contribution</u>

ComEd seeks to include the $92.5 million jurisdictional rate base effect of its 2009 pension trust contribution in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev., 28:559-61. AG/CUB witness Effron proposes to disallow the entirety of this amount, and Staff witness Pearce proposes to disallow recovery of a significant portion of the costs based on a novel and unsupported limitation. Pearce Reb., Staff Ex. 18.0, 6:136-38; Effron Dir., AG/CUB Ex. 2.0, 15:337-38; Effron Reb., AG/CUB Ex. 8.0, 9:200. The defined benefit pension plan covering ComEd employees (as well as those of other Exelon affiliates) became significantly underfunded due to the stock market crash in 2008 and persistent low interest rates. As a result, by December 31, 2008, before the contribution was made, the plan was approximately 40% underfunded. Houtsma Reb., ComEd Ex. 29.0, 17:346-50, 19:387-89. To mitigate this significant increase in the unfunded status of the plan, ComEd made an additional $152 million contribution to the plan in 2009. *Id.*, at 21:442-44. ComEd's rate filing includes in rate base the $92.5 million jurisdictional rate base effect resulting from this contribution. Houtsma Dir., ComEd Ex. 6.0 Rev., 28:559-71, 29:583-85.

In its direct case, Staff opposed inclusion of the $92.5 million jurisdictional rate base effect of ComEd's pension contribution, contending in part that the contribution was discretionary and that ComEd should have limited its contributions to the minimum pension funding amount required by law. Pearce Dir., Staff Ex. 3.0 Rev. Public, 3:77-4:84. In rebuttal testimony, however, Ms. Pearce revised her position, agreeing that the 2009 pension contribution was a prudent response to the decline in pension fund assets. Pearce Reb., Staff Ex. 18.0, 7:160-68. Nonetheless, Ms. Pearce continued to contend that the jurisdictional rate base effect of the contribution should be removed from rate base, and maintained that ComEd would be adequately compensated if it received a return on this investment equal to the amount by which the jurisdictional portion of pension *expense* is reduced because of this contribution. *Id.*, 8:190-92. However, limiting the recoverable costs to the amount by which pension expense is immediately lowered results in a $1.4 million reduction in the revenue requirement, a disallowance of about 17% of the revenue requirement associated with the $92 million contribution. *See* Ebrey Reb., Staff Ex. 16.0, Sched. 16.05 (underlying data).

Staff's position cannot be reconciled with applicable cost recovery principles. Staff conceded and agreed that it was proper to make the contribution, as both Ms. Houtsma and Dr. Susan Tierney testified in rebuttal to Staff's initial position. Houtsma Reb., ComEd Ex. 29.0, 17:340-54; Tierney Reb., ComEd Ex. 39.0, 19:412-21:440. In addition, the rebuttal testimony of Dean Apple, President of the International Brotherhood of Electrical Workers ("IBEW") Local 15, which represents 3,800 ComEd employees and 5,638 retirees whose pension benefits and retirement security depend on the pension fund, strongly supports ComEd's decision to address the increase in the unfunded status of the plan. Apple Reb., ComEd Ex. 27.0, 3:53-4:82. The contribution being prudent, Staff cannot justify providing to ComEd anything less than full recovery of its costs incurred in making this contribution. Capping cost recovery at the level of customer benefit (the amount of the reduced pension *expense*) bears no relationship to the economic cost incurred by ComEd in making the contribution, and improperly denies ComEd cost recovery. Furthermore, providing less than full cost recovery would create a perverse incentive to the utility, encouraging it to divert its finite capital resources to other investments that would produce a full return, thereby undermining the goal of adequate pension funding (Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 17:344-55), a goal Staff conceded is appropriate and that is established in federal law as a result of the Pension Protection Act of 2006. Accordingly Staff's proposed disallowance should be rejected.

AG/CUB witness Effron contends that ComEd should be denied recovery of the cost of the $92.5 million jurisdictional pension contribution, not because the underfunding should have been allowed to continue, but because he believes that it could have been addressed in prior years with larger contributions in 2006 through 2008. Effron Dir., AG/CUB Ex. 2.0, 15:335-38; Effron Reb., AG/CUB Ex. 8.0, 9:184-87. In effect, Mr. Effron would simply penalize ComEd for not doing sooner what it did in 2009, even though he made no suggestion customers would be better off. Ms. Houtsma explains, first, that the investment losses that gave rise to the 2009 contribution did not occur until 2008 and that it was thus unnecessary to have made any additional contributions in prior years. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 19:390-410. Second, Ms. Houtsma explains that even if the contributions had been greater in 2006-2008, the balance of the jurisdictional rate base effect of the pension contribution would have been greater in those years but substantially the same at year end 2009 as it now is, and the impact on ComEd's rate base would have been roughly the same. Houtsma Reb., ComEd Ex. 29.0, 25:514-24; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 20:411-28.

For all of these reasons the $92.5 million jurisdictional amount of the 2009 contribution should be allowed in ComEd's rate base, so that ComEd can recover its costs associated with that investment (in this case, the weighted average cost of capital), as it does on all other prudent investments. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 20:431-32.

6. Capitalized Incentive Compensation

Staff and AG/CUB propose disallowances of capitalized incentive compensation. The issues presented by these proposed disallowances are addressed in connection with the discussion of incentive compensation expense in Section V. C. 1.

7. Customer Deposits

ComEd believes it is appropriate to reduce its rate base by $44,705,000 in customer deposits. Houtsma Dir., ComEd Ex. 6.0 Rev., 33:663-65; ComEd Ex. 6.1, Sched. B-1, p.1 line18. AG/CUB witness Brosch and Staff witness Tolsdorf seek to increase this amount and reduce rate base by $130,510,000 in customer deposits. AG/CUB Ex. 7.1, Sched. B-8; Tolsdorf Reb., Staff Ex. 19.0, Sched. 19.02. Customer deposits, which are accounted for as a reduction to rate base, are generally based on the entire amount of customers' expected total bill for service – including charges for energy or supply. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 26:545-48. Two disputed issues arise in connection with customer deposits: (1) whether an average balance or year-end balance should be used to calculate the amount of customer deposits reflected in the rate base calculation; and (2) whether all customer deposits or only delivery related customer deposits should be accounted for in that calculation. The parties agree that interest payable to customers should be offset against customer deposits otherwise considered in establishing rate base.

First, as ComEd witness Houtsma testified, the use of an average, rather than a year end, balance is appropriate because it smoothes out seasonal variations, providing a more accurate reflection of customer deposit amounts. Houtsma Reb., ComEd Ex. 29.0, 37:786-95. Both AG/CUB witness Brosch and Staff witness Tolsdorf contend, however, that ComEd's customer deposits should be determined using a year-end, rather than an average balance. Brosch Dir., AG/CUB Ex 1.0, 37:814-19, Brosch Reb., AG/CUB Ex 7.0, 31:673-84; Tolsdorf Reb., Staff Ex. 19.0, 4:77-5:99. They believe that over the past three years customer deposit balances have trended upwards and use of a year-end figure "would be more representative of ongoing levels." *Id.* Mr. Tolsdorf also presumes that new business will be accompanied by increased customer deposits. Tolsdorf Reb., Staff Ex. 19.0, 5:93-99.

No party has presented any evidence showing that the three year "increasing trend" posited by Messrs. Brosch and Tolsdorf is likely to continue in the future, and it is therefore not appropriate for the Commission to use a year-end balance, particularly when the Commission has 12 (or 13 as Staff initially proposed) months of test year data that the Commission can utilize to set an appropriate level of customer deposits. Likewise, the record contains no evidence that new business will be accompanied by increased customer deposits. Further, Mr. Tolsdorf's use of a year-end balance cannot be reconciled with his recommendation to use an average balance for materials and supplies inventories. *See* Tolsdorf Dir., Staff Ex. 4.0, 2:45-3:49.

Second, ComEd has reduced its delivery services rate base by those customer deposits related to delivery services. Houtsma Dir., ComEd Ex. 6.0 Rev., 33:663-65. Both Messrs. Brosch and Tolsdorf contend that total customer deposit balances should be included in this rate base reduction, as opposed to just delivery related jurisdictional amounts. Brosch Dir., AG/CUB Ex. 1.0, 37:805-39:855; Brosch Reb., AG/CUB Ex 7.0, 29:634-30:672; Tolsdorf Reb., Staff Ex.

19.0, 5:100-12. They rely on the fact that ComEd has not specifically assigned the balance of customer deposits to another jurisdiction, namely transmission, and they therefore conclude that the total amount should be assigned to the delivery jurisdiction. *Id.*

This logic is flawed. Both Brosch and Tolsdorf contend that rate base component for customer deposits should include not only deposits for delivery services, but deposits based on supply and transmission as well. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 26:545-48. Whether or not the calculation of that rate by FERC expressly includes a rate base adjustment for customer deposits is not determinative of the appropriate treatment in this proceeding. *Id.*, 27:577-79. They also ignore that FERC is required to set an overall transmission rate that is just and reasonable. While FERC ratemaking may employ different measurement approaches, the ICC may not lawfully go behind FERC's determination and assume that some portion of transmission costs (or credits) have not been properly reflected in that rate and, therefore, should be included as an adjustment to the distribution rate. This is a distribution rate case, the outcome of which should not – and, legally, cannot – be affected by the inclusion of non-jurisdictional supply, or transmission, related amounts. Houtsma Reb., ComEd Ex. 29.0, 37:776-38:814; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 25:529-27:582.

In essence, AG/CUB witness Mr. Brosch and Staff witness Mr. Tolsdorf seek to treat the delivery services rate as a residual or catch-all rate for revenue or cost components not assigned or collected elsewhere. It is no more appropriate to do this than to reflect non-jurisdictional plant in ComEd's delivery services rate base because it is not recoverable elsewhere. Houtsma Reb., ComEd Ex. 29.0. 37:796-38:806; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 27:569-82. This logic is identical to that supporting the allocation of late payment charges, discussed in the Revenues section of this brief. In that instance, Staff agrees that it would be inappropriate to attribute to delivery all late payment charges not assigned to transmission, and the Commission should reach the same result here. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 26:545-57.

Third, AG/CUB, Staff, and ComEd agree that accrued interest on customer deposits must be considered by the Commission. Houtsma Reb., ComEd Ex. 29.0, 37:781-785; Brosch Dir., AG/CUB Ex 1.0, 39:863-69; Brosch Reb., AG/CUB Ex 7.0, 31:685-91; Tolsdorf Reb., Staff Ex. 19.0, 6:116-21. AG/CUB and Staff support an annual interest accrual included in operating expense. ComEd also supports that methodology and alternatively supports a reduction in the customer deposit balance. Houtsma, ComEd Ex. 29.0, 37:781-785.

8. Material and Supplies Inventories

ComEd seeks to include $26,586,000 in Material and Supplies Inventories in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev., 28:550-57; ComEd Ex. 6.1, Sched.B-1, l.11. Staff witness Mr. Tolsdorf proposes to disallow $3,265,000 of this amount. Tolsdorf Reb., Staff Ex. 19.0, 3:47-54, Sched. 19.01. He proposes that a thirteen month average balance be used for materials and supplies inventories, and recommends that the balance be reduced by the related accounts payable. Tolsdorf Dir., Staff Ex. 4.0, 2:45-3:50. These disallowances should be rejected. Ms. Houtsma testified that Staff failed to show any abnormal variations in balances that would call for an averaging approach. Further, accounts payable balances relating to inventories are simply a form of cash working capital, which is measured through the lead-lag study, making a further disallowance in this area unnecessary and duplicative. Houtsma Reb., ComEd Ex. 29.0, 42:883-95; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 30:640-32:679. Ms. Houtsma's surrebuttal testimony explains that, if Mr. Tolsdorf's proposal to reduce Materials and Supplies inventory balances for accounts payable were to be accepted, consistency would require that the $4.9 million thirteen month average of accounts payable (rather than the $12.4 million estimate proposed by Mr. Tolsdorf) be used. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 31:666-32:679.

9. Severance Cost - Regulatory Debit

This issue has been discussed under “V.C.3.h. – Severance Expenses.”.

D. Rate Base (Total)

ComEd’s total rate base is $ 7,349,227,000. Houtsma Sur., ComEd Ex. 55.1, Sched. A-4-Rev.

V. OPERATING EXPENSES

A. Overview

ComEd Chief Financial Officer Joseph Trpik testified that ComEd has significant increased costs attributable to investment in plant ($116 million revenue impact), depreciation expense ($63 million), pension and retiree health care costs ($55 million), bad debt expense ($22 million), cost of capital ($95 million), and other items. Trpik Dir., ComEd Ex. 4.0 Rev., 4:68-76; Trpik Sur., ComEd Ex. 54.0, 2:19-3:60. He explained that, despite the major cost reduction efforts ComEd has undertaken, which actually *decreased* operating expenses before *pro forma* adjustments (other than pension and retiree health care) by $10 million when compared to the amount allowed in ComEd’s last rate proceeding, ComEd has incurred many additional cost increases that are beyond its control. *Id.*, 4:72-6; *see also* Guerra Dir., ComEd Ex. 1.0 2nd Rev., 3:53-6, 6:122-32 (ComEd’s aggressive cost cutting reduced expenses by $85 million between 2008 and 2009). This section identifies the issues that have been raised by Staff and Intervenors concerning ComEd’s operating expenses.

B. Potentially Uncontested Issues

1. 2009 Amortization Adjustment of Existing Regulatory Assets (Staff)

ComEd accepted the proposal by Staff witness Hathhorn to reduce the unamortized balances of six regulatory assets to their May 2011 levels to be recovered over a three-year period. Fruehe Reb., ComEd Ex. 30.0 Public, 7:131-41. This reduces ComEd's revenue requirement by $8.387 million. ComEd Ex. 30.1, Sched. C-26 Rev.

2. Outside Professional Services – Jacobs Consultancy (Staff)

ComEd has accepted the proposal by Staff witness Tolsdorf to remove the jurisdictional portion ($200,000) of costs related to Jacobs Consultancy from the revenue requirement. Fruehe Reb., ComEd Ex. 30.0 Public, 10:197-205.

3. Advertising Expense (Staff)

ComEd has accepted the proposal by Staff witness Tolsdorf to remove $51,538 of advertising expenses from the revenue requirement. Fruehe Reb., ComEd Ex. 30.0 Public., 10:206-11.

4. Investment Tax Credit Amortization (AG)

ComEd has agreed to the proposal by AG/CUB witness Effron to reduce income tax by $113,000 by including the amortization of proceeds from the sale of investment tax credits in ComEd's income tax expense. Fruehe Reb., ComEd Ex. 30.0 Public, 13:262-68.

C. Potentially Contested Issues

1. Incentive Compensation Cost and Expenses

ComEd seeks to include a total of $27.562 million of incentive compensation costs in its jurisdictional operating expenses, broken down as follows: $23.281 million for Annual Incentive Program ("AIP") expense, $2.158 million for Long-Term Incentive Plan ("LTIP") expense, and

$2.123 million for Exelon 2009 Key Manager Restricted Stock Award. Smith Dir., AG/CUB Ex. 3.0 Corr., 10:217-21; AG/CUB Ex. 3.2 PUBLIC, pp.2-5 (ComEd's Response to Staff Data Request BAP 2.03 Corrected). AG/CUB witness Smith proposes to disallow 50% of ComEd's 2009 AIP expense. Smith Dir., AG/CUB Ex. 3.0 Corr., 16:313-17:324. Staff recommends a disallowance of about $2.7 million of the LTIP costs and AG/CUB witness Smith seeks to disallow any LTIP cost recovery. Trpik Sur., ComEd Ex. 54.0, 6:109-11; Smith Dir., AG/CUB Ex. 3.0 Corr., 22:448-54. Both Staff and AG/CUB seek to disallow 100% of the costs of the Exelon 2009 Key Manager Restricted Stock Award. *Id.*, 25:538-45; Pearce Dir., Staff Ex. 3.0 Rev., 33:787-92.

ComEd sets employee compensation at levels necessary to remain competitive in the marketplace. The total compensation ComEd pays its employees is the amount needed to attract and retain qualified personnel. ComEd uses a "pay at risk" approach under which all employees are at risk of receiving less than competitive compensation if plan goals are not attained. Trpik Dir., ComEd Ex. 4.0 Rev., 24:449-64; Trpik Reb., ComEd Ex. 28.0, 1:17-3:58.

ComEd has two basic incentive compensation programs: the Annual Incentive Program ("AIP") and the Long-Term Incentive Program ("LTIP"). One of the issues the Commission has had with ComEd's incentive plans in prior cases has been that some of the plan "metrics" are thought to primarily benefit shareholders, not customers. Mindful of those issues, ComEd has revised its plans to accommodate those concerns. The terms of both the AIP and the LTIP have been established specifically to comply with the Commission's standards for incentive compensation cost recovery as set forth most recently in the Order in Docket No. 07-0566. For the 2009 test year, ComEd revised the AIP to eliminate the net income metric that the Commission disapproved in Docket No. 07-0566, and, therefore, all of the costs incurred under the AIP during the 2009 test year are attributable to meeting operational goals of the type approved by the Commission in that case. Similarly, ComEd addressed the concerns identified in Docket No. 07-0566 with the LTIP metrics by eliminating the net income and legislative / regulatory goals from the plan for 2010, thereby insuring that all LTIP costs ComEd will incur in the future meet the Commission's cost recovery standards. Trpik Dir., ComEd Ex. 4.0 Rev., 24:448-27:530.

The importance of assuring cost recovery for incentive compensation expense is underscored by the testimony of Dean Apple, President of IBEW Local 15, who explains that ComEd employees represented by IBEW rely on incentive compensation as part of their pay and proposals to disallow recovery of those costs threaten the interests of IBEW employees in this component of their compensation. As Mr. Apple testifies, if ComEd sought to discontinue portions of the IBEW incentive compensation package to address disallowances proposed by Staff, AG and CUB, employees would essentially be taking a pay cut, causing further harm to the Illinois workforce. Apple Reb., ComEd Ex. 27.0, 6:113-29.

AG/CUB witness Smith proposes to disallow 50% of ComEd's 2009 AIP expense because of ComEd's extraordinary 2010 cost reduction efforts. Smith Dir., AG/CUB Ex. 3.0 Corr., 16:311-24. This disallowance is inappropriate because the extraordinary one-time limitations ComEd imposed on the 2010 incentive compensation plan were intended to reduce expenses below the reasonable levels reflected in the 2009 test year. The expected reduction in 2010 incentive compensation does not reflect the reasonable, ongoing costs ComEd will incur and is not an appropriate basis on which to determine the amount of incentive compensation expense properly recoverable in this proceeding. Trpik Reb., ComEd Ex. 28.0, 3:60-4:70. Staff witness Pearce initially proposed significant reductions in AIP cost recovery, but has withdrawn those proposals in light of information provided by ComEd in its rebuttal testimony. Pearce Reb., Staff Ex. 18.0, 18:417-19. The AG/CUB proposed AIP disallowance should be rejected.

In ComEd's last rate case the Commission disallowed two-thirds of the costs of the LTIP, reasoning that two of the three metrics governing benefits under the plan – setting net income and legislative/regulatory goals – did not benefit customers and therefore shareholders should bear the associated costs. ICC Dkt. No. 07-0566, Order at 61. In this case, ComEd witness Trpik noted that for years 2010 and following, ComEd has eliminated these net income and regulatory goals, and that since the LTIP has been brought into compliance with the Commission's directives in Docket No. 07-0566, all of the LTIP costs should be allowed. Trpik Dir., ComEd Ex. 4.0 Rev., 26:506-27:517.

Staff witness Pearce initially opposed recovery of the two-thirds of the LTIP costs addressed by Mr. Trpik, but upon review of Mr. Trpik's rebuttal testimony, Ms. Pearce acknowledged that ComEd had, in fact, eliminated the net income and legislative/regulatory goals from the 2010 LTIP. Pearce Reb., Staff Ex. 18.0, 19:434-37. On the other hand, she observed that a new goal related to Exelon had become part of the 2010 LTIP, a goal within which two of the three milestones are either not related to delivery services or have not been approved for recovery in delivery services rates. Accordingly, Staff recommends a disallowance of two-thirds of this 25% weighted goal, or about 17% of the LTIP costs. *Id.,* 19:437-48. This disallowance has a value of about $2.7 million. Trpik Sur., ComEd Ex. 54.0, 6:109-11.

Staff's modified disallowance should be rejected. Mr. Trpik testified that the two milestones found objectionable by Staff - - specific emissions targets and Smart Grid - - are specific operational metrics of the type the Commission has repeatedly approved as appropriate bases for recoverable incentive compensation expenses. Both provide benefits to customers and are appropriate goals for a delivery services company to aspire to achieve. Trpik Sur., ComEd Ex. 54.0, 6:112-17.

AG/CUB witness Smith continues to oppose any LTIP cost recovery on the grounds that no customer benefits are provided at all. This position, however, is markedly out of step with (a) the Commission decision in Docket No. 07-0566 which found at least one of the three metrics to produce customer benefit; (b) ComEd's actions in changing the 2010 LTIP to eliminate the two metrics the Commission found not to provide customer benefits; and (c) Staff's position that only 17% of the LTIP costs are questionable (a position that is overly restrictive for reasons discussed above).

Finally, both Staff and AG/CUB continue to press for a disallowance of 100% of the costs of the Exelon 2009 Key Manager Restricted Stock Award. The basis for this argument is that the objective of the Award is to further the financial and operational success of Exelon, not ComEd, and that the Award provides no direct benefit to customers. The evidence shows, by contrast, that this long-term incentive program for ComEd's Key Managers provides the same sort of benefits as the LTIP. Providing compensation in the form of restricted stock incentivizes managers to remain focused on the long-term health of the business. Denial of recovery of this cost would require ComEd to adjust its Key Manager compensation program to provide an alternative form of compensation to attract the talent required to effectively run the business, but would lose the linkage to long-term performance. Ultimately, customers would bear the same cost, but would not be likely to receive the same level of benefit. Trpik Reb., ComEd Ex. 28.0, 8:160-74.

2. Rate Case Expenses

ComEd is seeking to recover $8.5 million in expenses of this rate case and the alternative regulation case over three years, and has included a $2.833 million amortization amount in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev., 50:1016-20; ComEd Ex. 6.1, Sched. C-2.12.

a. Rate Case Expenses of the Instant Case

Staff proposes to reduce rate case expenses of the instant case by $796,000, or by $263,000 of annual amortized expense. Hathhorn Reb., Staff Ex. 17.0, Sched. 17.01. AG/CUB proposes a much larger reduction, in the amount of $1.567 million annually or a total disallowance of $4.7 million. Smith Reb., AG/CUB Ex. 9.0 Rev., 31:664-66.

The Order in Docket No. 07-0566 accepted ComEd's projected rate case expenses of $11,500,000 but reduced that amount by $1 million based upon Staff's recommendation that a ComEd/Staff stipulation in that case substantially narrowed the issues to be litigated. ICC Dkt. 07-0566, Order at 52-53. The total amount in this case is 20% less than the amount authorized for recovery in Docket No. 07-0566. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 13:260-65. This case is no less complicated, nor does it present fewer issues, than Docket No. 07-0566. The reduced amount reflects ComEd's hard bargaining with those outside parties providing services for ComEd in connection with this case. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 13:260-67; Fruehe Reb., ComEd Ex. 30.0 Public, 14:303-06. It further reflects ComEd's sensitivity to the current state of the economy and conditions in its service area generally. As to Mr. Smith's contention that ComEd has failed to provide sufficient documentation showing details of services provided, Mr. Fruehe points out that through discovery ComEd provided on-going status updates regarding its rate case expenses with invoices and descriptions, and only privileged information was redacted. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 13:268-79. Mr. Smith has not, with few exceptions, voiced any objection to any of that detailed information.

Staff's proposed disallowance is the result of three disallowances. First, Staff would disallow $746,000 in legal and consulting fees that Ms. Hathhorn attributes to work on ComEd's ongoing Alt Reg docket (No. 10-0527). Second, Staff would disallow $25,000 and $20,000 for costs attributable to the testimony of Dr. Hewings and Dr. Andrade, respectively. The total disallowance of $791,000 gives rise to a $263,000 reduction in the three-year amortization proposed by ComEd. Hathhorn Reb., Staff Ex. 17.0, 3:41-9; Staff Ex. 17.1. The disallowance attributed to the Alt Reg case is discussed in subsection 2.b., below.

Mr. Smith, testifying on behalf of AG/CUB, argues that a series of additional costs should be disallowed as well, including those related to particular witnesses and consultants, and then a final "for-good-measure" disallowance for what he considers likely overestimating of costs. Smith Reb., AG/CUB Ex. 9.0 Rev., 29:629-36. In total, Mr. Smith would reduce ComEd's $8.5 million in rate case expenses to $3,798,660. *Id.*, 31:665-66. The proposed $4.7 million disallowance is more than 55% of the amount requested by ComEd. Mr. Smith's proposals are improper, individually and collectively, and should be rejected.

For example, Mr. Smith proposes to disallow $225,000 of rate case costs representing amounts spent on the Economic Development/Jobs Creation issues. A large portion of this is attributable to work done by Chicago Partners, who did not present testimony. However, the work done by Chicago Partners was instrumental and very valuable in helping to frame the issue and provide additional avenues of research and exploration. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 14:287-96. This proposed disallowance also includes costs related to the work performed by Dr. Hewings and Dr. Andrade. Given the fact that the testimony of both Dr. Andrade and Dr.

Hewings has been admitted as rebuttal and surrebuttal testimony, this dispute should be moot, and the disallowance for these two witnesses proposed by Staff and AG/CUB should be rejected.

Mr. Smith's disallowance for ComEd's cost of capital witnesses – capping those fees at $100,000 (Smith Reb., AG/CUB Ex. 9.0 Rev., 25:568-69) – is also not proper. It is not the case, as Mr. Smith implies, that all four witnesses provided cost of equity calculations and testimony. Only Dr. Hadaway and Mr. Seligson provided testimony regarding the calculation of ComEd's base cost of equity. Dr. Tierney testified about the propriety of ComEd's proposed 40 basis point adder to the base cost of equity to account for the risks of load and revenue loss due to the State of Illinois' aggressive energy efficiency requirements (as well as on the prudence of ComEd's 2009 pension contribution). Ms. Abbott, whose direct testimony was adopted by Mr. Fetter after her death during this proceeding, provided the perspective of these financial experts as to why maintaining or improving ComEd's credit rating is critical to allow ComEd to continue to finance successfully its huge capital needs, and explained the outcome of this case and ComEd's credit ratings. *See* Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 15:304-14. They also explained the relationship between this case and credit ratings. *Id.* Mr. Smith's proposed disallowance for the work of P. Moul and Associates is also inappropriate because, as Mr. Fruehe describes in his rebuttal testimony, Mr. Moul provided additional insight to the critically important cost of equity issue, an issue that accounts for nearly $100 million of the difference between ComEd's revenue request and Staff's recommendation. Especially in these volatile and uncertain times, ComEd is of the opinion that it was necessary and appropriate to solicit a range of opinions. Fruehe Reb., ComEd Ex. 30.0, 16:340-47.

Mr. Smith's proposed disallowance for the work of Sullivan and Associates ought to be rejected because, as Mr. Fruehe explained, Mr. Sullivan is an accounting and financial contractor who provides a necessary and cost effective augment to ComEd's regulatory staff during rate case preparation. Because the heavy work load associated with rate cases is intermittent, ComEd does not staff for the peak work load. In addition to having provided assistance with the voluminous Part 285 filing requirements, Mr. Sullivan assisted with the response to over 1,550 individual data requests (with their numerous subparts). Mr. Sullivan was instrumental in allowing ComEd to meet the stringent time deadlines imposed in this case for data request responses. Expenses related to his work are a proper and necessary rate case expense.

The Commission should reject Mr. Smith's proposed disallowance of the so-called "overrun" associated with ComEd's Cash Working Capital study. Smith Reb., AG/CUB Ex. 9.0 Rev., 29:639-30:640. This recommendation follows from AG/CUB witness Brosch's characterization of that study as "severely flawed and unreliable." *Id.*, 29, n. 16. Mr. Smith does not contest that ComEd in fact spent what it claims on the CWC study, he simply feels it was "too much." It should go without saying that the allowance of rate case expenses for a particular piece of testimony should not depend upon whether an intervenor witness (or even ultimately the Commission itself) finds that testimony to be persuasive or not. ComEd is required to perform and present a lead-lag analysis to support its cash working capital component of rate base. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 17:358-18:365. The study was done by an eminently qualified expert, Mr. Subbakrishna of Navigant Consulting, using methods that are consistent with studies accepted by the Commission in numerous recent cases involving Illinois utilities, and the costs should be allowed.

Mr. Fruehe also rebuts Mr. Smith's point that, even after all of the individual expenses he finds objectionable are eliminated, ComEd has still "over-estimated" its rate case costs, and thus another $555,000 as part of the direct case and $661,000 as part of the post-direct case should be disallowed. Smith Reb., AG/CUB Ex. 9.0 Rev., 28:615-31:661. As Mr. Fruehe demonstrates, however, data through the end of November 2010 show that the amount ComEd has paid to consultants and expert witnesses for the direct case is relatively close to the estimate. *See* ComEd Ex. 56.3 CONFIDENTIAL, p.2. Notwithstanding Mr. Smith's seeming incredulity, it is not at all surprising that the "post-direct case" is likely to cost more than the "direct case," inasmuch as that phase of the case includes the preparation and filing of both rebuttal and surrebuttal testimony, preparation of hundreds of Data Request Responses, preparation and presentation of the witnesses at the hearing, preparation for and cross-examination of Staff and intervenor witnesses and preparation and filing of four rounds of post-trial briefs as well as a proposed order and pretrial memorandum. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 18:366-79. Mr. Fruehe showed that five months after the filing of its last rate case ComEd had incurred $7.1 million of rate case expenses, or about 68% of the total $10.5 million allowed (and about 62% of the $11.5 million without the ComEd/Staff Stipulation). Over the same time period in this case, ComEd has incurred just over $5 million, or about 59% of its estimated $8.5 million. This shows not only that ComEd's actual costs so far have been reduced by about $2 million compared to its last rate case, but also that ComEd is on track to incur the estimated $8.5 million. *Id.*, 18:380-19:397.

Finally, Mr. Smith adopts Staff's initial allocation of 50% of ComEd's legal fees to the Alt Reg proceeding and would disallow those as well, for an additional $2.5 million. *See* Smith Reb., AG/CUB Ex. 9.0 Rev., 31:664-65,. Staff no longer supports a 50% disallowance, and in any event as explained in the next section, no disallowance is appropriate for Alt Reg costs.

All in all ComEd has presented extensive data and other information more than sufficient to show that its requested rate case expenses are reasonable and meet the standards of the new

Section 9-229 of the Act. The Commission should allow the full $8.5 million requested, amortized over three years.

b. **<u>Alternative Regulation Case</u>**

Both Staff witness Hathhorn and AG/CUB witness Smith recommend disallowances from the $8.5 million of rate case expenses (a $2.833 million amortized amount) that they claim are related to the Alt Reg case. The Staff disallowance includes $496,000 for attorneys' fees attributable to two law firms and another $250,000 for consultants. Hathhorn Reb., Staff Ex. 17.0, Sched. 17.01, p.2, lines 2, 3, 7, 8 and 9. Mr. Smith adopts each of these disallowances, but relies on a withdrawn Staff recommendation to support his $2.5 million Alt Reg legal fee disallowance. *See* Smith Reb., AG-CUB Ex. 9.0, 5:97, 31:666; Hathhorn Dir., Staff Ex. 2.0, Sched. 2.04 CONFIDENTIAL, p. 2

With respect to the issue of legal fees, although ComEd has estimated that through October 2010 Alt Reg legal costs were about 11% of total legal costs, the fact is that virtually all of these costs would have been incurred even in the absence of the Alt Reg proceeding because one of ComEd's outside law firms – Rooney, Rippie & Ratnaswamy ("R3") – agreed to a flat rate for all work on the rate case with no additional charge imposed for whatever work the firm did on the Alt Reg matter. Fruehe Reb., ComEd Ex. 30.0, 14:301-06. Despite that fact, and despite the overall estimate of 11%, Ms. Hathhorn bases her Alt Reg disallowance of 18.33% of the total R3 fixed fee based on the percent of Alt Reg work for only September and October 2010. Hathhorn Reb., Staff Ex. 17.0, 4:78-5:84. But any disallowance is inappropriate because of the fundamental point that these fees would have been incurred and paid even had no Alt Reg proceeding been filed. And even more fundamentally, the overall $8.5 million figure is reasonable – 20% lower than ComEd's last rate case – and should be allowed.

3. Administrative and General (A&G) Expenses

a. Exelon Way Severance Amortization

AG/CUB witness Effron proposes that the Commission terminate any further recovery of the Exelon Way severance costs approved in Docket Nos. 05-0597 and 07-0566, a proposal that would reduce ComEd's jurisdictional revenues by approximately $18.8 million (reflecting the 7.5 year amortization period authorized by the Order in Docket No. 05-0597). As Mr. Effron notes, the Exelon Way program was designed to achieve savings of $70 million annually. Effron Dir., AG/CUB Ex. 2.0, 22:485-86. Mr. Effron does not contend that those savings have not been, or will not continue to be, realized. Instead, he claims that amortization of the costs "should have commenced" when the costs were incurred in 2003 and 2004. Had that occurred, the amortization of the costs would be complete by the time rates authorized in this case go into effect. *Id.*, 22:497-23:510.

Mr. Effron's recommendation, which would disallow recovery of 40% of costs ComEd has twice been authorized to recover, based merely on what he believes "should have been done" and on no new or different facts, ought to be rejected. Amortization of these costs began in January 2007 pursuant to the Commission's authorization in Docket No. 05-0597. ComEd could not have recorded a regulatory asset and begun to amortize it in 2003 or 2004 because the Commission had not yet provided any authorization to do so. The Commission reaffirmed this cost recovery in ComEd's last rate case, Docket 07-0566, again overruling efforts by Mr. Effron to limit recovery of these costs. Dismissing Mr. Effron's recommendation is necessary to assure fair cost recovery and adherence to the Commission's orders in Docket Nos. 05-0597 and 07-0566. Houtsma Reb., ComEd Ex. 29.0, 44:927-47:1010; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 29:623-30:639.

b. Accounts 920-923

An Account 923 issue raised by Mr. Effron is discussed under the Legal Fees-IRS Dispute heading in Section V.C.3.j.

c. Pension Costs

(i) Recovery of Actuarially-Determined 2010 Pension and OPEB Costs (Uncontested between Company and Staff)

ComEd seeks to include $65,536,000 in jurisdictional and actuarially determined 2010 pension costs in its revenue requirement. ComEd Ex. 6.1, Sched. C-2.2, line 3, col. (F). AG/CUB witness Smith recommends several disallowances to ComEd's pension costs. First, he would "normalize" the amount (using an average of 2006-2008 costs that excludes the 2009 and 2010 amounts) because, in his view, the $2009 amount of $53,008,000 appears to be abnormally high compared to other previous years. Second, he would reject entirely the *pro forma* pension expense based on the actuarial report issued in March 2010 (but, notably, not the *decrease* in OPEB costs reflected in that report). The combined effect of these two disallowances is to reduce ComEd's pension expense by $37.4 million. Houtsma Reb., ComEd Ex. 29.0, 34:711-13. Neither of these disallowances is consistent with reality, and both are inappropriate.

ComEd retains Towers Watson, a leading actuarial firm with years of expertise in determining pension and post-retirement benefit costs, to prepare a pension valuation report that is used to determine pension costs based on the funded status of the pension plan. Towers Watson prepared such a report in March 2010, and ComEd relied upon Towers Watson's work when establishing pension costs for approval in this proceeding. Ms. Houtsma explained that the use of an actuarial report of this type is standard practice in rate cases. In Docket No. 05-0597, ComEd relied upon an August 2005 actuarial report to document pension and post-retirement welfare costs for 2005. In Docket No. 07-0566, ComEd relied upon a May 2007 actuarial report to document pension and post-retirement welfare costs for 2007. Ms. Houtsma testified that in both of these proceedings, the reports were comparable to the March 2010 report and were accepted as providing known and measureable verification of ComEd's pension and post-retirement benefit costs. ComEd Ex. 29.0, 31:648-36:775.

AG/CUB witness Smith simply dismisses reality and substitutes his own subjective judgment the actuarial determination of Towers Watson reflected in their report. The fact that he believes these costs are abnormally high should be completely disregarded inasmuch as he has no demonstrated expertise in estimating pension costs. He conceded on cross examination that he does not contend that the actuarial report contained any errors (Tr. 527) and that economic conditions have not returned to the pre-recession conditions (*Id.*, 540-41). He has presented no reason to believe that any normalization is necessary, especially one based on 2006-2008 costs, or that pension costs when the rates set in this case go into effect are likely to return to the level of what they were in 2006-2008. The Towers Watson report shows that ComEd's actual costs are significantly higher. Houtsma Reb., ComEd Ex. 29.0, 31:648-36:775, 34:710-23; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 21:446-23:487. Staff concurs that ComEd's adjustment based on the Towers Watson report is appropriate. Pearce Reb., Staff Ex. 18.0, 40:926-38. The Commission has consistently based recovery of pension costs on actuarial reports. It should not deny ComEd recovery of $37.4 million in such costs simply on the basis of Mr. Smith's wishful thinking. Disallowing these costs would saddle ComEd with massive unrecovered pension costs.

Mr. Smith also recommends a separate reduction of $2.424 million to remove the costs of ComEd's Supplemental Executive Retirement Plan ("SERP"). Smith Dir., AG/CUB Ex. 3.0 Corr., 35:788-89. Mr. Smith does not deny that ComEd actually incurred this cost, but simply says that this "is not a reasonable expense that should be recovered in rates" and that if ComEd wants to provide these benefits it should do so at the expense of its shareholders. *Id.*, 34:775-35:783. Mr. Smith again appears to be relying upon his own subjective view of what is reasonable, as he offers no evidence that the costs are unreasonable. Indeed, Mr. Smith recognizes that "[c]ompanies usually maintain that providing such supplemental retirement benefits to executives is necessary in order to ensure attraction and retention of qualified employees" (*Id.*, 34:764-66), but he provides no information to refute that necessity.

(ii) <u>2005 Pension Funding Cost Recovery</u>

In 2005, ComEd made an $803 million pension fund contribution for which the Commission, in Docket No. 05-0597, authorized recovery in the amount of $25.5 million per year, a return equal to the cost that ComEd would have incurred had ComEd issued debt to fund the contribution. Houtsma Reb., ComEd Ex. 29.0, 13:260-14:281; *Commonwealth Edison Co.*, ICC Dkt. 05-0597, Corrected Order on Rehearing (Dec. 20, 2006) at 26-28. This return is lower than what would have resulted from application of ComEd's overall rate of return, as ComEd claimed was appropriate. The amount was also included, without any challenge, in ComEd's approved revenue requirement in Docket No. 07-0566. In accordance with the Commission's orders in those cases, the $25.5 million is included in ComEd's revenue requirement in this case. The Order in the 2005 case was affirmed on the debt rate of return for the pension contribution in *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 398 Ill. App. 3d 510, 519-522, 924 (2^{nd} Dist. 2009).

In direct testimony, Staff proposed to simply terminate all recovery of the Commission- and court-approved $25.5 million annual cost of this contribution. But, in rebuttal, Staff modified its position and contended that the $25.5 million cost authorized and unchanged in Docket Nos. 05-0597 and 07-0566, should be cut by $6.329 million. The basis of this argument is the assumption that this hypothetical ComEd long-term debt will amortize to zero. Pearce

Dir., Staff Ex. 3.0Rev., 16:364-71; Pearce Reb., Staff Ex. 18.0, 9:211-20. The evidence shows, however, that the presumption of diminishing debt value is not just unsupported, but unrealistic. Of the $5.6 billion of ComEd's long-term debt, only 0.7% is amortizing debt. These are sinking fund debentures issued in 1961, which mature in December 2011. The vast majority of ComEd's debt securities do not amortize over time; instead ComEd pays interest periodically and the principal balance remains outstanding in its entirety until the maturity date, at which point it is either paid off or re-financed. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 13:258-76. And, at maturity, they are often refinanced. Moreover, the $6 million amount of Ms. Pearce's proposed disallowance was contrived from the equally unsupportable use of a 30-year mortgage bond amortization schedule calculated as if the debt was issued years before the pension contribution was actually made. Pearce, Tr. 2560:5 – 2562:5; *see also* Staff Sched. 18.02, ComEd Cross Ex. 23, and Pearce, Tr. 2563:14 – 2564:9 (describing calculations on cross exhibit).

The *overall* pension asset *will* decrease over time by an amount equal to each year's pension accruals. However, ComEd has used the pension accruals to diminish the pension asset not accounted for by the $803 million contribution because that part of the asset should receive a greater return (weighted average cost of capital), thereby resulting in a lower overall revenue requirement. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 14:277-15:307.

For the above reasons, the Commission should continue to reflect the $803 million pension contribution in ComEd's rates in the same manner as it did in Docket No. 05-0597 (affirmed on appeal) and Docket No. 07-0566.

d. Wages and Salaries *Pro Forma* Adjustment

ComEd seeks to include $8.809 million in *pro forma* wages and salaries expense in its revenue requirement. ComEd Ex. 6.1, Sched. C-2.1. AG/CUB witness Effron and Staff witness

Pearce propose to cut ComEd's *pro forma* wage and salary expense by $4.15 million and $6.2 million, respectively. Effron Reb., AG/CUB Ex. 8.0, 13:285-87; Pearce Reb., Staff Ex. 18.0, Sched. 18.03. Ms. Pearce claims that the increase is not "known and measurable" and would improperly impact the revenue requirement by failing to consider offsetting salary and wage decreases that may occur in 2010. Pearce Dir., Staff Ex. 3.0 Rev., 24:560-66; Pearce Reb., Staff Ex. 18.0, 13:296-14:323. Mr. Effron cites a lower number of employees in 2010 compared to 2009 levels as his justification for his recommendation. Effron Dir., AG/CUB Ex. 2.0, 18:409-19:413, 20:449-54. The amount of the 2010 wages and salaries increase is known and measureable, being based on an agreement with the Union effective April 1, 2010, and a non-union wage increase that went into effect on March 1, 2010. Fruehe Reb., ComEd Ex. 30.0 Public, 18:396-393. Also as Mr. Fruehe pointed out, these recommendations should be rejected because ComEd's proposed revenue requirement already takes into account $3.69 million in what ComEd has already determined are sustainable savings from the reductions. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 5:87-90. Moreover, the proposed disallowance overlooks offsetting increases in overtime and fringe benefits. ComEd's adjustment also does not include any wage increases applicable in 2011, which would increase the revenue requirement and which are also known and measureable. Fruehe Reb., ComEd Ex. 30.0 Public, 5:102-6:116; 18:383-19:405; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 4:71-6:108.

e. <u>Directors' Fees and Expenses</u>

Staff proposes to reduce the requested amount of directors' fees and expenses sought by the Company by 50%, or $312,000. The stated rationale is that because the ComEd Board "primarily represent[s] the interests of shareholders in their activities and decision-making," the costs should be shared. Pearce Dir., Staff Ex. 3.0 Rev., 36:851-59. There is no dispute that a utility operating as a corporation is required by law to have a board of directors to manage its business and affairs (805 ILCS 5/8.05) and the costs of a board of directors are therefore a necessary, non-discretionary expense associated with the business of operating a public utility. Neither is there any dispute that the fees are reasonable in amount. Fruehe Reb., ComEd Ex. 30.0, 17:363-18:381; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 20:405-415. These costs are, in short, reasonable and necessary costs of providing utility service to customers. The Supreme Court has rejected requiring a utility to share reasonable amounts incurred in light of legal requirements. *Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 121, 651 N.E.2d 1089, 1095 (1995) (reversing ICC Order directing the sharing of costs incurred by utilities under environmental laws). That is the end of the inquiry.

Staff's argument is also without factual basis. Staff not only provides no factual support for the claim that the ComEd Board represents "primarily" the interests of shareholders, but also improperly assumes that the interests of shareholders and customers are mutually exclusive. As Mr. Fruehe testified, the Board's duties include: (1) overseeing ComEd's utility operations, including reliability and safety; (2) monitoring ComEd's financial condition; (3) overseeing staffing and employee benefits; (4) directing needed capital and other business investment and overseeing establishment of operating budgets; (5) approving material commercial contracts; (6) reviewing collective bargaining matters; (7) setting corporate policy; (8) monitoring legislative and public affairs and complying with legal and ethical requirements; and (9) setting corporate citizenship and diversity initiatives. Fruehe Reb., ComEd Ex. 30.0, 17:370-18:378. To say that the discharge of any of these duties "primarily" benefit shareholders as opposed to customers, or *vice versa*, is unrealistic and inconsistent with the nature of the responsibilities undertaken. They are all necessary to ensure the smooth and proper operation of a utility that has numerous constituencies to which it is responsible, including but not limited to shareholders and customers.

Staff's proposed disallowance of one-half the Board costs should be rejected.

f. Corporate Aircraft Costs (Now Uncontested)

Staff witness Ms. Pearce and AG/CUB witness Mr. Brosch proposed disallowance of 100% and 50% respectively of ComEd's corporate aircraft costs. To limit the issues in dispute, ComEd has agreed to reduce aircraft expense by 50% or $384,000. Fruehe Reb., ComEd Ex. 30.0 Public, 6:117-30. Staff accepted this adjustment and withdrew its proposed full disallowance. Pearce Reb., Staff Ex. 18.0, 39:909-40:924.

g. Perquisites and Awards

ComEd seeks to recover $3.495 million in perquisites and awards costs. Pearce Dir., Staff Ex. 3.0, Sched. 3.05 (citing ComEd's response to Staff Data Request BAP-7.06). AG/CUB Ex. 3.2 Public, pp.70-71. Staff witness Pearce proposes a disallowance of $501,000 of operating expenses and $62,000 of rate base (Staff Ex. 18.0, Sched. 18.05) of perquisites and awards on the ground that these costs (principally stock awards or executive perquisites) were not necessary for the provision of utility service and did not provide direct ratepayer benefits. Pearce Reb., Staff Ex. 18.0, 24:549-59. AG/CUB witness Smith proposes disallowance of $1,392,000 of such costs. Smith Reb., AG/CUB Ex. 9.0, 5:98-102; AG/CUB Ex. 7.1, Sched. C-13, lines 3-5. ComEd witness Trpik testified that these disallowances should be rejected because perquisites and awards are reasonable business expenses that benefit customers. He explained that the majority of the expenses represent retention awards, special recognition performance awards and meter reader performance awards designed to improve accuracy and completeness of meter reads. The retention awards are intended to insure that employees filling critical roles within the organization continue in those roles by providing a long term financial incentive. Trpik Reb., ComEd Ex. 28.0, 8:175-9:197. Mr. Trpik testified that disallowance of such expenses is inappropriate and would discourage the very type of performance that most benefits customers.

h. **<u>Severance Expenses</u>**

ComEd incurred $12.8 million in jurisdictional severance costs in the test year, and proposed to amortize that amount over a three-year period, including $4.277 million in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev., 48:982-49:989; ComEd Ex. 6.1, Sched. C-2.5, C-22. ComEd incurs expenses for employee severance related to cost cutting initiatives. This is properly recoverable pursuant to well established rate making principles and as evidenced by Section 285.3125 of the Part 285 filing requirements. Staff witness Mr. Tolsdorf proposes to reduce ComEd's jurisdictional severance expense to about $1.1 million, or $370,000 annually, for an annual disallowance of $3.867 million. Tolsdorf Dir., Staff Ex. 4.0, 8:164-77 and Sched. 4.04; Tolsdorf Reb., Staff Ex. 19.0, 9:189-11:231 and Sched. 19.04. AG/CUB witness Effron seeks to disallow all recovery. Effron Dir., AG/CUB Ex. 2.0, 24:527-45.

This disallowance are improper and the Commission should reject it. Disallowance of these costs would create an inequitable situation where costs that are indisputably prudent, reasonable, and beneficial to customers would not be recovered. These costs are attributable to an initiative that is expected to save more than $6 million annually (on a jurisdictional basis), savings which have been fully reflected in ComEd's rate filing. Houtsma Reb., ComEd Ex. 29.0, 44:940-43. The Commission authorized recovery of similar severance costs in Docket No. 05-0597 (those related to the "Exelon Way" severance program) and reached a similar conclusion in Ameren's rate case, *Central Ill. Light Co., et al.*, ICC Dkt. Nos. 09-0306 (*cons.*), (Order April

29, 2010), providing for amortization of the costs in both situations. Recovery of severance costs is also consistent with the intent of the Section 285.3125 filing requirements for rate cases (information requirements relating to requests for recovery of cost savings programs with savings of $1,000,000 or more).

AG/CUB witness proposed to disallow recovery of the severance costs on the ground on the ground that reduced salary expense reflected in rates now in effect but no longer being incurred because of the severance will adequately compensate ComEd for its severance costs. Staff witness Tolsdorf proposes to reduce ComEd's recovery of 2009 severance costs in two ways. First he would remove about $119,000 from the unamortized amount related to stock compensation. Second, he adopts Mr. Effron's hypothesis that the severance costs were effectively recovered under current rates via the salary savings for the positions eliminated, Effron Dir., AG/CUB Ex. 2.0, 24:527-45.

Mr. Tolsdorf claimed that his treatment of these 2009 severance costs is "consistent" with that accorded other regulatory assets, citing ComEd's treatment of the cost of retired meters (Tolsdorf Reb., Staff Ex. 19.0, 9:201-02, 10:215-20), but that overall claim is incorrect and the retired meter example is not comparable. As Ms. Houtsma explained, that ComEd reduced its retired meter regulatory asset for costs it has previously recovered through Rider SMP is a matter far different from reducing a regulatory asset on the assumption those costs were recovered through "savings." In the former case, the costs were explicitly and expressly recovered through rates; in the latter case, the costs were not recovered at all, except by an incorrect and unwarranted assumption. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 28:593-601. Indeed, Mr. Tolsdorf admits that "he is not aware of any Commission decision in which the Commission reduced the amount of an otherwise proper regulatory asset on grounds that the underlying expense was being recovered by cost savings." Staff Group Cross Ex. 1 (Staff Response to ComEd Data Request ComEd-Staff 12.01 (Public)).

Moreover, this disallowance would be improper because it focuses exclusively on a single element of ComEd's costs, and ignores how other costs during the same period may have *exceeded* those reflected in existing rates. The Commission rejected a similar argument proposed by the AG in Docket No. 08-0312 (ComEd's Original Cost Audit docket), and Staff there opposed the kind of disallowance its witness makes here. In that case, the AG, through Mr. Effron, claimed that a change in ComEd's accounting policy in 2002, pursuant to which ComEd would capitalize certain cable fault repair costs instead of expense them, led to double recovery of those costs, first as an expense (under then-existing rates) from the time of the change and then as an element of ComEd's rate base established effective January 2, 2007, in Docket No. 05-0597. This is virtually identical to the "double recovery" premise underlying both Mr. Tolsdorf's and Mr. Effron's recommendation regarding the 2009 severance costs. *See, e.g.*, Effron Dir., AG/CUB Ex. 2.0, 24:538. In that case, however, Staff opposed Mr. Effron's proposal, arguing (according to the Commission's order) that "[a] single element of a revenue requirement should not be viewed in isolation as a matter of regulatory policy. All the elements of a revenue requirement should be viewed in the aggregate so that changes in one element are netted against changes in all other elements." *Commonwealth Edison Co.*, ICC Dkt. No. 08-0312, Final Order (Jan. 12, 2010) at 4. Here, for example, Ms. Houtsma points out that in 2009 ComEd's earned ROE was 8.5%, well below the 10.3% authorized in Docket No. 07-0566, indicating that any savings from the cost savings initiative were more than offset by other cost increases relative to the test year in that case and hence excess revenues were not available for the so-called recovery of severance costs. *See also* Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 27:584-30:639; Houtsma Reb., ComEd Ex. 29.0, 44:928-47:1010.

Alternatively, Mr. Effron proposes that if recovery of these severance costs is allowed, the amortization period should be 7.5 years. Effron Dir., AG/CUB Ex. 2.0, 24:546-25:551. A 7.5 year period is wholly inconsistent with Mr. Effron's primary claim that the severance costs will be recovered in the two years between the time the costs were incurred (July 2009) and the time this rate case is concluded (May 2011). Houtsma Reb., ComEd Ex. 29.0, 46:982-87.

The Staff and AG/CUB disallowances to the proposed 2009 severance cost recovery should be rejected.

i. <u>Charitable Contributions</u>

ComEd seeks to include $6.3 million (total amount, before removal of non-jurisdictional portion) in charitable contributions in its revenue requirement. Fruehe Reb., ComEd Ex. 30.0, 8:163-66. Inclusion of charitable contributions in the revenue requirement is provided for in Section 9-227 of the Act, 220 ILCS 5/9-227.

Staff witness Tolsdorf proposes a disallowance of $2.574 million (before jurisdictional allocation) of ComEd's charitable contributions. Tolsdorf Dir., Staff Ex. 4.0, Sched. 4.03, p.5. Mr. Brosch also proposes a disallowance to accomplish 50-50 "sharing" of these contributions, to give ComEd "some incentive" to "carefully prioritize" its charitable giving. Brosch Dir., AG/CUB Ex. 1.0, 47:1032-38.

Neither Mr. Tolsdorf nor Mr. Brosch contends that the recipients of the amounts in question are not *bona fide* charitable organizations, or even that the overall contributions are excessive. Mr. Tolsdorf contends that most of the amount he seeks to have disallowed was not expended directly by ComEd but rather incurred in conjunction with Exelon Business Services

Company ("EBSC") ($1.915 million), and that some of this amount was acknowledged through use of the ComEd logo ($170,000) or contributed to charities outside ComEd's service territory ($214,000). Tolsdorf Dir., Staff Ex. 4.0, 5:94-8:162. In addition, Mr. Tolsdorf claims that about $659,000 of ComEd's direct contributions (to, *e.g.*, the Black Ensemble Theatre, the Illinois Black Chamber of Commerce, the National Museum of Mexican Art, the Puerto Rican Arts Alliance and Women's Business Development, to name a few of the larger contributions, (Tolsdorf Dir., Staff Ex. 4.0, Sched. 4.03, p.4)) are not properly allowable as they are "promotional" in nature, because ComEd is recognized for, *e.g.*, its "past and present generous support" or its "commit[ment] to making Chicago a better place to live and visit." Tolsdorf Dir., Staff Ex. 4.0,, 6:120-8:162, 7:139-49. Mr. Tolsdorf recognizes that "[p]romotional value may not have been *the purpose* of these contributions, but ComEd *received* promotional and/or goodwill advertising nonetheless …." *Id.*, 8:160-62 (emphasis added). Mr. Brosch, by contrast, apparently believes that ComEd makes contributions wantonly because it knows it will be able to recover them dollar for dollar. Brosch Dir., AG/CUB Ex. 1.0, 47:1034-42. These proposed disallowances should be rejected. They are contrary to the facts and to Section 9-227.

ComEd's total charitable contributions for which it seeks recovery in this case – $6.3 million – is lower than the $6.8 million (both amounts before jurisdictional allocation) of contributions approved in Docket No. 07-0566. Fruehe Reb., ComEd Ex. 30.0 PUBLIC, 8:163-66. The contributions made in conjunction with EBSC are functionally equivalent to the donations made by ComEd in its own name. It is nearly certain that had ComEd made those donations directly, no question would have been raised about the propriety of those contributions (to such organizations as the United Way of Metropolitan Chicago, the Kellogg School of Management, the Chicago 2016 Committee, and the Field Museum (Tolsdorf Dir., Staff Ex. 4.0, Sched. 4.03, pp.2, 3)). The average contribution level of 23 utility companies in 2008 was approximately $8.5 million, more than one third higher than the amount for which ComEd seeks recovery in the 2009 test year. Fruehe Reb., ComEd Ex. 30.0 PUBLIC, 8:166-71. Moreover, the fact that ComEd may receive some unintended positive recognition for its contribution is no reason to characterize the contribution, to an admittedly *bona fide* charity as "promotional" or "goodwill" in nature. As Mr. Fruehe pointed out, such contributions are quite different from, for example, a promotional billboard at U.S. Cellular Field. *Id.*, 9:177-86.

The only proper tests are whether the donation is made for "charitable, scientific, religious or educational purposes" and whether it is "reasonable in amount." Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 6:123-28; 220 ILCS 5/9-227. ComEd's $6.3 million of charitable contributions qualify on both counts and should be approved in their entirety. Fruehe Reb., ComEd Ex. 30.0, 7:143-9:195; Fruehe Sur., ComEd Ex. 56.0, 6:110-8:166; ComEd Ex. 6.1, Sched. C-7 (details of contributions).

j. <u>Legal Fees – IRS Dispute</u>

ComEd seeks to include $2.187 million in operating expenses for legal costs related to an IRS dispute associated with the gain on the sale of fossil generating units. Fruehe Reb., ComEd Ex. 30.0 PUBLIC, 10:213-11:221 AG/CUB witness Effron proposes to disallow this entire amount. Effron Dir., AG/CUB Ex. 2.0, 21:460-76. Staff adopted this recommendation in its rebuttal case. Hathhorn Reb., Staff Ex. 17.0, 11:216-12:239.

This recommendation, which focuses on only one of the thousands of costs included in Account 923, should be rejected. Many of the costs comprising that account are more closely related to the distribution function than to any other function. ComEd, however, uses a labor allocator to allocate all costs in Account 923. As a result, some costs are over allocated to distribution and some costs are under-allocated to distribution, but this methodology is necessary because Account 923 contains thousands of line items, which can vary from year to year and this methodology provides a reasonable estimation of the jurisdictional cost. To "cherry pick" one cost from the account because it is not distribution, but to overlook all of the other costs that may be exclusively distribution but are allocated only in part to the distribution function, or that may be more closely distribution than suggested by the allocator, improperly biases the distribution revenue requirement downward. Costs in Account 923 fluctuate dramatically from year to year, as shown by the fact that Account 923 included \$174 million in the 2006 test year, but only \$139 million in the 2009 test year in this case, demonstrating that use of the general allocator is a reasonable way of allocating these costs. Fruehe Reb., ComEd Ex. 30.0, 10:213-11:221; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 8:167-9:179.

k. Professional Sporting Activity Expenses

Staff witness Tolsdorf and AG/CUB witness Smith propose to remove costs associated with professional sporting activities, individual game tickets and catering expenses associated with skybox usage. According to these witnesses, the amount of this disallowance should be \$511,000 (\$467,000 jurisdictional). Tolsdorf Dir., Staff Ex. 4.0, 12:256-72; Smith Dir., AG/CUB Ex. 3.0 Corr., 53:1163-54:1188; AG/CUB Ex. 3.1, Sched. C-13. As Mr. Fruehe explained, these proposals should be rejected because these costs represent reasonable business expenses for employee recognition, team building and development of business relationships with key customers. Fruehe Reb., ComEd Ex. 30.0 PUBLIC, 11:222-229; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 9:180-94. Moreover, as Mr. Fruehe clarified during his cross examination at the hearing, the \$511,000 number is not correct. The vast majority of that amount, all but \$64,000 plus \$8,000 allocated to a capital account, was reclassified "below the line." As a result, the revenue requirement contains, for this category of expense, only $64,000 in operations and maintenance expense and $8,000 in rate base. Hearing Tr., 2445-47

l. Workforce Expense Reduction

This is the same issue as that discussed in part V.C.3.d., supra.

4. AMI Pilot Expenses

In his rebuttal testimony, Staff witness Tolsdorf proposes to disallow all costs ComEd expects to incur in connection with the AMI Pilot program between December 2010 and June 2011, claiming that ComEd has not produced sufficient documentation to establish that they are "known and measurable." Tolsdorf Reb., Staff Ex. 19.0, 11:244-12:278. The amount in question is $1.306 million, although Tolsdorf would allow $130,000 of that. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 26:540-44; Hearing Tr., 1291. The costs in question are those incurred in connection with an AMI pilot program that the Commission, in Docket No. 09-0263, ordered ComEd to complete. ComEd has subsequently proceeded with the pilot. Furthermore, because an Appellate Court decision (now on appeal) precluded rider recovery of these costs, the Commission approved a separate tariff providing that any costs not recovered through the tariff would be included "in a general rate case …. There, they would be recovered … like any other operating expenses." Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 27:564-28:583. ComEd Ex. 56.6 provides a detailed list of ComEd's latest estimate of the project expenses it will incur through June 2011, along with a list and description of the activities and the service providers. Hearing Tr., 1293-95. Mr. Tolsdorf recognizes that the "rate case" referenced in the tariff language quoted above is this case. *Id.*, 1290. The Commission's pro forma rule (83 Ill. Admin Code 287.40) requires projects proposed as "known and measurable" adjustments to be "individually identified;" Mr. Tolsdorf agrees that ComEd Ex. 56.6 "individually identifies" the projects associated with the AMI pilot project through June 2011. *Id.*, 1295.

Mr. Tolsdorf's position boils down to an assertion that a project cannot be known and measurable unless it is covered by a contract or purchase order. *Id*., 1297. The Commission's rule does not contain any such requirement and Mr. Tolsdorf acknowledges that he has not cited any authority for such an interpretation. In fact, relevant precedent demonstrates that even under a prior rule that required the Commission to consider such written documentation to support *pro forma* adjustments, the absence of such documents as purchase orders, written contracts and invoices did not by itself justify a conclusion the projects were not known or measureable. *Commonwealth Edison Co. v. Ill. Commerce Comm'n,* 322 Ill. App. 3d 846, 851-52, 751 N.E.2d 196, 201 (2nd Dist. 2001).

The AMI project is one the Commission specifically approved in Docket No. 09-0263, and ordered to be completed. Mr. Tolsdorf has never suggested nor does the record reflect anywhere that ComEd will or may not complete this project. The Commission has further suggested the costs in question be recovered in this docket. Combining all of those facts with Mr. Tolsdorf's unprecedentedly strict interpretation of the *pro forma* rule strongly suggest that Mr. Tolsdorf's proposed disallowance should and must be rejected.

5. <u>New Business Revenue Credit</u>

This issue is discussed in the Revenues section of this Initial Post-Trial Brief, specifically section IX. E.

6. <u>Tax Repair Methodology – New IRS procedures</u>

AG/CUB witness Effron notes that recent issuances from the IRS suggest that the deductibility of certain expenditures that are capitalized for financial reporting purposes is being substantially enhanced. Effron Dir., AG/CUB Ex. 2.0, 28:629-29:646. He further notes that the effect of this change could have a material effect on ComEd's revenue requirement, largely through a reduction to rate base because of an increase to the ADIT balance, but he does not recommend a change to the rate base or revenue requirement in this proceeding. *Id.,* 31:687-32:726. Mr. Effron claims that ComEd has not yet availed itself of this enhanced deduction, largely because of uncertainty concerning the scope of the IRS policy. *Id.,* 29:648-59. Mr. Effron recommends that to "preserve" the benefit of this deduction for customers, the Commission should (if the change is not made during the pendency of and is not reflected in the revenue requirement established by this case) require ComEd to maintain the effect of any future adjustment in a "reserve account" and accumulate future additions to the enhanced deduction from the effective date of the accounting change so that the accumulated revenue requirement impact of this changed policy can be "credited" to customers and recovered with appropriate "carrying charges" at the time of ComEd's next rate case. *Id.,* 33:741-49.

At present, ComEd is collaborating with the Edison Electric Institute and other electric utilities to obtain specific implementation guidance from the IRS in order to request the described change in accounting. Although a handful of utilities have filed a request for change in the method of accounting, a significant number are awaiting the IRS guidelines before implementing the change. Once guidelines for the new method are issued and can be implemented by ComEd, customers will benefit because any resulting cash flows will help finance new plant investment; the costs of this new investment will substantially outweigh any expected benefits from the new policy but which will not be recovered by ComEd between rate cases. In addition, the cumulative accelerated tax benefits that may ultimately result from the change in policy will be reflected as a reduction to rate base in future rate cases, and thereby be flowed through to customers just like all other tax benefits. Houtsma Reb., ComEd Ex. 29.0, 38:815-40:856.

Not only would it be unnecessary to create a separate account as Mr. Effron proposes to "preserve" the tax benefits for customers, but it would be inappropriate to do so. ComEd presently records all of its accumulated deferred income taxes in separate accounts, and the Uniform System of Accounts requires that tax timing differences be recorded in separate asset/liability accounts; ComEd's records track the various categories of tax differences. Upon implementation of the new repair guidelines, ComEd will record the tax deductions separately within the existing, proper accounts reflecting tax timing differences. Houtsma Reb., ComEd Ex. 29.0, 41:866-72. Finally, Mr. Effron's suggestion that "carrying charges" be accumulated on these tax benefits would be inappropriate single-issue ratemaking, particularly in light of the fact that no mechanism exists (or has been suggested by Mr. Effron) by which "carrying charges" on the investment made between rate cases can be similarly deferred and recovered in future rate cases.

Moreover, while Mr. Effron referred to other utilities' having obtained automatic consent from the IRS for the change, he acknowledged that those utilities remained subject to audit, and that he did not know if any of them had been audited for the year in which they made the change. Hearing Tr., 1594. He further agreed that the IRS has designated this as a "Tier 1" issue, where the IRS assembles an Issue Management Team to prepare for comprehensive auditing. *Id.*, 1600-01. In addition, he acknowledged that without IRS guidance there has not been a resolution between the IRS and taxpayers on this issue and that such guidance has not been provided. *Id.*, 1595-98; ComEd Cross Ex. 19.

Staff also opposes the Effron recommendations for several additional reasons: that it is not known if a tax change will occur at all; that because of the "normalization" method followed by the Commission the benefits of reduced taxes will be reflected in rate base in future cases; and the Uniform System of Accounts already makes sufficient provision for the types of accounts Mr. Effron proposes. Hathhorn Reb., Staff Ex. 17.0, 12:255-13:264.

7. Depreciation of Intangible Plant

ComEd seeks to include $70,983,000 in its revenue requirement for costs associated with depreciation of general and intangible plant. Houtsma Dir., ComEd Ex. 6.0 Rev., 41:824-29. AG/CUB witness Effron proposes that amortization expense on post test year intangible plant should be adjusted not only for plant additions (as ComEd has done) but also to reflect retirement of intangible plant or the fact that some intangible plant will be fully amortized by the end of the *pro forma* period (in his case, March 31, 2011). Based on a schedule of post test year retirements, Mr. Effron derives a reduction of amortization expense of $4.987 million, reflecting elimination of amortization on 2002 and 2005 vintage plant (which will be completely retired by March 31, 2011). Effron Dir., AG/CUB Ex. 2.0, 27:595-617; Effron Reb., AG/CUB Ex. 8.0, 19:412-430. This disallowance should be rejected.

This argument is nothing short of an attempt at single issue ratemaking. As Ms. Houtsma explained, although plant will be retired before the end of the *pro forma* period, other factors must also be considered. As an example, she notes that ComEd placed several large information technology projects in service in December 2009, causing 2009 depreciation expense to include only one-twelfth of an annual amount of depreciation expense for those large projects; the full year's effect of depreciation on those projects (and the related expense) - - estimated to be $9.5 million - - will more than offset the $4.987 million impact on depreciation expense of the retirements. Houtsma Reb., ComEd Ex. 29.0, 47:1012-48:1025; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 34:733-35:757; ComEd Ex. 55.7. Accordingly, Mr. Effron's proposed amortization disallowance should be rejected.

8. Late Repayment Charge Reclassification

This issue is discussed in the Revenues section of this Initial Post-Trial Brief, specifically section IX.D.

9. Illinois Electric Distribution Taxes ("IEDT")

Illinois Electric Distribution Taxes are taxes on the quantity of electricity delivered in the state of Illinois. See generally 35 ILCS 620. The Public Utilities Revenue Act requires that they be calculated and collected based on a percentage of kilowatt hours used. *Id*. ComEd seeks to include $108.8 million in its revenue requirement for costs associated with IEDT. Houtsma Dir., ComEd Ex. 6.0 Rev., 51:1035-42, ComEd Ex. 6.1 Sched. C-2.17. AG/CUB witness Brosch proposes to disallow $1.387 million of this amount. Brosch Dir., AG/CUB Ex. 1.0, 51:1118-21, AG/CUB Ex. 7.1, Sched. C-19.

The issue here is whether it is more appropriate to calculate the IEDT liability by using a weather-normalized tax and an off-setting credit based on a six-year average of credits as ComEd has done, or by using the actual tax paid in 2009 and an estimated credit for 2009 as AG/CUB witness Brosch proposes. In support of the ComEd method (with which Staff concurs, *see* Hathhorn Reb., Staff Ex. 17.0, 10:204-11:213), Mr. Fruehe testified that 2009 was an abnormally cool summer, having the fewest cooling degree days since 1992, and therefore the tax for that year will not be representative. Thus, ComEd has weather normalized the tax, just as it weather normalized billing determinants to develop rates that will best reflect normal conditions expected during the period rates set in this case will be in effect (a practice no party has opposed). Fruehe

Reb., ComEd Ex. 30.0, 12:249-58; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:196-210. Further, Mr. Brosch's approach mixes the 2009 tax with a credit that is not applicable to 2009 because the credit lags the tax by three years (resulting in a mismatch between the tax and the credit). Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:207-08. Use of the six-year average of the credit will smooth out year-to-year fluctuations and will provide a better estimate of the net amount of the tax ComEd will pay in a given year. Fruehe Reb., ComEd Ex. 30.0, 11:240-12:248; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:208-10. For these reasons, the AG/CUB approach to calculation of the test year IEDT should be rejected.

10. Depreciation and Amortization Expenses (Derivative and Direct)

11. Regulatory Asset Relating To Tax Liability for Medicare Part D (Uncontested between Company and Staff)

ComEd seeks to include $3,104,000 in operating expenses for the amortization of costs associated with loss of the Medicare Part D subsidy. Houtsma Dir., ComEd Ex. 6.0 Rev., 51:1043-45, ComEd Ex. 6.1, Sched. C-2.18. AG/CUB witness Effron proposes to disallow $2,173,000 of this amount. Effron Dir., AG/CUB Ex. 2.0, 26:579-84; AG/CUB Ex. 2.1, Sched. DJE-2.2e. Before the March 2010 federal health care reform legislation, cash subsidies paid to employers who provide prescription drug coverage to retirees were tax free. This subsidy was designed to encourage employers to continue their prescription drug programs so that their retirees would not become Medicare Part D participants. The tax-free subsidy was discontinued by the 2010 health care legislation, and all subsidies received in the future will be taxable even if they relate to prior years. Houtsma Reb, ComEd Ex. 29.0, 26:547-27:559, 29:606-07.

In prior rate cases, ComEd passed on to customers (through a reduction in post-retirement costs) the full estimated benefit of an accrual for the subsidies to be received from the federal government, even though actual payment of the subsidy to ComEd lagged significantly behind the rate of the accruals. The cumulative benefit to customers of this practice is at least $14.4 million as of year-end 2009. *Id.*, 27:565-77, 28:586-88. Now that the subsidies to be received will be taxable, it is clear that the reduction in post-retirement costs provided in the past (specifically 2004-09) were overstated. In order to fund the tax payment, ComEd proposed that a regulatory asset be established in an amount equal to the tax obligation imposed by the new legislation, and that the asset be amortized over a three year period. ComEd also provided for recovery of taxes due on subsidies for 2010-2012. *Id.*, 26:536-31:647. Staff concurs with ComEd's position on this issue. Pearce Reb., Staff Ex. 18.0, 38:892-39:907.

AG/CUB witness Effron acknowledges that recognition of a regulatory asset is appropriate, but argues for a longer ten-year amortization period. As Ms. Houtsma explained, however, this lengthy amortization period could very likely leave ComEd with insufficient funds to make required tax payments when they become due. She further explained that Mr. Effron's amortization period might be appropriate if ComEd had passed on to customers only the actual cash subsidies ComEd received instead of the full amount expected to be received. But in fact, customers have already enjoyed the full amount of the subsidy even though ComEd has received only a fraction of the subsidy (in the aggregate 13%) from the government. Houtsma Reb., ComEd Ex. 29.0, 27:572-74, 30:630-39; ComEd Ex. 29.09. ComEd is asking for symmetrical treatment: Because ComEd has passed on to customers each year the full benefit of the subsidy as if it will receive the full amount of the subsidy from the government, ComEd should be allowed to recover the full amount of the taxes to be paid on the subsidies as if ComEd received or will receive the full amount of the subsidy each year. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 24:513-18. The three year amortization period proposed by ComEd allows this outcome to be achieved, and accordingly, that three-year period is appropriate and should be approved.

12. Taxes Other than Income Taxes (Derivative Adjustments)

13. Income Taxes (Derivative Adjustments)

While the evidentiary hearing in this docket was pending, the Illinois state corporate income tax rate changed from 7.3% to 9.5% and new federal tax provisions were enacted which accelerated the tax deductions applicable to the 2010 and 2011 pro forma plant additions. Houtsma Hearing Tr., 2410-11. Both of these new provisions should be incorporated into the revenue calculations. Because of the derivative nature of income taxes, the ultimate impact of these changes will vary depending on the final revenue requirement. Staff Cross Ex. 15, which is DLH 21.01 Revised, reflects the mechanics of making this change and provides the impact to Staff's rebuttal position. *Id.* The schedules that are attached to DLH 21.01 reflect where the tax increase adjustment has been made. *Id.*

14. Photovoltaic Pilot Costs

In order to narrow the issues in this proceeding, and without conceding the validity of the disallowance, ComEd accepted Mr. Tolsdorf's proposed disallowance of the $10,251 in costs related to the Photovoltaic Pilot program. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 34:724-732.

15. Customer Deposits – Interest Expense Component

D. Operating Expenses (Total)

ComEd's total operating expenses are $1,451,540,000. ComEd Ex. 55.1, Schedule C-1.

VI. RATE OF RETURN

A. Overview

The following chart summarizes the rate of return recommendations of ComEd and the Staff and Intervenor witnesses addressing cost of capital issues, showing the individual components on which the overall weighted average cost of capital is based.

Party	Capital Structure	Long Term Debt Cost	Short Term Debt Cost	Return on Equity	Rate of Return
ComEd	LTD 52.54% STD 0.18% Equity 47.28%	6.52%	0.39%	11.30%[7]	8.98%
Staff	LTD 52.53% STD 0.54% Equity 47.11%	6.52%	0.54%	10.0%	8.24%
IIEC	LTD 52.56% STD 0.11% Equity 47.33%	6.53%	0.73%	9.60%	8.10%
AG-CUB	LTD 52.56% STD 0.11% Equity 47.33%	6.53%	0.73%	8.94%	7.79%

The key issue here is recognizing a reasonable cost of equity for ComEd. Investors see ComEd as a distribution company subject to significant financial, operational, and regulatory risks. In accordance with the Commission's recent decision in *North Shore Gas Co.*, ICC Docket No. 09-0166/09-0167 Consol., ComEd provided results of established financial models as well as evidence of the real world conditions ComEd and utilities like it face in the competitive capital markets. ComEd also acknowledges that, since the filing of its tariffs more than six months ago, investors' demands have edged downward by about 20 basis points, and that ComEd's base cost of equity now falls in the upper half of Dr. Hadaway's updated range, which extends from 10.3% to 10.9%. Hadaway, ComEd Ex. 37.0, 31:587-90. ComEd will not recover its costs with a lower ROE. The consequences of ComEd's failing to recover its capital costs on

[7] This represents the upper portion of Dr. Hadaway's updated range (10.9%) plus 40 basis points, as supported by Dr. Tierney.

its ability to operate in the future are identical to any other disallowance of ComEd's actual costs of service.

Staff and IIEC, nonetheless, argue for costs of equity at or somewhat below 10%, based almost entirely on the results of mathematical models. Unlike ComEd, they presented little testimony – and no evidence that survived rebuttal – of how investors and capital markets actually perceive ComEd. Moreover, while their mathematical models are in most respects very similar to those ComEd used, such "models are also highly dependent on analyst judgment as to the inputs …." *North Shore* at 123. The whole point of using these models is to find a proxy for a cost of equity that is not directly observable. If the data underlying the model are suspect – or, worse, slanted, then the model does not serve its function, no matter how theoretically and methodologically sound.

In this case, just a few unfair and unreasonable inputs drove Staff's unrealistically low result. For example, Staff's Capital Asset Pricing Model ("CAPM") analysis used an atypical risk free rate reached only during a few deviant weeks in all of 2010 – a rate more than 50 basis points below that which investors generally demanded during 2010, and nearly 70 basis points below the risk free rate at the end of 2010. McNally, Tr. 1879:3-1880:21. Staff witness McNally also used a sample that was small (and thus easily skewed) and that included two New Jersey gas companies that are quite unlike ComEd – they are both far smaller and derive the majority of their revenues from *unregulated* activities. *Id*, 1872:16-1874:10. Simply using a fair 2010 risk free rate and a sample comprised of actually comparable companies predominately in the regulated distribution business moves Staff's calculated ROE to near the midpoint of Dr. Hadaway's range.

AG-CUB advocates a far lower ROE arrived at only by replacing recognized measurements of what investors actually demand with pronouncements of what some academics believe they should demand. Thomas, Tr. 1787:6-1788:21. This notion is contrary to law, unaccepted by regulators generally, and repeatedly rejected in Illinois. It should again be rejected here.

Finally, parties suggest reducing ComEd's ROE by up to 32 basis points if its Straight Fixed-Variable ("SFV") rate design proposal is approved. This adjustment is far out of line as compared to other adjustments, even for decoupling. It is a measure of its unfairness that, while ComEd's believes in better aligning its rates with the fixed-cost nature of its business, ComEd cannot accept this penalty. If the Commission determines that adopting an SVF proposal would result in an adjustment driving its ROE below 10.6%, the midpoint of the reasonable range, ComEd would respectfully withdraw its SFV proposal. The inability to earn the revenues required to support ComEd's capital investment – and the resulting harm to customers – is too high a price to pay.

B. <u>Capital Structure</u>

ComEd proposes to use its actual capital structure adjusted as in past proceedings to remove goodwill. This is a reasonable capital structure, appropriate for ratemaking, and if coupled with an appropriate rate of return, will allow ComEd to compete in the capital markets as necessary for its operations. Trpik Dir., ComEd Ex. 4.0 Rev, 20:366 – 22:387. With the exception of a small issue concerning the balance of short-term debt discussed in the next section, the witnesses addressing capital structure issues agree on the components and percentage weights used in ComEd's capital structure.

C. Cost of Short-Term Debt

ComEd's short-term debt balance is $15,870,000 when measured using a time period consistent with other components of ComEd's capital structure, *i.e.*, an average balance for the 13-month period ending March 31, 2010 -- the month in which the balances of the other components of ComEd's capital structure were determined.

Staff proposes a balance of $49,344,124. Arriving at Staff's balance, however, requires using a 13-month average balance ending September, 2010 (Fruehe, ComEd Ex. 30.0:541-550). While ComEd acknowledges that Staff's proposal is an alternative, use of an average balance for the consistent 13-month period ending March 31, 2010 is preferred. Fruehe, ComEd Ex. 56.0, 25:510-519. ComEd notes that IIEC and AG-CUB also used the March 31 balance in their direct testimony, before Staff proposed using inconsistent periods. Gorman, IIEC Ex. 1.0-C, 12:332 – 13:336; Thomas, AG-CUB Ex. 4.0, 37:767.

D. Cost of Long-Term Debt

ComEd's cost of long-term debt is 6.52%. That value is based on Staff's slightly-revised version of ComEd's original 6.53% calculation, which ComEd accepts. IIEC and AG-CUB accepted ComEd's 6.53% cost of long term debt and do not dispute the small adjustment that that ComEd and Staff have concluded is appropriate. No contested issues remain.

E. Cost of Common Equity

1. Summary

The legal standards applicable to ComEd's

> … entitlement to a fair and reasonable return on its investment are well established. These classic and enduring pronouncements were set out by the United States Supreme Court in [the] *Bluefield Water Works…* and *Federal Power Comm'n v. Hope Natural Gas Co.* … cases. A public utility has a constitutional right to a return that is 'reasonably sufficient to assure confidence in the financial soundness of the utility and [is] adequate, under efficient and economical management, to maintain and support its credit and enable it to raise

> the money necessary for the proper discharge of its public duties.' The authorized return on equity 'should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.'

North Shore at 123 at 89-90 (citations omitted).

Providing ComEd with a realistic return is not simply a matter of academics or of fairness ComEd and its shareholders. If the Commission sets ComEd's return on equity below that of comparable alternatives, it will ultimately harm customers, as Staff witness McNally acknowledges (Staff Ex. 5.0, 2:36-42).

> [I]f the authorized rate of return is lower than the overall cost of capital, the financial strength of the utility could deteriorate, making it difficult for the utility to raise capital at a reasonable cost. Ultimately, the utility's inability to raise sufficient capital would impair service quality.

ComEd's cost of equity is supported by the testimony of three expert witnesses, who provided both a detailed quantitative analysis using established models, and who provide "financial market information to ensure that the model results presented are generally consistent with real world conditions, and to guide our determination of reasonable rates of return on equity based on the models that we deem appropriate for our consideration." *North Shore* at 123.

- Dr. Samuel Hadaway, a professor of economics and finance and a principal in FINANCO, Inc., Financial Analysis Consultants, provided the results of both discounted cash flow ("DCF") and CAPM models, using a broad sample of companies representative of ComEd. Under these market conditions Dr. Hadaway's recommends relying on the DCF models, which (using updated data) result "in the range of 10.3 to 10.9 percent." Hadaway, ComEd Ex. 37.0, 31:587-90; ComEd Ex. 62.0, 1:17.

- Carl Seligson, an independent consultant of nearly 50 years' experience specializing in utility industry finance, performed an independent assessment of ComEd's cost of equity using both a risk premium and a comparable earnings analysis. These models, while not traditionally used to set ROEs in Illinois, do focus on the return on actual investor alternatives to ComEd stock and thus provide valuable insight into investor demands. That analysis concluded that ComEd's cost of equity is 12.0%, strongly suggesting that even if only traditional models are used, the ROE should be at the top end of the range produced by such models. *See generally* Seligson, ComEd Exs. 12.0, 38.0.
- Mr. Stephen Fetter, a former Chair of the Michigan Public Service Commission and ratings agency executive, explained the importance of risk to ComEd's cost of capital and underscored that ComEd's distribution business is far from risk free, and that if ComEd is to operate well it's return must be competitive in the capital markets with that of other comparable investments. *E.g.*, Fetter, ComEd Ex. 66.0, 2:35 – 4:71.

In addition to ComEd's base cost of equity, Dr. Susan Tierney, a Managing Principal at the Analysis Group and former Assistant Secretary for Policy of the United States Department of Energy and Commissioner of the Massachusetts Department of Public Utility Control, analyzed how ComEd's successful implementation of energy efficiency and demand response programs could harm ComEd financially. She testified that the resulting risks and revenue erosion justify a 40 basis point cost of equity adder proposed by ComEd. *See generally* Tierney, ComEd Exs. 13.0, 39.0, 64.0. If the Commission determines that volumetric risks are not adequately captured in the base ROE, Dr. Tierney's testimony supports an adjustment that more than offsets Staff's proposed 32 basis point downward adjustment for SFV (even were that proposal adequately supported, which it is not).

2. Economic Factors Affecting the Cost of Equity

Electric utilities' cost of capital is determined by investors in a competitive worldwide capital market. There, utilities must compete with numerous other alternative investments. Seligson, ComEd Ex. 38.0, 3:47-48, Tr. at 1764. What investors typically value most in utility stocks are stable earnings and regular dividends supported by consistent and fair regulation. Seligson Dir., ComEd Ex. 12.0, 12:257-258. The return on a utilities' equity must reflect that market and cannot lag behind comparable investments. Investors require assurance that allowed returns on equity, and the actual earnings that they produce, will be sufficient to warrant investment in the utility and not some other option. Seligson, ComEd Ex. 12.0, 11:241-243.

The economic and financial uncertainties generated by the credit crisis have significantly impacted the cost of equity for the capital intensive electric utility industry (Hadaway, ComEd Ex. 11.0, 19:409-30:616), testing the financial standing of the sector "like never before." Fetter, ComEd Ex. 45.0, 11:212-213. Unlike typical industrial firms, which make annual capital expenditures of approximately 35% of their operating cash flow, electric utilities often must devote 100% of operating cash flow to new capital expenditures. Seligson, ComEd Ex. 12.0, 4:90-91. ComEd is no exception. Since its last rate case, ComEd has made more than $2 billion of new distribution infrastructure investments and continues to invest about $900 million each year to maintain and modernize its system. Higher risks facing utilities for major construction initiatives, the mounting need for external financing, increasing costs for medical, post-retirement, and pension benefits, and other factors require correspondingly higher returns on equity. *Id.*, 7:141-147.

Although the capital needs of electric utilities are high, authorized returns on equity for utilities have been extremely low for a number of years, prompted in part by a decline in interest rates to record lows. Seligson Dir., ComEd Ex. 12.0, 7:138-139. Developments in the capital markets also show that higher returns are now warranted. While the S&P 500 has increased significantly during the past year, utility prices have remained relatively flat, indicating that the cost of equity for utility companies has not declined to the same extent that interest rates have fallen or to the same extent that the cost of equity may have come down for the broader equity market. The relatively lower prices for utility shares indicate that the cost of capital for utilities is higher. Hadaway Dir., ComEd Ex. 11.0, 25:511-25:516.

All of these factors call for a return on equity for ComEd in excess of the range the Commission has approved in recent proceedings – and certainly rebut any claim that ComEd's return should be reduced from the 10.3% authorized in the last two cases. A strong case can be made that ComEd's cost of equity is well over 11%, based on evidence of actual investor alternatives. Nonetheless, ComEd understands that the Commission may take a different view based on, for example, DCF analyses. However, the 10% cost of equity proposed by Staff and the even lower costs of equity proposed by IIEC, AG, and CUB are not consistent with the market.

Apart from any theoretical debate about methodology, the models underpinning those recommendations are simply not fair measures of ComEd's costs. For example, as noted above, Staff witness McNally's CAPM analysis places sole reliance on a risk free rate (30 year Treasury bonds, in his case) he chose to measure on September 22, 2010. The Commission has recently rejected use of such a pure "spot date" approach in its *North Shore* decision (Tr. at 1783), and noting the problems that can result from using such data. *North Shore* at 92, 125-6. In this case, moreover, Mr. McNally's choice of a September 22 spot date was particularly and extraordinarily unfair to ComEd. The 3.77% rate measured on that date is not only nearly an all-time low (McNally, Staff Ex. 5.0, 25:504-05; Tr. 1879-1880), but fully 67 basis points below the rate on December 29, 2010 (the last trading day in 2010) and well below the risk free rate investors demanded generally throughout the entire year (Hadaway, ComEd Ex. 62.0, 9 fn 1; McNally, Tr. 1784-1785; ComEd Cross Ex. 20). It is inappropriate and unfair to set ComEd's delivery rates – rates that must recover its costs going forward – based on a short-lived blip in bond interest that the data now show to have been strikingly anomalous.

The significance of using this unrepresentative spot data is hard to understate. By way of illustration, if Mr. McNally's CAPM were adjusted upward by those 67 basis points alone, the results of his CAPM model would have been 10.99%, not 10.32%. *See* McNally, Staff Ex. 5.0, 43 (Table 3). That result would, in turn, have significantly increased his total recommended cost of equity.

A similar criticism can be made of the particular data underlying Staff's DCF analysis. A critical part of any DCF analysis is to pick a sample of *comparable* companies to analyze. If members of the sample are not comparable, the model will not accurately measure the required return for the utility and its value as a proxy is compromised. Mr. McNally acknowledged that the preferred method of selecting a comparable group of companies that "mirror [the utility's] business." Tr. 1872. Yet, his sample group includes two natural gas companies that receive the lion's share of their revenues, not from regulated distribution, but from unregulated activities. Tr. 1872; Hadaway Reb., ComEd Ex. 37.0:242-243. The influence of these non-comparable companies is exaggerated because Mr. McNally's sample is relatively small (he used 12 companies, while Dr. Hadaway used 31). These non-comparable gas companies thus account for

16.6% of Mr. McNally's DCF sample and its results. Just removing these two non-comparable companies – and retaining all of the major regulated distributors – would raise Staff's DCF results by 25 to 40 basis points. McNally, Tr. 1873. Again, this adjustment follows without beginning to address *any* issues with Staff's DCF methodology. If, in turn, 40 basis points were to Staff's "DCF Average," it would raise Staff's DCF result above 10%, to 10.09%. It would also raise the average of Staff's adjusted CAPM and adjusted DCF – the average on which Staff bases its recommendation – to 10.54%. *This is almost exactly the midpoint of Dr. Hadaway's 10.3% to 10.9% range.*

The 9.6% cost of equity recommended by IIEC witness Gorman not only fails to reflect current capital costs, but is lower than the allowed returns on equity in all but 9 of the 552 utility commission rate cases decided since 1989. Fetter Reb., ComEd Ex. 45, 16:317-321; Fetter Sur., ComEd Ex. 63.0. The 8.94% recommendation of AG-CUB witness Thomas is even more unrealistic and is based on an approach to estimating utility growth rates that has been rejected repeatedly by the Commission. Tr. 1779.

A fair consideration of all of the evidence, ComEd submits, shows that the cost of equity range recommended by Dr. Hadaway -- between 10.3% and 10.9% -- appropriately balances all of the relevant factors. Unlike the Staff and Intervenor recommendations, Dr. Hadaway's analysis takes into account the "ongoing effects of the recent financial crisis." Hadaway Reb., ComEd Ex. 37.0, 3:48-58. It reflects the real risks that ComEd faces when seeking to raise equity capital under current market conditions. The Commission should approve a cost of equity that is consistent with those conditions.

3. Dr. Hadaway's Cost of Equity Analysis

In arriving at his estimate that ComEd's cost of equity is between 10.3% and 10.9%, Dr. Hadaway applied three alternative versions of the DCF model to a comparable group of 31 investment grade electric utilities and 4 gas local distribution companies.[8] The three DCF models included (1) a constant growth format with long-term expected growth based on analysts' estimates of five-year utility earnings per share growth[9], (2) a constant growth model using the long-term projected gross domestic product ("GDP") growth rate, and (3) a three-stage growth rate approach using five-year analysts' estimates for the first stage (years 1-5), the long-term GDP growth rate in the third stage (years 11 and beyond) and the average of the two growth rates for the second stage (years 6 through 10). Dr. Hadaway developed his long-term GDP growth forecast from Federal Reserve Bank GDP data, giving more weight to the years since 1980 when lower inflation has resulted in lower overall GDP growth. Hadaway Dir., ComEd Ex. 11.0, 33:707-34:718. By increasing the weighting data for recent years, Dr. Hadaway arrived at a *more* conservative 6% long-term GDP growth rate, significantly lower than the actual 6.9% historic rate of GDP growth.[10]

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[8] Dr. Hadaway's comparable group included only investment grade companies with senior secured bond ratings of at least BBB from Standard & Poor's (S&P) or Baa from Moody's. Unlike Staff witness McNally's group, Dr. Hadaway required included companies to obtain at least 70 percent of their revenues from domestic regulated utility sales. He also restricted the group to companies that had consistent data from Value Line, no dividend cuts in the past two years, and no current involvement with mergers. Hadaway Dir., ComEd Ex. 11.0, 2:40-3:49.

[9] Dr. Hadaway used a 5.49% growth rate, which is the average of earnings growth projections from Value Line, Thomson, and Zacks. Hadaway, ComEd Exhibit 37.4, page 2. Use of analysts' growth rates in DCF models is a generally accepted approach that has been relied upon by the Commission, in whole or in part, in all utility rate cases for at least the last 12 years. Tr. 1776-1779.

[10] Dr. Hadaway also performed a risk premium analysis using *Moody's* average public utility bond yields and recent and projected triple-B utility bond interest rates, but discounted these results because they were affected significantly by recent artificially low interest rates resulting from the federal government's expansionary monetary policy. Hadaway Dir., ComEd Ex. 11.0, 35:755-36:762.

4. Mr. Seligson's Cost of Equity Analysis

Mr. Seligson used both the risk premium and comparable earnings methods to estimate that ComEd's cost of equity is 12%. Under the risk premium approach, Mr. Seligson determined a fair return on common equity for ComEd by adding a risk premium[11] to the cost of long-term U.S. Treasury securities.[12] The comparable earnings analysis used the median earnings level of 33 utility operating companies reported by Regulatory Research Associates.[13] While Mr. Seligson recognized that the Commission has declined to consider comparable earnings method results in the past, he urged the Commission to take a fresh look at the approach, pointing out that many other public utility commissions have found the analysis to be helpful in arriving at an appropriate cost of equity.[14]

5. Dr. Tierney's Analysis Of The Impact Of Energy Efficiency Requirements On ComEd's Cost of Equity

Dr. Tierney analyzed the groups of companies used by Dr. Hadaway and Mr. Seligson in their cost of equity studies to determine whether the included companies were subject to energy efficiency requirement risks comparable to those confronting ComEd in Illinois. Her analysis showed that the vast majority of companies in the groups do not reflect the combination of

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[11] Mr. Seligson's risk premium is based on Ibbotson Associates 2010 Valuation Yearbook analysis, concluding that from the beginning of 1926 to the end of 2009, common stock investors have historically realized a premium of 6.7% over the return available on long-term U.S. Treasury Bonds. Seligson, ComEd Ex. 12.0, 10:203-208.

[12] For the risk free rate, Mr. Seligson used the average of three independent sources projecting rates for 30 year Treasury Bonds in 2011 of 5.90%. ComEd Ex. 12.1.

[13] Electric Utility Quality Measures: Rankings and Trends of April 1, 2010. ComEd Ex. 12.1, p 1.

[14] As reported in Estimating the Cost of Equity: Current Practices and Future Trends in the Electric Utility Industry, Narayanaswamy, C.R.Publication: Engineering Economist Date: Wednesday, December 22 1999; http://www.allbusiness.com/government/380587-1.html, twenty five utility commissions around the country responded to a survey about the methods used by the commissions to estimate the cost of common equity. Twenty five percent of the commissions surveyed answered that they used the comparable earnings approach.

aggressive energy efficiency targets and absence of compensating ratemaking mechanisms[15] that face ComEd. Tierney, ComEd Ex. 39.0, 9:191-11:225. No witness presented any contrary evidence. ComEd Ex. 64.0. 1:14-20. Because the energy efficiency risks and revenue erosion to which ComEd is subject are not reflected in the cost of equity estimates presented by Dr. Hadaway and Mr. Seligson, a cost of equity "adder" is warranted to address those risks. Dr. Tierney presented an extensive analysis showing that the 40 basis point adder proposed by ComEd is justified. Tierney, ComEd Ex. 13.0, 19:37-28:551. As with all elements of the cost of equity estimation process, judgment must be exercised when determining whether a 40 basis point increase in ComEd's return on equity, or some lesser amount, is appropriate. However, the analysis presented by Dr. Tierney that ComEd is subject to additional uncompensated risk clearly calls for an upward adjustment in some amount in the allowed return on equity. Tr. 1769. (Investors will "take on additional risks … only if they can expect to receive a higher rate of return.")

6. Other Staff and Intervenor Recommendations

As noted above, other witnesses also made cost of equity recommendations. IIEC witness Gorman recommended a 9.6% return on equity. AG-CUB witness Thomas proposed an even lower return on equity of 8.94%. Dr. Hadaway explained that the principal difference in the cost of equity estimates using the DCF approach is that Messrs McNally, Gorman, and Thomas use unrealistically low growth rate assumptions. Hadaway Reb., ComEd Ex. 37.0:279-300, 369-375, 407-423, 506-533. In addition, Mr. Thomas substitutes the subjective opinions of academics for data that best predicts actual investor expectations, a stratagem that has not been

[15] ComEd has a relatively high target for implementation of energy efficiency measures but no ratemaking adjustment for revenue decoupling, lost revenues or shareholder incentives. Tierney Sur., ComEd Ex. 64.0, 1:18-20.

accepted in Illinois. Thomas, Tr. 1788:9-21. Dr. Hadaway identifies other issues affecting the ROE estimates of Messrs McNally, Gorman and Thomas, all of which will be discussed in more detail in ComEd's reply brief. Hadaway, ComEd Exs. 37.0, 62.0.

F. Adjustments to Rate of Return

Staff proposes a downward adjustment of between 20 and 32 basis points to ComEd's return on equity in the event that ComEd's straight fixed variable proposal is adopted. McNally Dir., Staff Ex. 5.0, 41:807-42:827. Dr Tierney's rebuttal testimony explains why no such adjustment is appropriate and why Mr. McNally's reliance on Dr. Tierney's testimony in support of his adjustment is misplaced. Tierney Reb, ComEd Ex. 39.0, 6:114-13:288; Tierney Sur., ComEdEx.64.0. Moreover, as noted above, ComEd cannot earn a fair return on its investments if a 32 basis point downward adjustment were to drive its allowed return on equity below 10.6%. If the Commission nonetheless believes that such an adjustment is warranted because of ComEd's proposed SFV rate design, then ComEd respectfully withdraws its request to approve that rate design. However economically efficient an SFV rate design may be, the harm to ComEd and, ultimately, to customers from the loss of the cost recovery is too great to justify its adoption under those circumstances.

VII. COST OF SERVICE AND ALLOCATION ISSUES

A. Overview

ComEd's embedded cost of service study ("ECOSS") reasonably allocates embedded distribution and customer costs among the retail delivery service classes. ComEd witness Alan Heintz testified that the structure of the ECOSS is substantially the same as studies that ComEd presented, and the Commission used as part of its rate setting process, in prior ComEd delivery service rate cases. Heintz Dir., ComEd Ex. 15.0 Rev., 1:17-2:31. Accordingly, ComEd recommends adoption of its ECOSS as revised and set forth in ComEd Ex. 75.1, which also incorporates ComEd's revised revenue requirement.

ComEd also presented an exemplar ECOSS ("Preferred Exemplar ECOSS") prepared in compliance with the Commission's directives in its Rate Design Investigation Order, Docket No. 08-0532, entered April 21, 2010. ("RDI Order"). ComEd Ex. 22.1. The Preferred Exemplar ECOSS distinguishes between shared (primary and secondary voltage) facilities and secondary voltage facilities, provides for cost allocation to an exemplar primary voltage delivery class, and distinguishes primary voltage transformers. Heintz Reb., ComEd Ex. 51.0, 3:58-61. The Preferred Exemplar ECOSS was subsequently revised to incorporate subclasses for the exemplar primary voltage delivery class to differentiate between nonresidential customers establishing electric demands that do not exceed 10,000 kW and nonresidential customers establishing electric demands in excess of 10,000 kW. The Preferred Exemplar ECOSS, as revised, also included other limited revisions. See Heintz Reb., ComEd Ex. 51.0, 3:66-4:81; ComEd Ex. 51.2. The Preferred Exemplar ECOSS was subsequently further revised to incorporate, among other things, ComEd's revised revenue requirement. ComEd Ex. 75.2. While ComEd urges the Commission to adopt the ECOSS set forth in ComEd Ex. 75.1, if the Commission determines that the creation of a new primary voltage delivery class is appropriate, the Commission should approve ComEd's Exemplar ECOSS, as set forth in ComEd Ex. 75.2, and set rates based upon the Preferred Exemplar ECOSS. 16

[16] ComEd also presented a third ECOSS – the Alternative Exemplar ECOSS – which is presented in ComEd Ex. 75.3. ComEd prepared the Alternative Exemplar ECOSS in response to an IIEC data request and first presented this study in rebuttal testimony, ComEd Ex. 51.3. The Alternative Exemplar ECOSS was presented for illustrative purposes , and ComEd does not support the adoption of this study.

B. Potentially Uncontested Issues

C. Potentially Contested Issues

1. Embedded Cost of Service Study Issues

a. Class Definitions

(i) Residential Classes

ComEd is proposing to consolidate its current four residential delivery classes into two by eliminating distinctions between customers with and without electric space heat while maintaining distinctions between single family and multi-family premises. That proposal is addressed in Sec VIII,C,3, a of this brief. The allocation of costs in ComEd's ECOSS reflects this consolidation proposal. Accordingly within its COSS ComEd appropriately utilized two distinct noncoincident peak ("NCP") NCPs, one for each of its proposed residential delivery classes. Alongi Sur., ComEd Ex. 73.0 2nd Rev., 17:372-73. AG/CUB, on the other hand, would have ComEd utilize a single NCP allocation factor for all residential customers. Rubin Dir., AG/CUB Ex. 6.0, 10:197-201. AG/CUB takes this position even though they conclude that there are significant differences in the cost of serving the different types of residential customers. *Id.*, 3:55-58. Not only is AG/CUB's conclusion in conflict with their cost allocation proposal, it conflicts with the position that the AG presented in a prior ComEd rate case. In the Commission's Order in ComEd's 2005 Rate Case, the Commission summarized the AG's argument stating, "[t]he AG argues that *the cost to install and maintain the distribution system is not dramatically different for a heating or non-heating customer*, and that cost does not vary significantly with the annual number of KWh the customer purchases." Docket No. 05-0597, Order at 180 (emphasis added).

In support of their proposal to utilize a single NCP cost allocation factor for all residential customers, AG/CUB suggest that there is "really just one residential delivery class." AG/CUB further claim that the designations given to the groups within what they suggest is one class is not important. Rubin Reb., AG/CUB Ex. 11.0, 8:140-9:169. The Commission should reject AG/CUB's proposal. ComEd's tariffs define its residential delivery classes. ComEd Ex. 16.22 Rev. 1st Revised Sheet No. 135. These definitions are required by Section 16-108(c) of the PUA:

> The electric utility's tariffs shall define the classes of its customers for purposes of delivery services charges. Delivery services shall be priced and made available to all retail customers electing delivery services in each such class on a nondiscriminatory basis …. Charges for delivery services shall be cost based, and shall allow the electric utility to recover the costs of providing delivery services through its charges to delivery service customers that use the facilities and services associated with such costs.

220 ILCS 5/16-108(c). ComEd's allocation of costs within its ECOSS necessarily and properly reflect its defined delivery classes as prescribed by the Commission's Part 285 Rules. Specifically, Section 285.5110, which sets forth the rules related to the filing of an ECOSS, provides in relevant part:

> b) [T]he utility shall provide a copy of all materials relied on in developing the cost-of-service study. This shall include: …
>
> > 2) The following data on demand and/or energy loss factors used in the cost-of-service study:
> >
> > > A) A list of all demand and/or energy loss factors by customer class used in the study ….

83 Ill. Admin.Code § 285.5110(b). AG/CUB's proposal to use a single NCP for all residential customers for cost allocation purposes is illogical, violates the Commission's rules, and inappropriately increases the cost responsibility of other customer classes. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 14:311-316. AG/CUB's proposal for just one NCP for the residential sector while maintaining four residential customer class designations should be rejected. ComEd's proposal, which utilizes a distinct NCP allocation factor for each of its proposed residential delivery classes, is reasonable, complies with the Commission's established

rules and produces equitable and fair interclass allocations. ComEd's approach should be approved by the Commission.

(ii) <u>Non-residential Classes</u>

ComEd's ECOSS separately identifies costs associated with its primary and secondary distribution systems while maintaining its current delivery class definitions for nonresidential customers. Alongi Dir., ComEd Ex 16.0 3rd Rev., 31:578-86. It shows that 86.4% of ComEd's overall distribution costs are related to its primary distribution system, while 13.6% are associated with its secondary distribution system. *Id.* The primary/secondary analysis is presented in ComEd Ex. 16.5. It provides a reasonable analysis of such costs and should be used as the basis to allocate these costs. CG witness Baudino agrees that ComEd's primary/secondary analysis is reasonable. Baudino Dir., CG Ex. 1.0, 18:336-39.

ComEd also presented the Preferred Exemplar ECOSS, which included an alternative primary/secondary analysis to incorporate an exemplar primary voltage delivery class in the nonresidential sector. ComEd Ex. 21.5. This alternative analysis was further revised to account for additional customers with service points at which electricity is delivered at or above 4 kV, and to reflect that customers with demands in excess of 400 kW do not utilize certain secondary distribution facilities. ComEd Ex. 49.4. The Preferred Exemplar ECOSS was updated in surrebuttal testimony. ComEd Ex. 75.2. If the Commission determines that a delivery class differentiation based upon primary versus secondary voltage should be incorporated with respect to nonresidential customers, ComEd urges the Commission to adopt its Preferred Exemplar ECOSS. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 3:57-59.

b. Primary/Secondary Split

(i) Appropriate Methodology/Compliance with Docket No. 08-0532

Historically, ComEd did not record, nor was it required to record, the separate costs used for primary voltage delivery (meaning at or above 4kV phase-to-phase but below 69 kV phase-to-phase) and secondary voltage delivery (meaning below 4 kV phase-to-phase). Alongi Dir., ComEd Ex. 16.0 3rd Rev., 3:71-81.) In ComEd's 2007 Rate Case, the Commission determined that future ECOSS proposals from ComEd should distinguish primary distribution costs from secondary distribution costs. 2007 Rate Case Order at 207. In addition, the Commission's recent RDI Order directed the following:

> ComEd is to develop and provide: 1) direct observation or sampling and estimation techniques of ComEd's system to develop more accurate and transparent differentiation of primary and secondary costs; 2) other utilities' methods in differentiating primary and secondary systems and costs; 3) function based definitions of service voltages for facilities other than the line transformers already addressed; 4) an analysis of which customer groups are served by which system service components; and 5) consideration of redefining rate classes on the basis of voltage or equipment usage to better reflect the cost of service.

RDI Order at 40. The Commission also stated:

> ComEd is to identify customers receiving power at 4 kV or higher as primary system customers and customers receiving power at levels below 4 kV as secondary system customers.

RDI Order at 84.

ComEd complied with the Commission's directives and incorporated a primary/secondary analysis into its ECOSS and proposed rate design filed in this proceeding on June 30, 2010. In direct testimony, ComEd witness Alongi presented the analysis of ComEd's distribution system identifying costs associated with its primary distribution system separately from costs associated with its secondary distribution system. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 31:578-81. ComEd could not fully address all aspects of the RDI Order by that initial filing date; in particular, the requirement that ComEd identify specific customers receiving electric service at or above 4kV. ComEd subsequently supplemented its testimony by using the definition of primary customers provided in the RDI Order to identify specific customers that would be considered primary customers and performing a supplemental primary/secondary analysis reflecting that definition. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 31:571-76; Alongi Supp. Direct, ComEd Ex. 21.0 2nd Rev., 18:244-46.

In the supplemental primary/secondary analysis, costs identified as "Secondary" were allocated to customers in delivery classes with service points at which a secondary voltage is provided by ComEd transformation. Costs identified as "Primary Voltage Transformer" were assigned just to customers in the exemplar Primary Voltage Delivery Class or High Voltage Delivery Class with service points at which ComEd provides transformation to a primary voltage. Costs identified as "Shared" for facilities used in ComEd's general distribution system were assigned to all delivery classes. The supplemental analysis identified several categories of costs that could be assigned to Secondary, Primary Voltage Transformer, or Shared: transformer costs, underground conduit, bar copper wire, poles, secondary cable and bus, network transformers and transformer brackets, and weather resistant wire. ComEd employed actual data when available and appropriate engineering assumptions to determine the allocators to assign primary and secondary costs in each category. Alongi Supp. Direct, ComEd Ex. 21.0 2nd Rev., 20:298-308.

ComEd further revised this supplemental primary/secondary analysis to make it more accurate, properly accounting for additional customers identified with service points to which electricity is provided at primary levels and to reflect that customers with demands in excess of

400 kW do not utilize certain secondary distribution facilities. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 22:298-23:502.

ComEd's primary/secondary analyses represent a thorough, judicious effort to differentiate primary and secondary distribution system costs and allocate them consistently to classes of customers who respectively are responsible for the costs. The primary/secondary analysis balances efforts to achieve appropriate cost allocation with the problem of becoming too granular in the review and allocation of costs. The identification of individual assets and allocation of their costs to individual customers or even small groups of customers is not useful for allocating costs for rate design purposes. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 28:630-32. Attempts to segment ComEd's 3.8 million customers into small groups of customers that use some or all of ComEd's various facilities would require a costly, complicated, and highly controversial analysis. *Id.*, 30:673-77. Moreover, ComEd's distribution system is highly integrated and dynamic, continuously being reconfigured and upgraded to meet the changing needs and mix of customers. Attempts to further segment the system would likely be inappropriate soon after they are completed. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 21:462-68.

The Commission has likewise identified these problems and stated in a prior 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 evaluation of each individual large customer 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.

2007 Rate Case Order at 210. It is ComEd's position that the primary/secondary analysis presented in ComEd Ex. 16.5 is reasonable for use in the allocation of primary and secondary distribution costs. However, in the event that the Commission rejects the primary/secondary analysis presented in ComEd Ex. 49.4, ComEd seeks approval of its supplemental primary/secondary cost analysis presented in ComEd Ex. 21.5 for the allocation of primary and secondary distribution costs as compliant with each of the Commission's directives in the RDI Order.

(ii) <u>Functional Identification of Costs</u>

ComEd satisfied the Commission's directive in the RDI Order to provide function based definitions of service voltages for facilities other than the line transformers with its primary secondary analysis presented as revised in ComEd Ex. 49.4. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 2:39-40; Alongi Supp. Dir., ComEd Ex. 21.0 Rev., 27:485-28:517.

IIEC and REACT each propose to modify ComEd's primary/secondary analysis that is used in the Preferred Exemplar ECOSS by requiring ComEd to further segment certain costs of the primary distribution system. Stowe Dir., IIEC Ex. 3.0, 13:297-15:326; Terhune Dir., REACT Ex. 3.0, 18:439-47. Staff agrees with ComEd that these proposals are unreasonable and should be rejected. Lazare Reb., Staff Ex. 26.0, 17:382-89.

Specifically, IIEC contends that 24.78% of ComEd's costs for overhead primary voltage conductor and 32.82% of ComEd's costs for underground primary voltage conductor should be allocated as secondary costs and only customers that take service from a single-phase circuit should be responsible for those costs. However, ComEd demonstrated that these proposals are inequitable to other customers that do not use other parts of ComEd's distribution system. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 23:523-25:557. Furthermore, this proposal would require a much more complex analysis than IIEC has presented to take into account the parts of ComEd's system that certain customers use more intensively than others, while maintaining equity among customers. *Id.* ComEd witness Alongi also observed that further segmenting the system as IIEC and REACT request would likely be inappropriate moments after it is completed – or even while the analyses were in process – because ComEd's primary distribution system is not static. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 21:460-65. Rather, the system is continuously being reconfigured and upgraded to meet ever-changing customer needs on each of the 6,400 circuits that comprise ComEd's primary distribution system. *Id.* at 21:465-68.

CTA and Metra similarly argue that the costs of 4 kV facilities should not be allocated to the Railroad Delivery Class' rates.[17] ComEd presented evidence demonstrating that further segmentation of its primary distribution system is inappropriate. Specifically, ComEd demonstrated that it is not appropriate to exclude all costs for these facilities from these classes because there are instances in which such customers use circuits or facilities that operate at 4 kV or 34kV. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 29:651-30:682. Consequently, any attempt to segment ComEd's 3.8 million customers by usage of 4kV, 12 kV and 34kv facilities would be costly, complicated and fraught with assumptions. *Id.* For the reasons set forth in the testimony of ComEd witness Alongi (Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 23:523-28:626; Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 19:411-24:517), and in the testimony of Staff witness Lazare (Lazare Reb., Staff Ex. 26.0, 15:354-17:389), the Commission should reject proposals which seek to further segment the primary distribution system.

(iii) <u>Direct Observation of ComEd Facilities</u>

The Commission directed ComEd in the RDI Order to perform a primary/secondary analysis of its distribution system using a direct observation. RDI Order at 40. ComEd defined "direct observation" to mean the manual review of ComEd facilities in the field and/or the

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[17] CTA/Metra initially argued that costs associated with both 4 kV and 34 kV facilities should be excluded from the Railroad Delivery Class' rates. However, in rebuttal testimony, CTA/Metra witness Bachman acknowledged that the Railroad class utilizes the 34kV system and should be allocated these costs. Bachman Reb., CTA/Metra Ex. 2.0, 9:187-10:202.

manual tabulation of data from the review of ComEd records. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 32:719-23. With this definition of direct observation, ComEd conducted its primary/secondary analysis that is applied in the Preferred Exemplar ECOSS, and developed the allocators used for the analysis.

Staff witness Lazare disagrees with ComEd's definition of "direct observation" And instead narrowly defines "direct observation" to mean directly observing the system out in the field, and not a review of system maps. Lazare Dir., Staff Ex. 10.0, 19:445-20:468. Staff's definition is in error and should be rejected.

"Direct observation" appropriately includes both manual review of ComEd facilities in the field and analysis of ComEd's system maps. Experience has shown that ComEd's maps provide a reasonable representation of the facilities that are in the field when the facilities are mapped, making additional analysis of the type proposed by Mr. Lazare unnecessary. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 32:713-39:885; ComEd Ex. 68.0. ComEd's maps are not subject to the "interpretation" of the mapmaker as Staff witness Lazare suggests. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 20:469-76. ComEd personnel cannot safely operate ComEd's system unless ComEd maps accurately represent ComEd's distribution wire, poles transformers, switchgear and other facilities necessary to operate a complex, interconnected distribution system. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 32:729-32. ComEd's maps must provide a reliable representation of the facilities mapped as ComEd personnel depend on this information for their safety. *Id.* at 33:733-34. Consequently, ComEd has demonstrated why its maps can be relied upon to present an accurate representation of what facilities are in the field. *Id.*, 33:735-34:760. In contrast, Mr. Lazare offers only conjecture as to the value of using system maps in performing direct observation of ComEd's distribution system.

While Staff does not suggest that ComEd should directly observe all of its facilities in the field (Lazare Reb., Staff Ex. 26.0, 9:189-91), it also admits that direct observation as defined by Mr. Lazare does not guarantee useful information for determining the primary and secondary facilities and related costs. Lazare Dir., Staff Ex. 10.0, 24:568-71. No compelling evidence supports incurring the substantial costs of conducting direct observations in the manner that Mr. Lazare suggests. While ComEd will continue to look for ways to improve the accuracy of its estimates, or look for new ways to allocate these costs, ComEd's method of conducting direct observations of its system in this proceeding is reasonable, and results in a fair allocation of primary and secondary costs. Accordingly, the Commission should approve ComEd's approach for conducting the direct observation of its distribution system for its primary/secondary analysis.

(iv) Sampling

ComEd's supplemental primary/secondary analysis reflected in the Preferred Exemplar ECOSS responded to the Commission's directives in the RDI Order to explore whether sampling techniques could be used "to develop a more accurate and transparent differentiation of primary and secondary costs," and "to explore in any subsequent rate proceeding whether sampling techniques can be used to allocate costs to customer classes for underground circuits operating at primary voltage serving customers only at secondary voltages." RDI Order at 38, 40. Staff witness Lazare confirmed that ComEd did explore the use of sampling techniques, but expressed concern that ComEd's sample of four primary circuits may not be representative of the large population, and suggested a larger sample be examined. Lazare Dir., Staff Ex. 10.0, 26:607-17.

In rebuttal testimony, ComEd witness Alongi explained why examining a larger sample of information was unnecessary. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 37:830-39:885. Specifically, Mr. Alongi presented information for all of ComEd's 6,400 circuits to show that its sample circuits were representative of the majority of ComEd's circuits which deliver electricity across both overhead and underground facilities in its primary distribution system and serve a variety of customers in the residential, nonresidential, and lighting delivery classes. ComEd Ex. 49.6. Comparing that information to what Mr. Alongi provided in his Supplemental Direct Testimony, ComEd Ex. 21.6, he concluded that ComEd Ex. 49.6 supports the fact that a larger sample of ComEd's circuits and ComEd's customers would be an arbitrary and unnecessarily complicated undertaking to identify at what point in ComEd's system each of the almost 4.8 million service points for ComEd's approximately 3.8 million customers are connected to one of ComEd's almost 6,400 interconnected primary voltage circuits to determine if an overhead or underground portion of the circuit serves a particular customer. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 38:850-65. Mr. Alongi explained the complexities of examining customer's use of ComEd's 6,400 primary voltage circuits given ComEd's extensive and integrated distribution system, as well as the costs associated with such an undertaking, and testified that no information suggests that this examination would result in a more precise segmentation of ComEd's distribution system. *Id.*, 38:850-39:885. Staff did not attempt to refute Mr. Alongi's testimony. Accordingly, the Commission should conclude that ComEd's sampling technique complies with the Commission's directive in the RDI Order, and that the sampling technique that ComEd used is reasonable.

(v) <u>Review of Other Utilities Treatment of Primary/Secondary Issues</u>

The RDI Order directed that ComEd examine "other utilities' methods in differentiating primary and secondary systems and costs." RDI Order at 40. ComEd witness Alongi explained that the Commission's order involved two tasks: examining how utilities distinguish between primary and secondary systems, and how they allocate the costs. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 40:897-900. Although Staff was critical of ComEd's examination of how other utilities addressed the differentiation of primary and secondary costs (Lazare Dir., Staff Ex. 10.0, 29:678-84), ComEd demonstrated that its analysis reasonably evaluated the issue.

Mr. Alongi explained that Mr. Lazare's testimony failed to account for the first task, which ComEd performed by examining the tariffs of 35 unbundled distribution utilities in California, Texas, the Midwest, the Mid-Atlantic, and the Northeast. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 40:901-904. Additional information was obtained from utility employees in telephone conversations and through emails. *Id.*,40:904-06. ComEd's review showed that most utilities use a specific voltage level (i.e., a bright line) to distinguish between primary and secondary systems, and several use 4 kV as that bright line at which the primary system is defined - which confirms that the basic approach used by ComEd is consistent with the approach used by other utilities. *Id.* at 40:907-13.

In addition, ComEd made significant efforts to investigate the second task – how those utilities allocated the costs. *Id.*, 41:914-42:939. However, ComEd concluded that the necessary cost allocation information was simply unavailable. *Id.* Absent available and reliable information concerning other utilities cost allocation methods, ComEd could not further refine its primary/secondary analysis. *Id.*, 43:968-44:989. In sum, ComEd demonstrated that Mr. Lazare's proposals for more elaborate efforts to discover additional facts are neither practical nor likely to be productive. *Id.*, 39:886-44:989.

The record demonstrates that ComEd met the Commission's directive to examine "other utilities' methods in differentiating primary and secondary systems and costs." RDI Order at 40. The evidence further demonstrates that, at this time, no additional analysis of other utilities' methods is warranted. Accordingly, the Commission should reject Staff's claims on this issue.

(vi) **Other Primary/Secondary Split issues**

Please see Section VII C. 1. b. i. a.

c. **Investigation of Assets Used To Serve Extra Large Load Customer Class**

REACT argues that the Commission should require ComEd to investigate and identify those distribution assets used to serve the customers comprising the Extra Large Load Customer Class. See, e.g., Terhune Reb., REACT Ex. 6.0, 39:911-40:936. However, REACT's position fails to recognize that ComEd's ECOSS is prepared consistent with Part 285.5110 of Commission' Rules concerning the presentation of an ECOSS in a rate case. Alongi Tr. 1/19/11, 2134. Nothing within Part 285.5110, or in any other Commission Rule or Order, establishes a requirement that a utility conduct a special investigation of the assets used to serve any particular customer class for the purposes of preparing a cost study. The reason no such requirement exists is clear – requiring a utility to investigate and identify the assets used to serve a particular class of customers is contrary to the way a cost study is conducted. Accordingly, the Commission should reject REACT's request for special treatment.

In evaluating REACT's claim for special treatment, the Commission should consider facts identified during the evidentiary hearings, facts which at minimum go to the weight to be given REACT's arguments. For example, of the 12 purported entities that comprise the *ad hoc* organization called REACT, only four have customer premises in the Extra Large Load Customer Class.[18] Alongi Tr. 1/19/11, 2125-2126. To place this number in perspective, the Extra Large Load Customer Class is comprised of 57 customer premises. Thus, the

[18] REACT's witness proposing customer-specific asset identification for the Extra Large Load customer class was not aware of how many members of REACT, much less which particular members, are part of the Extra Large Load customer class. Terhune, Tr. 1623-24, 1626.

overwhelming majority of this customer class has not presented any evidence supporting REACT's position.

Further, despite his testifying about cost allocation issues related to the preparation and analysis of a cost study, REACT witness Terhune was never principally responsible for preparing an ECOSS or a marginal cost of service study, nor does he have knowledge of the Commission's Rules related to the filing of an ECOSS under Part 285.5110. Terhune Tr. 1/14/11, 1629-30, 1635-36. ComEd, on the other hand, presented testimony by witnesses with demonstrated experience in preparing and relying upon ECOSSs (Messrs Heintz and Alongi), such as those used by the Commission in previous ComEd rate cases.

These facts suggest that little weight should be given to Mr. Terhune's testimony. Further, the Commission should reject REACT's request for an investigation of assets used to serve the Extra Large Load Delivery customer class for the same reasons it has rejected similar requests from REACT in prior proceedings. In ComEd's last rate case, the Commission rejected REACT's request for customer-specific cost studies, stating:

> 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 the evaluation of each individual large customer 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.

Commonwealth Edison Co., Docket No. 07-0566 (Order, Sept. 9, 2008) at 210 (emph. added). Also, in the RDI proceeding, the Commission rejected REACT's request to obtain customer specific information based on a claim that such information would assist in evaluating a prior cost study. Docket No. 08-0532, Denial of REACT's Petition for Interlocutory Review (Aug. 25, 2009). As Commissioner Elliott stated:

> I think REACT's requests have gotten a little far afield of what we were contemplating here; and it appears to me that they're asking for sort of individual cost studies within a class, and I think that's going a little far afield. … It may be information that is relevant to REACT; but I'm not sure from the Commission's perspective, when we're looking at customer class, cost of service, that it's going to be particularly informative.

Commission Minutes, Tr. 15:10-16:19. In this proceeding, the Commission has again rejected REACT's attempts to require ComEd to investigate and produce customer-specific information. Order (Denying REACT's Petition for Interlocutory Review, (Jan. 20, 2011)).

Not only is REACT's request in conflict with prior Commission decisions, it is at odds with how costs are compiled and allocated in an embedded cost of service study. Like all such studies, ComEd's ECOSS compiles ComEd's costs for providing distribution service and allocates such costs to the appropriate customer classes. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 29:646-50. No ECOSS, including ComEd's, is conducted by compiling the costs to serve individual customers and then aggregating the costs to serve individual customers into class costs. *Id.*

Accordingly, the Commission should reject REACT's request to have ComEd conduct an investigation into all of the distribution facilities used to serve each customer in the Extra Large Load Customer Class.

d. NCP vs. CP

Consistent with the Commission's direction in the RDI Order, ComEd has allocated primary lines and substation costs using a coincident peak ("CP") allocation method. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 29:543-44; Garcia Reb., ComEd Ex. 50.0, 5:108-6:133. While it remains ComEd's position that the NCP allocation method is the appropriate method for allocating these costs, it is not making that proposal in this proceeding.

e. Allocation of Primary Lines and Substations

This issue is discussed above in Section VII.C.1.(d) of this Initial Brief.

f. Functionalization of General and Intangible Plant

The functionalization of ComEd's General and Intangible Plant ("G&I Plant") is necessary both for determining rate design and the Company's appropriate revenue requirement in this rate case. As ComEd witness Alan Heintz testified, "ECOSS, of necessity, must functionalize general and intangible plant in the same manner as described by ComEd witness Houtsma … in the development of the overall revenue requirement." Heintz Reb., ComEd Ex. 51.0, 9:197-200. This issue is discussed more fully in, Section IV.C.3.(e) of this Initial Brief.

g. Street Lighting

In the RDI Order, the Commission directed ComEd to exclude from its ECOSS certain secondary system costs attributed to the Dusk to Dawn Lighting Delivery Class, as calculated by the City of Chicago (the "Chicago Method"). Any excluded costs would be reallocated to other customer classes. RDI Order at 51-54. ComEd complied with the Order in its proposed cost allocation, but ComEd asks that the Commission reconsider its decision due to several flaws inherent in the Chicago Method.

ComEd continues to oppose use of the Chicago Method. The adjustments based on the Chicago Method result in an unfair and illogical reallocation of secondary facilities and service connections costs from the Dusk to Dawn Lighting Delivery Class to other delivery classes. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 32:608-10. Overall, the defects of the Chicago Method include:

- The Chicago Method understates the cost of providing and maintaining ComEd's secondary wire by picking an allocator outside ComEd's ECOSS; specifically, average plant cost for a foot of secondary wire adjusted for depreciation and return on rate base. This factor does not account for all the costs ComEd incurs to provide service to customers in the Dusk to Dawn Lighting Delivery Class, thereby understating the value of the secondary facilities used by this class. The other secondary costs include ongoing maintenance and operating costs, overhead and indirect costs, pole and attachment costs to support the secondary wire, and labor and materials to connect Chicago's wire to ComEd's secondary system. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 32:612-33:623.

- The secondary costs are recognized in ComEd's ECOSS using specific accounts of the Uniform System of Accounts. This information does not reveal the customers or classes of customers who take service directly or indirectly from specific assets at any particular time CP and NCP based allocators are generally used to allocate these costs. Therefore, the allocation of certain secondary costs for one subset of customers results in an inappropriate adjustment to ComEd's CP and NCP allocators within the existing ECOSS. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 38:866-39:876.
- The Chicago Method treats dusk to dawn street lighting located in Chicago differently from similar lighting elsewhere in ComEd's service territory. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 32:624-28.

Accordingly, ComEd requests that the Commission reverse its prior decision directing use of the Chicago Method.

If the Commission nonetheless decides to retain the Chicago Method, ComEd offers two recommendations to improve it. First, the Chicago Method should not assume a zero cost for service connections, and such costs should be appropriately allocated to the Dusk to Dawn Lighting Delivery Class in ComEd's ECOSS. Second, the Chicago Method should also apply to alley lights, which are included in the customer class and connect to the same secondary distribution system as the arterial lights. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 47:1069-48:1083.

h. <u>Allocation of Illinois Electricity Distribution Tax</u>

ComEd's ECOSS, as well as both of its exemplar ECOSSs presented in this case, properly allocates costs associated with the Illinois Electricity Distribution Tax on the basis of kWh delivered because the Illinois Electricity Distribution Tax is imposed upon ComEd on the basis of kilowatt-hours delivered. ComEd Exs. 75.1, 75.2, and 75.3; Alongi Dir., ComEd Ex. 16.0 3rd Rev., 18:392-393. IIEC suggests that these costs should be allocated in a different manner. Stephens Dir., IIEC Ex. 2.0, 3:90-4:102, 25:584-26:599. The suggestion made by IIEC to allocate Illinois Electricity Distribution Tax costs as described by Mr. Stephens is inappropriate because it does not reflect the manner in which ComEd incurs the costs, and IIEC's suggested allocation of these costs should be rejected by the Commission. The manner in which ComEd allocated costs associated with the Illinois Electricity Distribution Tax in its ECOSSs is appropriate and should be approved by the Commission.

i. <u>Indirect Uncollectible Costs and Uncollectible Costs</u>

In the *RDI Order*, the Commission reaffirmed its decision in ComEd's last rate case directing ComEd to allocate uncollectible debt expense costs uniformly across residential classes. *RDI Order* at 80. ComEd's proposal complies with the Commission's directive to allocate uncollectible costs. Garcia Reb., ComEd Ex. 50.0, 8:180-84.

City of Chicago witness Bodmer argues that ComEd did not similarly allocate "indirect uncollectible costs of collecting, administering, managing, disconnecting, and reconnecting uncollectible accounts." Bodmer Dir., City Ex. 1.0, 63:1234-36. Mr. Bodmer's argument must be rejected for several reasons. First, while a similar proposal was made by the City of Chicago in the RDI proceeding, there were no express Commission decisions or directives regarding the allocation of these costs in the RDI Order. Second, Mr. Bodmer has not produced any evidence or study that identifies or defines what constitutes indirect uncollectible costs, nor has he explained why such costs are related to the uncollectible costs themselves. For example, there is no clear reason to differentiate the reconnection of service from an initial service connection. Garcia Reb., ComEd Ex. 50.0, 7:151-59. ComEd recommends that the Commission approve ComEd's proposed allocation of uncollectible costs in its ECOSS.

j. <u>**Customer Care Cost Allocation**</u>

Customer services or "customer care" costs encompass nearly every aspect of a customer's direct interaction with ComEd.[19] Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 5:111-6:117. Whether these costs should be recovered in delivery service rates or functionalized to supply and recovered from supply (and PORCB) customers turns on the sound application of the principle of cost causation. ComEd has undertaken a systematic examination of these costs and performed two distinct studies of the services that produce these costs. The first study has been denominated the "Switching Study" because it considers the impact on ComEd's costs of customers switching suppliers. Costs that are driven by the provision of delivery service should not change when customers look to an alternative supplier and are thus properly fully recovered in delivery charges. The Switching Study identifies these costs. ComEd has also performed a second study, denominated the "Allocation Study," aimed at splitting or apportioning between

[19] These costs include Field and Meter Services, billing and mail services, the Customer Contact Center, Large Customer Solutions, Revenue Management, payment processing, and customer relations, as well as costs related to back office support of these functions, such as project and support services, Information Technology, Demand Management, Electric Supplier Services, and Market Research. *Id.*

the two functions any costs properly attributable to both functions and that are thus deemed common costs. The principal issue with regard to ComEd's customer services costs in this case is whether the Commission should utilize the Switching Study – as supported by ComEd and Staff – or whether it should disregard the results of the Switching Study and instead turn to the Allocation Study – as supported by REACT.

Two additional issues are material only if the Commission rejects the switching study: (1) whether the proper pool of costs to apportion is the direct operating and maintenance ("O&M") costs that ComEd analyzed, or direct and indirect costs (the "total cost to serve" as described by REACT); and (2) whether to accept certain adjustments to ComEd's allocators as recommended by REACT. If the Commission adopts the Allocation Study, it should find that ComEd analyzed the correct pool of costs and reject REACT's proposed adjustments to the Allocation Study.

(i) <u>Allocation Study vs. Switching Study</u>

The Switching Study shows that, both now and in the near future, ComEd realizes virtually no cost savings when its supply customers switch to a retail electric supplier ("RES"). Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 1:18-2:27; ComEd Ex. 19.1. REACT for its part offered practically no criticism of the Switching Study other than to dismiss its results as "speculative." Merola Dir., REACT Ex. 2.0, 17:356-364; Merola Reb., REACT Ex. 5.0, 9:177-10:196. The Switching Study examined the impact on ComEd costs of 1%, 10%, and 100% customer switching to RES supply. With 1% of ComEd customers already taking service from a RES, there is nothing speculative about the 1% scenario. The other two scenarios, which come to similar results as the 1% scenario, only confirm that there will likely be no material reduction in ComEd costs as additional customers switch suppliers. Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 2:23-27; Garcia Supp. Dir., ComEd Ex. 24.0, 7:155-9:200.[20]

In evaluating whether to adopt the results of the Switching Study, the Commission should be mindful that ComEd as a delivery service provider is required to incur the costs of providing delivery service to each of its delivery customers, regardless of from whom the customer obtains its supply. Arbitrarily shifting costs to supply that are truly driven by the provision of delivery service understates the true costs of the delivery service that ComEd provides to customers, and thereby sends improper signals to both customers and the market. Garcia Supp. Dir., ComEd Ex. 24.0, 5:104-6:132, 7:155-8:165, 9:193-95.

The cost of providing metering services illustrates this point. Each customer receiving delivery service from ComEd is entitled to a meter provided by ComEd. Of course, that meter measures the amount of energy delivered by ComEd and also measures the amount of electric supply that customer uses. It is undisputed that 100% of the costs of metering are delivery service costs and none of those costs should be functionalized to supply. Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 6:122-7:141; Rukosuev Reb., Staff Ex. 28.0, 8:194-9:199, n.4; Merola Dir., REACT Ex. 2.0, 15:304-14. The logic of this is simple. When a customer taking supply service from ComEd switches to an alternative supplier, the costs that ComEd incurs in providing delivery service to this customer, such as the cost of the meter, are not reduced. Mr. Merola for REACT agreed with this proposition – that even though metering costs are attributable to both supply and distribution, metering costs should be assigned 100% to the delivery function because metering services "are provided by ComEd regardless of whether or

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[20] While the Switching Study shows no change to costs at 1% switching, it does project both increased and decreased costs at levels of 10% and 100%, with the increases offsetting the decreases, resulting in overall cost increases. ComEd Ex. 19.1.

not they provide the supply." Hearing Tr., 2008. In other words, as Mr. Merola agreed, "customers taking supply service from ComEd do not drive the level of ComEd's metering service costs." *Id.*, 2009.

Although Mr. Merola assumed that ComEd's other customer services costs – such as billing and payment processing – change when ComEd is not providing supply (*Id.*, 2008), the Switching Study shows that assumption to be inaccurate. Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 1:19-2:23, 10:229-11:239, 12:265-13:287, 15:321-16:345, 17:374-18:389, 19:414-28, 21:451-60, 22:483-23:492, 24:519-25:540, 26:558:65, 28:598-29:624; ComEd Ex. 19.1. As Staff witness Rukosuev stated:

> The Switching Study recognizes that the cost of providing customer care for unbundled customers is almost equal to the combined cost for bundled customers. … For example, for billing, the Company incurs almost identical costs in preparing, sending and processing bills for bundled and unbundled customers. (See ComEd Ex. 19.0 Revised, p. 12) In both cases, the meter must be read, the bill prepared and mailed, the payment received and processed.

Rukosuev Dir., Staff Ex. 12.0, 30:688-96.

Staff witness Rukosuev went on to note that "regardless of the number of customers switching, ComEd must incur the necessary costs to stand ready to serve them again due to ComEd's ongoing responsibility of default supply service provider for all customers." *Id.*, 31:727-32. The Switching Study also comports with the Commission's treatment of customer services costs in the past: as part of delivery services costs. Garcia Supp. Dir., ComEd Ex. 24.0, 3:64-4:69. Disregarding this logical approach "in favor of an arbitrary allocation between supply and distribution" would set an undesirable precedent for all Illinois utilities. Rukosuev Dir., Staff Ex. 12.0, 31:709-18.

As described in the Rate Design Section (specifically VIII.C.11.b), ComEd will be made whole however the Commission allocates responsibility for customer service costs. ComEd nonetheless supports the Switching Study because it more accurately captures the actual causation of ComEd's customer services costs.

(ii) Direct Operation and Maintenance (O&M) Costs vs. Total Costs

If the Commission agrees with both ComEd and Staff and finds that the Switching Study presents a more accurate picture of cost causation than the Allocation Study, the question whether to analyze direct O&M costs or "total costs" is immaterial because the answer has no real impact on the results of the Switching Study. In any event, ComEd identified the costs to be reviewed for purposes of the customer service studies as the 2009 direct O&M costs submitted in ComEd's June 30, 2010 rate case filing. Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 4:78-5:94. This is consistent with both the *RDI Order* and the treatment of ComEd's administrative supply costs in Rider PE – Purchased Electricity ("Rider PE"). Garcia Supp. Dir., ComEd Ex. 24.0, 4:70-5:103; Garcia Reb., ComEd Ex. 50.0, 11:253-258.[21] Thus, ComEd's analysis of direct O&M costs is appropriate and should be accepted by the Commission.

(iii) Adjustment of Allocation Study Allocators

If the Commission adopts the Switching Study, it will be unnecessary to address the issue of Mr. Merola's adjustments to ComEd's allocators. If, on the other hand, the Commission adopts the Allocation Study, the Commission should reject these results-driven adjustments. ComEd has acknowledged that the Allocation Study is based on assumptions that are not directly related to ComEd's actual operations. Donovan Reb., ComEd Ex. 48.0, 7:134-43. "While the allocators are admittedly imperfect, they are a reasoned attempt to determine a rational allocation

[21] Staff has stated that ComEd may have an incentive to inflate the supply rate, and therefore recovery of administrative costs in Rider PE should not include common costs otherwise allocable to supply. Garcia Supp. Dir., ComEd Ex. 24.0, 4:70-5:103. ComEd's analysis of only direct O&M costs (and not indirect administrative costs) is consistent with this approach. *Id.*

of costs." *Id.*, 7:139-40. However imperfect the allocators are, they are based upon the work functions of customer services and are more logical than Mr. Merola's arbitrary adjustments. *Id.*, 7:140-42.

Staff agrees with ComEd that Mr. Merola's proposed adjustments are unsupported and arbitrary, and have previously been rejected by the Commission. Rukosuev Reb., Staff Ex. 28.0, 14:324-16:379. Staff stated that utilizing Mr. Merola's adjustments would impose "an artificial distinction" that "pretends to give effect to cost causation where none exists." *Id.*, 16:384-85. Both ComEd and Staff therefore recommend that the Commission reject Mr. Merola's proposed adjustments to ComEd's allocation factors.

Indeed, Mr. Merola's proposed adjustments are admittedly REACT's latest attempt to reallocate "a significantly higher proportion of Customer Care Costs … to the supply function." REACT Pre-Hearing Memorandum at 10. In ComEd's 2007 Rate Case, REACT unsuccessfully proposed to reallocate exactly 40% of customer services costs to ComEd's supply function. Merola Hearing Tr., 1995-97; *see also* ICC Dkt. No. 07-0566, Merola Reb., REACT Ex. 7.0 Corr., 13:287-22:485; *Commonwealth Edison Co.*, ICC Dkt. No. 07-0566, Final Order (Sept. 10, 2008) at 207. Then, in the Rate Design Investigation, REACT unsuccessfully requested that 50% of customer services costs be removed from ComEd's distribution revenue requirement and shifted to ComEd's supply function. Merola Hearing Tr., 1997-2001; *see also* Merola Dir., REACT Ex. 2.0, 16:336-25:528; REACT Ex. 2.5 Corr.; ICC Dkt. 08-0532, Merola Reb., REACT Ex. 4.0 Corr., 9:173-76. The RDI Order properly concluded that REACT's suggested 50% functionalization factor was "arbitrary," thereby rendering REACT's study "almost useless." Merola Hearing Tr., 2000-01; RDI Order at 68. In this proceeding, REACT once again proposed adjustments amounting to arbitrary 50/50 splits between delivery and supply.

Merola Hearing Tr., 2001-03; *see also* Rukosuev Reb., Staff Ex. 28.0, 15:322-23. The Commission should once again reject these proposed adjustments.

In the event the Commission orders allocation of customer care costs to the supply function, provision must be made for ComEd's recovery of those costs. That subject is addressed in Section VIII.C.11.b of this brief.

k. <u>Other Docket No. 08-0532 Compliance Issues</u>

l. <u>Other Issues</u>

(i) <u>Utilization of Railroad Facilities</u>

In ComEd's 2007 Rate Case, the Commission directed ComEd, the Chicago Transit Authority ("CTA"), and the Northeast Illinois Regional Commuter Railroad Corporation ("METRA") to conduct an appropriate study to determine to what extent ComEd uses or needs Railroad delivery class facilities to serve other customers. 2007 Rate Case Order at 220. ComEd and the railroads agreed upon a study methodology that focused on a sample of 24 of the 71 railroad traction power facilities. The study showed that flows through railroad owned equipment to other ComEd customers do occur; the study did not show that the flows were necessary to serving customers under normal conditions or that restoration from power outages requires the railroad facilities. Hemphill Dir., ComEd Ex. 14.0 Rev., 24:486-25:496; *see also* ComEd Ex. 16.4. Based on that study, ComEd has proposed to reflect a cost allocation adjustment in the ECOSS that reallocates approximately $452,000 from the railroad classes to other classes. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 13:275-282.

ComEd does not normally make a cost allocation adjustment when a customer unilaterally operates its facilities in a way that makes it harder or easier for ComEd to serve other customers. However, four unique circumstances lead ComEd to propose a cost allocation adjustment for the Railroad delivery class. First, the Commission has directed that CTA and METRA receive special rate consideration. 2007 Rate Case Order at 223. Second, power is actually flowing through the railroads' equipment to serve other customers, rather than incidentally helping them or improving local conditions. Third, the systems serving the railroads were installed in cooperation with ComEd over several decades, and the installation of the equipment cannot be deemed unilateral. Fourth, the railroad equipment is constructed to utility standards and operated in a manner comparable to how a utility would operate it, which allows ComEd to make use of the equipment during contingency conditions. Hemphill Dir, ComEd Ex. 14.0 Rev., 25:499-26:521.

ComEd determined the appropriate cost allocation in a manner analogous to how it allocates cost for equipment that is used in a shared manner for service to ComEd retail customers and others. Due to the lack of precise data about the equipment's installation date and original owner, ComEd adopted a very favorable assumption for the railroads that the total costs equaled the costs that ComEd would incur to install 12kV busses and breakers on a completely undepreciated basis. Data is not available to reflect the numerous contingencies that could result in ComEd's use of railroad facilities to serve other customers, and use alone would not reflect the dependability and insurance created from the railroad's facilities. ComEd therefore estimated a usage ratio (the ratio of ComEd's use to serve other customers over railroad use) of 1/3 to determine the shared costs, which is almost certainly favorable to the railroads. Hemphill Dir., ComEd Ex. 14.0 Rev., 26:531-27:556.

The proposed adjustment would reallocate to other customer classes 1/3 of the annual carrying cost of the undepreciated investment that would be required for ComEd to install 12kV busses and breakers at locations equivalent to such railroad owned facilities located at the 71 railroad traction power substations. This formula led ComEd to propose a cost allocation adjustment of $452,000 from the Railroad delivery class to the other classes. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 13:264-67. ComEd asks the Commission to approve the adjustment.

D. Rate Moderation

Please see Section VIII C. 4. a.

VIII. RATE DESIGN

A. Overview

The issues of interclass revenue allocation and rate design must be placed in their proper perspective. Hemphill Rate Design Reb., ComEd Ex. 46.0, 6:133-34. The rate design portion of the case is not about determining ComEd's revenue requirement, but concerns the allocation of the revenue requirement among customer classes and rate elements. *Id.*, 6:134-36. This is a zero-sum (revenue neutral) process, with the objective of allocating the revenue requirement among customer classes in a manner that is fair to customers, while allowing for full recovery of these revenues. *Id.*, 6:136-7:138. If one customer class does not pay its fair share of costs, another customer class ultimately must pay those costs, which results in a subsidy. *Id.*, 7:138-40.

ComEd proposes to apportion costs using the Commission's preferred embedded cost approach to minimize interclass rate subsidies. *Id.*, 7:141-43. In making decisions concerning interclass revenue allocation and rate design, ComEd sought to balance the interests of all customers that receive services and pay Commission-approved rates. *Id.*, 7:143-45.

In its initial filing, for most non-residential rate classes ComEd proposed rates using the same rate design methodology employed in its last rate case, Docket No. 07-0566, ("proposed rate design"). See, e.g., Alongi Dir., ComEd Ex. 16.0 3rd Rev., 27:502-29:536; Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 4:97-104; ComEd Ex. 73.1. Pursuant to the RDI Order, ComEd submitted, among other things, an exemplar rate design and exemplar tariff revisions that would be implemented in the event the Commission directs ComEd to create a Primary Voltage Delivery Class ("exemplar rate design"). Alongi Supp. Direct, ComEd Ex. 21.0 2nd Rev., 15:189-16:217; ComEd Ex. 21.3; Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 4:107-5:118; ComEd Ex. 73.2. In response to certain concerns raised during the proceeding, ComEd submitted an alternative exemplar rate design in which the demand-based nonresidential classes are subdivided to incorporate certain charges for service points to which electricity is delivered above a certain threshold ("alternative exemplar rate design"). Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 6:141-49; Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 5:119-29; ComEd Ex. 73.3. The three rate designs differ mainly in their recovery of the costs of the primary distribution system. ComEd's preferred rate methodology for most non-residential customer classes would incorporate a differentiation in recovery of the costs of ComEd's primary and secondary distribution systems, as called for by prior Commission orders. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 3:68-70, 31:578-81; ComEd Ex. 16.5.

For residential and small general service or watt-hour customer classes, ComEd is proposing a rate design that properly reflects fixed and variable delivery service costs. Hemphill Dir., ComEd Ex. 14.0 Rev., 4:81-82. Those delivery services costs that vary with a customer's short-term use should be recovered through use and demand charges that vary each period. *Id.*, 4:82-84. Those costs that do not so vary should be recovered through fixed charges. *Id.*, 4:84-85. ComEd is proposing rates that accomplish this gradually over three years in a revenue neutral way, without any change in its total revenues. *Id.*, 4:85-86.

Although various customers and customer groups propose to shift costs to other customer classes to reduce their own rates, ComEd seeks to set delivery service rates on traditional cost-causation and other rate design principles to ensure that all customers will pay their fair share for delivery service. *Id.*, 7:156-8:190. Accordingly, ComEd asks the Commission to approve its proposed interclass allocation and rate design. *See, e.g.*, ComEd Ex. 73.1.

B. <u>Potentially Uncontested Issues</u>

1. <u>High Voltage Rate Design Simplification</u>

ComEd proposes to simplify rate design for the High Voltage Delivery Class as follows: (1) for both the customer charge and the standard metering service charge, the six possible charges would be reduced to a single customer charge and a single standard metering service charge (Alongi Dir., ComEd Ex. 16.0 3rd Rev., 14:289-93); (2) with respect to the distribution facilities charges ("DFCs"), the five possible standard voltage DFCs would be reduced to a single DFC for all load provided at voltages entering customer premises below 69 kV (*Id.*, 14:293-95); and (3) for all load provided at voltages entering the customer premises at or above 69 kV, there would continue to be two DFCs, one applicable if the customer's highest thirty minute demand in the past twelve monthly billing periods exceeded 10 MW and the other applicable if the customer's highest thirty minute demand in the past twelve monthly billing periods did not exceed 10 MW (*Id.*, 14:295-300). No party objected to these proposals. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 21:480-82; *see also* Stephens Dir., IIEC Ex. 2.0, 9:234-35. ComEd's proposal is reasonable as well as unopposed and should be approved. *See* Alongi Dir., ComEd Ex. 16.0 3rd Rev., 14:289-16:343.

2. <u>Rate MSPS</u>

ComEd proposed changes to certain charges under Rate MSPS – Metering Service Provider Service ("Rate MSPS"), applicable where a retail customer elects to be provided metering service from a metering service provider ("MSP"). *See* ComEd Ex. 16.22 Rev., ILL. C.

C. No. 10, 1st Revised Sheet Nos. 99-101. ComEd Ex. 16.12 Revised shows how the charges in Rate MSPS were determined. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 4:87-89.

Staff witness Harden recommends that the increases for Meter Reading Charges, and charges to read additional meters or for special exchanges, be limited to 50%. Harden Dir., Staff Ex. 11.0, 34:703-07. Ms. Harden also recommends an increase in the amounts charged to read the first meter and any additional meters or special exchanges. *Id*., 34:707-10. ComEd has accepted Staff witness Harden's recommendation to limit the increase in these fees to 50%. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 57:1279-81.

Staff witness Rockrohr recommends additional language for Rate MSPS to eliminate any ambiguity related to the equipment removal charges. Rockrohr Dir., Staff Ex. 6.0, 12:277-14:316. ComEd has agreed to make clarifying revisions to address Mr. Rockrohr's concern. Alongi Reb., ComEd Ex. 41.0, 2:39-3:47; ComEd Ex. 41.1. Neither Mr. Rockrohr nor any other party objected to the amendments reflected in ComEd Ex. 41.1. Alongi Sur., ComEd Ex. 68.0, 2:29-35.

ComEd's proposed changes to certain charges in Rate MSPS, as modified in this proceeding, are reasonable, unopposed and should be approved.

3. <u>General Terms and Conditions</u>

a. <u>New Customers with load that includes motors equal or greater than five horsepower</u>

ComEd proposed to revise the General Terms and Conditions ("GTC") to clarify that when a customer has load that includes motors equal to or greater than five horsepower, a 3-phase voltage is provided as standard. ComEd Ex. 16.22, 1st Revised Sheet No. 169. Staff witness Rockrohr recommends inclusion of a "grandfather provision" that states ComEd will not require existing single-phase customers with single-phase five horsepower motors to convert their electrical entrance equipment to receive 3-phase. Rockrohr Dir., Staff Ex. 6.0, 14:318-15:349. Although ComEd believes appropriate clarifying language is already included in the revisions to GTC proposed by ComEd in its June 30, 2010 filing, ComEd has made additional clarifying tariff revisions as shown in ComEd Ex. 41.2. Alongi Reb., ComEd Ex. 41.0, 3:56-63. Neither Mr. Rockrohr nor any other party objected to the amendments reflected in ComEd Ex. 41.2. Alongi Sur., ComEd Ex. 68.0, 2:29-35.

4. Miscellaneous Charges and Fees

ComEd proposed to change the following miscellaneous charges and fees: (1) Single Bill Option Credit; (2) Interval Data Fee; (3) Direct Access Service Request (DASR) Fees; (4) Nonstandard Switching Fee; (5) Off-Cycle Termination Fee; (6) Metering Service Provider Service (MSPS) Fees; (7) Cable Television (CATV) Power Supply Test Fee; (8) Duplicate Information Fee; (9) Invalid Payment Fee; (10) Reconnection Charge; and (11) Meter Lease Charge. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 34:653-36:663.

Staff witness Harden recommends approval of ComEd's proposed change to the Single Bill Option Credit. Harden Dir., Staff Ex. 11.0, 5:95-6:112. With respect to the Off-Cycle Termination Fee, the CATV Fee, the Duplicate Information Fee, the Invalid Payment Fee, the Reconnection Charge, the Meter Reading Charges, the Nonstandard Switching Fee, and the Split Load DASR Fees, Ms. Harden recommends the proposed increases in those fees be reduced by 50% and that corresponding adjustments be made to ComEd's revenue requirement. *Id.*, 3:61-4:78. ComEd has accepted Staff witness Harden's recommendation in both respects. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 57:1279-81.

Based upon its analysis in connection with this proceeding and discussions with Staff and RESA, ComEd has updated its calculation regarding the Interval Data Fee. Alongi Sur., ComEd

Ex. 68.0, 5:90-102; ComEd Ex. 68.1. In particular, ComEd proposes an Interval Data Fee of $3.45 per meter, which is appropriate based upon the costs of providing interval data for each meter on a customer's account and which coincides with the per meter fee proposed in the rate design rebuttal testimony of Staff witnesses Harden and Clausen. Alongi Sur., ComEd Ex. 68.0, 5:94-101. The updated calculation of the Interval Data Fee is different than the $3.32 per meter fee proposed by Ms. Harden and Mr. Clausen in rebuttal testimony (Staff Exs. 27.0 and 30.0) because it reflects the fact that Staff witness Pearce has withdrawn her proposed adjustment for ComEd's Annual Incentive Plan ("AIP") as discussed in the surrebuttal testimony of ComEd witness Trpik (ComEd Ex. 54.0). Alongi Sur., ComEd Ex. 68.0, 5:96-100. Accordingly, ComEd did not remove the AIP component from the calculation of the Interval Data Fee. *Id.*, 100-01.

For the reasons discussed in this section and elsewhere in this brief, ComEd's proposed changes to certain miscellaneous charges and fees should be approved.

5. <u>Meter Lease Charges</u>

ComEd proposed revisions to Rider ML – Meter-Related Facilities Lease ("Rider ML"), which update meter lease charges and simplify the manner in which meter leases are administered. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 36:665-39:738. No party objects to ComEd's proposal. This proposal is reasonable and should be approved.

6. <u>Residential Real Time Pricing Program Costs</u>

ComEd proposed (a) a change in the recovery of costs associated with its residential real time pricing program ("RRTP") in Rider RCA – Retail Customer Assessments ("Rider RCA") that would reduce the charge from $0.14 per month to $0.05 per month and (b) to eliminate the $2.25 monthly participation fee for the first 110,000 customers taking service under rate RRTP.

Garcia Dir., ComEd Ex. 23.0, 20:423-21:449; ComEd Ex. 23.2. ComEd updated the calculation of this charge to include the cost of meter exchanges related to the real time pricing program that was inadvertently omitted from the original calculation set forth in ComEd Ex. 23.2. Garcia Reb., ComEd Ex. 50.0, 12:278-82; ComEd Ex. 50.4. While the addition of meter exchange cost did not cause a change (increase) in the proposed charge for the recovery of the costs associated with the RRTP program ($0.05), ComEd noted the update so that it is clear in future proceedings what costs are being recovered from residential customers to fund the program. *Id.*, 12:282-13:286.

Staff witness Harden recommended approval of ComEd's proposed reduction to this charge from $0.14 per month to $0.05 per month provided that the Commission approves Staff witness Dr. Schlaf's recommendation regarding the termination of the monthly $2.25 participation fee. Harden Dir., Staff Ex. 11.0, 38:800-40:827. Staff witnesses Harden and Schlaf raise no other issues with respect to ComEd's proposals as updated. *See*, *e.g.*, Harden Reb., Staff Ex. 27.0; Schlaf Reb., Staff Ex. 31.0.

7. Standard Meter Allowances

The Standard Meter Allowances used in the simplified manner in which meter leases are administered were changed to adjust for the identification of additional customers eligible for the exemplar Primary Voltage Delivery Class and to correct an error as to the number of customers in the Extra Large Load Delivery Class. Alongi Reb., ComEd Ex. 49.0, 59:1312-17. No party objected to ComEd's proposal. This proposal is reasonable and should be approved.

C. **<u>Potentially Contested Issues</u>**

1. **<u>SFV</u>**

a. **<u>ComEd's Proposal</u>**

ComEd witness Hemphill testified that the single most important step in bringing ComEd's rate design in line with its costs is to properly align the fixed and variable portions of ComEd's delivery rates with the fixed and variable costs ComEd incurs to provide delivery service. Hemphill Dir., ComEd Ex. 14.0 Rev., 8:177-81. This is accomplished by moving towards an SFV rate design. *Id*., 8:181-9:182. The SFV rate design, as proposed by ComEd, pertains only to residential customers and nonresidential customers in the Watt-Hour Delivery Class and establishes fixed and variable charges that track the fixed and variable costs of serving those customers. *Id*., 9:182-84, 12:239-41. In an SFV design, distribution costs are first classified as fixed or variable. *Id*., 14:292-93. Fixed costs, which do not vary from billing period to billing period based on monthly energy use, are collected through charges (such as the customer charge and the standard metering service charge) that also do not vary with energy use. *Id*., 14:293-95. Those delivery costs that do vary with a customer's energy use are recovered though charges that also change with the customer's energy use (such as the proposed Illinois Electricity Distribution Tax Charge ("IEDT")). *Id*., 14:295-98.

Failing to properly make the distinction between fixed and variable costs results in misallocations of costs. *Id*., 12:248-50. Charges to individual customers are further distorted as their consumption patterns change, because changes in their bills would not reflect actual changes in cost of service. *Id*., 12:250-52. The current rate structure recovers an inordinate proportion of fixed costs through rates that are not fixed, but that vary with volume. *Id*., 12:252-53. This sends a distorted price signal to customer and penalizes utilities for implementing conservation programs. *Id*., 12:252-58.

ComEd proposed that the delivery service rate design for the residential delivery classes and the Watt-Hour Delivery Class move toward SFV in a manner similar to that approved for other delivery utilities. *Id.*, 14:290-92. Dr. Hemphill concluded that the Commission should approve ComEd's proposal to gradually move to an 80% SFV because that proposed rate design more closely reflects the correct division between fixed and variable costs. Hemphill Rate Design Reb., ComEd Ex. 46.0, 9:206-09.

Staff witness Boggs raised several concerns about ComEd's SFV proposal. Boggs Dir., Staff Ex. 13.0, 16:294-27:541. Dr. Hemphill refuted these concerns and noted that Mr. Boggs' positions were either arbitrary or inconsistent with ratemaking principles. Dr. Hemphill also pointed out that Mr. Boggs' positions are contrary to recent Commission decisions to either decouple or move toward an SFV in rate cases filed by North Shore/Peoples Gas, the Ameren Illinois Companies ("Ameren"), and Nicor Gas Company ("Nicor Gas"), all of which recognize the importance of recovering fixed costs predominantly through fixed charges. Hemphill Rate Design Reb., ComEd Ex. 46.0, 9:215-10:241. In direct testimony, Dr. Hemphill discussed the Commission's Orders in recent cases involving the Ameren and Nicor Gas, where the Commission adopted SFV rate designs recovering 80% of fixed costs in fixed customer charges. Hemphill Dir., ComEd Ex. 14.0 Rev., 13:266-14:287. Dr. Hemphill also presented extensive testimony refuting various concerns about the proposed SFV rate design raised by City of Chicago witness Bodmer, NRDC witnesses McDermott and Cavanagh, and AG-CUB witness Rubin. *Id.*, 10:242-26:588.

The evidence demonstrates that a SFV rate design is appropriate for ComEd because it more closely aligns fixed and variable prices to effectuate cost recovery with the correct division between fixed and variable costs. Accordingly, the Commission should approve ComEd's proposal in this proceeding to gradually move to an 80% SFV rate design for all residential customers and nonresidential customers in the Watt-Hour Delivery Class.

If the Commission were to approve Staff's proposed downward adjustment of between 20 and 32 basis points to ComEd's return on equity while approving an SFV rate design for ComEd, then ComEd would have to reconsider its support for SFV. For example, if the Commission approves a 32 basis point reduction in ComEd's return on equity as the "price" of approving the SFV proposal, and if that 32 basis point reduction takes ComEd below the return on equity supported by Dr. Hadaway's analysis, then ComEd cannot afford the SFV rate design and, under such circumstances, will withdraw the proposal. *See, e.g.*, Tierney Reb, ComEd Ex. 39.0, 6:114-13:288; Tierney Sur., ComEd Ex. 64.0. Therefore, if the Commission concludes, after considering all the evidence and despite ComEd's objection, that such an ROE reduction would be warranted, the Commission should instead decline to adopt SFV rates at this time.

b. Decoupling (NRDC Proposal)

There was also testimony that a revenue decoupling rate design should be considered as an alternative means to SFV of eliminating or significantly weakening the link between the revenue of a utility and the utilization of its system by customers. For example, NRDC witness Cavanagh offered a decoupling proposal as an alternative to ComEd's SFV proposal. *See, e.g.*, Cavanagh Dir., NRDC Ex. 2.0. ComEd addressed the merits and the shortcomings of the NRDC proposal in testimony (*see* Hemphill Rate Design Reb., ComEd Ex. 46.0, 22:499-26:588), and also provided additional information for the Commission's consideration with respect to the issue of decoupling (Lowry Reb., ComEd Ex. 47.0; ComEd Ex. 47.2). While ComEd believes that SFV is a superior solution, it did offer a sample tariff reflecting Mr. Cavanagh's proposal to ensure that the NRDC proposal, if approved, is implemented in a way that is consistent with

ComEd's other tariffs. Hemphill Rate Design Reb., ComEd Ex. 46.0, 25:569-72; ComEd Ex. 46.2.

2. <u>Class Definitions</u>

a. <u>Residential Rate Design – Consolidation of Classes</u>

ComEd proposes to reduce the number of residential delivery classes from four to two. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 16:345-17:372. First, ComEd proposes to combine the two single family delivery classes into one class: the Residential Single Family Delivery Class. *Id.* Second, ComEd proposes to combine the two multi-family delivery classes into one class: the Residential Multi Family Delivery Class. *Id.* In doing so, ComEd proposes to have one DFC for all single family customers and one DFC for all multi-family customers. *Id.* The effect of this proposed change is to eliminate separate rates for those customers with electric space heat and those without electric space heat. *Id.* This change is reflective of the fact that the cost of delivering electricity is not affected in any way by whether the electricity is used for space heating or anything else. *Id.*, 17:363-68; Section VII.C.1.a.i. of this Brief. ComEd's proposal is reasonable and should be adopted.

ComEd demonstrated that designing electric delivery service rates based on the end use of electricity by customers - such as for space heat - is inappropriate, because it requires ComEd to, among other things, police the use of electricity within customers' homes (or businesses, as the case may be) for billing purposes. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 17:359-63. Moreover, the Commission has already taken steps to eliminate the distinction between residential customers with electric space heat and those without electric space heat. Specifically, the Commission approved Rider PE – Purchased Electricity ("Rider PE"), which has specific grandfather provisions. Docket No. 05-0159. Under Rider PE, separate supply charges for electric space heat are applicable only to residential customers (and their successors) who were eligible on January 1, 2007, to take service under ComEd's then effective residential electric space heat rate (ILL. C. C. No. 10, Rider PE Original Sheet No. 322). Those charges are not applicable to any residential customer whose home was either was built on or after January 2, 2007, or had electric space heating facilities installed for the first time on or after January 2, 2007. Because electric space heat customers were being provided with a significant subsidy, rather than implementing a flash-cut, this grandfathering approach allows for a gradual movement toward cost-based rates for customers with electric space heat. This is consistent with the Commission's rulings over many years to phase-out end-use rates for governmental buildings, schools, nonresidential electric space heating, pumping and sewage treatment facilities, and residential and nonresidential electric water heating. Alongi Rate Design Reb. ComEd Ex. 49.0 Rev., 12:267-286.

Staff witness Boggs finds reasonable ComEd's proposal to consolidate the four residential delivery classes into two and thereby eliminate delivery rate distinctions between space heat and non-space heat customers. Boggs Dir., Staff Ex. 13.0, 31:615-16. However, Mr. Boggs voiced concern about the elimination of separate supply charges for residential customers with electric space heat and recommends the consolidation of the four residential delivery classes at this time as long as the Commission does not order ComEd to eliminate the differentiation in supply charges in this proceeding. *Id.* 34:680-85. Staff witness Clausen recommends that the Commission initiate a separate proceeding to investigate ComEd supply charges. Clausen Dir., Staff Ex. 14.0, 2:29-39. ComEd agrees with these recommendations of Mr. Boggs and Mr. Clausen. Alongi Reb., ComEd Ex. 49.0 Rev., 13:289-92.

AG/CUB argues to preserve the current four residential delivery classes "because of significant differences in the usage characteristics and the cost of serving each type of customer." Rubin Dir., AG/CUB Ex. 6.0, 3:55-58, 42:854-56. . As noted in Section VII. C. 1. a. i. of this Initial Brief, the AG/CUB's claim conflicts with positions that the AG presented in a prior ComEd rate case. *See, e.g.*, Docket No. 05-0597, Order (July 26, 2006) at 180.

Further, the phase-in of the SFV proposal results in a significant reduction in revenue obtained through the application of the volumetric per kWh DFC charges and eliminates meaningful distinctions between distribution rates for customers with and without electric space heat, thereby obviating any rationale for maintaining separate delivery classes for customers with electric space heat. Alongi Dir. ComEd Ex. 16.0 2nd Rev. 17:368-372. Consequently, AG/CUB's position in this proceeding that the current four residential delivery classes should be maintained should be rejected.

Moreover, if AG/CUB's proposal to use a single NCP for the residential sector for cost allocations in the ECOSS were to be adopted (despite the directions provided in the PUA and 83 Ill. Admin Code 285.5110, as described in Section VII. C. 1. a. i. of this Initial Brief), consistency would require that there be only one DFC applicable to all residential customers. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 13:279-15:328.

b. <u>New Primary Voltage Delivery Class vs. Primary Subclass Charges</u>

ComEd's proposed nonresidential delivery classes account for voltage differences in that they include a delivery class for customer premises at which electricity is delivered at or above 69 kV. ComEd Ex. 16.22 Rev., 3rd Revised Sheet No. 64. In addition, all nonresidential customers in demand-based delivery classes for customers that establish demands in excess of 400 kW are considered to be primary voltage customers as provided in ComEd's primary/secondary analysis used to prepare the ECOSS for ComEd's proposed rate design. ComEd Ex. 16.5. ComEd's proposed rate design also provides for a rate reduction for customers that provide their own transformation through the application of a credit under Rider ACT – Allowance for Customer Owned Transformers ("Rider ACT"). ComEd Ex. 73.1; *see also* Alongi Tr. 1/19/11, 2115. These provisions of ComEd's proposed rate design are reflective of Commission directives in the RDI Order and prior Commission Orders regarding how nonresidential customers should be classified. ComEd's proposed nonresidential delivery classes and charges are reasonably defined, take ComEd's historical rate design into account, are reflective of cost causation, and should be approved by the Commission.

While it is not ComEd's proposal, ComEd submitted an Exemplar Rate Design to provide for the institution of a Primary Voltage Delivery Class. ComEd Ex. 21.1. The Exemplar Rate Design was subsequently revised and submitted as ComEd Ex. 73.2. Should the Commission direct ComEd to institute a Primary Voltage Delivery Class, then ComEd's preferred Exemplar Rate Design set forth in ComEd Ex. 73.2 should be adopted. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 5:113-117.

ComEd also prepared an alternative exemplar rate design, in which the existing demand-based nonresidential classes are subdivided to incorporate DFCs and transformer charges for service points to which electricity is delivered at or above 4 kV but below 69kV. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 6:142-49. As such, the alternative exemplar rate design does not create a new delivery class. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 24:531. ComEd does not support this alternative because customers who receive primary voltage without transformation are similar in terms of the facilities required to provide service. Alongi Reb., ComEd Ex. 49.0 Rev., 6:152-55; Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 25:543-26:566. Furthermore, ComEd identified a number of problems with creating multiple primary voltage DFCs within the five demand-based delivery classes. *Id.*, 7: 156-69. Thus, if the Commission directs ComEd to establish a rate for customers taking service from only ComEd's primary distribution system, then a single class of service for primary customers is appropriate, as set forth in ComEd's preferred Exemplar Rate Design. ComEd Ex. 73.2.

3. Non-Residential

a. Movement Toward ECOSS Rates

(i) Extra Large Load, High Voltage Customer Classes

ComEd's proposed rates reflect the next step in a Commission-directed progression towards charges that reflect the cost of service. As the Commission noted during ComEd's 2007 rate case, the DFCs for non-residential customers in the Extra Large Load ("ELL"), High Voltage ("HV"), and Railroad delivery classes are set at levels that result in significant under recovery of the costs necessary to serve them, and ComEd must therefore over-recover from other nonresidential customer classes to meet ComEd's revenue requirements.[22] Alongi Dir., ComEd Ex. 16.0 3rd Rev., 12:243-45. In that proceeding, the Commission ordered ComEd to move these customer classes 25% towards cost of service. 2007 Rate Case Order at 213.

ComEd now seeks to undertake the second step of that process with a 33% movement from the current DFCs of the ELL and HV delivery classes towards cost based DFCs. This would follow the 25% movement ordered by the Commission as the first step. This 33% movement simply reflects the fact that there are now only three steps left. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 6:150-7:162. ComEd's proposal is consistent with the

[22] The customer charges and standard metering service charges have already been set at cost based levels, so the only charges that needed to be moved toward cost based rates are the DFCs. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 6:153-56.

Commission's long standing goal of assigning cost to cost causers. However, ComEd's proposal also reflects the Commission's concerns regarding rate shock by applying the principle of gradualism. Hemphill Rate Design Reb., ComEd Ex. 46.0, 27:616-21; Alongi Dir., ComEd Ex. 16.0 3rd Revised, 12:247-53 (citing Order, Docket No. 07-0566, Sept. 10, 2008 ("2007 Rate Case Order") at 213).) The four-step process toward cost-causation for the ELL and HV delivery classes reflects both of those principles, cost-causation and gradualism. ComEd's proposed mitigated rates for the ELL and HV delivery classes provide for movement toward costs based rates in accordance with previous direction provided by the Commission and should be approved.

(ii) <u>Railroad Customer Classes</u>

The Commission has also given special attention to the Railroad Delivery Class and expressed that this particular class should not face rate shock due to public interest considerations. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 9:212-15; Hemphill Rate Design Sur., ComEd Ex. 71.0, 8:181-9:184. ComEd has therefore proposed a ten-step process to move the Railroad Delivery Class to cost of service in order to mitigate the effects of rate shock. Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 8:197-9:201. IIEC disagrees with this proposal for the Railroad Delivery Class. Stephens Dir., IIEC Ex. 2.0, 6:156-59. IIEC suggests that the DFC for Railroad Delivery Class should be treated in the same fashion as the Extra Large Load and High Voltage Delivery Classes. *Id*. Staff also disagrees with ComEd's proposal and proposes a more aggressive movement toward cost-based rates for the Railroad Delivery Class. Boggs Dir., Staff Ex. 13.0, 9:166-12:210. Under ComEd's proposal, rates for the Railroad delivery class reflect a 10% movement towards cost-based rates. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 9:209-12. ComEd's proposed mitigated rates for the Railroad Delivery Class provide for movement toward cost-based rates in accordance with previous

Commission direction and should be approved. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 10:222-26.

b. Allocating Secondary Costs Among Customer Classes

Please see Section VII.1.b. of this Initial Brief.

c. Railroad customers - Utilization of Railroad Customers' Facilities

Please see Section VII.C.1.l.i. of this Initial Brief.

d. Dusk to Dawn Street Lighting

The delivery service rate design for the Dusk to Dawn Lighting Delivery applies delivery service rates on a per kWh basis. It is notable that the proposed rates for this class provide for a reduction of over 50% in the delivery service charges paid by this class. ComEd Ex 73.1. As directed by the Commission, ComEd made cost allocation adjustments that reallocate certain secondary costs from the Dusk to Dawn Lighting Delivery Class to other customer classes. As a result of (i) the Chicago Method adjustments to certain secondary costs (*see* Section VII C 1 g of this Initial Brief) and (ii) the use of CP factors to allocate costs of primary distribution lines and substations (Section VII C 1 d. of this Initial Brief), the delivery charges applicable to the Dusk to Dawn Lighting Delivery Class would decrease by 52.8% under ComEd's proposed rates. ComEd Ex 73.1. The significantly reduced rates would leave only the High Voltage Delivery Class paying a lower overall average per kWh rate than Dusk to Dawn Lighting Delivery Class. Furthermore, these rates would likely be one of the lowest for similarly categorized customers across the nation. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 19:431-20:466.

4. **Collection of Illinois Electricity Distribution Tax**

ComEd proposes to modify its rate design to provide a separate volumetric charge for the recovery of the Illinois Electricity Distribution Tax ("IEDT") and uncollectible costs associated with the application of the tax. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 18:388-90. The IEDT would be collected as a separate line item on customer bills. The Commission already has approved a similar allocation methodology for recovery of the IEDT in the recent Ameren rate cases. *Central Ill. Light Co., et al.*, Docket Nos. 09-0306 (cons.), Order dated Apr. 29, 2010("Ameren Order") at 243; *see also* Heintz Reb., ComEd Ex. 51.0, 6:129-32; Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 18:406-10. Further, Staff agrees that ComEd's proposal is reasonable.

ComEd seeks to recover the IEDT in the same manner that this tax is imposed on ComEd itself - on the basis of total kilowatt-hours delivered. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 18:392-94. The proposed change would have no impact upon residential, watt-hour, and lighting customers because costs associated with the IEDT are already recovered through per kWh DFCs for these customers. *Id.*, 19:401-03. However, no per kWh charge exists for delivery service for demand-based nonresidential delivery classes. The tax instead is currently recovered through *per kW* DFCs for these classes. Accordingly, low load factor customers are currently subsidizing the high load factor customers with respect to recovery of this tax from these customers. ComEd's proposed recovery of the IEDT associated with these customers would eliminate this intraclass subsidy. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 17:382-90.

In the Ameren rate cases, the Commission reviewed the legislative history of the Public Utilities Revenue Act ("PURA") and determined that the General Assembly intended "to replace the invested capital/plant in service tax with a kWh tax in response to the changing nature of the Illinois electric utility industry." Ameren Order at 243. The legislature was anticipating that vertically integrated utilities like ComEd and Ameren might shed their generation assets (a significant part of plant in service), an event that has, in fact, occurred. Recognizing this point the Commission further stated that "[t]Accordingly, the Commisison should approve ComEd's proposal for the same reasons articulated in its Ameren Order.

5. Distribution Loss Factors

No electric distribution system can be fully efficient, and an inevitable consequence of electricity flowing through a system is distribution system losses. Thus, Distribution Loss Factors ("DLFs") are calculated for each delivery class to account for losses that occur in delivering electricity to customers across ComEd's distribution system. DLFs are used to determine the amount of electricity that must be procured for a retail customer in accordance with the formula provided in Rate RDS – Retail Delivery Service ("Rate RDS"). Alongi Dir., ComEd Ex. 16.0 3rd Rev., 40:747-51.

ComEd has conducted its distribution system loss study using accepted engineering principles and the most accurate data practically available to determine the extent of these losses so that they can be used when determining customer needs and the amount that must actually be distributed. Donnelly Dir., ComEd Ex. 8.0, 64:1369-65:1382. The distribution losses were determined by subtracting the energy delivered to retail and wholesale customers plus transmission losses from the ComEd Zone Load, which is the summation of the net output of all generators within the ComEd Zone plus net transmission interchange. ComEd Ex. 67.1 Rev., p. 2.

During this proceeding, ComEd has adjusted its distribution system loss study and DLFs in several ways to improve the allocation of energy losses to the customer classes:

- ComEd modified the assignment of secondary and service losses to certain classes to reflect the material energy losses in the service conductors.
- ComEd also excluded the Dusk to Dawn Lighting Delivery Class when reconciling its value for peak losses because the peak load reconciliation used in the loss analysis employs the coincident loss for all classes and it would be inappropriate to include the non-coincident class peak of the Dusk to Dawn Lighting Delivery Class in this calculation.
- The distribution system loss study was amended where certain retired transformers had been included in the total calculation and some new installations had been omitted.
- ComEd updated the allocation of losses in 138-69kV transformers to the High Voltage Electric Service Station ("HVESS") class. Born Reb., ComEd Ex. 34.0, 7:152-9:191.
- The distribution system loss study was amended to recognize that customers metered at 138kV and higher that have no material distribution losses because there are no step-down transformers or significant conductor losses between the transmission system and the meter location and that that the average of no load and full load percentages for HV ESS and 138-60 TSS transformers be calculated as MVA weighted averages. Born Sur., ComEd Ex. 67.0, 2:38-3:59.

ComEd also adopted the most recent data related to transmission losses. Transmission losses are those losses assessed for power system components that are classified as transmission in accordance with Federal Energy Regulatory Commission ("FERC") regulations. ComEd utilized the magnitude of transmission losses as a factor to determine distribution losses. The most recent analysis of ComEd transmission losses is contained in a 1998 report, according to which annual energy losses are 1.6% of the transmission load. The magnitude of transmission losses was determined by multiplying 1.6% by the total energy delivered plus distribution losses. Though the transmission loss study is somewhat dated, it is imperative to consider the existing factor for transmission losses in the distribution loss study because ComEd must remain consistent with the manner transmission losses are allocated at the FERC level. A new transmission loss study requires significant time, labor, and resources to complete, and ComEd plans to complete an update of the study by the end of 2011. Born Reb., ComEd Ex. 34.0, 6:114-7:147.

ComEd recognizes that updated data as to transmission losses and other indicators of distribution losses will allow for a more accurate class load study. Under the particular circumstances in this proceeding, ComEd does not object to filing a tariff revision to reflect updated distribution loss factors as recommended by Staff (Rockrohr Reb, Staff Ex. 21.0, 19:397-402), but the Commission should authorize in its order that any change in DLFs used for determining charges should be made concurrently with the corresponding change in transmission losses. The Commission should also authorize ComEd to update its class load study, which must be reflected in an updated ECOSS and possibly changes to rate design. Alongi Non-Rate Design Sur., ComEd Ex. 68.0, 7:134-47.

The Commission should further authorize ComEd to file revisions of other charges (such as Purchased Electricity Charges) for informational purposes that are affected by changes in distribution and/or transmission loss factors. Finally, the Commission should authorize ComEd to apply the revised charges affected by such updates in DLFs in the next monthly billing period after such revised tariffs and information sheets become effective. Alongi Non-Rate Design Sur., ComEd Ex. 68.0, Alongi 7:147-54.

With Respect to REACT's proposal to require ComEd to update DLFs annually, ComEd urges the Commission to reject such a proposal because of the sizeable efforts necessary in updating distribution losses. Such efforts would unnecessarily complicate and burden the rate setting process for what would likely be small changes in the values of the DLFs. Alongi Rate Design Sur., ComEd Ex. 73.0, 40:894-903.

6. <u>General Terms and Conditions</u>

a. <u>Residential Service Station (Ownership of Non-Standard Residential Connections)</u>

In its direct case, ComEd proposed to add one word, "pole", to an existing section of General Terms and Conditions describing responsibilities for installation of a Residential Service Station (ILL. C. C. No. 10, 1st Revised Sheet No. 165) to further clarify ComEd's existing practice that the residential customer "must furnish, install, own and maintain the remainder of the overhead primary service connection including the first support on private property" that already exists in ComEd's General Terms and Conditions (ILL. C. C. No. 10, Original Sheet No. 160). Alongi Sur., ComEd Ex. 68.0, 2:42-3:48.

Staff witness Rockrohr recommends that ComEd somehow "assume" ownership of certain non-standard customer-owned facilities used to bring power from the ComEd system into privately owned residential property. Rockrohr Dir., Staff Ex. 6.0, 16:351-20:454; Rockrohr Reb., Staff Ex. 21.0, 12:258-13:275. ComEd responded with evidence of several reasons why Mr. Rockrohr's proposal is problematic. Alongi Reb., ComEd Ex. 41.0, 4:87-5:108. First, the revision proposed in ComEd's General Terms and Conditions is merely further clarifying long-standing terms and service policy for such residential customers that have existed since at least

1955. *Id.*, 4:88-5:93, Alongi Sur., ComEd Ex. 68.0, 3:49-53. Second, it is unclear how or when ComEd will "assume" ownership of property that is customer-owned. Alongi Reb., ComEd Ex. 41.0, 5:93-94. Third, even if ComEd could "assume" ownership, Mr. Rockrohr's proposal does not grant ComEd the easement that would be needed to access a customer's property to perform necessary maintenance nor does it solve clearance issues relating to trees and other vegetation. *Id.*, 5:94-97. Fourth, offering customers the ability to have ComEd assume ownership on a prospective basis would create (1) confusion and (2) a permanent dual system of those customers who own their own overhead primary facilities and those customers who have let ComEd assume ownership. *Id.*, 5:97-101. Fifth, ComEd already offers residential customers who are willing to pay the associated costs the option to replace customer-owned overhead primary facilities and the ComEd-owned overhead Residential Service Station transformer with ComEd-owned underground direct-buried primary facilities and a pad-mounted Residential Service Station transformer. *Id.*, 5:101-05. Last, and perhaps most importantly, there appears to be a labor jurisdiction issue regarding International Brotherhood of Electrical Workers ("IBEW") labor union work. *Id.*, 5:105-07; see also McMahan Reb., ComEd Ex. 33.0, 20:433-40.

ComEd also provided evidence of why Mr. Rockrohr's proposal is unnecessary for any operational, safety or reliability reason, and would be expensive and difficult (if even possible) to accomplish. McMahan Reb., ComEd Ex. 33.0, 18:404-21:458; Alongi Sur., ComEd Ex. 68.0, 4:74-5:88. ComEd agrees that safety issues are unquestionably important and emphasizes that it is committed to operating at an industry-leading level of safety. McMahan Sur., ComEd Ex. 60.0, 16:353-54. To justify his recommendation, Mr. Rockrohr simply assumed that private ownership of non-standard primary voltage facilities located on customer property poses a safety risk. *Id.*, 16:354-56. While Mr. Rockrohr presented no evidence substantiating his assumption or documenting any safety issues, ComEd pointed to its decades of experience on which to base a sound conclusion about the safety of its practices regarding customer-owned facilities. *Id.*, 16:357-63. ComEd recognizes that the inquiry presented by Mr. Rockrohr is important; however, the data simply does not bear out Mr. Rockrohr's assumption about potential safety issues. McMahan Sur., ComEd Ex. 60.0, 16:350-17:365. Mr. Rockrohr also assumes certain facts about ComEd and public records that are simply not accurate and he misunderstands ComEd's testimony regarding the identification of the facilities at issue as non-standard and the ownership of such facilities by the customers. *Id.*, 17:366-18:396.

ComEd presents an alternative proposal to address Mr. Rockrohr's safety and reliability concerns. *Id.*, 18:397-19:413. In particular, ComEd proposed to work jointly with Staff to study the issues that Mr. Rockrohr has raised to encompass both the safety and performance of these facilities as compared to similar ComEd-owned facilities and examine the costs, benefits, and potential legal and practical obstacles to ComEd attempting to acquire ownership of these facilities. *Id.*, 18:401-05. ComEd would bear the cost of the study and record it in a regulatory asset, with the goal of returning a report to the Commission by the end of 2011. *Id.*, 18:405-19:407

In the event the Commission determines not to reject Staff's proposal regarding ownership of certain non-standard customer-owned facilities, it should accept ComEd's alternative proposal to study the issues raised by Staff relating to these facilities.

b. <u>Limitation of Liability Language</u>

A second proposed modification to ComEd's GTC would add specific Limitation of Liability language to the Nature of Service portion of the GTC. The purpose of this modification is to incorporate limitation of liability language that is uniform with the other Illinois utilities, and ComEd's proposed language has been modeled on the corresponding provisions of the other Illinois utilities. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 41:781-42:786; Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 41:1151-54. The provision ensures consistency as it applies universally to retail customers, applicants for electric service, RESs, MSPs, and other entities with which ComEd interacts. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 42:786-88. Moreover, the limitations apply only to parties that have some connection between the claimed liability and ComEd's provision of electricity to the party. The provision is inapplicable to non-service liability matters, such as a bystander whose injury and damages were unconnected to the provision of electrical service. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 53:1204-08.

7. <u>Rider UF</u>

The terms of ComEd's Rider UF – Uncollectible Factors ("Rider UF") – provide that the incremental amounts collected under the rider represent the difference between actual uncollectible expense incurred and the amount included in base rates. Houtsma Dir., ComEd Ex. 6.0 Rev., 38:775-77. Staff witness Pearce correctly pointed out an error in the direct testimony of Ms. Houtsma regarding the computation of uncollectible factors in Rider UF. Pearce Dir., Staff Ex. 3.0, 45:1073-46:1090. ComEd identified and corrected this error in ComEd Ex. 41.3. Further, ComEd identified that Ms. Pearce inappropriately used the Company's total operating revenues for 2009 in computing her proposed 1.51% attributable to uncollectible expenses. Alongi Reb., ComEd Ex. 41.0, 9:186-97. Instead, an appropriate computation of the percentage attributable to uncollectibles expenses associated with delivery service should only consider amounts related to delivery service provided by ComEd to customers. *Id.*

In response to Mr. Alongi's rebuttal testimony, Ms. Pearce revised her calculation of uncollectibles and incorporated the use of net write-offs instead of bad debt expense. Alongi

Sur., ComEd Ex. 68.0, 8:156-63.; Pearce Reb., Staff Ex. 18.0, 37:860-38:876. ComEd Ex. 68.2 provided a computation of the distribution-related uncollectible percentage using net write-offs instead of bad debt expense, resulting in an overall distribution related uncollectible percentage of 1.37%, which is consistent with the value provided by Ms. Pearce. Alongi Sur., ComEd Ex. 68.0, 8:163-68.

Because this issue is now uncontested between ComEd and Staff, ComEd's proposal should be adopted. The recovery of base uncollectible costs has been reflected in the design of each delivery service charge - the customer charge, standard metering service charge, and DFC – in proportion to the revenues derived from these charges. This method fairly and proportionally assigns revenue responsibility to customers. (ComEd Ex. 50.0 (Garcia) at 8:187-9:195.). In addition, base uncollectible cost factors pertaining to supply services provided by ComEd as proposed in ComEd Ex. 16.22 Rev. Revised Sheet No. 267 should be approved by the Commission. Finally, in the event that the Commission determines that net write-offs should be used instead of bad debt expense in the determination of uncollectible cost factors, the computation of the factors should be performed in accordance with the model provided in ComEd Ex. 68.2. Alongi Non-Rate Design Sur. ComEd Ex. 68.0, 8:158-168. If approved by the Commission, such use of net write-offs in the determination of uncollectible cost factors would begin in the calendar year following the Order in this rate case.

8. Notification Regarding Elimination of Self Generation Customer Group

ComEd proposed to eliminate the Self-Generating Customer Group because it is applicable to only nine customers. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 46:892-47:916. ComEd agrees with Staff witness Harden's recommendation that ComEd should notify the nine customers affected by the ComEd's proposal to eliminate the Self-Generating Customer Group.

Alongi Rate Design Sur., ComEd Ex. 73.0 2nd Rev., 41:934-42:937. If the Commission approves the elimination of the Self-Generating Customer Group, ComEd will send a direct notice to the affected customers that explains the options the customers have available to them upon the elimination of the Self-Generating Customer Group. *Id*., 42:937-40. Further, ComEd's notice will explain the billing structure of each of the available options. *Id*., 42:940-41.

9. Docket No. 08-0532 Compliance Issues

On June 30, 2010, ComEd submitted proposed rates that incorporated, to the extent practical, the directives set forth in the Commission's Order in Docket No. 08-0532. Alongi Dir., ComEd Ex. 16.0 3rd Rev., 5:117-26, 29:537-32:595. ComEd's proposed rates filed on June 30, 2010 were developed using (i) the Company's proposed ECOSS which reflects ComEd's primary/secondary analysis, (ii) voltage differentiation through the administration of a High Voltage Delivery Class, (iii) a credit provided via Rider ACT to customers that provide their own transformation, and (iv) classification of all nonresidential customers establishing demands in excess of 400 kW to be primary customers. *See, e.g.*, Hemphill Dir., ComEd Ex. 14.0 Rev.; Heintz Dir., ComEd Ex. 15.0 Rev.; Alongi Dir., ComEd Ex. 16.0 3rd Rev. On August 9, 2010, ComEd submitted supplemental direct testimony that provided an exemplar rate design with an exemplar Primary Voltage Delivery Class for the Commission's consideration, as well as the allocation of customer care costs. *See*, *e.g.*, Donovan Supp. Dir., ComEd Ex. 19.0 Rev.; Alongi Supp. Dir., ComEd Ex. 21.0 Rev.; Heintz Supp. Dir., ComEd Ex. 22.0 Rev.; ComEd Ex. 22.1. Therefore, the Company has complied with the directives of the Commission's Order in Docket No. 08-0532.

10. Other Issues

a. Street Lighting

Please refer to Section VIII.C.4.d.

b. Recovery of Costs Associated with Customer Care if Allocated to the Supply Function

Since the inception of open access, the Commission has directed ComEd to recovery customer services costs through delivery services rates. Garcia Supp. Dir., ComEd Ex. 24.0, 3:64-4:69. No Illinois electric utility recovers such costs through any means other than delivery service rates. REACT's proposal regarding the recovery of customer service costs would improperly inflate ComEd's supply prices for the benefit of RESs and create a subsidy that will hamper efficient competition and is contrary to principles of cost causation. *See* Rukosuev Dir., Staff Ex. 12.0, 40:951-41:970; *see also* Garcia Supp. Dir., ComEd Ex. 24.0, 10:213-226. However, in the event that the Commission reverses its many previous, consistent directives and determines that a portion of ComEd's customer service costs should be allocated to the supply function, then ComEd must be allowed to institute a charge to recover those costs from two groups of customers - those for which ComEd provides supply, as well as those for which RESs provide supply and for which ComEd purchases the RESs' receivables for the supply provided by the RESs to those customers.

IX. REVENUES

Although the issues in this section are addressed separately from the Rate Base and Operating Expenses sections of this Initial Brief, it is important to note that the issues discussed herein have similar revenue requirements impacts.

A. Uncontested Issues - Other Revenues – Rate Relief Payment (Staff)

ComEd accepted the proposal by Staff witness Hathhorn and AG/CUB witness Effron to adjust Other Revenues to eliminate an inadvertent and incorrect $8 million reduction for a rate relief payment. Fruehe Reb., ComEd Ex. 30.0, 19:407-15; Hathhorn Dir., Staff Ex. 2.0, 7:140-49; Effron Dir., AG/CUB Ex. 2.0, 17:377-94.

B. Uncontested Issues – Miscellaneous Revenues

In light of the rate relief payment adjustment discussed above, AG/CUB withdrew its proposed disallowance to miscellaneous revenues as unnecessary. AG/CUB Ex. 7.1, Sched. C-2.

C. Uncontested Issues – Weather Normalization

ComEd proposed to use weather-normal billing determinants to develop rates in order to best reflect normal conditions expected during the period that rates are in effect. ComEd Ex. 6.1, Sched. A-1, p.2, ll. 36-38. No party opposes the use of weather-normal billing determinants.

D. Late Payment Charge Revenues

ComEd assesses late payment charges upon unpaid and delinquent customer account balances. Brosch Dir., AG/CUB Ex. 1.0, 40:873-76. Revenues from these late payment charges that are related to the delivery services function are appropriately included in ComEd's Other Revenues, which correspondingly reduces ComEd's Illinois jurisdictional revenue requirement. ComEd believes it is appropriate to reduce its revenue requirement by $11.1 million in delivery services related late payment charge revenues. Houtsma Dir., ComEd Ex. 6.0 Rev., 43:869-71. AG/CUB witness Brosch seeks to further reduce ComEd's Illinois jurisdictional revenue requirement by including $13,987 million of additional late payment charges revenues in ComEd's Other Revenues. Fruehe Reb., ComEd Ex 30.0 Public, 20:416-21:452; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 23:484-24:500; Brosch Reb., AG/CUB Ex. 7.0, 33:734-34:747.

To determine the amount of late payment charge revenues that are properly allocated to delivery services, ComEd determined the ratio of 2009 delivery services revenues to ComEd's total 2009 revenues and applied that to the total late payment charge revenues. Houtsma Dir., ComEd Ex. 6.0 Rev., 43:869-72; ComEd Ex. 6.2, WPA-5. It is undisputed that the additional charges that Mr. Brosch seeks to include are not related to *delivery* services – they are indisputably related to *supply*. Fruehe Reb., ComEd Ex 30.0 Public, 20:416-21:452; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 23:484-24:500. Whether or not the calculation of other rates includes an adjustment for non-delivery services late payment charges revenues is not determinative of the appropriate treatment in this proceeding. This proposal to offset the *delivery* services revenue requirement with *supply* revenues is inappropriate and should not be accepted by the Commission. Indeed, Staff witness Dianna Hathhorn agreed with ComEd and recommended that the ICC reject Mr. Brosch's proposed disallowance. Hathhorn Reb., Staff Ex. 17.0, 10:191-201. Quite simply, these late payment charges are not a function of delivery services and should therefore not be allocated to delivery revenues.

E. New Business Revenue Credit

ComEd believes it is appropriate to reduce its revenue requirement by $3.513 million through the application of the new business revenue credit. Fruehe Reb., ComEd Ex. 30.0 Public, 24:524-25:530; ComEd Ex. 30.1 Sched. 2.9 Rev. AG/CUB witness Effron seeks to increase this amount and reduce ComEd's revenue requirement by an additional $3.800 million. Effron Reb., AG/CUB Ex.8.0, 11:239-42; AG/CUB Ex. 2.1, Sched. DJE-2.1a. As ComEd has done in its last two rate cases (ICC Docket Nos. 05-0579 and 07-0566), ComEd has included a new business revenue credit to account for the estimated revenue from growth in customers during the *pro forma* period. Fruehe Reb., ComEd Ex 30.0 Public, 21:453-22:462. In other words, ComEd offsets the cost increase from its *pro forma* additions with the revenues that it may receive from new customers in the *pro forma* period. *Id.* To accurately determine the amount of the credit, ComEd must ascertain which customers are new, and thus ComEd must take into account customer migration between classes. Fruehe Sur., ComEd Ex 56.0 3rd Rev., 21:429-22:456.

AG/CUB witness Effron seeks to artificially inflate this new business revenue credit by only including growth in customer classes without providing an offset to reflect a *decline* in customer classes due to customer migration. *Id.*; Effron Reb., AG/CUB Ex. 8.0, 10:209-11:242. Mr. Effron's approach is flawed because under his approach, a migrating customer – who does not provide ComEd with any new revenue – is treated like a new customer who does provide ComEd with new revenue. Effron Reb., AG/CUB Ex. 8.0, 10:209-11:242.

In addition, if the length of ComEd's *pro forma* plant additions period is reduced, the new business revenue credit should be correspondingly reduced. Fruehe Reb., ComEd Ex. 30.0 Public, 25:531-537; Fruehe Sur., ComEd Ex 56.0 3rd Rev., 22:461-23:469. Staff agrees with this principle, but has improperly calculated the corresponding adjustment. Ebrey Reb., Staff Ex. 16.0, 25:523-26:532; Fruehe Sur., ComEd Ex 56.0 3rd Rev., 22:461-23:469. In addition to a mathematical error, Staff used the capital associated with customer operations instead of the New Business plant additions to determine the adjustment. Fruehe Sur., ComEd Ex 56.0 3rd Rev., 23:470-79. In short, if Staff's recommendations regarding the *pro forma* period are adopted, then the proper new business revenue credit adjustment is a reduction of 33% or $1,142,000. *Id.*, 23:480-83; ComEd Ex. 56.5 Rev.

X. OTHER

A. RES Services Issues

ICEA witness Fein and RESA witness Boston raised a variety of issues relating to ComEd's business processes or to terms and conditions of ComEd's tariffs that were not the subject of ComEd's filed tariffs. Fein Dir., ICEA Ex. 1.0, 4:16-5:24; Boston Dir., RESA Ex. 1.0, 3:46-4:55. Both ICEA and RESA represent the interests of Retail Electric Suppliers ("RESs") in this proceeding. Hemphill Reb., ComEd Ex. 40.0, 3:41-42. ComEd immediately began working with these parties to resolve the issues raised and, through their collaboration, the parties agreed that the RES service issues should be addressed outside of this rate case proceeding. *See, e.g.*, Hemphill Sur., ComEd Ex. 65.0, 12:236-45, 14:282-86; Lesniak Sur., ComEd Ex. 66.0, 1:21-4:79. Accordingly, there are no RES service issues for the Commission to address in this proceeding.

B. UUFR

ComEd proposed the Urban Underground Facility Reinvestment ("UUFR") program (also referred to as Urban Underground Infrastructure Reinvestment ("UUIR")) as an 18-month pilot during which ComEd would expend nearly $50 million to explore a new way of improving the reliability of certain types of underground mainline feeder cables. Hemphill Sur., ComEd Ex. 65.0, 2:35-37. The UUFR program does not generally accelerate the replacement of lead insulated mainline cable or the refurbishment of manholes; instead, during its 18-month lifespan, UUFR program work would only occur on a small subset of those mainline cables and associated manholes. *Id.*, 2:37-40. The pilot program was proposed as part of ComEd's alternative regulation plan in Docket No. 10-0527. *Id.*, 3:41-42.

Staff witness Stutsman recommends that the Commission order ComEd to proceed with a $45 million UUFR project that ComEd initially proposed as part of its alternative regulation proposal "irrespective of whether ComEd receives approval of its alternative regulation proposal." Stutsman Dir., Staff Ex. 9.0, 3:47-50, 6:115-19; Stutsman Reb., Staff Ex. 24.0, 13:244-45. Mr. Stutsman's recommendation should be rejected as it suffers from several flaws. Hemphill Sur., ComEd Ex. 65.0, 3:43-4:76. First, ComEd witness Hemphill explains that although the UUFR project would provide additional reliability benefits, it is not required in order for ComEd to meet its service reliability obligations. Hemphill Reb., ComEd Ex. 40.0, 11:226-12:243; Hemphill Sur., ComEd Ex. 65.0, 3:55-4:62; *see also* McMahan Reb., ComEd Ex. 33.0, 14:307-23. Second, Dr. Hemphill explains that Mr. Stutsman's recommendation constitutes a request that the Commission issue an unfunded mandate, compliance with which would necessitate significant cutbacks in other areas. Hemphill Reb., ComEd Ex. 40.0, 12:244-13:258; *see also* McMahan Reb., ComEd Ex. 33.0, 15:335-40. Finally, Dr. Hemphill explains why the Commission should consider and provide for the funding of the UUFR project under ComEd's alternative regulation proposal and not in the context of this rate case. Hemphill, ComEd Ex. 40.0, 13:264-72; *see also* McMahan Reb., ComEd Ex. 33.0, 15:324-34, 15:341-43. Accordingly, the Commission should deny the request to require ComEd to proceed with an unfunded UUIR project and, instead, should consider and provide for the funding of the project under ComEd's alternative regulation proposal.

C. <u>Updated Distribution Loss Study</u>

This issue is discussed in Section VIII.C.6.

D. <u>Meters and Meter Reading</u>

Staff witness Rockrohr and ICEA witness Fein express concerns about meter reading and estimated bills and, in Mr. Fein's case, unbilled meters. Rockrohr Reb., Staff Ex. 21.0, 25:525-37; Fein Reb., ICEA Ex. 2.0, 8-10. ComEd attempts to read meters in accordance with the Commission's rules governing meter reads and bill estimation. Marquez Sur., ComEd Ex. 61.0

Rev., 12:274-13:280; Marquez Reb., ComEd Ex. 36.0 2nd Rev., 26:580-96. However, to address those circumstances where ComEd is prevented from reading meters for reasons outside of ComEd's control, ComEd is looking to an Information Technology solution to assist customer service agents and others faced with such a circumstance. Marquez Sur., ComEd Ex. 61.0 Rev., 13:280-88. Further, there have not been significant delays in delivering meter data to RESs. *Id*., 13:289-94. Finally, ComEd is working on process improvements and assigning additional resources to mitigate the volume of delayed bills. *Id*., 13:295-300. In light of this testimony, ComEd believes that it has addressed all the issues regarding meter reading, estimated bills and unbilled meters.

E. Competitive Retail Market Development Issues

ICEA witness Fein testified that the Commission should "strive to direct ComEd to adopt tariff provisions and business practices that facilitate the continued development of competition and customer choice." Fein Dir., ICEA Ex. 1.0, 4:10-12. ComEd has long supported policies that promote efficient retail competition, so ComEd immediately began working with ICEA to resolve these competitive market issues and the parties agreed that such issues should be addressed outside of this rate case proceeding. *See, e.g.*, Fein Reb., ICEA Ex. 2.0, 12-14; Hemphill Reb., ComEd Ex. 40.0, 4:82-5:84; Hemphill Sur., ComEd Ex. 65.0, 12:242-43, 13:254-60. To the extent that the issues cannot be resolved informally, Staff proposes that the Office of Retail Market Development will initiate a proceeding pursuant to Section 9-250 of the Act and all interested parties are supporting of this approach. Staff Clausen Reb., Staff Ex. 25.0, 1:8-5:101. Accordingly, there are no competitive retail market issues for the Commission to address in this proceeding.

F. New Section 9-250 Investigation of ComEd's electric rate design

Please refer to Section VIII.C.3.a.

G. <u>Other</u>

Staff witness Rockrohr recommended that ComEd somehow "assume" ownership of certain non-standard customer-owned facilities used to bring power from the ComEd system into privately owned residential property. Rockrohr Dir., Staff Ex. 21.0, 12:249-13:275. ComEd witness McMahan testified that this proposal is unnecessary for any operational, safety or reliability reason, and would be expensive and difficult (if even possible) to accomplish. McMahan Reb., ComEd Ex. 33.0, 18:404-21:458. While ComEd recognizes that the inquiry presented by Mr. Rockrohr is important, the data simply does not bear out Mr. Rockrohr's assumption about potential safety issues. McMahan Sur., ComEd Ex. 60.0, 2:28-29. Mr. Rockrohr also misunderstands ComEd's testimony regarding the identification of the facilities at issue as non-standard and the ownership of such facilities by the customers. *Id*., 18:389-96.

ComEd presented an alternative proposal to address Mr. Rockrohr's safety and reliability concerns. *Id.*, 18:397-19:407. In particular, ComEd proposes to work jointly with Staff to study the issues that Mr. Rockrohr has raised to encompass both the safety and performance of these facilities as compared to similar ComEd-owned facilities and examine the costs, benefits, and potential legal and practical obstacles to ComEd attempting to acquire ownership of these facilities. *Id*. ComEd would bear the cost of the study and record it in a regulatory asset, with the goal of returning a report to the Commission by the end of 2011. *Id*.

In the event the Commission determines not to reject Staff's proposal regarding ownership of certain non-standard customer-owned facilities, it should accept ComEd's alternative proposal to study the issues raised by Staff relating to these facilities.

XI. CONCLUSION

ComEd respectfully requests that the Illinois Commerce Commission approve ComEd's recommended rate base of $ 7,349,277, its weighted cost of capital of 8.98%, which reflects an estimate of the investor-required rate of return on common equity of 11.50%; its revenue requirement of $2,267,000,000, and ComEd's embedded cost of service study and rate design.

Dated: February 10, 2010	Respectfully submitted, COMMONWEALTH EDISON COMPANY By:____________________ One of its Attorneys
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