STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY	**)**	
	)	**Docket No. 10-0467**
	)	
Proposed general increase in electric rates	**)**	

INITIAL BRIEF OF THE CITIZENS UTILITY BOARD

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NOW COMES the Citizens Utility Board ("CUB"), pursuant to Section 200.800 of the Rules of Practice[1] of the Illinois Commerce Commission ("ICC" or "the Commission") and the briefing schedule established by the Administrative Law Judges ("ALJs") in this case, to file this Initial Brief. This proceeding concerns a request for an increase in delivery services rates filed by Commonwealth Edison Company ("ComEd" or "the Company"). This brief addresses the factual and legal issues raised by the evidence of record and by the application of the controlling provisions of the Public Utilities Act (the "Act" or "PUA")[2] and relevant Illinois case law to the circumstances of this case. The sections of this brief are organized in accordance with the outline of issues circulated amongst the parties after the conclusion of the evidentiary hearings in this case. Together with the People of the State of Illinois, acting through the Illinois Attorney General's Office ("AG" or "the People"), CUB collectively presented the testimony of four witnesses in this case addressing various accounting issues and the appropriate return on common equity for Commonwealth Edison ("ComEd" or "the Company"): Michael Brosch, AG/CUB Exhibits 1.0 through 1.8 and AG/CUB Exhibits 7.0 through 7.5; David Effron, AG/CUB Exhibits 2.0 through 2.1 and AG/CUB Exhibits 8.0 through 8.1; Ralph Smith, AG/CUB Exhibits 3.0 through 3.2 and AG/CUB Exhibit 9.0; and Christopher Thomas, AG/CUB Exhibits 4.0 through 4.6 and AG/CUB Exhibit 10.0. A summary of the overall adjustments proposed by the AG/CUB witnesses is contained in AG/CUB Exhibit 7.1, attached to the testimony of Mr. Brosch. AG/CUB also presented the testimony of Scott J. Rubin, AG/CUB Exhibits 6.0 through 6.17 and AG/CUB Exhibits 11.0 through 11.4, and Michael Brosch, AG/CUB Exhibit 12.0, which addressed the Company's proposed rate design.

[1] 83 Ill. Adm. Code Part 200.

[2] 220 ILCS 5/1-101 *et seq*.

I. INTRODUCTION/STATEMENT OF THE CASE

The Public Utilities Act charges the Illinois Commerce Commission with the responsibility of evaluating proposed utility rate increases. In evaluating a utility's proposed general increase in rates, the Commission shall include in the rate base investments which are prudently incurred and are used and useful. 220 ILCS 5/9-211. The Commission shall establish rates that it finds to be just and reasonable. 220 ILCS 5/9-201(c). The Commission is obligated to ensure that rates are affordable for ratepayers. 220 ILCS 5/1-102(d)(viii). The price that utility consumers pay for utility service should "accurately reflect the long-term cost of such services," while providing the utility with an adequate return on its investment. 220 ILCS 5/1-102; 1-102(a)(iii).

CUB and the People, along with other Intervenors such as the Staff of the Illinois Commerce Commission ("Staff"), have reviewed in detail almost every aspect of the Company's sweeping request. AG/CUB witnesses Michael Brosch, David Effron and Ralph Smith Identified specific issues relating to the Company's rate base and expenses that remain in dispute include the most significant components of the Company's revenue requirement: post-test year plant additions and the associated reserves for accumulated depreciation and income taxes, cash working capital, incentive compensation expenses, rate case expenses, pension costs and even sporting event expenses. CUB and other Intervenors present specific reasons for the Commission to adjust ComEd's request.

The Company and Intervenors also present very different views of how the Commission should determine the appropriate return on equity ("ROE") for the Company. At one end of the continuum, CUB recommends an ROE based on objective market factors to the maximum extent possible. At the other end of that continuum, the Company suggest that the Commission's goal

should be to find a ROE estimate that satisfies investors' subjective expectations and compares well with other states. The legal principles that define the return utilities are entitled to earn and those that define the Commission responsibilities require an ROE determination based on objective market data, not biased analyses or subjective expectations. Moreover, the Commission is obligated to consider how other Company requests in this case would affect its financial security, such as how a new rate design to enhance its chances of fully recovering whatever the final revenue requirement is in this case. AG/CUB witness Chris Thomas analyzed how investors are likely to view an investment like ComEd. He found that current market conditions are leading investors to correctly perceive public utilities as less risky investments than other investments such that companies like ComEd would have earn a lower ROE.

Finally, CUB addresses the proposed rate design offered by both the Company and the National Resources Defence Council ("NRDC"). AG/CUB witness Scott Rubin has examined the proposed "straight fixed variable" rate design in the context of the traditional principles which have governed rate design, and concluded the Company's proposal should be rejected. Mr. Rubin concluded ComEd's proposal to drastically increase its customer charge and reduce distribution (per kWh) charges bears no relationship to the reasons why various facilities are sized and installed on ComEd's system. Electric distribution rates should reflect consumer demand for electricity, and not just the number of customers. Moreover, prices should send customers an appropriate price signal that increases in their energy demand result in increases in costs to the system, and reflect the fact that increased consumption results in increased costs to the system. ComEd's proposal does not promote efficiency or social welfare and is unfair to residential customers. As an alternative Mr. Rubin proposes that ComEd's rates be structured to include (1) customer charges that vary depending on whether the customer is in a single-family

or multi-family building; (2) the same meter charge for all customers; and (3) a distribution charge that reflect each residential subclass' unique costs of service.

Both Mr. Rubin and Mr. Brosch examined the proposal of NRDC to adopt a decoupling mechanism for ComEd. Each concluded that the proposal ignores the fact that utility expenses, rate base, and cost of capital are dynamic and shifts business risks associated with changes in sales volumes from the utility to utility customers. Moreover, protection of ComEd's revenue stream would come at the expense of ComEd customers without any evidence that it will lead to any increased investment in energy efficiency

The Commission should adopt the recommendations made by CUB, the AG and Staff, and lower ComEd's delivery services rates to match its actual expenses. Doing so will continue to provide the utility with an opportunity to fully recover its costs and provide its investors with a sound return on their investment. Adoption of the AG/CUB proposed rate design will mean that opportunity will not come at the expense of ComEd's customers.

II. OVERALL REVENUE REQUIREMENT AND REVENUE DEFICIENCY

The expert review of all four witnesses presented by AG/CUB conclude that ComEd's request for an increase in its existing delivery services rates is not only not necessary, but inappropriate in that ComEd's existing rates should be decreased by $40,359,000. AG/CUB Exhibit 7.1.

III. RATEMAKING AND THE NEED TO BALANCE SHAREHOLDER AND RATEPAYER INTERESTS

IV. TEST YEAR

V. RATE BASE

A. OVERVIEW

Mr. Brosch discusses the importance of the "test year" in regulation utilities because it preserves the balance, or "matching," of revenues, expenses, cost of capital and rate base investments so as to avoId over- or under-stating the revenue requirement. AG/CUB Ex. 1.0 at 5-16; AG/CUB Ex. 7.0 at 11. This framework provides an incentive for utility to manage its costs to maximize its overall rate of return protects. Mr. Brosch examines ComEd's proposal to extend the test year in this case by another 18 months to recognize growth in plant in service without recognizing the concurrent growth in accumulated depreciation and other elements of the revenue requirement that would offset increasing plant costs. Failure to recognize this growth would lead to an inflated rate base, and Mr. Brosch demonstrates how an inflated rate base will result if ComEd's proposal is accepted by comparing its total asserted jurisdictional delivery service and transmission service rate base with its cost of capital summaries in this case, which show an overstatement of invested capital by nearly a half a billion dollars.

B. POTENTIALLY UNCONTESTED ISSUES

2. General and Intangible Plant

The Company's forecast of additions to general and intangible plant are well in excess of both spending in recent years and the actual rate of spending in the early months of 2010, suggesting that the forecasts were overestimated. AG/CUB Ex. 2.0 at 6. For example, in the three years 2007-2009, the average annual total company additions to jurisdictional general plant were $51.1 million. Id. at 6-7. The Company is forecasting that additions to jurisdictional general plant of $82.5 million. Id. at 6. Likewise, from 2007-2009 the Company spent an average of $28.5 million on jurisdictional intangible plant, but is requesting $66.9 million for the

same. Id. at 7. In this case, the Company proposes to spend more than twice as much on intangible plant as it has in the past three years. Id.

Actual spending on general plant through June 2010 was 41% below budget and actual spending on intangible plant through that same time was 34% below budget. Id. ComEd's actual spending suggests that its forecasts are overestimated, and that its actual spending will be closer to its historical average spending.

Therefore, Mr. Effron recommends using actual capital spending in 2010 through June 30 to be used to project the additions through March 31, 2011. Id. at 8. This results in a pro forma reduction of $56.868 million to general plant, and a reduction of $29.933 million to intangible plant. Id. These numbers should be considered "place-holders" until the actual expenditures as of March 31, 2011 are known, at which time the adjustment should be trued up. Id. See discussion below in Pro Forma Capital Additions for explanation of the use of March 31, 2011 as the correct date to use for making this adjustment.

C. POTENTIALLY CONTESTED ISSUES

1. Post-Test Year Adjustments

a. *Pro Forma* Capital Additions

The Company's forecast of plant additions for the second quarter of 2011 should be eliminated, as those forecasts represent costs that cannot be characterized as "known and measurable" with any degree of certainty. AG/CUB Ex. 2.0 at 4-5. As Staff witness Ebrey has explained, the Company's forecasts through June 2011 have changed significantly through the course of this case. Staff Ex. 16.0 at 10. Changes of the magnitude described by Ms. Ebrey have previously resulted in disallowance by the Commission, and signify that the expenses for which the Company seeks recovery are not known and measurable at this time. Id. at 10-11.

Therefore, Mr. Effron proposes to eliminate all plant additions after March 31, 2011, which can be trued up to match actual expenditures through that date before the final order in this case. AG/CUB Ex. 2.0 at 5. No party in the case suggests that ComEd will not make expenditures between March 31 and June 30; however, the Company cannot recover forecasted costs unless they are known and measurable. In ComEd's last rate case, their actual expenditures on pro forma post-test year plant additions were $41 million less than the Company's forecast. AG/CUB Ex. 2.0 at 5. The Company reduced its 2010 forecasted plant additions by $52 million from direct to rebuttal testimony in this case. AG/CUB Ex. 8.0 at 3. Limiting the plant adjustment to additions through March 31, 2011, approximately three months before the rates in this case go into effect, will allow the Company's forecasts to be trued up to actual additions to plant in service through that date. Id. at 5.

Additionally, the Company's actual gross additions to jurisdictional plant in service in the first quarter of 2010 averaged about $41 million per month, while depreciation expense and growth in ADIT, combined, were approximately $39 million per month. AG/CUB Ex. 8.0 at 3. A small shortfall in actual spending below forecasted spending—as little as 5%-- would result in the plant additions being offset by depreciation expense and growth in ADIT. AG/CUB Ex. 8.0 at 3. Such a shortfall seems likely in light of the Company's actual vs. forecasted spending in its last case, as well as its decreased forecast in this case. Not only are these forecasts not known or measurable, but the plant additions are unlikely to result in an increase to rate base if actual numbers were relied on.

To remove the Company's forecasts of plant additions for the second quarter of 2011, rate base should be reduced by $233,693,000 on capital additions to distribution plant

($164,041,000), general plant ($45,482,000) and intangible plant ($24,170,000). AG/CUB Ex. 7.1 Schedule B-1.

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

The Company has requested inclusion of eighteen months worth of pro forma plant additions after the test year, but has failed to reflect the corresponding growth in accumulated depreciation on existing plant through that time as well. AG/CUB Ex. 2.0 at 11-12. In doing so, the Company has chosen to ignore the directive of the Illinois Appellate Court, in an appeal from ComEd's most recent rate case, to adjust the depreciation reserve to the same date as pro forma plant additions are included in rate base. *Commonwealth Edison Co. v. Ill. Commerce Comm'n* et al., 937 N.E.2d 685 (Ill. App. Ct. 2010). "The increase in accumulated depreciation on the existing plant during the post-test-year period, in which the additional plant is being factored into the rate base, is a change that affects ratepayers and therefore must be factored into the rate base." Id. at 704. The Company states that they have ignored this directive because they have appealed that ruling to the Illinois Supreme Court and therefore the issue has not yet been decided. ComEd Ex. 55.0 Rev. at 7. There is no certainty that the Illinois Supreme Court will elect to hear ComEd's appeal, and even if it does, the decision of the Appellate Court is law until and unless the Illinois Supreme Court decIdes differently. The Company has failed to cite any precedent (absent a stay, which has not been granted in this case) for ignoring an Appellate Court decision simply because one or more parties have appealed that decision to the Supreme Court.

The Appellate Court correctly found it necessary to acknowledge growth in accumulated depreciation correspondent with the date to which the Company has included post-test-year plan additions. Pro forma adjustments are allowed by the Public Utilities Act only if "all known and measurable changes" are taken into account. *Commonwealth Edison Co.*, 937 N.E.2d at 704,

citing 83 Ill. Adm. Code §§ 287.20, 287.40. The Company has already accounted for post-test-year changes in depreciation reserve related to retirements, depreciation expense on post-test-year plant additions, salvage value, and cost of removal. AG/CUB Ex. 2.0 at 12. Depreciation on embedded test year plant in service is a known and measurable change that must be taken into account. Id. The Company's approach of selectively choosing which factors it would prefer to have included in post-test year calculations is both poor policy and is inconsistent with the law.

As explained above, Mr. Effron proposes to allow post-test-year plant additions through March 31, 2011. Therefore, all depreciation, including depreciation on test year embedded plant, should also be calculated through that date. AG/CUB Ex. 2.0 at 10-13; AG/CUB Ex. 8.0 at 6-7. This adjustment increases the depreciation reserve by $490,108,000. AG/CUB Ex. 7.1, Schedule B-3.

c. Accumulated Deferred Income Taxes (ADIT)

The recent Appellate Court decision cited above dictates that the date from which the ADIT reserve is calculated must also match the date to which post-test-year additions are allowed. *See* Section IV C 1 b. The Company has recognized the incremental ADIT that would be generated by pro forma adjustment to post-test-year additions to plant in service, but has failed to recognize the growth in ADIT related to embedded plant as of the end of the test year. AG/CUB Ex. 2.0 at 13. By failing to properly calculate ADIT, the Company ignores the fact that the growth in ADIT related to plant in service as of December 31, 2009 is a source of funding for post-test-year plant additions. Id. It is also contrary to Illinois law.

In accordance with his proposal to include adjustments through March 31, 2011, Mr. Effron has proposed to increase ADIT by $39,209,000. AG/CUB Ex. 2.0 at 13-14; AG/CUB Ex. 8.0 at 7-8; AG/CUB Ex. 7.1, Schedule B-3.

2. Construction Work in Progress ("CWIP")

Construction work in progress can be included in rate base under the Public Utilities Act, and ComEd has elected to include CWIP by capitalizing Allowance for Funds Used During Construction ("AFUDC") on CWIP with a total expected expenditure of greater than $25,000 and an expected construction period of greater than 30 days. AG/CUB Ex. 1.0 at 18. The Company also seeks recovery of "short-term CWIP," which is not eligible for AFUDC because it has a shorter construction period. Id. Mr. Brosch recommends disallowance of this short-term CWIP because, due to its short construction period, it is likely that ComEd did not actually pay for the construction until after it was already completed. Id. at 18-19. ComEd's study of cash flows has shown that payment to ComEd employees occurs an average of 14.64 days after labor costs were incurred, and miscellaneous cash voucher payments to vendors occur with average of 64.34 day delay. Id. at 19. In essence, the vendor who performs the work finances the project during this delay of payment, and by the time payment is made, the work is complete. Where the Company has little or no actual cash investment, no return from customers is appropriate. Id.

ComEd witness Ms. Houtsma mischaracterizes Mr. Brosch's disallowance by making it appear that his recommendation is contrary to the PUA. In fact, Mr. Brosch does not take issue with the Company's AFUDC, which accounts for construction work in progress, and he even recommends that the Company should include all CWIP in AFUDC rather than counting short-term CWIP separately. AG/CUB 7.0 at 27-28. Mr. Brosch suggests that all CWIP could and should be included in rate base in this manner. The Company chooses to count short-term CWIP separately from AFUDC. Id. at 28. This is likely because if the short-term CWIP balances were reduced for vendor-provided working capital, there may be no significant remaining balances that would accrue any AFUDC at all. Id.

Removing short-term CWIP from rate base results in a disallowance of $12,591,000. AG/CUB Ex. 7.1, Schedule B-7.

3. Specific Plant Investments

c. Underground Cable

The Company has requested inclusion in rate base of underground cable costs incurred outside of the test year, in 2005-2006, previously disallowed in their last rate case, ICC Docket 07-0566. AG/CUB 2.0 at 9. The Company's explanation is that ComEd disagreed with that disallowance at the time, though it didn't oppose it as part of a stipulation with Staff, and the Final Order in that case did not state explicitly that the costs would be excluded in the future as well if the Company re-introduced them. ComEd Ex. 29.0 at 11. ComEd argues that in its Brief on Exceptions in that case it stated that it was not precluded from seeking to include those costs in the future, and therefore it should be allowed to here. Id. However, as evidenced by the fact that ComEd can only cite to its own brief on exceptions as authority for that premise, the Commission chose not to make such a finding in the Final Order of the case.

There is no precedent for reconsideration of costs incurred three to four years before the test year, which were previously presented in a rate case and disallowed, to be included in a later rate case. These costs were not disallowed simply because the Company entered into a stipulation with Staff. The Commission made specific findings and made a specific adjustment to the disallowance proposed by Staff based on evidence provided by ComEd. ICC Docket No. 07-0566 September 10, 2008 Final Order at 46. The Commission should give no credence to the Company's repeated arguments as to the prudency of these costs. This issue has already been litigated and there is no precedent for reconsideration. ComEd's rate base should be reduced by $15,222,000 to remove these previously-disallowed costs. AG/CUB Ex. 7.1, Schedule B-2.

Additionally, the Company should be prohibited from attempting to re-litigate disallowances in the future, as it is unnecessarily burdensome on Staff and Intervenors, and it detracts from the relevant issues in the case.

4. Cash Working Capital

The Company initially requested $95.7 million of cash working capital, and revised that request in Surrebuttal to $67.7 million. ComEd Ex. 7.0 Rev. at 2, ComEd Ex. 57.0 at 2. These requests are the result of a flawed Lead/Lag study, which if accurate, would mean that the timing of ComEd's cash flows have changed dramatically since its late rate case. AG/CUB Ex. 1.0 at 22-23. It is unlikely that such a change has occurred; rather, the incorrect calculation of the revenue lag in the Lead/Lag study has radically skewed the results. Id. Rather than precisely calculating when ComEd actually collects revenues, the Company's study used unreasonable assumptions to group revenue collections into several broad categories, using the mad-points of those categories as the assumed age of all receivables in that group. Id. However, the ages assigned to those categories are mad-points, not averages. For example, with regard to customer bills, or receivables, the Company has lumped together all receivables that are 31-60 days old and assigned them an age of 45 days old, without any analysis or supporting data. *Id.* at 27. It is possible that 90% of receivables 31-60 days old are actually 31-35 days old. *See* Id. at 28-29.

The problem is that ComEd doesn't know whether that might be the case because its Lead/Lag study conducted no analysis beyond its lumped categories. *Id.* at 28. The results of the study are skewed by the inclusion of receivables over 90 days old in the results, as the Company has recognized that older receivables are most likely uncollectible. *Id.* at 31. Though the Company arbitrarily chose to designate only receivables greater than 365 days older as uncollectible, they have produced no evidence to show that receivables greater than 90 days old

are also not largely uncollectible. *Id.* Mr. Brosch did his own calculation to demonstrate the arbitrariness of choosing 365 days as the uncollectible cut-off. AG/CUB Ex. 1.0 at 33. He found that if the receivables aging data in the 91-120 and 121-365 day intervals was excluded, using the other figures from the ComEd Lead/Lag study, would yield a negative $45 million CWC requirement. *Id.* It is entirely likely that many if not most receivables older than 90 days are uncollectible, and therefore that a negative CWC is appropriate. In fact, Mr. Brosch found that excluding even just the 121-356 day interval would result in a negative $21.2 million CWC. *Id.* at 34. However, Mr. Brosch has not advocated for these positions because without calculations and analysis to back up the assumptions, they are just as arbitrary as what ComEd has done. *Id.* at 33. Unfortunately, no party could perform an accurate analysis of receivables aging data because the Company cited information technology limitations as preventing them from providing more precise information. Tr. at 1080, 1085, 1086, 1088, 1092, 1102, 1106, 1107, 1120.

The Company recognized flaws in its Lead/Lag study, as it amended its calculations to include more granular data on Surrebuttal. ComEd Ex. 57.0 at 3-4. However, the Company continued to use inordinately large lump groups, and continued to use 365 days as the arbitrary cut-off for when a receivable becomes an uncollectible.

Mr. Brosch recommends the Commission adopt a zero allowance for CWC. AG/CUB Ex. 1.0 at 21-35; AG/CUB Ex. 7.0 at 11-25. He explained that a properly prepared Lead/Lag study that fully considers the timing of all cash expenses will often return a negative or nearly-zero CWC result because of the extended periods of time over which utilities often pay certain taxes and interest expenses. AG/CUB Ex. 1.0 at 22. Such a proper study is not possible without more detailed information from ComEd, and it is clear that this study is fatally flawed and cannot

be relied upon. Therefore, Mr. Brosch recommends a total disallowance of $89,703,000 to remove CWC. AG/CUB Ex. 7.1, Schedule B-5.

5. 2009 Pension Trust Contribution

The Company made a "catch-up" contribution to its pension fund in 2009 to improve the underfunded status of the plan. AG/CUB Ex. 2.0 at 15. For the three years prior to 2009, 2006-2008, the Company made inadequate contributions to its pension plan, accruing $106 million during those years while the contributions were only $15 million. Id., AG/CUB Ex. 8.0 at 8. If the Company had made adequate contributions to its pension plan from 2006-2008, then the unusually large contribution in the test year would not have been necessary. AG/CUB Ex. 8.0 at 9. Although the cumulative effect on the balance sheet would be the same whether the contributions were spread out or made all at once, the amount included in the test year would have been much smaller. Id. Additionally, if the contributions in 2006-2008 would have been equal to the accruals in those years, there would be no prepaid pensions that should be included in rate base. Id.

The Company's argument that making the contribution "was the right thing to do" (ComEd Ex. 4.0 at 23) holds no water because it was also the right thing to do in 2006, 2007 and 2008—yet the Company chose to underfund the plan in each of those years and instead do a catch-up contribution in the test year, 2009. At the point where the Company chose to underfund the plan three years in a row, it then becomes shareholders' responsibility, because shareholders benefitted from bigger returns in each of those years where an inadequate contribution was made.

This adjustment reduces ComEd's rate base by $68,750,000, which is the difference between the $92,591,000 in deferred debits ComEd has included in rate base minus the offsetting

adjustment to remove ADIT of $23,841,000. AG/CUB 8.0 at 9-10, AG/CUB Ex. 7.1, Schedule B-4 and Schedule DJE 1.5.

6. Capitalized Incentive Compensation

The discussion of this issue is included in connection with the discussion of incentive compensation in Section V I 1.

7. Customer Deposits

Customer deposits are a low cost source of capital for the Company. AG/CUB Ex. 1.0 at 36. Because they represent ratepayer-provided capital that is continuously available to the utility, customer deposits are typically subtracted from rate base with corresponding interest paid recovered from customers. Id. at 36-37. It is in the Company's interest to recognize the smallest amount of customer deposits as possible since they are subtracted from rate base. ComEd made several errors in calculating customer deposits which resulted in underestimation and increased rate base.

The Company's calculation of customer deposits using a thirteen month average[3] balance rather than the 2009 year-end balance is inappropriate. The balances of customer deposits have been consistently growing since 2006 and throughout 2009. AG/CUB Ex. 1.0 at 37. Therefore, using a 2009 average serves only to underestimate the amount of customer deposits. The "seasonality" ComEd uses to justify using this average (ComEd Ex. 29.0 at 37) does not explain this consistent, year-over-year growth. AG/CUB Ex. 7.0 at 31.

Additionally, the Company claims that only a portion of its total collected customer deposits are "jurisdictional." Id. All of the customer deposits that have been collected by

[3] The Company initially proposed using a 12-month average, but accepted Staff's recommendation to use a thirteen month average. ComEd Ex. 29.0 at 37.

ComEd have been collected in Illinois, and none have been used to reduce FERC rate base. Id. at 37-38. The Company's comparison of customer deposits to jurisdictional plant (ComEd Ex. 29.0 at 38) is a straw man argument. There are only two jurisdictions between which a cost can be split-- non-jurisdictional plant is used for transmission rather than delivery, and is claimed in FERC rate base rather than Illinois jurisdictional rate base. Customer deposits neither relate to transmission nor are used to reduce FERC rate base. Both in testimony and when asked in a data request, ComEd has failed to Identify what other jurisdiction customer deposits are attributable to. AG/CUB Ex. 7.0 at 29-30. ComEd's choice to claim some part of its customer deposits balance as "non-jurisdictional" does nothing more than increase rate base and allow ComEd to retain the benefit of this low-cost source of funding supplied by ratepayers. Id. One hundred percent of customer deposits balances should be attributed to retail delivery services and calculated as a reduction to rate base. AG/CUB 1.0 at 38. ComEd pays interest on its Customer Deposits; therefore they are a low-cost capital, not zero-cost capital. AG/CUB Ex. 7.0 at 31. Therefore, the annual cost of such interest must be included in operating expenses. AG/CUB Ex. 7.0 at 31.

To recognize one hundred percent of customer deposits, and to calculate the effect of customer deposits fairly using the 2009-year end balances, ComEd's rate base should be reduced by $85,962,000. AG/CUB Ex. 7.1, Schedule B-8.

D. RATE BASE (TOTAL)

The Company has attempted to skew the Commission's decisions on each of the above costs upward in recognition of the supposed "ripple effect" that ComEd's expenditures have on the overall regional economy, and ComEd's supposed upstanding corporate character. *See* ComEd Ex. 43.0, 44.0, 69.0, 71.0. As has already been noted in this case, a corporation cannot

have a "character." The only purpose of Mr. Andrade's testimony is to sway the Commission based on the good deeds of ComEd and its employees.

Any supposed economic impacts that increased spending by ComEd would have are surely negated by the harm to ratepayers caused by higher rates. ComEd has no way of knowing what the total impact, that is, benefits from spending versus detriments to ratepayers, would have on the economy. Mr. Hewings employed a standard econometric model and simply input data provided to him by ComEd. Tr. at 1612-13. Neither he, nor his group, did any personal research to verify those numbers. Tr. at 1614. The only inputs they used related to ComEd's expenditures (Tr. at 1612-13), Mr. Hewings did not perform any calculations on the effects of those expenditures on customer bills, or the effects of increased bills on consumers' daily lives. The Commission should give no weight to the irrelevant arguments of Mr. Hewings or Mr. Andrade in considering the overall rate base total. Instead, the Commission should adopt the recommendations of AG/CUB witnesses Brosch, Effron, and Smith, and set the Company's rate base at a value of $6,522,071,000. AG/CUB Ex. 7.1, Schedule A.

VI. OPERATING EXPENSES

B. POTENTIALLY UNCONTESTED ISSUES

1. 2009 Amortization of Existing Regulatory Assets

Mr. Smith recommended amortizing lease abandonment cost over three years, which resulted in an adjustment of $970,000. AG/CUB Ex. 3.0 at 57, AG/CUB Ex. 1.3 Schedule C-22. In rebuttal, ComEd accepted Staff witness Hathhorn's recommendation to amortize six regulatory assets, including lease abandonment cost, reducing this expense by $980,000. ComEd Ex. 30.0 at 7.

4. Investment Tax Credit Amortization (AG)

The Company agreed to Mr. Effron's proposal to amortize proceeds from the sale of investment tax credits. AG/CUB Ex. 2.0 at 28. This amortization reduces pro forma jurisdictional income tax expense by $113,000. AG/CUB Ex. 7.1 Schedule C-9.

C. POTENTIALLY CONTESTED ISSUES

1. Incentive Compensation Cost and Expenses

It is well-established by the Commission that the Company can recover those incentive compensation costs that are reasonable, related to utility services, and of benefit to ratepayers or utility service. ICC Docket No. 07-0566 Final Order at 61. Only when a tangible benefit to ratepayers can be shown, or specific dollar savings calculated, should incentive compensation be recovered from ratepayers. ICC Docket No. 04-0779, Final Order at 44, ICC Docket No. 01-0432 Final Order at 42-43. The Company has failed to identify tangible benefits to ratepayers in its incentive compensation plans, and each should be adjusted accordingly.

The Company claims that its incentive compensation "is not extra compensation." ComEd Ex. 28.0 at 2. This is of course not true—incentive compensation is not part of employees' regular salary, and receipt of incentive compensation is not a given. Employees have an opportunity to earn it, but in actuality they might not. ComEd claims that because other utilities also offer incentive compensation (*Id.*), they cannot be competitive unless they do too. That argument is flawed in two ways. First, even if employees have the opportunity to earn incentive compensation, it is not a given that they will. Second, disallowance of all or part of ComEd's incentive compensation does not make ComEd less competitive with other utilities for human resources—the Company is free to continue offering the programs in the exact same manner, using shareholder funds. The Company fails to address the impact of the current

unemployment rate on its ability to attract and retain employees. The levels of incentive compensation that were once the norm are no longer necessary to attract and retain quality employees.

The Company has included three types of incentive compensation in its revenue requirement: the Annual Incentive Plan ("AIP"), Executive Long-Term Incentive Compensation ("Executive LTIP" or "LTIP"), and the Restricted Stock incentive program. The AIP should be limited to 50%, the amount of the actual payout under the plan in 2010. The cost of the Executive LTIP should be borne solely by shareholders, as it is driven by financial and legislative objectives and is closely related to the interests of Exelon's shareholders. The Restricted Stock incentive program should also be borne by shareholders, as it is incurred to improve ComEd and Exelon performance for the benefit of shareholders, not to improve customer service or meet other regulated utility's service requirements. Each will be addressed in turn below.

a. Annual Incentive Plan ("AIP")

ComEd's AIP is calculated for employees based on various factors, including: 1) the employee's salary, 2) a Company Performance Multiplier ("CPM"), and 3) an Individual Performance Multiplier ("IPM"). AG/CUB Ex. 3.0 at 11. The factors considered in the CPM are achievement of Key Performance Indicators ("KPIs") and financial performance under the Net Income Limiter. *Id.* The KPIs associated with the AIP are ComEd O&M, ComEd capital expenditures, SAIFI (frequency of customer outages), CAIDI (duration of customer outages), OSHA (employee safety), Focused Initiatives and Environmental Index (productivity and environmental commitment), and customer satisfaction. *Id.* at 12-13. The purpose of the Net

Income Limiter is the limit the payout on the AIP based on ComEd's financial performance. *Id.* at 13.

In its materials regarding AIP, ComEd has made it clear to employees and shareholders that the AIP is subject to reduction. *Id.* at 14-15. In December 2009, Exelon announced significant changes that will affect the AIP, effectively cutting AIP payouts in half for 2010. *Id.* This is in association with the Net Income Limiter of the plan. *Id.* However, the Company has failed to account for this 50% reduction in this case, and thus has over-calculated the amount of recovery it should receive for AIP. *Id.* at 16. It is also simply appropriate for shareholders to bear some or all of the incentive plan costs—the CPM involves metrics that benefit both shareholders and ratepayers. In both of ComEd's most recent rate cases, the Commission required ComEd shareholders to bear some of the cost of incentive compensation programs. As a result, the Company redesigned its AIP in an attempt to circumvent the sharing of such costs between ratepayers and shareholders. AG/CUB Ex. 9.0 at 7. The Company is open about the fact that it redesigned its program to eliminate the metric that was the basis of the Commission's disallowance in 07-0566. ComEd Ex. 28.0 at 4. ComEd claims "regulatory certainty is essential to enable utilities to manage their businesses..." The Company's choice to change its programs to get as much recovery as possible from ratepayers does not provide regulatory certainty, it only shifts responsibility from the Company and its shareholders onto ratepayers. AG/CUB Ex. 9.0 at 7.

The Company has failed to show that 100% of its costs under the AIP provide tangible benefits to ratepayers, and the Company does not plan to pay on 100% of its plan in 2010. There is no certainty that it will pay to that level again in coming years. Therefore, Mr. Smith's

recommendation to reduce AIP by 50% is appropriate. This results in an adjustment of $12.060 million. AG/CUB Ex. 9.0 at 9, AG/CUB Ex. 7.1 Schedule C-10.

b. Long-Term Incentive Plan ("LTIP")

The Company's executive LTIP pays out to executives who meet certain operational and cost controls over time. AG/CUB Ex. 3.0 at 17. It is limited to officers and executives of ComEd. *Id.* Similar to its changes to the AIP, ComEd made changes to the executive LTIP in an attempt to gain the Commission's approval to include those costs in rates. *Id.* at 18. However, the performance goals under the plan continue to driven by financial and legislative goals that benefit shareholders. *Id.* at 18-19. For example, Exelon's 10-K, in its description of the executive LTIP specifically names avoidance of adverse legislation as one of the metrics considered. *Id.* at 19. The Company is well aware that lobbying is typically disallowed for ratemaking purposes. *Id.* at 20. The 10-K also names financial goals, such as a certain return on equity. *Id.* at 20.

The expense of executive LTIP should be borne by shareholders. The Company has requested inclusion of 100% of executive LTIP in rates, but has failed to demonstrate tangible benefits to ratepayers for any part of LTIP. Its claim that "programs like" executive LTIP incent managers to make long-term business decisions that will benefit the business over the long term (ComEd Ex. 28.0 at 8) is not a tangible benefit to ratepayers. Therefore this cost should be disallowed, resulting in a reduction of adjusted by $2.158 million. AG/CUB Ex. 9.0 at 9-11, AG/CUB Ex. 7.1 Schedule C-10

c. Key Manager Restricted Stock Plan

ComEd's Key Manager Restricted Stock program is limited primarily to directors and managers, who are awarded shares of Exelon stock. AG/CUB Ex. 3.0 at 23. Stock-based

compensation expense should not be charged to ratepayers. *Id.* at 25. The program is designed to improve ComEd and Exelon performance for the benefit of shareholders, and provides no tangible benefit to ratepayers. AG/CUB Ex. 9.0 at 11. The objectives of maximizing shareholder value are generally opposed to the objectives of minimizing costs to ratepayers. AG/CUB Ex. 2.0 at 25. Additionally ComEd has admitted that key managers will see an approximate 33% reduction in the 2010 grant value of restricted stock, which it does not appear that ComEd has accounted for in its request. AG/CUB Ex. 9.0 at 11.

Such a program so obviously tied solely to shareholder interests must be disallowed. This results in a reduction of $2.123 million. AG/CUB Ex. 9.0 at 11-12, AG/CUB Ex. 7.1 Schedule C-10.

2. Rate Case Expenses

a. Rate Case Expenses of the Instant Case

The PUA allows attorney and expert witness fees incurred to prepare and litigate a general rate case filing to be recovered by a utility. 220 ILCS 5/9-229. The Commission must "specifically assess the justness and reasonableness" of these amounts, and the issue must be "expressly addressed in the Commission's final order." Id.

The Company has requested recovery of $8.5 million in rate case expenses for the current case. AG/CUB Ex. 9.0 at 18. The Company has failed to meet the requirements of the PUA to show that these costs are just and reasonable. ComEd has not provided information with the level of specificity required to make such a determination, such as failing to turn over the hours charged in order to determine the reasonableness of attorneys fees, and has failed to justify paying exorbitant rates, up to almost $1,000 per hour, to some consultants. AG/CUB Ex. 9.0 at 20, 22. The Company has included in its calculations costs incurred as a result of its alternative

regulation litigation, docket 10-0527, although the PUA allows recovery only for costs related to litigating a general rate case (See discussion below). ComEd has also presented multiple witnesses on the same topic, such as presenting four cost of capital witnesses and three others who comment on cost of capital. AG/CUB Ex. 9.0 at 24. The Company has even included expenses for consultants who provide no testimony of rate analysis, and bill $225 to $980 per hour, and with no more detail than "services rendered in the month of April" to justify some amounts. *Id.* at 22. Given the poor economy and the high unemployment rate, one would expect the Company to show a higher degree of sensitivity to holding down rate case costs. $980 an hour to a consultant who presents no testimony, with no description of services, is outlandish to ask ratepayers to pay. While the Company is free to present its case as it chooses, it cannot recover the excessive cost of unreasonable and unjustified witnesses from ratepayers. *Id.* at 26. It is likely that the Company will not even spend up to its estimate of $8.5 million based on the costs it has incurred to date; as of October 31, deep into the case since much of the attorney and consultants' work comes before the case is even filed, ComEd had only incurred $4.274 million of expense, about one-half of the claimed total estimate. *Id.* at 20. Requests such as $890,000 for "Post Direct Testimony Witnesses," which are not itemized by the Company, should be reduced to a reasonable level.

Specific adjustments supported by the testimony of Mr. Smith, AG/CUB 3.0, AG/CUB 9.0, are shown below:

Summary of AG/CUB Adjustments to ComEd's Rate Case Expense

Description		**Amount**
Economic Development/Jobs	$	(225,000)
Cost of Capital	$	(260,000)
Sullivan and Co., rate case support	$	(150,000)
Alternative Regulation witnesses and consultants	$	(250,000)
Over-estimate – Direct	$	(555,340)
Budget Overrun for CWC consultant	$	(100,000)
Adjustment to Post Direct witnesses	$	(661,000)
Attorneys Fees (per Staff)	$	(2,500,000)
Total AG/CUB adjustments	**$**	**(4,701,340)**
Company request	$	8,500,000
AG/CUB Proposed Total Allowance	**$**	**3,798,660**
Normalization Period, in Years		3
AG/CUB Proposed Annual Allowance ($1,000s)	**$**	**1,266,000**
ComEd Requested Annual Amortization Expense	$	2,833,000
AG/CUB Adjustment to ComEd's Annual Amount	**$**	**(1,567,000)**

Rate case expenses should be normalized over three years rather than amortized, as the Company as proposed. AG/CUB Ex. 3.0 at 46-47. Ratepayers are at risk for over-paying for a utility's rate case expense if too short of a period for amortization is used. *Id.* at 46. For example, ComEd's amortization of its 2005 rate case was due to expire on December 31, 2009, but because new rates have not yet gone into effect, the Company has continued to recover on that expense which has already been fully reimbursed. Id. That same risk is present here—if a three-year amortization is used, and rates are in effect for longer than three years, ComEd will recover more than it has actually expended on this rate case. Id. Moving to a normalization approach for rate case expense, such as that which is used for O&M expense, helps to mitigate that risk. Id. at 47-48.

Normalized over a three-year period, Mr. Smith's adjustments to reduce or remove ComEd's unreasonable and unjustified rate case expenses result in a $1,567,000 reduction. AG/CUB Ex. 7.1 Schedule C-12.

b. Alternative Regulation Case

ComEd has included alternative regulation litigation expenses in their request for recovery, though the PUA allows recovery only for fees incurred as part of a "general rate case filing." (AG/CUB Ex. 9.0 at 27-28, 220 ILCS 5/9-229), and the Company has refused to specify exactly what amounts for which it seeks recovery are actually related to the alternative regulation litigation for every attorney and witness involved in both cases. ComEd Ex. 30.0 at 14. The Company claims that it negotiated a flat rate with the R3 law firm, who gets the lion's share of the $8.5 million ComEd seeks to recover, for both the rate case and alternative regulation dockets. Id. This was ComEd's own mistake. The PUA is clear that only expenses related to a rate case filing are recoverable. At the very least, the Company should have turned over the hours each attorney and witness has worked on each case so that a specific percentage of their time could be clearly allocated to each case. Instead, the Company has taken the unbelievable position that R3 law firm charged nothing extra to take on the alternative regulation docket. Id. Both the Company and the Commission know that is simply not true, and ComEd's attempt to collect legal fees from alternative regulation through this case by making such a claim is incredible.

Mr. Smith's adjustment to this item, a $250,000 disallowance, is included in his overall rate case expense adjustment listed in subsection (a) above.

3. Administrative and General (A&G) Expenses

a. Exelon Way Severance Amortization

The Company has proposed to include severance expenses resulting from its restructuring program, "The Exelon Way," that it incurred in 2003 and 2004. AG/CUB Ex. 2.0 at 22. The restructuring program was designed to achieve savings of $70 million annually, and the

Company incurred $158 of costs to achieve those savings. Id. However, the Company chose not to begin amortizing those costs until 2007, rather than when they were incurred, and when the savings from the program were realized, three to four years earlier. *Id.* The benefits of the restructuring were retained solely by shareholders from 2003 through 2006. *Id.* at 23. In 2007, the Company chose to begin a 7.5 year amortization period for those expenses, approximately $21 million of which is included in the 2009 test year operation and maintenance expenses. *Id.* at 22. The Company began seeing savings from the restructuring program in 2003, immediately after it was implemented. AG/CUB Ex. 8.0 at 16. Therefore, the Commission should calculate the amortization of these expenses as if it has begun in 2003, when those savings were first retained by the Company and its shareholders, which using a the Company's preferred 7.5 year amortization would mean that the expenses would now be fully recovered. Id. at 15-16. By the time the rates in this case go into effect, the Company will have collected on this amortization for almost five and a half years, and received savings from the program for an additional four years prior. The Company has fully recovered this expense, and it should now be removed. This results in an adjustment of $18,665. AG/CUB Ex. 7.1 Schedule C-4.

b. Accounts 920-923

This issue is addressed in the Legal Fees- IRS Dispute heading.

c. Pension Costs

The 2009 test year recorded amount of pension expense, which is based on a 2010 actuarial report rather than the 2009 test year expense, was abnormally high in comparison with recent years. AG/CUB Ex. 3.0 at 25, AG/CUB Ex. 9.0 at 17. In fact, the Company's request for $51.427 million exceeds the amount in each prior year since at least 2004. AG/CUB Ex. 9.0 at 17. The Company has claimed that this is primarily a result of investment losses experienced in

2008 as a result of the market recession. AG/CUB Ex. 3.0 at 31. Using this abnormally high amount is in appropriate.

The Company claims that use of the 2010 actuarial report is appropriate here because actuarial reports have been used in other cases in the past. ComEd Ex. 29.0 at 32-33. However, the pension expense in those cases was significantly lower, by as much as 259%, than what has been requested here. AG/CUB Ex. 9.0 at 14. Use of the actuarial reports in those cases cannot then be compared to this case, where the markets have significantly changed the Company's pension expense. Additionally, the report relied on by the Company was issued in March of 2010, and just since this case was filed, the Company's 2010 estimate, on which it based its request, had decreased. Id.

The 2010 actuarial study, which exceeds the test year recorded amount by 27.6 percent, should not be the basis for the pension expense allowance. *Id.* at 30. Instead, Mr. Smith recommends that the amount should be reduced by $14.209 million, the amount actually expended in the test year. *Id.* at 30, AG/CUB Ex. 7.1 Schedule C-11.

Moreover, Mr. Smith recommends that the cost of the Supplemental Executive Retirement Plan ("SERP") should be disallowed, since provision of additional compensation to Exelon's highest paid employees in retirement benefits relative to the Company's other employees is not a reasonable expense that should be recovered in rates. AG/CUB Ex. 3.0 at 33-35. SERPs provide retirement benefits to executives in excess of the limits placed by the IRS regulations on pension plan calculations. *Id.* at 34. Therefore, the Company's executives would still receive the exact same retirement benefits available to any other employee without the SERP, and those benefits would even be proportional to their significantly higher salary. Id. Ratepayers should not be charged for this extra benefit that is available only to a select group of

highly compensated individuals, particularly during a period of deep economic recession and high unemployment. AG/CUB Ex. 9.0 at 18. ComEd is free to continue providing this benefit to its executives, but not at a cost to ratepayers. Therefore, 2009 SERP should be disallowed. Settlement costs for retired executives under the SERP should also be disallowed.

The above discussions result a total reduction of $39,478,000 to (1) correct for the company's increase from 2009 to 2010 pension expense ($14,209,000), (2) remove 2009 Supplemental Executive Retirement Plan [SERP] and SERP settlements expense ($2,424,000) and (3) to normalize abnormally high 2009 defined benefit pension expense based on prior year average ($22,845,000). AG/CUB Ex. 7.1, Schedule C-11.

d. Wages and Salaries *Pro forma* Adjustment

The number of ComEd employees has steadily declined from early 2009 through August 2010, including a sharp drop from June to July of 2009 related to the 2009 severance program. AG/CUB 2.0 at 18-19. The pro forma adjustment recognized by the Company was of only 108 employees; however, the actual number of employees had decreased by 300 from January 2009 through August 2010. *Id.* at 19. The Company stated that it did not recognize this full decrease because overtime offset the difference. *Id.,* ComEd Ex. 30.0 at 5. However, Mr. Effron determined that the decrease in payroll for those employees significantly exceeded the increase in overtime. AG/CUB Ex. 2.0 at 19-20, AG/CUB 9.0 at 11-12. Based on the Company's requested pro forma adjustment, payroll expense in 2010 should actually be about $5.1 million higher than in 2009. AG/CUB Ex. 9.0 at 12. However, the Company anticipates that payroll costs will actually be $286,829 lower than 2009. Id. Clearly, ComEd's calculations are flawed.

Mr. Effron recommends an adjustment to reflect the decrease in employees through August 2010, net of the effect of overtime. AG/CUB Ex. 2.0 18-20; AG/CUB Ex. 8.0 at 11-13.

This adjustment results in a reduction of $4,152,000 to pro forma test year expenses. AG/CUB Ex. 9.0 at 12, AG/CUB Ex. 7.1, Schedule C-3.

f. Corporate Aircraft Costs (Uncontested b/t Company and Staff)

ComEd initially requested $918,000 for the fractional ownership interest in three corporate jets. AG/CUB Ex. 1.0 at 48. The Company claimed that use of corporate aircraft rather than commercial carriers was more efficient, but was unable to produce any plausible calculations or analyses to support that notion. Id. at 48-49. Mr. Brosch recommended that ComEd be allowed to recovery only half of the costs allocated to corporate aircraft, based on his calculation of what last-minute first-class flights would cost. *Id.* at 49. ComEd has adopted the recommendation of Mr. Brosch. ComEd Ex. 29.0 at 2. No additional adjustment is necessary. AG/CUB Ex. 7.1, Schedule C-18.

g. Perquisites and Awards

Mr. Smith recommends that retention awards of $566,000 ($501,000 jurisdictional) that were not already removed by ComEd should be removed. AG/CUB Ex. 3.0 at 54-56. In the 2009 test year, a year with a severe recession and high unemployment, ComEd exceeded the total it had spent on retention awards for the previous three years. AG/CUB Ex. 9.0 at 35. Company policy is clear that management retains the right to modify or revoke its retention bonus policy at any time, but chose not to do so during this tumultuous time. AG/CUB Ex. 3.0 at 55. The Company has not explained why it was significantly more difficult to retain employees during this period of high unemployment than it was when the economy was healthier. Additionally, ComEd included amounts from affiliates that are beyond the amounts provided for in the annual incentive plans. AG/CUB Ex. 3.0 at 54.

A normalized amount is more appropriate than use of the extraordinarily high payout of retention awards in 2009. Mr. Brosch has proposed a reasonable, four-year average, which provides for an annual allowance of $688,000. *Id.* at 55. This results in an adjustment of $737,000 ($519,000 jurisdictional).

Mr. Smith also recommends that Company shareholders share the cost of performance-based recognition awards 50/50 with ratepayers. Performance-based awards are designed to reward significant employee contributions to Exelon's success. *Id.* at 56. Awards under this policy include cash awards up to $5,000, gift certificates, and other non-cash spot awards. Id. Given that these awards are discretionary and are designed to benefit both shareholders and consumers, Mr. Smith recommends 50/50 sharing of these costs. Id. Like the retention awards described above, the Reward and Recognition policy also provides that the program may be modified or revoked at any time. Id. Again, the Company chose not to make changes during the test year. This results in an adjustment of $419,000 ($372,000 jurisdictional). The total appropriate adjustment for perquisites and awards of $1.392 million jurisdictional. AG/CUB Ex. 3.0 at 54-56; AG/CUB Ex. 7.1 Schedule C-13.

h. Severance Expenses

Mr. Effron proposes two adjustments to the Company's severance expenses. The first recognizes that correct balance of amortized Exelon Way severance costs since the amortization of those costs should be deemed to have commenced when the cost savings were commenced. See above discussion in section XXX of Exelon Way Severance Amortization, AG/CUB Ex. 2.0 at 22-23; AG/CUB Ex. 8.0 at 14-17.

The second adjustment removes 2009 severance costs from the Company's revenue requirement, which the Company seeks to recover and amortize. AG/CUB Ex. 2.0 at 24. The

savings retained by shareholders since the program was implemented in mId-2009 will be in excess of $25 million by the time rates from this case go into effect in June 2011. Id. The 2009 severance program cost the Company $14.4 million. Id. Therefore, allowing the Company to recover 2009 severance expenses in this case would be double recovery—once from the savings already retained by shareholders, and a second time by consumers. Id.

If the Commission does authorize the inclusion of 2009 severance costs, the amortization period should be 7.5 years rather than three years as the Company has proposed. *Id.* at 24-25. The amortization period should be extended to better match the realization of benefits. *Id.* at 25. Ms. Houtsma argued that Mr. Effron did not justify a 7.5 year amortization period (ComEd Ex. 29.0 at 46); however, she does not dispute that benefits from the program should continue beyond just those years. AG/CUB Ex. 8.0 at 18. ComEd's argument that disallowing these costs is single-issue ratemaking (ComEd Ex. 55.0 at 29) is a straw man argument. Although the Company would prefer to downplay the validity of Mr. Effron's arguments, along with Staff witness Mr. Tolsdorf who makes similar points, the Commission's duty is to evaluate each cost separately, and doing so does not constitute single-issue ratemaking.

The total adjustment Mr. Effron makes to ComEd's projected severance expenses reduces the Company's operational and maintenance expenses by $22,942,000 to the severance expense amortization. AG/CUB Ex. 7.1 Schedule C-4.

i. Charitable Contributions

Mr. Brosch proposes that the cost of test year charitable contributions that management elected to incur in the test year should be shared between ratepayers and shareholders. AG/CUB Ex. 1.0 at 47. Sharing those costs would provide ComEd with incentive to carefully prioritize its funding. Id. ComEd seeks cost-plus, full recovery regulatory treatment of its charitable

contributions. Id. While CUB supports ComEd participating in charitable giving, that giving is just that—charitable. If ComEd expects its ratepayers to be charitable, then its shareholders should be as well. If charitable contributions were not included in rates, then ratepayers would be left with more discretionary income from which they may be able to select and contribute to the charities of their choice. Id. at 47-48. Instead, ComEd collects from ratepayers and funds charities that might not be the charities ratepayer would prefer, and ComEd receives the benefit of the goodwill engendered by such giving. Id. at 47-48. ComEd receives other benefits as well, such as having its logo on materials distributed by the charitable organization and the benefit of listing that organization in its own promotional materials. Id. Mr. Brosch testified that he is not aware of any utility outside of Illinois, or any unregulated business, that is able to fund discretionary charitable contributions out of anything other than its earnings. Id. at 47. However, rather than proposing that shareholders should bear 100% of these contributions, Mr. Brosch has proposed that they may recover 50% from ratepayers. Id. ComEd witness Mr. Fruehe's argument that the 50% disallowance should be rejected because it is arbitrary ignores the fact that this issue is a matter of regulatory policy, and thus some discretion is necessarily involved. AG/CUB Ex. 7.0 at 31. These are discretionary expenditures that are not necessary, and in fact have no bearing whatsoever on the provision of safe and reliable service for customers. A disallowance is appropriate, and Mr. Brosch's proposal that ratepayers would bear even half of the expense is generous.

Mr. Brosch's proposed adjustment is a reduction of $2,803,000 to reflect reasonable ratepayer funding of charitable contributions. AG/CUB Ex. 7.1, Schedule C-17.

j. Legal Fees – IRS Dispute

Legal fees associated with an IRS dispute associated with the sale of fossil generating units in 1999 are non-jurisdictional and should be disallowed. AG/CUB Ex. 2.0 at 21-22, AG/CUB Ex. 8.0 at 13-14. The Company has recognized as much by removing ADIT related to the sale from the deferred taxes deducted to plant in service in calculating rate base. AG/CUB Ex. 2.0 at 21. ComEd stated that it did so because "The tax being deferred relates to the gain incurred on the sale of fossil generating stations previously owned by ComEd, thus it is non-jurisdictional." Id. The legal fees associated with a dispute of the sale cannot be jurisdictional of the sale itself was not.

ComEd claims that because the Company used a general allocator to allocate expenses between transmission and distribution in Account 923, the account to which the legal fees were charged, it is appropriate to claim a portion of those fees as jurisdictional. ComEd Ex. 30.0 at 10. ComEd Mr. Fruehe acknowledges, however, that some individual items in that account are "more closely related" to particular functions. Id. The Company's use of a general allocator for an account, when it is undisputed that particular line items are solely related to a particular function, is inappropriate.

This results in a reduction of jurisdictional operations and maintenance expenses by $2,187,000. AG/CUB Ex. 7.1 Schedule C-6.

k. Professional Sporting Activity Expenses

The Company has requested that ratepayers reimburse executives for attending professional sporting events. They have included the costs of tickets, catering, and well-appointed skyboxes. AG/CUB Ex. 3.0 at 53-54. However, ComEd claims it is unable to provide any more detailed information, such as exactly how much was spent on catering, alcohol, etc. Id.

at 54. ComEd's justification for inclusion of these expenses is that they are good for team building, development of customer relationships, and employee recognition. ComEd Ex. 30.0 at 11. CUB is curious just how many ComEd customers receive the privilege of having ComEd pay for their skyboxes to "build customer relationships," and why ComEd feels the need to build customer relationships in this matter at all considering they hold a monopoly on electric delivery service in their territories. Obviously this expense is not necessarily for the provision of utility service. ComEd is free to treat its executives to lavish skyboxes on shareholders' dime.

Disallowance of this costs results in a reduction of $511,000 ($467,000 on a jurisdictional basis. AG/CUB Ex. 7.1 Schedule C-13.

l. Workforce Expense Reduction

This issue has been addressed above in the section entitled Wages and Salaries Pro Forma Adjustment.

6. Tax Repair Methodology – New IRS procedures

The IRS recently issued a new Procedure, introducing a new method of tax accounting for repair charges. AG/CUB Ex. 2.0 at 28. The effect of the change is to enhance the current repair allowance deduction for certain expenditures, including "network assets," that are capitalized for financial reporting purposes. Id. at 28-29. The change would decrease the income taxes currently payable and its authorization is automatic; however, ComEd has not implemented the change. Id. at 29. The Company states that it, along with other utilities, is awaiting further clarification from the IRS on this point. ComEd Ex. 29.0 at 38-39. However, Mr. Effron testifies that the majority of other electric transmission and distribution companies have taken advantage of the enhanced income tax deduction. AG/CUB Ex. 8.0 at 20.

Absent any mechanism to preserve the benefits of the increased tax deductions for ratepayers, shareholders will receive a windfall if the Company decides to make the changes

after this case. AG/CUB Ex. 2.0 at 33. ComEd claims that the benefits will simply serve to reduce the non-recovery of new investments that ComEd will make between now and its next rate case. ComEd Ex. 29.0 at 29-30. If this was a plausible argument, then ComEd could choose not to include any rate base deductions in its rate case, such as depreciation and ADIT, on the theory that they would surely be balanced out by investments they would make later. Even if it were a plausible argument, the benefits of the repair allowance may well be more than the investments ComEd will make before its next rate case once depreciation and ADIT are considered. AG/CUB Ex. 8.0 at 20.

If ComEd implements this change before the record in this case closes, then its rate base should be adjusted. AG/CUB Ex. 2.0 at 33. Otherwise, the Commission should order the Company to: 1) maintain the effect on any Section 481(a) adjustment related to the new repair allowance in a reserve account; and 2) keep a record of any increase to the ongoing repair allowance decision from the effective date of the accounting change. Id. The cumulative revenue requirement effect of the change, with appropriate carrying charges, should then be credited to customers at the time of the Company's next rate case. Id.

7. Depreciation of Intangible Plant

The Company has requested amortization on additions to post-test year intangible plant. There must be a matching adjustment to recognize reductions to amortization from intangible plant becoming fully amortized by March 31, 2011. AG/CUB 8.0 at 19. Certain assets of intangible plant which began their amortization period in 2002 will be fully amortized by March 31, 2011. Id. ComEd agrees with that fact. ComEd Ex. 55.0 Rev. at 34. ComEd's only argument against removing those fully-amortized assets from rate base is that ComEd made other investments in late 2009 should balance out the amortized assets. Id. The Company included all of its 2009 investments in rate base, and its assertion that "A full year's effect of the

depreciation on these projects would more than offset the impact of the lower amortization related to the fall off of the older projects" is not justification for keeping fully-amortized assets in rate base. Allowing such would result in recovery well beyond the Company's actual expense for these assets.

Disallowing continued amortization of 2002 intangible plant, reducing pro forma amortization expense by $4,721,000, and elimination of the amortization of 2005 intangible plant, reducing pro forma amortization expense by $908,000 results in a total reduction to amortization expense is $5,629,000, which on a jurisdictional basis, this reduces pro forma amortization expense by $4,987,000. AG/CUB Ex. 8.0 at 19, AG/CUB Ex. 7.1 Schedule C-7.

8. Late Repayment Charge Reclassification

Late payment charges are levied on customers who have unpaid and delinquent customer account balances. AG/CUB Ex. 1.0 at 40. These charges are 1.5% for all customers except for municipalities and qualifying schools, which are assessed a 1.0% charge. Id. ComEd has excluded $13.986 million of its 2009 test year recorded late fees as non-jurisdictional; however, not all the late fees collected by ComEd have been recognized by FERC, the only other jurisdiction to which they could be claimed. Id. at 40-41. ComEd has failed to explain how charges collected from delivery service customers for not paying their delivery service bills could not be considered jurisdictional. Instead, it argues that allocating all late fees as jurisdictional would result in a subsidy for RES customer (ComEd Ex. 30.0 at 21), but does not explain how this is so. To reflect the late payment charge reclassification to include all non-FERC late payment charges, an adjustment to revenues of $13,986,000 is necessary. AG/CUB Ex. 7.1 Schedule C-14.

9. Illinois Electricity Distribution Taxes

The Company has proposed a ratemaking adjustment to increase the recorded amount of the IEDT by $7.0 million more than it actually paid in the test year. AG/CUB Ex. 1.0 at 50. Two separate numbers go into this calculation—the tax paid and the credit received from the Illinois Department of Revenue. Id. A credit is issued by the IDOR to return to the Company the difference between the actual IEDT it pays and the statutory caps in place. Id. at 50-51. The Company has chosen to base these two figures on different calculations. Id. at 50. The Company employs weather normalization to estimate the gross tax, but a six-year average of historical IEDT credits to estimate the offsetting tax credit. AG/CUB Ex. 7.0 at 37. Mr. Brosch has proposed an adjustment, based on ComEd's own analysis, to include the Company's estimation of its 2009 gross tax. AG/CUB Ex. 1.0 at 50. The Company, however, objects to the inclusion of that information in calculations for purposes of this case because the Company does not actually receive the 2009 credit in 2009. ComEd Ex. 30.0 at 11-12.

ComEd's calculation is flawed, as it employs weather normalization to estimate the gross tax owed but a six-year average to calculate the credit it will receive. AG/CUB Ex. 7.0 at 37. It is more appropriate to base the calculation of IEDT on actual IEDT taxes paid in the 2009 test year, reduced by the Company's most recent estimate of the IEDT credit that is expected to be received for tax year 2009. AG/CUB Ex. 1.0 at 51. Both the tax and the credit should be calculated by the same standard, and the Company should not be permitted to choose actual figures for one and weather-normalized figures for another simply because it increases its recovery.

As such, ComEd's estimation of a weather-normalized IEDT produces a large upward adjustment. Mr. Brosch calculates a reduction of $1,387,000 by using a consistent approach to both the gross tax and the credit. AG/CUB Ex. 7.1 Schedule C-19.

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

The Company receives subsidies from the federal government for prescription drug benefits included in its retiree health plans. AG/CUB Ex. 2.0 at 25. As a result of the 2010 health care reform legislation, those subsidies will be subject to income taxes. Id. ComEd accrues liability for future retiree health care costs and also accrues the income tax effect of the accrued expense. Id. The accrued liability is a credit balance, while the offsetting income tax effect is a debit balance (or in other words, a deferred tax asset). Id. The Company seeks to establish a regulatory asset for the subsidy that was previously not adjusted for the income tax that ComEd had previously assumed would continue on a tax-free basis. Id.

CUB does not take issue with the establishment of a regulatory asset for this purpose, but disagrees with the Company's proposal to amortize that asset over only three years. Id. at 26. The benefits of the subsidy received in just 2009 will be realized over approximately eleven years. Id. Therefore, the regulatory asset should be amortized over at least ten years. Id. This is consistent with when the federal government remits the cash subsidies to ComEd, and is the only reasonable approach. AG/CUB Ex. 8.0 at 18. The result of this more reasonable amortization period is a downward adjustment of $2.207 million. AG/CUB Ex. 7.1 at Schedule E.

13. Income Taxes (Derivative Adjustments)

The Company is permitted to deduct interest expenses for income tax purposes, and the Commission does not typically approve a specific amount of debt as "reasonable" for recovery for that purpose because it is derivative of the overall rate base and weighted cost of capital. AG/CUB Ex. 1.0 at 44. However, in its order, the Commission can quantify and synchronize the amount of interest being allowed recovery by applying the weighted cost of debt to the approved rate base. Id. Because AG/CUB is proposing a revised level of Rate Base for ComEd, the

resulting change in deductible interest for income tax purposes is significant. Id. Mr. Brosch recommends an adjustment of $14.306 million based on the rate base recommended by AG/CUB witnesses. AG/CUB Ex. 7.1 at Schedule D, AG/CUB Ex. 7.1 at Schedule C-15. No party has objected to the Commission quantifying the amount of interest in its final order.

VII. RATE OF RETURN

A. OVERVIEW

The Commission is tasked with equitably balancing the needs of the company—that is, what investors require—with the requirement that rates be affordable for customers. 220 ILCS 5/1-102. Therefore, the Commission must be very careful not to award a higher rate of return than would actually be required in true market circumstances so it does not unfairly burden ratepayers. The final decision must be based on the facts and evidence put forth in this case. It must be confined to the legal standards underpinning the regulatory process.

E. COST OF COMMON EQUITY

1. Overview

For any company, the cost of equity is the return that investors require to choose an investment in the Company over other available investment options.[4] This return is a cost of doing business because any company needs to attract investors in order to maintain access to capital on reasonable terms. In this case, ComEd is a wholly-owned subsidiary of Exelon Corporation, so ComEd's single equity shareholder is Exelon, and is unlike a publicly traded company which would have many different equity investors. AG/CUB Ex. 4.0 at 5. Despite the alarmist testimony filed by the Company, ComEd is not a relatively risky investment.

[4] The terms "cost of equity" and "return on equity" are used interchangeably by the financial community, and as such are used interchangeably here.

Furthermore, the company has made requests in this case that would further reduce investors' risk by increasing fixed cost recovery. ComEd is requesting that the Commission approve a base return on equity of 11.5%, the product of an 11.1% "base return on equity" and a 0.40% adjustment to the allowed return on equity related to the implementation of energy efficiency and demand response programs. ComEd Ex. 4.0 at 389-385. Instead, AG/CUB witness Chris Thomas determined that the appropriate return on equity ("ROE") for ComEd is 8.94% based upon his analysis using models commonly adopted by the ICC for this task and the longstanding legal framework determined by two fundamental U.S. Supreme Court decisions. AG/CUB Ex. 4.0 at 37.

The first decision addressing an appropriate, or fair, cost of equity is *Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923) ("*Bluefield*"). The second is the *Federal Power Commission et. al. v. Hope Natural Gas Co.*, 320 US 591 (1944) ("*Hope*"). Together, the *Hope* and *Bluefield* decisions establish that utilities are entitled to the opportunity to earn a fair return on their prudent and reasonable investment that is commensurate with the returns earned by other firms of comparable risk. The Commission's task, therefore, is to ensure that the cost of equity capital used to develop rates compensates investors for their investment risk, while assuring that customers do not pay an excessive or unreasonable return in those rates. A return which accomplishes both objectives can only be based on an evaluation of the relative riskiness of the regulated company.

Evaluating the relative risk involved in an investment is by necessity a point-in-time evaluation: the measure of a fair return will change over time as the equity markets change. Like any regulatory commission, the ICC must approximate a fair return because ComEd is not a publicly traded company. There are no stock prices available which would make this task

simple. To do so, the Commission has relied on two well-established financial models – the Discounted Cash Flow ("DCF") model and the Capital Asset Pricing Model ("CAPM") – which attempt to approximate what return would induce someone to invest in ComEd if that option were available based on how risky an investment ComEd is perceived to be. Mr. Thomas identified a few simple principles that can help the Commission determine the appropriate ROE:

- To an investor, "risk" is the probability that an investor will not receive a sufficient return on their investment.
- Risk is important because of the correlation between the riskiness of an investment and the expected payout that investors require for making that investment — low risk investments require lower rates of return to entice investors.
- Utilities are generally less risky than other firms in the economy.

AG/CUB Ex. 4.0 at 4.

It is a well accepted fact that investors will take on additional risk only if they expect to receive a higher rate of return. As ComEd witness Dr. Samuel Hadaway discusses, literally dozens of textbooks and hundreds of academic articles have addressed the issue. ComEd Ex. 11, at 7. As a general rule, low-risk securities, such as U.S. Treasury bills, have the lowest returns; returns from longer-term Treasury bonds and corporate bonds are higher because of increased risk, and returns from common stocks and other more risky investments are even higher. ComEd Ex. 11, at 7. It is well accepted that returns on common stock are closely correlated with the risk of the underlying business, and that utility stocks are less risky than many other common stocks. AG/CUB 4.0. at 8.

Within the American economy, public utilities like ComEd have a relatively unique status. They have exclusive franchises to provide utility service in their service territories in

exchange their rates are regulated by public utility commissions like the ICC. This structure affords utilities the opportunity to earn a fair return on their prudent and reasonable investment that is commensurate with the returns earned by other firms of comparable risk, as established by the *Hope* and *Bluefield* decisions. Of course, this is not a risk free arrangement. Utility investments are still subject to some degree of risk; utilities often cite the after-the-fact prudence review as a risk to their ability to recover their investments. As ComEd founder Samuel Insull point out back in 1891:

> In order to protect the public, exclusive franchises should be coupled with the conditions of public control, requiring all charges for services fixed by public bodies to be based on cost plus a reasonable profit. It will be found that this cost will be reduced in direct proportion to the protection afforded the industry.
>
> The more certain this protection is made, the lower the rate of interest and the lower the total cost of operation will be, and, consequently, the lower the price of the service to public and private users. If the conditions of our particular branch of public service are studied in places where there is a definite control, whether by com- mission or otherwise, it will be found that the industry is in an extremely healthy condition, and that users and taxpayers are correspondingly well served.[5]

The protection afforded by public utility regulation reduces the risk of utility investments and allows them to access capital at cost lower than the costs incurred by other firms. The trick is then to determine what the costs incurred by other firms are and how the risk of utility investments compares.

Since the Commission's Final Order in ComEd's last rate case, issued September 10, 2008 in ICC Docket No. 07-0566, the capital markets have been rather chaotic. In fact, some have referred to this market turmoil as the worst since the 1929 Great Depression because there have been dramatic declines in equity valuations, numerous bankruptcies (especially in the

[5] Insull, Samuel. "Standardization, Cost System of Rates, and Public Control" (1898). Reprinted in S. Insull, *Central-Station Electric Service*, 34–47. Chicago: Privately Printed, 1915.

financial sector), and an overall instability in the economy during the last two years. While the economy has begun to recover, the Federal Reserve has noted that the recovery is slow and projected to stay that way:

> "Although output growth should be somewhat stronger in 2011 than it has been recently, growth next year seems unlikely to be much above its longer-term trend. If so, then job creation may not exceed by much the increase in the size of the labor force, implying that the unemployment rate will decline only slowly."[6]

During this time, utility companies have generally fared better than the overall economy. This observation is confirmed by an article published in Value Line on August 26, 2010:

> As of August 17, 2010, the average yield on electric utility equities was 4.5%. This was more than twice the median of all dividend-paying stocks under Value Line coverage.
>
> With the Federal Reserve keeping interest rates historically low, and reluctant to raise them anytime soon, investors seeking income don't have a lot of appealing options. Interest rates on savings accounts and money-market funds are minuscule. Rates on certificates of deposit aren't much higher. So, some investors are turning to electric utility equities. As of August 17, 2010, the Value Line Utility Average (which includes other kinds of utilities in addition to electric companies) was up 2.7% year to date. That's not much, but it compares favorably with the Value Line Composite Average, which was virtually unchanged over that span. When dividends are factored in, the relative advantage of utility stocks so far this year is even greater.[7]

Investor confidence in the sample utilities remains strong relative to the general economy. Both Dr. Hadaway and Mr. Thomas prepared summaries of data which demonstrate the same conclusion. Dr. Hadaway highlights the differences in the adjustment methodologies

[6] Taken on 10/15/10 from: http://thehill.com/blogs/on-the-money/801-economy/124369-bernanke-forecasts-slow-recovery-hints-at-further-fed-action

[7] Investing in Electric Utility Stocks, Paul E. Debbas, CFA, August 26, 2010, available at: http://www.valueline.com/Stocks/Commentary.aspx?Id=9382

applied by Yahoo Finance and S&P in presenting stock price information and the S&P 500 index,[8] and he presented "corrected" stock prices changes in the following table:[9]

Change in Stock Prices

	(1) High Price	(2) Low Price	(3) Present Price	(4) High to Low	(5) Low to Present	(6) High to Present
S&P 500 Index	$1,565.15	$ 676.53	$1,165.15	-56.8%	72.2%	-25.6%
Dow Jones Utility Average	$ 520.89	$ 290.68	$ 403.91	-44.2%	39.0%	-22.5%
Thomas Utility Prices	$1,375.11	$ 837.31	$1,275.25	-39.1%	52.3%	-7.3%

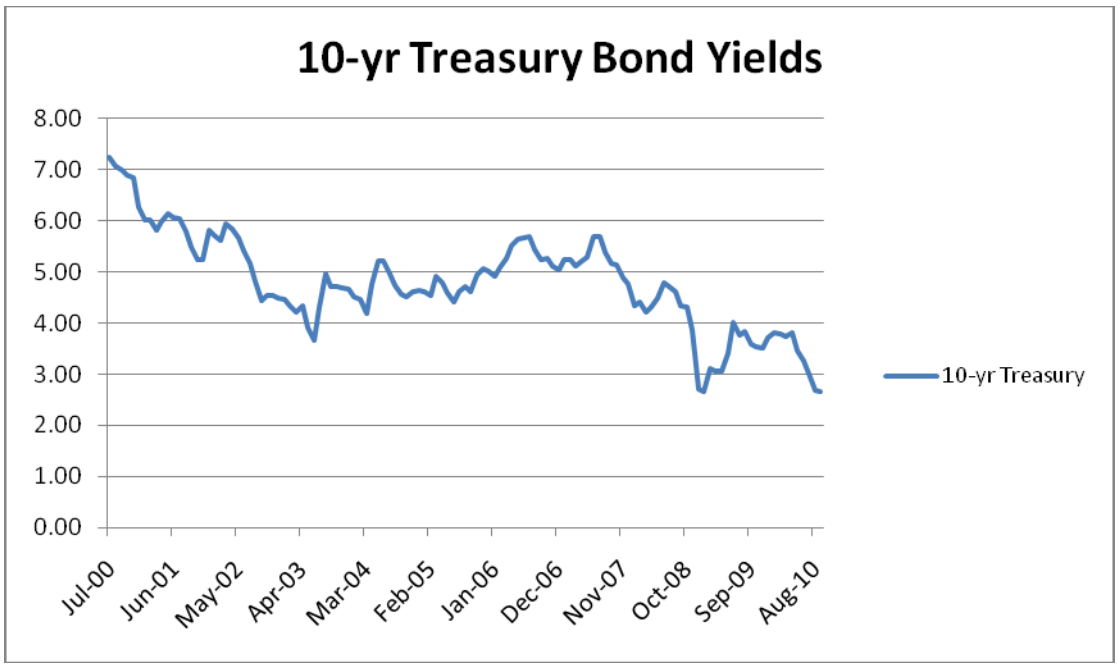
Notes:
Column 1: Closing price as of October 9, 2007, excluding dividends.
Column 2: Closing price as of March 9, 2009, excluding dividends.
Column 3: Closing price as of October 8, 2010, excluding dividends.
Column 4: Compound growth from column 1 to column 2.
Column 5: Compound growth from column 2 to column 3.
Column 6: Compound growth from column 1 to column 3.

The companies in this analysis declined by 39.1% at a time when the overall stock market declined by 56.8%. Even as the market was still 25.6% below its highest level, the sample utilities were only 7.3% below their collective high. As this data shows, investor confidence in public utilities is higher than it is in other firms in the economy.

By comparison, there is a distinct downward trend of treasury bond returns as investors seek to reduce their exposure to risk and invest in low risk securities. The following chart demonstrates this phenomenon:

[8] ComEd Ex. 37.0 at 28.

[9] ComEd Ex. 37.0 at 30.



AG/CUB Ex. 4.0 at 12.

It is of course true that utilities generally spend more of their cash flow on capital expenditures than other industrial firms. However, electric utilities like ComEd are monopolies which are the only entities obligated to deliver electricity, a service essential to almost every aspect of American life. In exchange for this obligation the utilities can take advantage of the general rate-making process, which allows them the opportunity to request an increase in their prices to customers through an increase in delivery services rates. In the context of a rate case like this one, a utility must show that its investments and expenses are reasonable. As the Commission recently noted, a utility "largely controls the outcome of any such prudence review so long as it acts prudently in attempting to recover unpaid amounts." ICC Docket No. 09-0306 (cons.) Final Order at 218. The risk that a utility will not recover its expenses is mitigated by the expectation that the utility will act reasonably. In the event of a rate increase, consumers do not have the option to use another company or entity to deliver electricity to them. This protection significantly reduces utility investment risk relative to other industrial firms which are not price

regulated and are unable to simply increase their prices without concern that they will lose customers. Accordingly, an investors' risk of recovering his or her investments is much higher for non-regulated, non-monopoly firms.

Both Dr. Hadaway and Mr. Thomas prepared summaries of data which demonstrate the same conclusion. Dr. Hadaway highlights the differences in the adjustment methodologies applied by Yahoo Finance and S&P in presenting stock price information and the S&P 500 index. ComEd Ex. 37.0 at 28. He presented "corrected" stock prices changes in the following table:

Change in Stock Prices

	(1) High Price	(2) Low Price	(3) Present Price	(4) High to Low	(5) Low to Present	(6) High to Present
S&P 500 Index	$1,565.15	$ 676.53	$1,165.15	-56.8%	72.2%	-25.6%
Dow Jones Utility Average	$ 520.89	$ 290.68	$ 403.91	-44.2%	39.0%	-22.5%
Thomas Utility Prices	$1,375.11	$ 837.31	$1,275.25	-39.1%	52.3%	-7.3%

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Column 4: Compound growth from column 1 to column 2.
Column 5: Compound growth from column 2 to column 3.
Column 6: Compound growth from column 1 to column 3.

ComEd Ex. 37.0 at 30.

The companies in this analysis declined by 39.1% at a time when the overall stock market declined by 56.8%. AG/CUB Ex. 10.0 at 9. Even as the market was still 25.6% below its highest level, the sample utilities were only 7.3% below their collective high. Id. As this data shows, investor confidence in public utilities is higher than it is in other firms in the economy.

In Illinois, the regulatory structure provides monopoly utilities like ComEd even more cost recovery mechanisms which further reduce the risk an investor would not get a return. For example, ComEd passes through to consumers the price of electricity supply purchased by the Illinois Power Agency, 220 ILCS 5/16-111.5; costs associated with energy efficiency programs,

220 ILCS 5/8-103; costs associated with services to alternative electric suppliers, 220 ILCS 5/16-118; and can recover their uncollectible expenses through a rider mechanism, 220 ILCS 5/16-111.8. These rate mechanisms increase utilities' ability to recover expenses and stabilize cash flow. The uncollectible rider, 220 ILCS 5/16-111.8, allows an electric utility like ComEd to recover through an automatic adjustment clause tariff incremental differences in its uncollectible accounts. ComEd faces less risk of recovering its expenses, since the cost of any uncollectible accounts is shared amongst all ComEd customers and recovered through an automatic adjustment charge.

This Commission has already concluded that there is a benefit to electric utilities with the adoption of the uncollectible riders, and that a portion of that benefit should accrue to ratepayers through a reduction in the cost of common equity. 09-0306 (cons.) Final Order at 218. Moreover, in this particular case, ComEd itself proposed a rate design mechanism that will further reduce its risk of failing to recover its fixed costs. According to ComEd witness Ross Hemphill "[A straight fixed-variable ("SFV")] rate design establishes fixed and variable charges that track the fixed and variable costs of serving each customer or customer class." ComEd Ex. 14.0 at 182-184. For purposes of estimating an appropriate ROE for ComEd, any increase in the amount of fixed cost recovery for the Company reduces the likelihood that the company will not recover its costs, which in turn further decreases risk for investors.

Instead of addressing these issues, the Company presents arguments which are largely rhetorical and without actionable substance. For example, ComEd witness Dr. Phil O'Connor argued that the recent strength of utility companies relative to other firms in the economy somehow broadly demonstrates that the extensive evidence presented by staff and all of the interveners in this docket is wrong. ComEd Ex. 26.0 at 11. He seemingly argues that ComEd

needs a huge and unsupported rate increase to improve Illinois's regulatory rating. Id. Similarly, Mr. Fetter's diatribe about the importance of credit ratings should not influence the Commission's decision. It's impossible, and inherently speculative, to peg an approved rate of return or rate increase to credit rating expectations. Engaging in such a practice essentially invalidates all of the other issues that arise in a rate case. The Company has not presented any specific evidence to demonstrate that it would be unable to attract capital on reasonable terms, thus the Commission should not consider the testimony on this issue as evidence. The only evidence in the record on the effect of an ICC decision on a utility's credit ratings was a discussion of whether credit ratings agencies had changed the ratings of the Ameren Illinois Utilities following the ICC's decision in ICC Docket No.s 09-0306 (cons.), Tr. at 1812. The ratings agencies did not change Ameren's ratings. Id.

The Commission has discussed that issue specifically in another case involving ComEd, ICC Docket No. 10-0138, where ComEd had presented very similar testimony as to the "negative regulatory climate" in Illinois. The Commission determined that testimony was not persuasive, finding:

> [The testimony] that when investors see that a prudence review of any cost is involved, they assume that some of those costs are at risk of disallowance. Yet, [the witness] presented no facts indicating that this Commission should rely upon what investors think or might think, in order to determine the rate of return involved here. ComEd posits no facts indicating that appealing to investors that do not understand what a prudence review is would be something that is within this Commission's purview or even within its statutory jurisdiction.
>
> Also, Ms. Abbott's opinion regarding investors' alleged caution regarding prudence reviews overlooks the fact that Standard & Poor's finds that a true-up mechanism effectively eliminates credit risk. Standard & Poor's also finds that a true-up mechanism provides strong credit support that has withstood 'AAA' stress criteria. (*See,* Staff Ex. 8.0 at 4). While Ms. Abbott relies upon credit-rating agencies like Standard & Poor's for other opinions she expressed, she does not explain why investors should ignore Standard & Poor's in this regard. Both

> ComEd and Ms. Abbott have attempted to differentiate transition bonds, in large part, because those bonds were AAA-rated.
>
> [T]estimony regarding the negative regulatory climate regarding Illinois utilities overlooks the fact that this Commission has been, for a long period of time, dedicated to ensuring that, only reasonable and legally-recognizable, costs are passed on to ratepayers. The fact that this Commission does not compare favorably to some other state regulatory commissions in similar positions is merely demonstrative of this Commission's efforts on behalf of the consuming public to ensure that all costs that are passed on to the general rate-paying public are reasonable.
>
> Additionally, Ms. Abbott acknowledges the fact that ComEd's current rating reflects the Illinois regulatory environment. (Tr. 85). This is some indicia that Illinois utilities, with ComEd in particular, are not suffering as a result of the negative regulatory climate that she claims to exist in Illinois.
>
> *In re Commonwealth Edison*, ICC Docket No. 10-0138 Amendatory Order at 49-50 (February 9, 2011).

The Company in this case uses several approaches to raise its recommended ROE. Dr. Hadaway uses the DCF model and checks his results using a risk premium analysis based on utility bond yields. ComEd Ex. 11. Dr. Hadaway argues that he chose not to perform a CAPM analysis "due to continuing abnormal market conditions and artificially low yields on U.S. Treasury securities." ComEd Ex. 11.0 at 14-17. In other words, Dr. Hadaway chose to ignore a model previously used by the Commission because in his opinion the model's inputs "tend to understate ROE" and produce results that the company doesn't like. ComEd Ex. 11.0 at 534. The only model ComEd relies on that the Commission has typically accepted is the DCF approach, and the Commission has explicitly denied the various risk premium and comparable earnings tests proposed by the company. ComEd witness Carl Seligson uses different risk premium and comparable earnings tests, both of which have been previously rejected by this Commission. ComEd Ex. 12. In fact, the Commission's analysis in recent cases has relied on combinations of DCF and CAPM analyses. AG/CUB Ex. 4.0 at 17.

Nothing in the Company's testimony justifies the Company's proposed rate of return on common equity ("return on equity," or "ROE"). Dr. Hadaway's updated analysis estimates ComEd's cost of equity is in the range of 10.3 percent to 10.9 percent. ComEd Ex. 37.0 at 32. This is a reduction from his direct testimony, which estimated a cost of equity from 10.6 to 11.1%. ComEd Ex. 11.0 at 37. Despite the drop in Dr. Hadaway's estimates, the company is still seeking the 11.5% ROE it sought in its direct case. This figure is well above the range of estimates put forth by various Staff and Intervenor witnesses – for example, Staff recommends a 10.0% and the IIEC 9.6%. Staff Ex. 5.0 at 10-34; IIEC Ex. 4.0 at 2. The difference between the ROE recommendations made by the various witnesses in this case exists for a variety of reasons, but the most significant are related to company growth expectations. As explained below, Mr. Thomas' analyses most accurately account for the actual potential growth and investor expectations. The Commission should instead adopt the rate of 8.94% which AG/CUB witness Thomas recommended in his testimony, and which continues to be appropriate.

2. Discounted Cash Flow Analysis

A DCF analysis is a method of valuing a company or asset using the concept of the time value of money, that is, the model assumes that investors who purchase stock do so paying a price that reflects the present value of the cash they expect to receive from the stock in the future. The analysis uses information about the current stock price and expected future cash flows, both incoming and outgoing, from dividend payments and earnings growth.

In its most basic form, the constant growth DCF model can be represented by the following equation:

$k = D_0(1+g)/ P_0 + g$ where

k = Investors required "rate of return", or the "cost of equity capital"

D_0 = The current dividend payment

P_0 = The current stock price

$D_0(1+g)/ P_0$ = The expected dividend yield

g = The expected sustainable growth rate

AG/CUB Ex. 4.0 at 21. The non-constant growth assumption enters the model through the specification of "g", the expected sustainable growth rate input. The multi-stage model comprises the combination of repeated calculations of the basic form of the DCF model, shown above, using distinct growth rates over discrete periods of time.

As AG/CUB witness Thomas noted, the DCF model has been widely recognized by utility commissions as an important tool in setting an appropriate cost of equity for regulated utility companies because it rests on two fundamentally strong theoretical principles. AG/CUB Ex. 4.0 at 18. The first principle is that the current market price of a financial asset, such as a share of common equity, is efficient and equal to the present value of all future cash flows that investors expect to receive from the asset. This means that the rate of return investors require for the risk they take that they will not receive any return on – or will lose the entire value of – their investment is the discount rate where present value of all future cash flows from an asset is equivalent to the current market price of the asset. (Future cash flows to investors come from either future dividend payments or the sale of the stock.)

The second principle is that a dollar received today is more valuable than a dollar received at some point in the future ("time value of money"). An investor could realize a return

in future periods by investing that a dollar today; if the investor receives only that same dollar in the future, she will have missed the opportunity to invest today and earn returns. The investor's required rate of return, or a company's cost of capital, is the return on the deferred payment that would induce the investor to wait. That return, when used as the discount rate in a present value calculation, makes the present value of a dollar received today equal to the present value of a dollar (plus the return) received at some point in the future.

AG/CUB witness Thomas performed four different DCF analyses: two different constant growth analyses using the historic and projected internal growth rate for the sample utilities, and two different analyses using the non-constant growth DCF model starting at the historic and projected internal growth rates for the sample utilities. Like the IIEC and Staff witnesses in this case, Mr. Thomas concluded that a non-constant growth DCF analysis would be most appropriate. Expected future growth is highly uncertain given turmoil in the credit markets, which creates uncertainty for investors. This makes investors focused on short-term changes in the equity markets simply because their long-term valuation models aren't able to accurately predict returns in a market where existing valuation models can't take into account deep, broad-scale declines in value like that which occurred in the recent recession. Both forecasted and historical growth rate information become highly subjective measures of expected future growth for individual firms. The Commission has already recognized this fact, and begun using a non-constant growth model. 09-0306 (cons.) Final Order at 215 (noting that as analysts projected growth rates for utilities have exceeded the projected growth rate of the U.S. economy as a whole).

a. Measuring Company Growth

Current stock price and dividend information is readily available for the sample utilities, and current information is commonly accepted as the most relevant to determine investor expectations in the DCF. The growth rate in the DCF model represents the sustainable growth that investors expect in their investment resulting from expected increases in a company's earnings. That growth rate must be consistent with, and supported by, the economic conditions and dividend payout policies expected to occur. The problem is that investor requirements for future dividends and rates of growth cannot be found in the pages of the Wall Street Journal and plugged into the model. The analysis is further complicated by the current market upheaval and by the fact that the Company does not have publicly traded stock to provide some type of current, objective dividend and price information.

The models used by financial professionals are used for only one purpose: to provide an estimate of the expectations that investors have for the investments they have made. This makes it critical that the growth component of the DCF model provide an accurate representation of the sample companies and their business activities. To ensure that the cost of equity determined in this proceeding is reasonable, the Commission can base its analysis on three basic supplemental criteria:

- Earnings growth rate inputs must be reasonable in light of anticipated growth in GDP;
- The long term growth rate must not implicitly require continued earnings above the regulated firm's cost of equity, as derived in the analysis; and
- The long term growth rates must not require dividend payout ratios that are not consistent with the capital expenditure growth rate and the return on equity.

The most relevant measure of growth for the Commission to consider is the internal growth of the sample utilities. In general company management is expected to retain some of the company's earnings within the business. Such retained capital is commonly referred to as

"retained earnings." Retained earnings are used by management to fund operations and to grow the business by investing in new facilities or more efficient processes that will produce greater future returns. This type of growth is known as "internal" growth because it comes from the capital retained within the business. Evaluating a company's internal growth can help the Commission to avoid the type of upward bias produced by the use of analysts' growth estimates.

Mr. Thomas used the following fundamental growth rate formula:

> **Earnings Growth = b x r** where
>
> **b** = the fraction of earnings not paid out as dividends (the "retention rate"), *i.e.* one minus the dividend payout ratio, and
>
> **r** = the expected rate of return on common equity

AG/CUB Ex. 4.0 at 24.

Two examples demonstrate how this formula captures internal growth, and how important internal growth is an input for investors analyzing potential returns.

- First, where the dividend payout ratio is 100% and the retention rate is zero. The earnings of the company do not grow, because no earnings are retained to reinvest in the business. If the dividend payout ratio is zero, then the retention rate is one, every dollar of earnings gets reinvested into the business. These reinvested earnings become equity on the company's balance sheet. This in turn increases income, because it is calculated as the return on equity multiplied by the amount of equity invested in the company. Since the number of shares outstanding has not changed, the earnings per share will increase.
- Second, look at situations where the dividend payout and retention rate are between zero and one -- *i.e.*, only a portion of total earnings are reinvested in the business. Here, the growth rate in earnings is the return on equity multiplied by the retention rate (the remainder being paid out as dividends). For example, if a

> firm retains 70% of its earnings and earns 12%, then its earnings growth will be 8.4% (70% x 12% = 8.4%). Thus, the growth rate in a company's earnings is determined by the earnings retained in the business, increasing invested equity, and the return on that equity. In circumstances where the dividend payout ratio is expected to decline, using the fundamental growth formula to estimate expected future growth is superior to the analysts' forecast complications, because the formula captures the effects of those changes.

In his analysis Mr. Thomas used two growth rates. AG/CUB Ex. 4.0 at 25. The first calculated the historic internal growth rate for each of the sample utilities over the period from 2004 to 2009. AG/CUB Ex. 4.0 at 25-26. The second calculated the anticipated internal growth for each sample utility based upon expectations from Value Line. AG/CUB Ex. 4.0 at 26. He then used the overall U.S. Gross Domestic Product ("GDP") growth rate as a baseline for comparison of his DCF results. Over the most recent 40-year period[10], GDP grew by 6.93%: from 1969 to 1989, the growth was 8.99% and from 1989 to 2009, the growth was 4.86%. Id. In checking his results, Mr. Thomas used a 20 year historical average because the most recent period of analysis, including the most recent multi-year economic crisis, shows far less growth in GDP. Id.

ComEd rejects this notion "as inappropriate and biased." While Dr. Hadaway may criticize a 4.86% estimate as being too low, it is actually above the published consensus economist estimates of GDP growth. As Illinois Industrial Energy Consumers (IIEC) witness Michael Gorman noted, *Blue Chip Economic Indicators* publishes consensus GDP growth projections twice a year. Based on its latest issue, the consensus economists' published GDP

[10] 1969-2009.

growth rate outlook is 4.8% to 4.7% over the next 5 to 10 years, respectively. IIEC Ex. 1.0 at 25. Given this data, and the fact that Staff witness Michael McNally relied on a 5.0% estimate of GDP growth, it is easy to see that Dr. Hadaway's 6% GDP growth estimate is the outlier.

The complete results of Mr. Thomas, found in AG/CUB Ex. 4.0 at 26, are summarized below:

	Hadaway Analysts' Growth	**Historic Internal Growth**	**Projected '13-15 Internal Growth**
Sample Average	5.59%	3.74%	4.42%

This analysis shows that the internal growth rates for the sample utilities:

- Are reasonable in light of anticipated growth in GDP;
- Do not require continued long-run earnings above the cost of capital; and
- The internal growth method calculates long term growth rates based on historical and projected dividend payout ratios that are consistent with the capital expenditure growth rate and the return on equity.

This is important because the DCF model assumes that a certain relationship between earnings and dividends. Analyzing how a company's earnings are expected to grow over time – the amount of cash that a company has to return to its shareholders, or to invest in expanding its operations – is one measure investors use to assess the overall health of the company, how it is expected to grow, and ultimately how risky investing in a given company might be. If a company chooses to retain less capital and pay out greater dividends, or retain more capital and retain payout smaller dividends, there is a definite effect on both dividends and growth. In all situations where the dividend payout ratio is not constant, the DCF model will produce inaccurate results. As the table below demonstrates, using dividends at the current dividend payout ratio along with expected future earnings growth in a declining payout environment

results in an upward bias to the DCF results – even though the firm's relevant financial circumstances are unchanged.

The Impact of Declining Dividend Payouts on DCF Results

	100% Dividend Payout	50% Dividend Payout	Declining Dividend Payout
ROE	8%	8%	8%
Earnings	$2	$2	$2
Payout Ratio	100%	50%	100% Declining to 50%
Current Dividend	$2	$1	$2
Share Price	$25	$25	$25
Yield	8%	4%	8%
Earnings Growth	0%	4%	4%
DCF Results	**8%**	**8%**	**12%**

AG/CUB Ex. 4.0 at 28.

When dividend payout ratios decline, investors expect more growth to come from earnings because more capital has been retained for internal investment in the business. As a result, the DCF model will overstate the cost of equity. Similarly, an increasing dividend payout ratio will cause investors to expect less growth from earnings, and the DCF will understate the cost of equity. When these ratios are expected to change, using only reported analysts' earnings growth rates will result in inaccurate estimates of the cost of equity. Mr. Thomas' method, because it considers such changes in payout and retention ratios, is therefore more accurate. Dr. Hadaway proposed a slightly higher dividend yield than the one used by Mr. Thomas. ComEd Ex. 11.4. The Commission should reject his proposal because comparing dividend yields in a vacuum doesn't provide any valuable information. Dr. Hadaway's decision to single out the differences in dividend yields simply obfuscates the issues in this case. Any differences in the dividend yield are merely derivative of other the other issues Identified by the experts in this

case. The dividend yield is the projected dividend (current dividend times the expected growth rates) divIded by the stock price. It is the difference in these factors that accounts for the differences in the dividend yield. Therefore any differences in the dividend yields used by Dr. Hadaway and Mr. Thomas are driven by the relationship of dividends to stock prices when the analyses were performed and the growth rates used in the respective analyses.

Dr. Hadaway inappropriately relies on growth rates that are not sustainable over the long run which means his model will overestimate the Company's ROE.

Comparing Results

	Thomas	Hadaway Average
Non-Constant Growth DCF		
Analysts' Growth		11.10%
Historic Internal Growth	8.98%	
Projected Internal Growth	9.65%	
Constant Growth DCF		
Analysts Growth Rates		10.70%
Long-term GDP		11.10%
Historic Internal Growth	8.22%	
Projected internal Growth	8.92%	
Recommendations	**8.94%**	**11.10%**

AG/CUB Ex. 4.0 at 34.

Dr. Hadaway calculates an 8.99% ROE using Staff witness Michael McNally's 10% estimate and the average retention rate of Mr. McNally's proxy sample. ComEd Ex. 37.0 at 18. Dr. Hadaway claims that this inconsistency with Mr. McNally's own recommendation somehow implies that the "BxR" method used by both Mr. McNally and Mr. Thomas should be rejected. Id. In fact, Dr. Hadaway's calculation confirms Mr. Thomas' 8.94% ROE estimate and highlights the bias introduced into Commission proceedings from analyses relying heavily on analysts' growth rates, as Mr. McNally does. Staff Ex. 5.0 at 15&17. Current analysts' 3 to 5

year growth projections do not meet these simple common sense tests. For an example, the Commission need only turn to the 5.53% analysts' growth rate used in Mr. McNally's constant growth DCF and in the first stage of his non-constant growth DCF. This is a rate above the 5% long-term growth in GDP that Mr. McNally assumes. Staff Ex. 5.0 at 15. Evaluating a company's internal growth can help the Commission to avoid the type of upward bias produced by the use of analysts' growth estimates.

Dr. Hadaway's proposed growth rates would require that the companies in the sample groups exceed their own historic growth, and also exceeded growth in GDP. He has not supported this inflated level of growth with any meaningful analysis. The Commission cannot rely on this analysis because it relies on growth expectations that are not sustainable in light of expected growth in GDP, expected dividend payout ratios, and would require sustained earnings in excess of the true cost of capital. Moreover, Dr. Hadaway's two key "required assumptions" for his analysis, constant earnings and retention rates, are not met in reality. ComEd Ex. 37.0 at 27. All of the witnesses in this case are addressing the constant earnings issues through the use of multi-stage DCF models (that is, DCF models that assume varying stages of growth rather than constant growth).

b. Determining How Consistently a Company Grows

Mr. Thomas performed a non-constant growth DCF analysis using a multi-stage growth analysis. AG/CUB Ex. 4.0 at 29. For the short term, he assumed that for a period of five years, the companies in the sample will grow at their (average historic and projected) internal growth rate. Id. After the end of the initial five year period, he assumed that there will be an additional five year period of transition, where growth slows from its historic levels before eventually settling at a long term level that is equivalent to the historic growth in GDP over the last 20

years. Id. Effectively, Mr. Thomas created a three-stage DCF model, similar to methods used by Staff in prior cases, and which is summarized in the chart below:

DCF Results

	Multi-Stage DCF		Constant Growth DCF	
	Historical BxR	***Projected BxR***	***Historical BxR***	***Projected BxR***
Sample Average	8.98%	9.65%	8.22%	8.92%
	Wtd Avg	**8.94%**		

AG/CUB Ex. 4.5. The DCF model produces an 8.94% rate of return on Common Equity. AG/CUB Ex. 4.0 at 29.

3. CAPM Analysis

The CAPM is an alternative analytical tool commonly used in regulatory proceedings to estimate investors' required rate of return, or the cost of equity capital for the firm. The CAPM can be represented by the following equation:

k = $R_f + B(R_m - R_f)$ where

- **k** = Investors' required rate of return, or the cost of equity capital
- R_f = The risk-free rate of return[11]
- **B** = Beta, a representation of the relative correlation between the market and the security or industry being analyzed, where 1.0 is perfect correlation
- R_m = The market return
- $(R_m - R_f)$ = The expected market risk premium ("EMRP"), or the market return in excess of the risk-free rate.

AG/CUB Ex. 4.0 at 30. For a utility, the investors' required rate of return is the risk-free rate plus the value of the non-diversifiable risk that investors take on by investing in the utility. Non-diversifiable risk is essentially the risk that is inherent in the marketplace.

[11] The risk free rate of return is readily available from the Federal Reserve Bank using current yields on long-term (30-yr) treasury bonds. Mr. Thomas used a risk-free rate of 3.72%.

Like the DCF, the CAPM is predicated on two key assumptions: (1) that in the market, investors are compensated only for non-diversifiable risk, quantifiable as a uniform EMRP, and (2) that beta is an accurate measure of the relative risk of an individual security when compared with the overall market. In recent cases, the Commission has made it clear that in determining the cost of equity, it prefers to use the mad-point of both the CAPM and DCF models (See ICC Docket No. 09-0319, Final Order at 113, ICC Docket No. 09-0306 (cons.), Final Order at 220). While there are problems, the CAPM can be useful to verify the results of independently performed DCF analyses, which is what Mr. Thomas did. No ComEd witness undertook a CAPM analysis.

a. The Beta Coefficient

The beta coefficient (B) represents the degree to which the price of a stock moves with the overall market, or the volatility of an individual stock compared to the volatility of the market. A beta of 1.0 represents a stock that moves in complete unison with the overall market. Thus, the stock has exactly the same risk as the overall market. If the beta is less than 1.0, then the stock is less volatile than the overall market, indicating that returns are more stable and presumably less risky. If the beta is greater than 1.0, then the stock is more volatile than the overall market, which indicates that its price changes more dramatically than prices in the overall market, and the stock is riskier than the market.

The Commission has traditionally accepted raw beta estimates, adjusted for mean reversion, as valid CAPM inputs. Commonly relied on by Value Line, this adjustment for an assumed reversion is one of the principal sources of the upward bias in Value Line betas.[12]

[12] For example see Michael J. Gambola and Douglas R. Kahl, *Time Series Processes of Utility Betas: Implications for Forecasting Systematic Risk*, Financial Management 92 (autumn, 1990). The betas used by Value Line The beta estimates reported by Value Line are much higher than the beta estimates reported by the other financial sources.

Based on this analysis, AG/CUB Ex. 4.6, which is summarized below, Mr. Thomas used a beta of 0.59:

Beta Analysis

	VALUE LINE				
	Reported	*Unadjusted*	**YAHOO**	**ZACKS**	**GOOGLE**
Sample Average	0.70	0.55	0.56	0.56	0.56

Average (VL Adjusted)	**0.59**
Average (VL Unadjusted)	**0.56**

c. The Expected Market Risk Premium ("EMRP")

The EMRP represents the premium, above the risk-free rate, that investors expect when they take on the risk of an investment in the market portfolio, or the universe of potential investment opportunities available to investors. There are two main approaches to specifying the EMRP input to CAPM analyses – using EMRP estimates derived from the academic studies of market performance or using EMRP estimates calculated for particular situations or cases. Mr. Thomas used three different approaches in his CAPM analysis:

- An EMRP based upon the financial literature, as I have proposed in various cases before the Commission.
- An EMRP based upon the decision the Commission made in the recent Ameren rate case; and,
- An EMRP based upon the testimony of Mr. Seligson (ComEd Ex. 12.0 at 207).

These three methods produce the following results:

CAPM RESULTS

	Literature	Seligson*	09-0306 Final Order #
RF	3.72%	3.72%	3.72%
EMRP	5.00%	6.70%	8.98%
b	0.59	0.59	0.59
CAPM	**6.69%**	**7.69%**	**9.05%**

* ComEd Ex. 12.0 at 207
\# Staff Ex. 6.0, Schedule 6.7

AG/CUB Ex. 4.0 at 33.

Mr. Thomas' CAPM analysis demonstrates that the appropriate ROE for a company like ComEd is in the range of 6.69% to 9.05%. Id.

4. Alternative ROE Analyses

ComEd witness Seligson presented two additional analyses, both of which have already been rejected by the Commission in prior cases, without offering any explanation as to why the Commission should use these analyses in this case. Mr. Seligson looks at returns of all common stocks over a projected risk free rate. ComEd Ex. 12.0 at 203-218. As the Commission stated in a recent Peoples Gas rate order:

> The Commission will not consider the results of the Utilities Risk Premium model that only the Companies have employed. We have repeatedly rejected this model as a valid basis on which to set return on equity. Our view remains unchanged.

ICC Docket No. 09-0166, Final Order at 128 (January 21, 2010).

Finally, the Company asks the ICC to use other states as a comparison for determining the appropriate ROE in this case. Dr. Hadaway argues that recent allowed ROEs for electric

distribution utilities have been approximately 9.98 percent. ComEd Ex. 37.0 at 9-10 and Ex 31.1. The Commission appropriately rejected the comparable earnings method in the past, and there is no reason to reconsider that decision. Mr. Seligson's comparable earnings analysis looks at utility operating companies reported by Regulatory Research Associates: 34 companies whose earned return on equity in 2009 averaged 12.2%. ComEd Ex. 12.0 at 185-193. In previously addressing this issue, the Commission stated;

> At several places in their evidence and briefs, the Utilities compare the ROE's recommended here with the ROEs approved in previous cases by this and other commissions. E.g., NS-PGL Ex. PRM-2.0 at 3-6. They assert that previously approved ROEs serve as "guideposts" for our analysis in these cases and insist that they "are not arguing that their returns should be based on the authorized returns of other utilities." NS-PGL BOE at 25. The Commission doubts that the Utilities' return comparisons were offered without the expectation that our decision-making would be affected by them. The Utilities are presumably reluctant to directly press for comparison-based ratemaking because of our previous rejection of that approach. In Commonwealth Edison's most recent rate case, we said:
>
> > ComEd asserts its cost of equity should reflect the costs of equity recently approved for electric utilities in the United States. The cost of equity appropriate to ComEd, however, is specific to that utility. ComEd may not simply adopt the cost of equity set for other utilities scattered around the country, for which the factors and circumstances are not necessarily similar. Rather, pursuant to Section 9-201 of the Act, ComEd must prove that its proposed cost of equity is just and reasonable. Commonwealth Edison, Docket. No. 05-0597, 1181 Order, at 153 (June 6, 2006).

Commission Final Order in Docket No. 07-0242, at 89-90. Thus, the Commission previously – and correctly – expressly rejected similar comparable earnings analyses and it should likewise do so here.

F. ADJUSTMENTS TO RATE OF RETURN

1. Compensation for Energy Efficiency Programs

ComEd witness Susan Tierney proposes a 0.40% adjustment based on ComEd's implementation of demand response and energy efficiency programs. ComEd Ex. 13.0 at 3. Ms. Tierney speculates that this adjustment would mitigate the "adverse financial complications that

will arise from successful implementation of [energy efficiency and demand response] programs required under the Act and other demand-side initiatives." Id. The complication in question is the "significant risk" she finds the Company will not recover regarding its chances of recovering its authorized return if it is in fact successful in meeting the legislative targets. Id. In short, ComEd asks the ICC to give it "compensation in support of achieving robust compliance with the underlying objectives of the Illinois legislation." Id. Ms. Tierney acknowledges that there are a wide range of tools which can be used to overcome any utility-perceived hurdles to "compliance" with state law. She notes that ensuring stable program funding through either including program costs in base rates or rate adjustment mechanisms to improve cost recovery. ComEd Ex. 13.0 at 9, 18. She discusses how rate designs can remove financial disincentives for utilities to aggressively implement energy efficiency programs, including revenue decoupling. ComEd Ex. 13.0 at 9. She acknowledges a future test year could address the use of forecasted billing determinants to set new rates could account for the effect of energy efficiency and demand-response programs. ComEd Ex. 39.0 at 5. What she fails to do is demonstrate why the Commission should adopt her recommendation.

Ms. Tierney examined only the reasonableness of ComEd's proposal for a 40-basis point addition to its requested ROE. ComEd Ex. 64.0 at 9. She did not attempt to quantify the effect of the risks she claims are present. She did not determine the correct amount of basis points to add in the context of the rate structure ComEd was proposing. She did not address why the only party who can select a test year, ComEd, determined a future test year would be insufficient for its purposes. The only thing Ms. Tierney examined was whether, in her opinion, ComEd's proposal to include a 40-basis point addition in its ROE recommendation in the context of a straight fixed variable rate design was reasonable. Tr. at 1821.

The Commission should reject ComEd's request. As Mr. Thomas noted, if the Company is truly concerned about the effects of the legislative mandates on its delivery services revenue and cost recovery, the effects of both programs are more accurately reflected in the rate-making process through appropriate billing units or the use of a future test year. AG/CUB Ex. 4.0 at 26. In fact, all parties besides ComEd who looked at this issue reached the same conclusion: There is no need to arbitrarily increase the ROE simply because the Company has chosen to avoid using more accurate mechanism to incorporate any impact that results from these programs. IIEC Ex. 1.0 at 54-55 and 4.0 at 22-24; Staff Ex. 5.0 at 55-58; Staff Ex. 23.0 at 4-9; Pre-Trial Memo of the Environmental Law and Policy Center at 1. As IIEC witness Mr. Gorman put it, Dr. Tierney's proposal rewards ComEd for a risk that can be largely managed, "eroding the efficiency of the rate-setting process." IIEC Ex. 4.0 at 23-24. The Company is in effect seeking to manage potential sales volume losses in future years solely on the basis of one factor (i.e. energy efficiency) that might reduce future sales without any consideration of the many other factors that affect sales – including those which might increase sales. Staff Ex. 5.0 at 57-58.

2. Fixed Cost Recovery Adjustment

Staff recommends a conditional adjustment to the cost of common equity depending on whether or not the Commission authorizes ComEd to move toward a more fixed/variable rate design, as the Company proposes. Staff Ex. 5.0 at 41-42. The greater the extent to which the Company's fixed costs are recovered through a fixed charge, the lower the Company's operating risk will be. Thus, to reflect the lower level of risk, Staff recommends a 40 basis point (0.40%) reduction to ComEd's ROE if the Commission adopts an 80/20 fixed/variable rate design for ComEd. Id. Similarly, Staff recommends a 20 basis point reduction if the Commission alternatively adopts a 60/40 fixed/variable rate design for ComEd. Id. As the Commission has consistently concluded, utility companies have a reduced risk of recovering their fixed costs,

including their allowed revenue requirement, when the fixed portion of the customer charge is increased. Final Order, ICC 09-0306, April 29, 2010 at 217. ICC Docket 08-0363, Final Order at 71 (March 25, 2009). ComEd has given the Commission no reason to depart from this practice, and Staff's proposed adjustment here should be adopted.

G. OVERALL COST OF CAPITAL (DERIVATIVE)

Using the capital structure and other information proposed by ComEd, the appropriate overall rate of return for the Company is 7.79%. AG/CUB Ex. 4.0 at 37. This reflects an 8.94% return on common equity is appropriate for ComEd and uses the capital structure and other information proposed by ComEd.

Weighted Average Cost of Capital

CAPITAL		AMOUNT	WEIGHT	COST	WEIGHTED COST
Long-Term Debt	$	4,772,707	52.56%	6.53%	3.43%
Short-Term Debt	$	9,736	0.11%	0.73%	0.001%
Common Equity	$	4,297,923	47.33%	8.94%	4.23%
Credit Facility Costs					0.12%
TOTAL	$	9,080,366			**7.79%**

All data but ROE from ComEd Ex 6.1 Schedule D-1

VIII. COST OF SERVICE AND ALLOCATION ISSUES

IX. RATE DESIGN

C. POTENTIALLY CONTESTED ISSUES

Introduction

Rate design is a revenue-neutral policy-driven exercise. There are many principles that must be considered in designing rate structures in order to fairly recover costs within a rate class while also accurately reflecting each class's cost of service. These principles include fairness,

equity, gradualism, and overall social welfare. Mr. Hemphill claims that ComEd's proposed residential rate structure meets these policy goals. ComEd Ex. 46.0 at 7. CUB and the AG, who are statutorily required to represent the interest of residential consumers in Illinois, strongly argue that ComEd's proposed rates do just the opposite. In weighing the evidence presented against the uncontroverted policy goals of any rate design proposal, it is important to remember that the consumer parties - CUB and the AG - have a unique expertise of evaluating the effect of rates on residential consumers and have a clear directive and responsibility to protect residential consumer interests.

The rate design proposals made by CUB and the AG allow ComEd to recovery its revenue requirement while simultaneously protecting residential customer interests – both small and large. The goal of ComEd's proposed rate design, in contrast, is primarily to insulate its revenue stream from variations in energy consumption and focuses solely on high-level cost causation principles that ignore the specific impacts on a large range of users in the residential class. See ComEd Ex. 14.0 at 34-35. ComEd's pledge to help low income customers, (ComEd Ex. 14.0 at 22), does not correct the significant inequities inherent in ComEd's proposed residential rates addressed by AG/CUB witness Rubin.

1. Straight Fixed Variable (ComEd Proposal)

ComEd proposes to change its current residential rates, which consist of a fixed customer charge, fixed meter charge and a volumetric distribution charge, to a phased-in so-called "Straight Fixed Variable" or "SFV" rate design, which would significantly raise the amount of the fixed portion of residential customers' bills over the next three years. In addition, ComEd proposes to eliminate two of the four residential rate "classes," which CUB will refer to as "sub-classes" herein: single family heating ("SF Heat"), multi-family heating ("MF Heat"), single-

family non-heating ("SF No Heat") and multi-family non-heating ("MF No Heat"). (This issue is largely addressed in section VII. C. 3.(a) infra).[13] ComEd proposes to eliminate any rate distinction based on space heating in order to achieve two residential subclasses: single-family ("SF") and multi-family ("MF").

Despite ComEd's protestations otherwise, these recommendations violate basic rate making principles of cost causation, efficiency, social welfare, fairness and equity. ComEd's proposal further ignores the inequitable and unfair customer impacts of its proposal, which would cause unreasonably large rate increases for the lowest users of energy in ComEd's territory. ComEd's proposal improperly shifts substantial costs related to the use of electricity out of the energy-related charge and onto the fixed charge. CUB therefore urges the Commission to reject ComEd's proposed SFV rate design and its proposed elimination of two residential rate classes and instead adopt Mr. Rubin's recommended residential rate structure discussed herein.

a. ComEd's proposed rates fail to satisfy important rate design policy goals.

CUB-AG witness Scott J. Rubin thoroughly examined ComEd's proposed residential rates and performed a detailed customer impacts analysis demonstrating the differences in usage characteristics within the residential class, as well as the different costs of serving each type of residential customer. Mr. Rubin asserts that ComEd's proposal to drastically increase its

[13] ComEd currently has four *residential* subclasses: customers in single-family buildings that do not use electricity for space heating (whom I will refer to as "SF No Heat"), customers in single-family buildings that use electricity for space heating ("SF Heat"), customers in multi-family buildings that do not use electricity for space heating ("MF No Heat"), and customers in multi-family buildings that use electricity for space heating ("MF Heat"). ComEd's existing rates have a customer charge, meter charge, and distribution (or consumption) charge. There are two *residential* customer charges: one for single-family customers and one for multi-family customers. The current single-family customer charge is $7.64 per month; the multi-family charge is $6.65 per month. The metering charge is the same for all *residential* customers and is currently $2.24 per month. There are two distribution charges: one for heating customers and one for non-heating customers. The current charge for heating customers is 2.023¢ per kilowatt-hour (KWH); the charge for non-heating customers is 2.407¢ per KWH. AG/CUB Ex. 6.0 at 4.

customer charge and reduce distribution (per KWH) charges bears no relationship to the reasons why various facilities are sized and installed on ComEd's system. AG/CUB Ex. 6.0 at 14-41; AG/CUB Ex. 11.0. First and foremost, electric distribution rates should reflect consumer demand for electricity, and not just the number of customers. Prices should send customers an appropriate price signal that increases in their energy demand result in increases in costs to the system, and reflect the fact that increased consumption results in increased costs to the system. To accommodate the principles of rate design and create rates that reasonably reflect the cost of servicing different types of residential customer, Mr. Rubin designed residential rates that maintain the Company's current four residential rate classes under both ComEd's proposed rates, as well as the revenue requirement recommended by AG/CUB in this docket.

ComEd's proposed SFV rate structure is presented as one way to align rates with costs primarily between their fixed and variable components. ComEd witness Hemphill claims that because almost none of its distribution costs vary with energy consumption, most of its revenue should be recovered through fixed charges. *See* ComEd Ex. 46.0 at 9. This, however, only represents one aspect of the goals of rate design. ComEd's approach ignores other cost-causation realities, such as the variance of demand-related costs within the residential class, as well as principles of gradualism, fairness and equity in its analysis. In fact, every ComEd cost-of-service study produced in this case recognizes that there are substantial demand-related costs incurred to serve residential customers – a fact recognized by ComEd current residential rate design, but ignored by its proposed rate design in this proceeding. ComEd's pricing proposal treats residential demand-related costs as being related solely to the number of customers, not to those customers' demands for electricity. AG/CUB Ex. 11.0 at 2. Further, ComEd's proposal to

drastically increase its customer charge bears no relationship whatsoever to the reasons why various facilities are sized and installed on ComEd's system.

As Mr. Rubin testified, utilities make long-lived investments based on long-term projections of customer location, demand, and consumption. AG/CUB Ex. 11.0 at 3. One would not expect utility costs to vary significantly with monthly energy consumption, but that does not mean that energy consumption has nothing to do with the utility's incurrence of costs. Id. Indeed, most aspects of ComEd's distribution system – including facilities such as substations and transformers – are based on ComEd's need to serve consumers' demands for electricity over the life of those facilities (which is measured in decades). Id. Utility pricing must send customers an appropriate price signal that increases in their energy demand result in increases in costs to the system. Id. ComEd's pricing proposal fails to do so.

b. Customer Rate Impacts

As Mr. Rubin's analysis showed, ComEd's proposal would result in some residential customers facing rate increases of 60%, 80%, or even 100%, even though overall rates would increase by about 20% under ComEd's proposed revenue requirement. AG/CUB Ex. 11.0 at 3. Imposing increases on some customers of four or five times the average rate increase – for no other reason than to further the utility's notion of an appropriate cost-causation rate design policy or theory – is grossly inconsistent with the principle of gradualism. Id.

The essential way to evaluate whether a rate design proposal promotes equity is to compare the resulting revenues for each affected group of customers to the cost of serving those customers. As Mr. Rubin testified, "an equitable rate design will recover revenues in rough approximation to the cost of service." AG/CUB Ex. 6.0 at 22. The fairness of a proposed rate design within a rate class is most effectively evaluated through examination of a customer impact

analysis. This is precisely what Mr. Rubin did in his direct testimony. Rather than review the rate impact on a "typical" or "average" customer, Mr. Rubin examined the effect on customers within the residential class over a wide range of usage characteristics, evaluating the extremes as well as customers with more typical usage patterns. AG/CUB Ex. 6.0 at 26. To conduct this analysis, Mr. Rubin used ComEd's actual billing data, which included customers who received 12 bills during 2009, or 2.9 million customers (out of 3.4 million total customers). Id. at 26. This data set is more than adequate to evaluate the fairness of ComEd's proposed residential rate design.

Mr. Rubin presented the findings of his customer-impact analysis in his direct testimony and in AG/CUB Ex. 6.08 (a distribution curve). AG/CUB Ex. 6.0 at 26-40. The results of his analysis demonstrate that there is a tremendous diversity among ComEd's residential customers, a diversity that is not properly addressed by ComEd's proposed residential rate structure. The data directly undercuts ComEd's rationale for placing most demand-related costs in the customer charge. ComEd's rate design erroneously assumes that each customer within the residential class is responsible for the same level of demand and is therefore should bear the same proportion of demand-related costs. However, because of the diversity of demand within the residential class, large residential energy users place much higher demands on the system than small energy users. ComEd's proposal, therefore, would require low-use customers to subsidize high-use customers within the same residential subclass. This is an inequitable method of designing rates.

As Mr. Rubin's analysis shows, ComEd's proposed residential rate design places an excessive burden on the lowest-use customers, while giving high-use customers a break, despite the fact that these large users cause significantly more costs. AG/CUB Ex. 6.0 at 31. This results in intra-class subsidies largely favoring larger users, customer mostly in the MF and SF

No Heat customers. For example, under ComEd's proposal, the lowest effective annual bill (that paid by fewer than 5% of customers) would be about $300 per year. Id. Under present rates, the equivalent annual bill is less than $200. Id. So ComEd's proposal would result in large percentage rate increases (in excess of 50% rate increases) for those who use the least amount of electricity (and, therefore, are least likely to cause ComEd to incur significant demand-related costs). Id. At the other end of the curve, the two percent of customers with the highest bills currently (and, therefore, the greatest energy usage) actually would receive rate decreases under ComEd's proposal. Id. In the SF No Heat subclass, the roughly 550,000 customers who use less than 5,500 KWH per year would provide as much of the revenue increase as the 1.1 million customers who use more than 8,000 KWH per year. Id. at 32. This cannot be considered a fair distribution of rates within the residential class. It is grossly unfair to increase some customers' bills by more than 50%, yet others within the class – those imposing the largest costs on the distribution system - receive a rate reduction.

c. AG/CUB's Recommended Rates

To correct the inequities inherent in ComEd's proposed residential rate design, Mr. Rubin proposes that ComEd's rates remain structured as they are currently exist, consisting of (1) customer charges that vary depending on whether the customer is in a single-family or multi-family building; (2) the same meter charge for all customers; and (3) a distribution charge that reflect each residential subclass' unique costs of service. AG/CUB Ex. 6.0 at 42-47. Mr. Rubin developed rates to satisfy an over-arching goal of recognizing the true cost of service, recovering the major categories of costs through charges that are related to the customer's use of facilities related to that cost category. *Id.* Gradualism and avoIdance of rate shock are also key policy concerns addressed by Mr. Rubin's proposal. To achieve this end, he used a benchmark that no

residential subclass should receive an increase more than 1.5 times the average increase for the whole residential class. Since ComEd has proposed an overall residential increase of 20.8%, Mr. Rubin's proposal ensures that no significant group of residential customers would receive more than a 31% increase under ComEd's proposed revenue requirement.

The specific rates Mr. Rubin recommends vary based on which revenue requirement is used. Mr. Rubin's recommended rates based on the Company's proposed revenue requirement is as follows:

Table 1: AG/CUB Proposed Rates Under ComEd's Proposed Revenue Requirement				
	SF No Heat	SF Heat	MF No Heat	MF Heat
Customer	$9.50	$9.50	$7.30	$7.30
Meter	$3.18	$3.18	$3.18	$3.18
Distribution	2.915¢	1.872¢	2.653¢	1.583¢

AG/CUB Ex. 6.0 at 44. To ensure the fairness and equity of this recommendation, Mr. Rubin conducted a customer-impact analysis for each of the 2.9 million customers in ComEd's billing data set, and compared the bill to the bill under present rates. His analysis concluded that no customer would receive an increase of more than 28%. Id. at 44.

Mr. Rubin's proposed rate design, based on the AG/CUB recommendation for a rate decrease, is as follows:

Table 3: AG/CUB Proposed Rates				
	SF No Heat	SF Heat	MF No Heat	MF Heat
Customer	$7.75	$7.75	$5.96	$5.96
Meter	$2.60	$2.60	$2.60	$2.60
Distribution	2.379¢	1.528¢	2.166¢	1.291¢

If the AG/CUB recommendations are adopted in their entirety, most residential customers would have the distribution portion of their electric bill stay about the same or by reduced. These rates fairly apportion the cost of service among the diverse types of customers in the residential class and will greatly reduce the disparity between rates and the cost of service that exists under

present rates. If the Commission authorizes a different revenue requirement than recommended by ComEd or AG/CUB, it should adopt the procedure outlined in Mr. Rubin's direct testimony at pages 48-50.

In conclusion, ComEd's residential rate design proposal is not equitable. Substantial costs related to the use of electricity are being shifted out of the energy-related charge and onto the fixed charge. AG/CUB Ex. 6.0 at 25. This has the effect of requiring lower-use customers to subsidize higher-use customers and removes an important price signal from the rates: informing customers that their increased use of electricity (particularly during peak periods) results in increased costs to the distribution system. *Id.* ComEd's proposed rates would remove the price signal that helps tell customers they need to control their consumption.

2. Decoupling (NRDC Proposal)

CUB opposes NRDC's decoupling proposal, which AG/CUB witness Brosch testifies has the effect of adjusting utility rates based solely upon changes in residential per-customer sales volumes without regard to other changes in the utility's rate base, operating expenses or cost of capital. AG/CUB Ex. 12.0 at 10-11. NRDC's plan ignores the fact that utility expenses, rate base, and cost of capital are dynamic and shifts business risks associated with changes in sales volumes from the utility to utility customers. NRDC's request for baseline recovery on the allowed revenue requirement per customer represents single-issue ratemaking. NRDC's proposal is technically deficient as well, as it does not include a proposed tariff, contains no supportive analysis or documentation and provides no evidence that the plan would lead to increased energy efficiency investments by ComEd.

Mr. Rubin also responds to the NRDC decoupling proposal, and concludes that it would protect ComEd's revenue stream at the expense of consumers, with no indication that such an

extreme measure would result in any increased investment in energy efficiency. AG/CUB Ex. 11.0 at 19. He points out that decoupling should be rejected because: (1) it is inconsistent with sound regulatory policies that have been developed over many decades; (2) there is no evIdence ComEd would increase its investment in energy efficiency programs if it decoupling was approved; and (3) there are better ways to promote energy efficiency investments. Id. at 15.

3. Class Definitions

a. Residential Rate Design – Consolidation of Classes

As discussed above, ComEd is seeking to collapse its residential rate structure from four sub-classes to two, which would result in rates that do not distinguish between heating and non-heating customers. CUB opposes ComEd's proposed restructuring of residential rates there is tremendous diversity among ComEd's residential customers. AG/CUB Ex. 6.0 at 28. The proposal to eliminate any distinction between heating and non-heating customers has a dramatic impact on heating customers. The cost to serve MF Heat customer is approximately $45.6 million, but under present rates those customers already are providing ComEd with $49.9 million in revenues. AG/CUB Ex. 6.0 at 23. ComEd's proposed rates would increase this even further to $54.7 million, even though those customers are already paying more than the cost to serve them. Id. The effect would be that MF heating customers would pay nearly 20% more than the cost to serve them. Id. Similarly, SF Heat customers, who currently pay rates almost exactly equal to their cost of service, would receive a rate increase of approximately $3.0 million, which would exceed the cost of serving SF Heat customers by more than 14%. Id. Obviously, if the two heating subclasses are paying rates that exceed the cost of service by more than $12 million, the non-heating customers are the ones who benefit. Id. at 24. This result is contrary to ComEd's claims that it is seeking to recover its costs from the cost-causers.

Mr. Rubin's analysis concluded that the present rates for heating customers are providing revenues in excess of ComEd's proposed cost of service for those classes. Residential heating subclasses already are providing revenues in excess of the cost of service. The result is that costs are being over-recovered from heating customers and under-recovered from non-heating customers, resulting in inequitable rate design. This problem is only exacerbated by ComEd's proposed elimination of heating sub-classes. ComEd's proposal would impose substantial rate increases on many heating customer, even though those customers already are paying rates in excess of the proposed cost of service. ComEd should retain the four existing residential subclasses (SF Heat, MF Heat, SF No Heat and MF No Heat) because of significant differences in the usage characteristics and cost of service each type of customer.

b. Residential sub-classes and ComEd's ECOSS

Mr. Rubin also identified a problem with the Company's embedded cost of service study ("ECOSS") that causes an increase to residential customers' share of costs related to NCP demands when the residential class is broken up into four subclasses instead of two. This is because the ECOSS treats each residential subclass as a wholly separate customer class. AG/CUB Ex. 6.0 at 8. To correct for this anomaly, Mr. Rubin's analysis took the residential costs from ComEd's two-subclass study and reallocated them among the four residential subclasses. Id. at 10. This approach produces no effect any other rate classes. Mr. Rubin therefore recommends that the Commission direct ComEd in any future rate filing to allocate costs first to the residential class as a whole, then reallocate those residential costs among the residential subclasses.

X. REVENUES

D. LATE PAYMENT CHARGE REVENUES

Mr. Brosch proposed an adjustment to properly allocate revenues received by ComEd between revenues received related to distribution service and revenues received related to transmission service. AG/CUB Ex. 7.0 at 32-34. The Commission should recognize the $2,009,000 of jurisdictional revenue credits which were collected by ComEd customers pursuant to tariffs. As such, these revenues are appropriately treated as jurisdictional revenues in determining the Company's net delivery services revenue requirement. AG/CUB Ex. 7.1, Schedule C-14.

E. NEW BUSINESS REVENUE CREDIT

Mr. Effron proposed an adjustment to ComEd's projected new business revenues to reflect updated sales forecasts by the Company which show higher growth in sales than the Company reflects in its pro forma adjustment for post-test year growth in sales. AG/CUB Ex. 2.0 at 16-17. This adjustment increases the Company's pro forma test year rates by $3,800,000. AG/CUB Ex. 7.1, Schedule C-1.

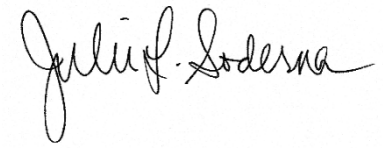
XI. OTHER

XII. CONCLUSION

The Commission should adopt the recommendations discussed herein and lower ComEd's delivery services rates to match its actual expenses. Doing so will continue to provide the utility with an opportunity to fully recover its costs and provide its investors with a sound return on their investment. Adoption of the AG/CUB proposed rate design will mean that opportunity will not come at the expense of ComEd's customers.

Dated: February 10, 2011

Respectfully submitted,



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