STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Commonwealth Edison Company	**:**	
	:	**10-0467**
Proposed general increase in electric rates.	**:**	

ADMINISTRATIVE LAW JUDGES' PROPOSED ORDER

April 1, 2011

Table of Contents

PROCEDURAL HISTORY 1
TESTIMONY, MOTIONS, AND RULINGS 4
LEGAL STANDARDS 10
ISSUES 10
I. Overall Revenue Requirement and Revenue Deficiency 10
II. Test Year 11
III. Rate Base 11
A. Overview 11
B. Potentially Uncontested Issues 11
1. Plant 11
a. AMI Pilot Costs (including AMI Meter Redeployment) 11
b. Other 11
2. General and Intangible Plant 12
3. Functionalization 12
C. Potentially Contested Issues 12
1. Post-Test Year Adjustments 12
a. *Pro Forma* Capital Additions 12
b. Accumulated Provisions for Depreciation and Amortization-Related Provisions for Accumulated Depreciation 23
2. Accumulated Deferred Income Taxes (ADIT) 30
3. Construction Work in Progress 30
4. Specific Plant Investments 35
a. West Loop Project Repair Disallowances 35
1. Plymouth Court Feeders 36
2. Underground Cable 36
3. Whether to Include PORCB (Purchase of Receivables and Consolidated Billing Service) Costs Here 37
4. Allocation of G & I Plant 41
5. Cash Working Capital 43
6. 2009 Pension Trust Contribution 49
7. Capitalized Incentive Compensation 52

8. Customer Deposits 52
9. Material and Supplies Inventories 55
10. Severance Cost - Regulatory Debit 57
D. Rate Base (Total) 58
IV. Operating Expenses 58
A. Overview 58
B. Potentially Uncontested Issues 59
1. 2009 Amortization Adjustment of Existing Regulatory Assets59
2. Outside Professional Services – Jacobs Consultancy..... 59
3. Advertising Expense 59
4. Investment Tax Credit Amortization 59
C. Contested Issues 59
1. Incentive Compensation Cost and Expenses 59
2. Rate Case Expenses 65
Rate Case Expenses of the Instant Case 65
3. Alternative Regulation (Alt. Reg.) Case Costs 80
4. Administrative and General (A&G) Expenses..... 85
a. Exelon Way Severance Amortization..... 85
b. Accounts 920-923 86
c. Pension Costs 87
(i) Recovery of Actuarially-Determined 2010 Pension and OPEB Costs (Uncontested between Company and Staff)..... 87
(ii) 2005 Pension Funding Cost Recovery..... 89
d. Wages and Salaries *Pro Forma* Adjustment..... 92
e. Directors' Fees and Expenses 94
f. Corporate Aircraft Costs (Now Uncontested)..... 95
g. Perquisites and Awards 95
h. Severance Expenses 97
i. Charitable Contributions 99
j. Legal Fees – IRS Dispute 103
k. Professional Sporting Activity Expenses..... 104
l. Workforce Expense Reduction 105

5. AMI Pilot Expenses 105
6. New Business Revenue Credit 106
7. Tax Repair Methodology – New IRS procedures 106
8. Depreciation of Intangible Plant 108
9. Late Repayment Charge Reclassification 109
10. Illinois Electric Distribution Taxes ("IEDT") 109
11. Depreciation and Amortization Expenses (Derivative and Direct) 111
12. Regulatory Asset Relating To Tax Liability for Medicare Part D (Uncontested between Company and Staff) 111
13. Taxes Other than Income Taxes (Derivative Adjustments) 112
14. Income Taxes (Derivative Adjustments) 112
15. Photovoltaic Pilot Costs 112
16. Customer Deposits – Interest Expense Component 113
17. Materials and Supplies Inventories Balance 113
18. Operating Expenses (Total) 113

V. Rate of Return 114
A. Overview 114
B. Capital Structure 114
C. Cost of Short-Term Debt 115
D. Cost of Long-Term Debt (Potentially Uncontested) 116
E. Cost of Common Equity 116
1. Discounted Cash Flow Analysis 131
2. CAPM Analysis 135
3. Alternative ROE Analyses 137
4. The Parties' Analyses 138
5. ComEd's Commentary Testimony 141
6. DCF Model Issues – Growth Rates 142
7. CAPM Analysis Issues -- Market Risk Premium 143
F. Adjustments to Rate of Return 146
G. Staff's Adjustments to Rate of Return 154
H. Overall Cost of Capital (Derivative) 155

VI. Cost of Service and Allocation Issues 156

A. Overview 156
B. Potentially Uncontested Issues 156
C. Potentially Contested Issues 156
1. Embedded Cost of Service Study Issues 156
a. Class Definitions 156
(i) Residential Classes 156
(ii) Non-residential Classes 156
b. Primary/Secondary Split 156
(i) The Appropriate Methodology/Non-Compliance with What the Commission Required in its Final Order in Docket 08-0532 157
(i) Functional Identification of Costs 157
c. Direct Observation of ComEd Facilities 163
d. Sampling 167
b. Review of Other Utilities' Treatment of Primary/Secondary Issues 169
(i) Other Primary/Secondary Split issues 171
c. Investigation of Assets Used To Serve Extra Large Load Customer Class 178
d. NCP (Noncoindent Peak) vs. CP (Coincident Peak) 182
f. Allocation of Primary Lines and Substations 189
g. Functionalization of General and Intangible Plant . 189
h. Street Lighting 189
i. Allocation of Illinois Electricity Distribution Tax 189
j. Indirect Uncollectible Costs 189
k. Customer Care Cost Allocation 190
(i) Allocation Study vs. Switching Study 196
(ii) Direct O&M Costs vs. Total Costs in the Switching Study 197
(iii) Adjustment of Allocation Study Allocators ... 199
l. Other Docket No. 08-0532 Compliance Issues 199
m. Other Issues 199
1. Imposition of AMI (Advanced Metering Infrastructure) Costs on the Railroad Class 199

D. Rate Moderation 201
VII. Rate Design 201
A. Overview 201
B. Potentially Uncontested Issues 202
1. High Voltage Rate Design Simplification 202
2. Rate MSPS 202
3. General Terms and Conditions 202
a. New Customers with load that includes motors equal or greater than five horsepower 202
4. Miscellaneous Charges and Fees 203
5. Meter Lease Charges 203
6. Residential Real Time Pricing Program Costs 203
7. Standard Meter Allowances 204
C. Potentially Contested Issues 204
1. SFV 204
a. ComEd's Proposal 204
b. Decoupling (NRDC Proposal) 218
VIII. THE COMMISSION SHOULD NOT DEFER A DECISION ON DECOUPLING 218
A. Decoupling Is Not Improper Single Issue Ratemaking. 219
B. Decoupling Does Not Shift Risk to Ratepayers. 220
C. Decoupling Does Not Allow ComEd to Retain All Revenues From New Customers 222
D. Decoupling Will Not Affect Regulatory Lag. 223
E. Decoupling Does Not Necessitate a Reduction in ComEd's Allowed Rate of Return. 223
F. Decoupling Will Have a Positive Impact on Energy Efficiency in the ComEd Service Territory. 223
1. Class Definitions 232
a. Residential Rate Design – Consolidation of Residential Classes 232
b. New Primary Voltage Delivery Class vs. Primary Subclass Charges 236
2. Non-Residential 242
a. Movement Toward ECOSS Rates 242

(i) Extra Large Load, High Voltage Customer Classes 242
b. Allocating Secondary Costs Among Customer Classes 251
c. Railroad Customers – ComEd's Use of Railroad Class' Facilities 251
d. Dusk to Dawn Street Lighting 260
3. Collection of Illinois Electricity Distribution Tax 265
a. Reasonableness of Current Allocation 267
b. IIEC Recommended Allocation 268
4. Distribution Loss Factors 270
a. High-Voltage Customers--The Issues Presented by the United States Department of Energy and the IIEC (Uncontested) 276
5. General Terms and Conditions 277
a. Residential Service Station (Ownership of Non-Standard Residential Connections) 277
b. Limitation of Liability Language 280
6. Rider UF 286
7. Notification Regarding Elimination of Self-Generation Customer Group 286
Analysis and Conclusions 287
8. Docket No. 08-0532 Compliance Issues 287
G. Other Issues 287
a. Street Lighting 287
H. Uncontested Issues - Other Revenues – Rate Relief Payment ... 287
I. Miscellaneous Revenues 287
J. Weather Normalization 287
K. Late Payment Charge Revenues 287
L. New Business Revenue Credit 290
IX. OTHER 293
A. Retail Electric Supplier Services Issues 293
1. Requiring ComEd to Provide Alternative Electric Suppliers with Historical Interval Data within One Business Day 293
2. Retail Electric Suppliers' Use of Multiple DUNS+4 Numbers293

3. ICEA's Contention that ComEd's Initial 814 Change Response Should Include an Effective Date 293

4. Proposed Changes to the PowerPath Website 294

5. Competitive Retail Market Development Issues 295

a. A Simple and Straightforward Price to Compare ... 295

b. Creation of an "Eligible Customer List" of Residential Customers 295

B. UUIR 295

C. Updated Distribution Loss Study 297

D. Meters and Meter Reading 297

1. Timely Meter Reading 297

E. New Section 9-250 Investigation of ComEd's Electric Rate Design299

F. Other 299

XI. FINDINGS AND ORDERING PARAGRAPHS 299

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Commonwealth Edison Company	**:**	
	:	**10-0467**
Proposed general increase in electric rates.	**:**	

ADMINISTRATIVE LAW JUDGES' PROPOSED ORDER

By the Commission:

PROCEDURAL HISTORY

On June 30, 2010, Commonwealth Edison Company ("ComEd") filed with the Illinois Commerce Commission (the "Commission"), pursuant to Section 9-201 of the Public Utilities Act (the "Act") (220 ILCS 5/9-201), the following tariff sheets: ILL. C. C. No. 10; 1st Revised Sheet No. 19; 3rd Revised Sheet No. 21; 2nd Revised Sheet No. 27; 1st Revised Sheet No. 29; 3rd Revised Sheet No. 33; 3rd Revised Sheet No. 34; 4th Revised Sheet No. 36; 2nd Revised sheet No. 38; 2nd Revised Sheet No. 40; 3rd Revised Sheet No. 45; 1st Revised sheet No. 58; 3rd Revised Sheet No. 60; 3rd Revised Sheet No. 61; 3rd Revised Sheet No. 62; 3rd Revised Sheet No. 63; 3rd Revised Sheet No. 64; 3rd Revised Sheet No. 65; 3rd Revised Sheet No. 66; 1st Revised Sheet No. 67; 1st Revised Sheet No. 75; 1st Revised Sheet No. 99; 1st Revised Sheet No. 100; 1st Revised Sheet No. 101; 1st Revised Sheet No. 125; 1st Revised Sheet No. 135; 1st Revised Sheet No. 138; 1st Revised Sheet No. 139; 1st Revised Sheet No. 140; 1st Revised Sheet No. 141; 1st Revised Sheet No. 146; Original Sheet No. 146.1; 1st Revised Sheet No. 147; 1st Revised Sheet No. 151; 1st Revised Sheet No. 152; 1st Revised Sheet No. 154; 1st Revised Sheet No. 155; 1st Revised Sheet No. 165; 1st Revised Sheet No. 169; 1st Revised Sheet No. 182; 1st Revised Sheet No. 184; 1st Revised Sheet No. 186; 1st Revised Sheet No. 187; 1st Revised Sheet No. 188; 1st Revised Sheet No. 189; 1st Revised Sheet No. 192; 1st Revised Sheet No. 195; 1st Revised Sheet No. 204; 1st Revised Sheet No. 205; 1st Revised Sheet No. 208; 2nd Revised Sheet No. 209; 1st Revised Sheet No. 215; 1st Revised Sheet No. 250; 1st Revised Sheet No. 251; 2nd Revised Sheet No. 257; 3rd Revised Sheet No. 267; 1st Revised Sheet No. 273; 1st Revised Sheet No. 274; 1st Revised Sheet No. 275; 1st Revised Sheet No. 276; Original Sheet No. 276.1; 1st Revised Sheet No. 286; 1st Revised Sheet No. 306; 1st Revised Sheet No. 330; 1st Revised Sheet No. 333; 2nd Revised sheet No. 345; 1st Revised Sheet No. 359; and 2nd Revised Sheet No. 367. This tariff filing embodied a proposed general increase in electric rates. The tariff filing

was accompanied by direct testimony, other exhibits, and other materials required under Parts 285 ("Part 285") and 286 ("Part 286") of Title 83 of the Illinois Administrative Code (the "Code"), 83 Ill. Admin Code Parts 285 and 286.

Notice of proposed tariff changes reflected in this rate filing was posted in ComEd's business offices and published in a secular newspaper of general circulation in ComEd's service area, as evidenced by publisher's certificates, in accordance with the requirements of Section 9-201(a) of the Act, 220 ILCS 5/9-201(a) and the provisions of 83 Ill. Admin. Code Part 255.

The Commission issued a Suspension Order on July 28, 2010, suspending the Tariffs for the period beginning August 14, 2010 through and including November 26, 2010, and initiating this proceeding. On November 4, 2010, the Commission issued a Resuspension Order, suspending the Tariffs to and including May 26, 2011.

In response to the Company's filing, the following parties filed Petitions to Intervene which were granted by the Administrative Law Judges ("ALJs"): AARP; Abbott Laboratories, Inc. ("Abbott"); People of the State of Illinois ("AG"); Citizens Utility Board ("CUB") (collectively, AG and CUB are referred to as "AG/CUB"); the Building Owners and Managers Association of Chicago ("BOMA"); the Chicago Transit Authority ("CTA"); Northeast Illinois Regional Commuter Railroad Corporation, d/b/a Metra ("Metra") (collectively, CTA and Metra are "CTA/Metra"); Corn Products International, Inc. ("Corn Products"); the City of Chicago (the "City"); the Coalition to Request Equitable Allocation of Costs Together ("REACT"); the Commercial Group ("CG"); Constellation NewEnergy, Inc. ("NewEnergy"); United States Department of Energy ("DOE"); Dominion Retail, Inc. ("Dominion"); Enbridge Energy, LLP ("Enbridge"); Environmental Law & Policy Center ("ELCP"); ExxonMobil Gas & Power Marketing Company ("ExxonMobil"); General Iron Industries ("General Iron"); the Illinois Competitive Energy Association ("ICEA"); Illinois Power Agency ("IPA"); Kroger Co. ("Kroger"); Merchandise Mart Properties, Inc. ("Merchandise Mart"), Nucor Steel Kankakee, Inc. ("Nucor"); National Resources Defense Council ("NRDC"); Retail Energy Supply Association ("RESA"); Sterling Steel Company, LLC ("Sterling"); Tenaska Taylorville, LLC ("Tenaska"); and Thermal Chicago Corporation ("Thermal") (collectively, Abbott, Corn Products, Enbridge, ExxonMobil, General Iron, Merchandise Mart, Sterling, and Thermal are styled as the "Illinois Industrial Energy Consumers" or "IIEC") (collectively, all of the foregoing parties are the "Intervenors").

Evidentiary Hearings were held on January 10-14 and 18-20, 2011, at the offices of the Commission in Chicago, Illinois. At the evidentiary hearings, ComEd, the Staff of the Commission ("Staff"), AG, City, CG, CTA, DOE, Dominion, ICEA, IIEC, Kroger, Metra, NRDC, REACT, RESA, CUB, REACT, BOMA of Chicago, RESA, the Commercial Group, IIEC, DOE, Kroger, AARP, and Metra entered appearances and presented testimony, either by live witness(es) or affidavit(s). Appearances were also entered for BOMA although they did not submit testimony.

The following witnesses testified on behalf of ComEd: Michael Guerra (ComEd Ex. 1.0 Rev., ComEd Ex. 25.0, ComEd Ex. 52.0); Geoffrey J.D. Hewings (ComEd Ex. 43.0, ComEd Ex. 69.0); Juan Andrade (ComEd Ex. 3.0, ComEd Ex. 44.0 Rev., ComEd Ex. 70.0); Joseph Trpik, (ComEd Ex. 4.0 Rev., ComEd Ex. 28.0, ComEd Ex. 54.0;

Kathryn Houtsma (ComEd Ex. 6.0 Rev., ComEd Ex. 29.0, ComEd Ex. 55.0 2nd Rev.); Nagendra Subbakrishna (ComEd Ex. 7.0, ComEd Ex. 31.0, ComEd Ex. 57.0); Terence R. Donnelly (ComEd Ex. 8.0, ComEd Ex. 20.0, ComEd Ex. 32.0, ComEd Ex. 58.0, ComEd Ex. 58.0 Rev.); Michael McMahan (ComEd Ex. 33.0, ComEd Ex. 60.0); Fidel Marquez (ComEd Ex. 10.0, ComEd Ex. 36.0 Rev., ComEd Ex. 61.0 Rev.); Samuel C. Hadaway (ComEd Ex. 11.0, ComEd Ex. 37.0, ComEd Ex. 62.0); Carl Seligson (ComEd Ex. 12.0 Rev., ComEd Ex. 38.0); Susan F. Tierney (ComEd Ex. 13.0, ComEd Ex. 39.0, ComEd Ex. 64.0); Ross C. Hemphill (ComEd Ex. 14.0 2nd Rev., ComEd Ex. 40.0, ComEd Ex. 46.0, ComEd Ex. 65.0, ComEd Ex. 71.0); Alan C. Heintz (ComEd Ex. 15.0, ComEd Ex. 22.0, ComEd Ex. 51.0, ComEd Ex. 75.0); Lawrence S. Alongi (ComEd Ex. 16.0 3rd Rev., ComEd Ex. 21.0 2nd Rev., ComEd Ex. 41.0, ComEd Ex. 49.0, ComEd Ex. 68.0, ComEd Ex. 73.0 2nd Rev.); Robert Garcia (ComEd Ex. 23.0, ComEd Ex. 24.0, ComEd Ex. 50.0, ComEd Ex. 74.0); Val R. Jensen (ComEd Ex. 17.0); Mary Anne Emmons (ComEd Ex. 18.0 Rev.); Ronald E. Donovan (ComEd Ex. 19.0 Rev., ComEd Ex. 48.0, ComEd Ex. 72.0); Phillip O'Connor (ComEd Ex. 26.0 Rev., ComEd Ex. 53.0); Dean Apple (ComEd Ex. 27.0); Michael F. Born (ComEd Ex. 34.0, ComEd Ex. 67.0 Rev.); Robert W. Donohue (ComEd Ex. 35.0 Rev., ComEd Ex. 59.0); Stephen L. Lesniak (ComEd Ex. 42.0, ComEd Ex. 66.0); Mark Lowry (ComEd Ex. 47.0) and Martin Fruehe (ComEd Ex. 30.0 Rev., ComEd Ex. 56.0 3rd Rev.).

The following witnesses testified on behalf of Staff: Theresa Ebrey (ICC Staff Ex. 1.0, ICC Staff Ex. 16.0); Dianna Hathhorn (ICC Staff Ex. 2.0, ICC Staff Ex. 17.0); Bonita Pearce (ICC Staff Ex. 3.0 Rev., ICC Staff Ex. 18.0); Scott Tolsdorf (ICC Staff Ex. 4.0, ICC Staff Ex. 19.0); Michael McNally (ICC Staff Ex. 5.0, ICC Staff Ex. 20.0); Greg Rockrohr (ICC Staff Ex. 6.0, ICC Staff Ex. 21.0); Mona Elsaid (ICC Staff Ex. 7.0, ICC Staff Ex. 22.0); David Brightwell (ICC Staff Ex. 8.0, ICC Staff Ex. 23.0); John V. Stutsman (ICC Staff Ex. 9.0, ICC Staff Ex. 24.0); Peter Lazare (ICC Staff Ex. 10.0, ICC Staff Ex. 26.0); Cheri I. Harden (ICC Staff Ex. 11.0, ICC Staff Ex. 27.0); Philip Rukosuev (ICC Staff Ex. 12.0, ICC Staff Ex. 28.0); Christopher L. Boggs (ICC Staff Ex. 13.0, ICC Staff Ex. 29.0); Torsten Clausen (ICC Staff Ex. 14.0, ICC Staff Ex. 25.0, ICC Staff Ex. 30.0); and Eric P. Schlaf (ICC Staff Ex.15.0, ICC Staff Ex. 31.0).

The following witness testified on behalf of AG: Roger Colton (AG Ex. 5.0 Rev., AG Ex. 9.0 Rev.).

The following witnesses testified on behalf of AG-CUB: Michael L. Brosch (AG-CUB Ex. 1.0, AG-CUB Ex. 7.0, AG-CUB Ex. 12.0); David J. Effron (AG-CUB Ex. 2.0, AG-CUB Ex. 8.0); Ralph C. Smith (AG-CUB Ex. 3.0, AG-CUB Ex. 9.0); Christopher C. Thomas (AG-CUB Ex. 4.0); Scott J. Rubin (AG-CUB Ex. 6.0, AG-CUB Ex. 11.0) and Christopher C. Thomas (AG-CUB Ex. 10.0).

The following witness testified on behalf of the City: Edward Bodmer (City Ex. 1.0, City Ex. 2.0).

The following witnesses testified on behalf of CG: Richard A. Baudino (CG Ex. 1.0, CG Ex. 3.0) and David F. Vite (CG Ex. 2.0).

The following witnesses testified on behalf of the CTA: James Harper (CTA Ex. 1.0, CTA Ex. 4.0); Emily Ziring (CTA Ex. 2.0); and Amy S. Kovalan (CTA Ex. 3.0).

The following witness testified on behalf of CTA/Metra: James Bachman (CTA-Metra Ex. 1.0, CTA-Metra Ex. 2.0).

The following witnesses testified on behalf of the DOE: Dwight Etheridge (DOE Ex. 1.0, DOE Ex. 3.0) and Kirk P. Patterson (DOE Ex. 2.0, DOE Ex. 4.0).

The following witness testified on behalf of Dominion: James Crist (Dominion Ex. 1.0, Dominion Ex. 2.0).

The following witness testified on behalf of ICEA: David Fein (ICEA Ex. 1.0, ICEA Ex. 2.0).

The following witnesses testified on behalf of IIEC: Michael P. Gorman (IIEC Ex. 1.0, IIEC Ex. 4.0); Robert R. Stephens (IIEC Ex. 2.0, IIEC Ex. 5.0); and David L. Stowe (IIEC Ex. 3.0, IIEC Ex. 6.0).

The following witness testified on behalf of Kroger: Neal Townsend (Kroger Ex. 1.0, Kroger Ex. 2.0).

The following witnesses testified on behalf of Metra: Richard Capra (Metra Ex. 1.0) and Lynnette Ciavarella (Metra Ex. 2.0).

The following witnesses testified on behalf of NRDC: Karl A. McDermott (NRDC Ex. 1.0) and Ralph Cavanaugh (NRDC Ex. 2.0, NRDC Ex. 3.0).

The following witnesses testified on behalf of REACT: Bradley O. Fults (REACT Ex. 1.0, REACT Ex. 4.0); Jeffrey Merola (REACT Ex. 2.0, REACT Ex. 5.0); and Harry L. Terhune (REACT Ex. 3.0, REACT Ex. 6.0).

The following witness testified on behalf of RESA: Roy Boston (RESA Ex. 1.0, RESA Ex. 2.0).

TESTIMONY, MOTIONS, AND RULINGS

On June 30, 2010, ComEd filed its direct testimony with its Part 285 Filing.

On July 28, 2010, the Commission entered its Suspension Order.

On August 9, 2010, ComEd filed a Motion for Leave to File Supplemental Direct Testimony in order to satisfy all directives the Commission made during its rate design investigation, Docket No. 08-0532. A number of the directives could not be met in the initial filing due to time constraints.

On August 13, 2010, ComEd filed a Motion for Entry of Protective Order to govern the treatment of certain confidential and proprietary information and materials.

Also on August 23, 2010, Staff filed its Response to ComEd's Motion for Entry of a Protective Order.

On August 26, 2010, CUB, the AG, and AARP jointly filed a Motion to Strike ComEd's direct testimony of Mr. Hewings in its entirety and portions of the direct testimony of Mr. Andrade, on the grounds that the testimony was irrelevant and created an undue burden on other parties to the proceeding.

Also on August 26, 2010, the AG and Dominion, jointly, and REACT, separately, filed responses to ComEd's Motion for Leave to File Supplemental Direct Testimony.

The filings also included a Motion to Dismiss ComEd's rate case, alleging that the initial filing failed to comply with the Commission's order in Docket 08-0532.

Also on August 26, 2010, the AG and CUB each filed a Response to ComEd's Motion for Entry of a Protective Order.

On September 3, 2010, ComEd filed its Reply in Support of Its Motion for Entry of a Protective Order.

On September 9, 2010, ComEd filed its Response to the Motion to Strike by CUB, the AG, and AARP.

Also on September 9, 2010, ComEd filed its Combined Reply in Support of its Motion for Leave to File Supplemental Direct Testimony and its Response to the AG and Dominion's and REACT's Motions to Dismiss.

Also on September 9, 2010, Staff filed its Response to CUB's Motion to Strike.

Also on September 9, 2010, Metra filed its Response in Support for the AG and Dominion's Motion to Dismiss.

Also on September 9, 2010, CUB filed its Response to the AG and Dominion's and REACT's Motions to Dismiss.

On September 13, 2010, REACT filed its Reply in Support of its Motion to Dismiss.

Also on September 13, 2010, CUB, the AG, and AARP jointly filed their Reply in Support of their Motion to Strike.

On September 14, 2010, the AG and Dominion filed their Reply to ComEd's Combined Reply in Support of Motion for Leave to File Supplemental Direct Testimony and Response to Motions to Dismiss.

On September 17, 2010, the ALJs granted the Motion to Strike filed by CUB, the AG, and the AARP.

Also on September 17, 2010, the ALJs granted ComEd's Motion for Leave to File Supplemental Direct Testimony and denied the AG and Dominion's and REACT's Motions to Dismiss. The ALJs found that though it did not appreciate the supplemental filing, the rate case was in the sufficiently early stages to allow the parties adequate time to process this information.

On September 21, 2010, the ALJs issued a ruling regarding the Protective Order, including language that was proffered by the AG and Staff, but declined to add the language proffered by CUB.

On October 8, 2010, REACT filed a Verified Petition for Interlocutory Review by the Commission of the ALJs' September 17, 2010 ruling regarding ComEd's Motion for Leave to File Supplemental Direct Testimony and REACT's Motion to Dismiss.

On October 13, 2010, the AG, AARP, CUB and the CTA jointly filed a Motion to Consolidate the pending rate case, Docket No. 10-0467, and ComEd's petition for alternative rate regulation, Docket No. 10-0527.

On October 15, 2010, ComEd filed its Response to REACT's Petition for Interlocutory Review.

On October 19, 2010, ComEd, Staff, and Metra each filed a Response to the AG, AARP, CUB and the CTA's Motion to Consolidate. Metra's Response was in support of the Motion to Consolidate.

On October 21, 2010, REACT filed its Motion to Strike Certain Portions of ComEd's Response to REACT's Petition for Interlocutory Review. REACT argued that ComEd had alleged new facts and arguments that ComEd had not made during the ALJs' consideration of the Motion to Dismiss.

On October 22, 2010, the AG, AARP, CUB, the CTA, and Metra jointly filed their Reply in Support of the Motion to Consolidate.

Also on October 22, 2010, ComEd filed its Response to REACT's Motion to Strike Certain Portions of ComEd's Response to REACT's Petition for Interlocutory Review.

October 25, 2010, REACT filed its Reply in Support of its Motion to Strike Certain Portions of ComEd's Response to REACT's Petition for Interlocutory Review.

On October 26, 2010, Staff, the AG, AG-CUB, CUB, Dominion, IIEC, ICEA, and RESA filed their respective direct testimony related to issues other than rate design.

On October 28, 2010, the ALJs denied the Motion by AG, AARP, CUB, and CTA to consolidate Dockets 10-0467 and 10-0527, which involved separate legal and factual issues. The ALJs held that combining the rate case and alternative regulation case could prejudice the parties and create unnecessary confusion.

On November 4, 2010, the Commission denied REACT's Petition for Interlocutory Review.

On November 5, 2010, the AG sent a letter to ComEd challenging the designation of certain information relating to the costs of consultants, experts, and outside counsel used in litigating the rate case.

On November 12, 2010, ComEd filed a Motion to Preserve the Confidentiality Designations of Certain Documents, specifically referring to the documents named in the AG's letter dated November 5, 2010.

Also on November 12, 2010, ComEd filed its Motion Directed to the Direct Testimony of Roger D. Colton, asking that the Commission reconsider and admit the testimony of Mr. Hewings, which had been struck from the record on September 17, 2010, as a rebuttal to the testimony of Mr. Colton. Alternatively, ComEd asked that the Commission strike certain portions of Mr. Colton's testimony as unrelated to the rate case.

On November 19, 2010, Staff, AG-CUB, CG, CTA-Metra, the City, DOE, Dominion, IIEC, Kroger, Metra, NRDC, and REACT filed their respective direct testimony related to rate design issues.

Also on November 19, 2010, the AG and CUB filed their Response in Opposition to ComEd's Motion to Preserve the Confidential Designation of Certain Documents.

On November 22, 2010, ComEd filed its rebuttal testimony related to issues other than rate design.

On November 23, 2010, Staff filed a Motion to Remove the Confidential Designation from Staff's Direct Testimony of Bonita A. Pearce. Also on November 23, 2010, the ALJs granted the Motion.

On November 24, 2010, ComEd filed its Reply in Support of its Motion to Preserve the Confidential Designation of Certain Documents.

Also on November 24, 2010, REACT filed its Motion to Compel ComEd's Responses to Certain of REACT's Second, Third, Fourth, and Fifth Sets of Data Requests, which pertained to actual costs incurred to provide service to ComEd's Extra Large Load customer class and to provide supply-related customer care service.

On November 29, 2010, the AG filed its Response to ComEd's Motion Directed to the Direct Testimony of Roger D. Colton.

On December 1, 2010, ComEd filed its Reply in Support of its Motion Directed to the Direct Testimony of Roger D. Colton.

On December 3, 2010, ComEd filed its Response to REACT's Motion to Compel.

On December 6, 2010, REACT filed an Application for Rehearing of the November 4, 2010 order entered by the Commission regarding REACT's Petition for Interlocutory Review of the ALJs' September 17, 2010 order.

On December 7, 2010, REACT filed its Reply in Support of Its Motion to Compel.

On December 8, 2010, ComEd filed its rebuttal testimony related to rate design issues.

On December 9, 2010, ComEd filed a Motion to Strike REACT's Application for Rehearing as barred by Commission rules.

On December 10, 2010, the ALJs issued a ruling regarding ComEd's Motion Directed to the Direct Testimony of Roger D. Colton. The ALJs granted the Motion to strike certain portions of Mr. Colton's testimony, but denied all other relief requested. The ALJs also denied ComEd's Motion to Preserve the Confidential Designation of Certain Documents and denied REACT's Motion to Compel.

Also on December 10, 2010, REACT filed its Response to ComEd's Motion to Strike REACT's Application for Rehearing.

On December 14, 2010, ComEd filed its Reply Supporting its Motion to Strike REACT's Application for Rehearing.

On December 16, 2010, AG filed a Motion for Leave to File Revised Testimony of Mr. Colton pursuant to the ALJs' ruling of December 10, 2010.

On December 21, 2010, the Commission in conference denied REACT's Application for Rehearing.

On December 22, 2010, the ALJs granted the AG's Motion for Leave to File the Amended Testimony of Mr. Colton.

Also on December 22, 2010, ComEd filed a Motion to Strike the Revised Direct Testimony of Mr. Colton, asserting that the revised testimony merely contained the stricken testimony in red, strike-through format, and should be entirely removed.

On December 23, 2010, the AG filed a Petition for Interlocutory Review to reverse the ALJs' December 10, 2010 decision to strike portions of Mr. Colton's direct testimony.

On December 23, 2010, Staff, the AG, AG-CUB, Dominion, ICEA, IIEC, and RESA filed their respective rebuttal testimony related to issues other than rate design.

On December 27, 2010, ComEd filed a Motion to Strike Rebuttal Testimony of Roger D. Colton, arguing that in many instances, the rebuttal testimony contained the identical language that the ALJs ordered stricken on December 10, 2010.

On December 29, 2010, REACT filed a Combined Motion for the following: (1) reconsideration of the ALJs' December 10, 2010 ruling denying REACT's Motion to Compel the response to certain data requests regarding cost causation; (2) an immediate stay of 21 days while seeking interlocutory review of the December 10, 2010 ruling; and (3) an ALJs ruling compelling ComEd to provide responses to other data requests related to cost causation.

On December 30, 2010, Staff, Kroger, AG-CUB, the City, CG, CTA-Metra, DOE, IIEC, NRDC, and REACT filed their respective rebuttal testimony related to rate design issues.

Also on December 30, 2010, ComEd filed its Response to the AG's Petition for Interlocutory Review to Reverse the ALJs' Ruling to Strike the Testimony of Mr. Colton.

Also on December 30, 2010, the AG filed its Response to ComEd's Motion to Strike the Revised Direct Testimony of Mr. Colton.

On January 3, 2010, ComEd filed its surrebuttal testimony related to issues other than rate design.

Also on January 3, 2011, REACT filed a Petition for Interlocutory Review of the ALJs' December 10, 2010 ruling denying REACT's Motion to Compel the response to certain data requests regarding cost causation.

Also on January 3, 2011, the ALJs issued a ruling addressing REACT's Motion to Compel. The ruling held that ComEd should provide a response as to why it does not have the records regarding the installation of customers in the Very Large Customer class or an affidavit stating that ComEd has provided REACT with the records regarding these installations.

On January 4, 2011, CUB filed a Motion to Compel Withdrawal of ComEd's rebuttal testimony of Messrs. Hewings and Andrade on the grounds that the testimony was submitted in violation of the ALJs' rulings dated September 17, 2010 and December 10, 2010.

On January 5, 2010, ComEd filed its surrebuttal testimony related to rate design issues.

Also on January 5, 2010, the Commission in conference granted REACT's Petition for Interlocutory Review to reverse the ALJs' Ruling to Strike Testimony of Mr. Colton that was filed on December 23, 2010, except as to testimony regarding ComEd's alternative regulation proceeding. With respect to the latter category of evidence, the Commission declined to reverse the ALJs.

Also on January 5, 2011, IIEC filed a Motion to Strike ComEd's surrebuttal testimony of Mr. Hadaway.

Also on January 5, 2011, Staff filed a Motion to Strike certain portions of ComEd's rebuttal testimony of Ms. Houtsma.

Also on January 5, 2011, ComEd filed its Response to REACT's Combined Motion for Reconsideration, Motion for Stay of Time, and Motion to Compel.

On January 6, 2011, ComEd filed its Response to CUB's Motion to Compel Withdrawal of Testimony.

Also on January 6, 2011, ComEd filed its Response to IIEC's Motion to Strike ComEd's surrebuttal testimony of Mr. Hadaway.

Also on January 6, 2011, ComEd filed its Response to Staff's Motion to Strike certain portions of ComEd's rebuttal testimony of Ms. Houtsma.

Also on January 6, 2011, the AG filed a Motion to Strike certain portions of ComEd's rebuttal testimony of Mr. O'Connor.

On January 7, 2011, ComEd, Staff, the AG, BOMA, CG, CTA, CUB, Dominion, DOE, ELCP, Metra, ICEA, IIEC, Kroger, NRDC, REACT, and RESA each filed their respective pre-hearing memorandum.

Also on January 7, 2011, REACT filed its Reply in support of its Combined Motion for Reconsideration, Motion for Stay of Time, and Motion to Compel.

Also on January 7, 2011, Staff filed its Reply to ComEd's Response to Staff's Motion to Strike certain portions of ComEd's rebuttal testimony of Ms. Houtsma.

Also on January 7, 2011, the ALJs granted Staff's Motion to Strike certain portions of ComEd's rebuttal testimony of Ms. Houtsma. Also, REACT's Motion to Compel was granted in part, such that ComEd must turn over certain cost causation records.

On January 10, 2011, the ALJs denied IIEC's Motion to Strike ComEd's surrebuttal testimony of Mr. Hadaway.

Also on January 10, 2011, ComEd filed its Response to REACT's Petition for Interlocutory Review of the December 10, 2010 Ruling.

On January 11, 2011, the City filed its Pre-Trial Memorandum.

On January 13, 2011, ComEd filed Petition for Interlocutory Review of the ALJs' January 7, 2011 ruling striking certain portions of ComEd's surrebuttal testimony of Ms. Houtsma.

On January 24, 2011, the Commission denied REACT's Petition for interlocutory review of the ALJs' December 10, 2010 ruling.

On January 25, 2011, ComEd withdrew its Petition for Interlocutory Review of the ALJs' January 7, 2011 ruling.

Initial Briefs were filed on February 10, 2011, by ComEd, Staff, AARP, the AG, the City, CG, CUB, CTA, DOE, Dominion, ELPC, ICEA, IIEC, Kroger, NRDC, REACT, and RESA. Reply Briefs were filed on February 23, 2011, by ComEd, Staff, the AG, the City, CG, CUB, CTA, Dominion, ELPC, IIEC, NRDC and REACT.

The ALJs Proposed Order was served on April 1, 2011.

LEGAL STANDARDS

The central legal principles governing this case are clear and longstanding. As in all contested ratemaking proceedings, the Commission's order must be within its jurisdiction and authority, must be lawful, and must be based exclusively on the evidence in the record. *E.g.*, 220 ILCS 5/10-103, 10-201(e)(iv); *Bus. & Prof. People for the Pub. Interest v. Ill. C. C.*, 136 Ill. 2d 192, 201, 227 (1989).

The Illinois Public Utilities Act (the "Act") requires that: "Charges for delivery services shall be cost based, and shall allow the electric utility to recover the costs of providing delivery services through its charges to its delivery service customers that use the facilities and services associated with such costs."[1] 220 ILCS 5/16-108(c). Allowing a utility to recover fully through rates its costs of providing Illinois-jurisdictional delivery services is a right established not only by Section 16-108(c) of the Act, but also by fundamental principles under the Act and the Illinois and federal constitutions. The Act long has mandated that rates adopted in a contested ratemaking proceeding must be just and reasonable. 220 ILCS 5/9-201(c). The "just and reasonable" mandate of Section 9-201(c) of the Act means that the rates must be just and reasonable to the utility and its stockholders as well as its customers. *Bus. & Prof. People for the Pub. Interest v. Ill. C. C.*, 146 Ill. 2d 175, 208 (1991). *See also Citizens Util. Bd. v. Ill. C. C.*, 166 Ill. 2d 111, 121 (1995) ("In setting rates, the Commission must determine that the rates accurately reflect the cost of service delivery and must allow the utility to recover costs prudently and reasonably incurred.") (citing 220 ILCS 5/1-102(a)(iv) (case involving riders for certain environmental expenses). Moreover, the full cost recovery principle incorporated in the Act is required by well-established constitutional standards ensuring for utilities providing regulated services the opportunity to recover their capital costs and operating expenses, including a reasonable rate of return of and on their capital investments. *E.g.*, U.S. Const., amend. XIV; *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989); *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 605 (1944); *Bluefield Waterworks v. Pub. Service Comm'n*, 262 U.S. 679, 690 (1923); Ill. Const. Art. I, § 15.

ISSUES

I. Overall Revenue Requirement and Revenue Deficiency

ComEd presented and supported with detailed evidence a final revised revenue requirement of $2.267 billion, which reflects a revenue deficiency under existing rates of $326.3 million. See, Houtsma Surrebuttal ("Sur."), ComEd Exhibit ("Ex.") 55.0 2nd Revised ("Rev.") at 6. Staff and certain intervenors proposed various adjustments to

rate base, operating expenses, revenues, and the rate of return. The Commission's findings and conclusions on the revenue requirement and revenue deficiency are set forth in the remainder of this Order.

II. Test Year

ComEd's revenue requirement is based on the historical 2009 test year with *pro forma* adjustments. The test year is uncontested. The Commission approves the test year.

III. Rate Base

A. Overview

ComEd's final proposed rate base is $7,349,227,000. ComEd Ex. 55.1, Schedule ("Sched.") A-4-Rev. ComEd also requests that the Commission approve the original cost of plant in service as of December 31, 2009, before adjustments, of $13,932,447,000. Houtsma Direct ("Dir."), ComEd Ex. 6.0 Rev. at 23.

Staff and certain intervenors proposed various adjustments to rate base. The Commission's findings and conclusions on rate base adjustments are set forth in the remainder of this Order.

Staff also proposed that the Commission approve an original cost of plant in service as of December 31, 2009, of $13,904,344,000, reflecting five adjustments. Staff Init. Br., Appendix A, page 24. The Commission's determination of those five adjustments are set forth in the remainder of this Order.

The Commission, based on ComEd's original cost of plant in service as of December 31, 2009, before adjustments, of $13,932,447,000, and reflecting the Commission's determination of Staff's five proposed adjustments to that figure, unconditionally approves as $13,925,117,000 as the original cost of plant as of said date.

B. Potentially Uncontested Issues

1. Plant

a. AMI Pilot Costs (including AMI Meter Redeployment)

ComEd's rate base includes $51,888,000 (gross plant amount) for AMI Pilot costs. Marquez Dir., ComEd Ex. 10.0 at 18-19; McMahan Dir., ComEd Ex. 9.0 Rev., ComEd Ex. 9.1, Sched. F-4. Staff initially proposed a $1.6 million disallowance to reduce ComEd's regulatory asset for 51,203 meters that were allegedly placed back in service, but, in rebuttal testimony, accepted ComEd's explanation that the vast majority of the 51,203 meters were retired and will not be reused. Staff and ComEd have since agreed to the number of meters that were retired. This issue is no longer contested. The Commission approves the agreed-to amount of meters.

b. Other

ComEd agreed to AG/CUB's proposal to adjust ComEd's rate base to include a $5.27 million customer advance that has been determined to be related to a distribution

project. Houtsma Reb., ComEd Ex. 29.0 at 38. The Commission approves AG/CUB's proposal.

2. General and Intangible Plant

3. Functionalization

C. Potentially Contested Issues

1. Post-Test Year Adjustments

a. *Pro Forma* Capital Additions

ComEd seeks to include $1.017 billion in rate base. This consists of investment in plant from the end of the 2009 test year through June 30, 2011. (ComEd Initial Brief at 7). Staff seeks to exclude $373,979,000 (Staff Initial Brief, Appendix A, at 24). AG/CUB witness Mr. Effron recommended reducing General Plant by $16,710,000 and Intangible Plant by $16,097,000, to reflect general and intangible plant balances as of March 31, 2011. (AG/CUB Memo at 3; AG/CUB Ex. 2.0 at 4-5; Schedule DJE-1.1). ComEd does not object to the AG/CUB adjustment.

Staff's Position

Staff states that this Commission should approve only those investment in plant projects that are in service by December 31, 2010. Staff points out that ComEd filed a historical test year that ended on December 31, 2009. 83 Ill. Adm. Code 287.40, which is entitled "Pro Forma Adjustments to Historical Test Year Data," sets forth the criteria that apply to a general rate increase. It provides that, for historical test years, *pro forma* adjustments must be made for all of the *known and measurable* changes in the operating results of the test year. "Known" adjustments, Staff states, are defined therein as those that "occurred during the selected historical test year, or are reasonably certain to occur subsequent to the historical test year within 12 months after the filing date of the tariffs." (83 Ill. Adm. Code 287.40).

Staff witness Ms. Ebrey testified that an adjustment may be measurable, but not known, as is the case where a utility has budgeted a defined dollar amount for a project, but, the specific projects that are to be completed are subject to change, either in scope, or in timing, and therefore cannot be determined with reasonable certainty. She also opined that therefore, when a project is known to be necessary, but it has not been completed, the evidence must be evaluated as to whether this project meets the known and measurable criteria. (Staff Ex. 1.0 at 7) . Staff cites Part 287, which further provides that:

> Any proposed known and measurable adjustment to the test year shall be individually identified and supported in the direct testimony of the utility. Each adjustment shall be submitted according to the standard information requirement schedules prescribed in 83 Ill. Adm. Code 285. (Emphasis added)

(83 Ill. Adm. Code 287.40). Staff reasons that ComEd should not be able to receive the benefits derived from filing a future test year without providing all of the information that is required to support a future test year.

Staff asserts that while ComEd identified the adjustment for *pro forma* plant additions in direct testimony, the amount and specific projects included in the adjustment have been updated at least three times since them. (Staff Initial Brief at 5). Staff states that projects have been dropped and other projects have been added throughout the six months since the case was filed. During cross-examination, ComEd witness Donnelly agreed that there will continue to be changes to the amount of new plant placed in service through June 2011. (Staff Initial Brief at 6; Tr. 659-662). Staff states that the fact that some projects can (and will) be dropped while others are added based on ever-changing priorities proves that the totality of the *pro forma* plant additions that ComEd has proposed is not known and measurable. Staff contends that ComEd has not identified which of the projects included in ComEd Ex. 55.2 are subject to revision; therefore, Staff has no alternative but to assume that any of the projects may change. (Staff Initial Brief at 6; Tr. 765-766).

In comparing the information supporting vehicle purchases in ComEd Ex. 55.10 with the evidence provided in ComEd Ex. 32.2, Mr. Donnelly admitted that ComEd Ex. 32.2 only provided "a sample of documentation of various scopes of work." (Tr. January 11, 2011 at. 628). However, Staff argues, providing a sample of the types of documentation available to support its *pro forma* plant additions does not obviate ComEd's burden of proof. During cross-examination, Staff witness Ms. Ebrey explained her concern with the information provided in ComEd Ex. 32.2. ComEd Cross Exs. 5, 6, and 7 showed information pertaining to ITN 45170, but as Ms. Ebrey explained, the information that ComEd provided presented conflicting information, with no explanation for the conflicts. Thus, Staff concludes that this evidence could not be relied upon to support the project in question.

Staff further posits that, based on information obtained from ComEd in discovery, ComEd's Future Test Year revenue requirement is quite similar to its historical 2009 test year requirement. In fact, ComEd will be experiencing a declining Net Plant and Rate Base from 2009-2011. According to Staff, ComEd Ex. 6.3 indicates that, while ComEd's Gross Plant is projected to increase by $214 million, its Net Plant is projected to decrease by $440 million, which is more than double the amount of the projected increase to Gross Plant. (Staff Ex. 16.0 at 22; ComEd. Ex. 6.3). Staff asserts that, in the past, this Commission has concluded that such mismatched *pro forma* capital additions would result in a mismatch of costs and revenues that may be expected for the period, during which, rates are in place. In the past, the Commission thus concluded that a reduction of the utility's post-test year capital additions and reduced depreciation was necessary. (*See,* Staff Ex. 16.0 at 22-23; Docket No. 02-0798, Order of October 22, 2003, at 10).

Ms. Ebrey stated that evidence that many of ComEd's 2011 planned projects are not known and measurable can be gleaned from the fact that during the course of this proceeding alone, ComEd has made many substantial changes to *pro forma* plant. Some of those changes have been from a 56.78% decrease to a 162.91% increase. (Staff. Ex. 16.0 at 8-11). She concluded that ComEd witness Mr. Donnelly's testimony

regarding the methodology used to support the certainty of ComEd's *pro forma* plant adjustments is the type of support that is typically seen in a rate case with a future test year. In her opinion, Mr. Donnelly did not address the known and measurable standard that is applicable to a historical test year. (*Id.* at 12-13).

Based on discovery responses provided by ComEd, Ms. Ebrey opined that for many programs extending beyond December 31, 2009, that were set forth in ComEd's rebuttal testimony, ComEd evinced that the projects anticipated to go into service have not received final approval. For other projects, ComEd did provide evidence supporting that these projects will be in service by June of 2011, which, she opined, is short of ComEd's "reasonable certainty" blanket statement for these projects. Still other projects were described as "core parts of the work we do every month" projects. She further stated that ComEd admitted that the "exact list of projects may change as we prioritize our work throughout the year." Staff contends that additionally, ComEd's direct support of "blanket" projects was based on "historical data and trends." (Staff Ex. 16.0 at 16-17; Com Ed Ex 32.0 at 56-68).

Staff further points out that, at the time when its rebuttal testimony was filed, Staff's recommended revenue requirement included amounts projected to be in service by December 31, 2010, as well as certain other discrete projects through June 2011 that Staff originally concluded were known and measurable. However, ComEd provided an update to its *pro forma* plant amounts in surrebuttal testimony. (*See,* ComEd Ex. 55.2, Workpaper WPB-2.1a, which revised the amounts for plant actually in service through November 2010 along with projections for December 2010 and the first and second quarters of 2011).

According to Staff, while Staff based its rebuttal position on the evidence available at the time of its rebuttal testimony, the updated plant support provided in ComEd's surrebuttal testimony calls into question whether even the discrete projects that Staff accepted in rebuttal testimony are indeed known and measurable. Of the limited projects deemed to be "Summer Critical" which Staff previously accepted, five have now been dropped from the *pro forma* schedule. In addition, the timing of various projects being placed in service has either slipped to a later date or has been expedited to an earlier period. Also, the total amount for the discrete projects being placed in service in 2011 accepted in Staff's rebuttal has changed from $46.995 million to $57.3 million, without any explanation. Staff states that it cannot recommend that the Commission violate its own rules by approving this "moving target," and is therefore recommending approval of plant to be placed in service through December 31, 2010. (Staff Initial Brief at 8-9).

Staff states that while ComEd asserts that it supplied Staff with ample documentation, most of the documents that ComEd furnished were for work that was completed before the end of 2010, which, Staff had already allowed in its adjustment. And, for most of the ITNs included in this exhibit (Confidential Staff Group Cross Ex. 1, Company response to TEE 14.03) nothing was provided to support the 2011 projects. (Staff Reply Brief at 5-6). Staff further states that ComEd witness Mr. Donnelly admitted during cross-examination that the actual projects that will be placed in service during January through June of 2011 will change from what was projected. (Tr. 659-662). He

also allegedly conceded that those projections decreased by $13 million between the time when ComEd's rebuttal testimony was filed (November 22, 2010) and the time when ComEd filed its surrebuttal testimony, on January 4, 2011, just six weeks later. (Staff Reply Brief at 6-7).

However, Staff witness Ms. Ebrey disagreed with AG/CUB witness Mr. Effron's proposal to allow *pro forma* plant additions through March 31, 2011, which is three months before the time when rates will actually go into effect. She averred that Mr. Effron is mistaken when stating that in ComEd's last rate case, docket 07-0566, the Commission allowed for a true-up of ComEd's forecasts to actual costs as of that date. She also opined that this proposal overlooks previous Commission decisions and test year rules. (Staff Ex. 16.0 at 18-21; Staff Reply Brief at 7).

ComEd's Position

ComEd witness Mr. Donnelly testified that ComEd will place $461.5 million of additional plant investments into service from December 1, 2010 through June 30, 2011. He opined that, when combined with the $555.8 million of plant that is already placed into service through November 30, 2010, *pro forma* plant additions totaling $1.017 billion are properly included in ComEd's rate base. (ComEd Ex. 58.0 at 67-68). He further stated that $461.5 million of additional plant to be placed in service from December 1, 2010 through June 30, 2011 is supported by a detailed, "bottom-up" analysis of the work to be done. Both unique investment projects and work managed through "blanket" investment project designations were analyzed for status, investment, and "in service" dates. Engineering and operating needs were assessed, and the individual projects and blankets were analyzed to determine the required level of activity by the responsible managers and category owners and their teams. (ComEd Exs. 32.0, at 15; 58.0 at 16-17).

ComEd witness Mr. Donohue averred that the process that ComEd used to determine the $461.5 million plant investment amount has proven to be reliable. It has been subject to review not only by ComEd, but also by independent experts who have 75 years of combined experience in managing electric utilities and in making the very types of investments ComEd included in its *pro forma* adjustment. (ComEd Ex. 59.0 at 2-3). A virtually identical process was used in ComEd's 2007 Rate Case in which *pro forma* plant additions were approved, and, according to ComEd, the Commission found no fault with ComEd's methodology. (ComEd Ex. 32.0 at 16; ComEd Initial Brief at 12).

ComEd witness Mr. Donnelly averred that the "data" supporting ComEd's work and work-plans for the plant additions has been available to all parties for months. None of the witnesses who propose disallowing *pro forma* adjustments dispute the validity of the "data" on which they are based. (ComEd Exs. 32.0 at 17; 58.0 at 11; 17-18). The documentation and evidence supporting ComEd's *pro forma* plant additions is included in electronic form in ComEd Ex. 32.2, which contains approximately 2.3 gigabytes of material with over 52,000 pages in 10,423 files and 1,064 folders. ComEd avers that *pro forma* plant additions were approved for the Ameren Illinois utilities in Docket No. 09-0306, based on summary spreadsheet documentation, similar to that provided in ComEd Ex. 8.2 and ComEd Ex. 32.1. ComEd asserts that the

documentation provided in ComEd Ex. 32.2 exceeds that documentation significantly in both scope and detail. (ComEd Ex. 32.0 at 18; ComEd Initial Brief at 10-11, 18).

Mr. Donnelly also testified that, where changes are made to project plans, they occur because specific changes affecting ComEd's system have altered investment priorities, and ComEd has responded by investing in the work that has a higher priority. According to Mr. Donnelly, changes in work orders are driven by need. In many cases, this is driven by ComEd's customers, or government entities. ComEd contends that the fact that it adapts, and changes its work orders, as needed, does not indicate that there is any flaw in the work scheduling process. It also, in his opinion, does not indicate any uncertainty in the overall work schedule. (ComEd. Ex. 32.0 at 19-20).

For unique projects in excess of $500,000, Mr. Donnelly explained the project specifically, why it was necessary, the equipment to be installed, the cost involved, and when it was expected to be placed in service. (ComEd Ex. 58.0 Rev. at 33- 36). For the blanket programs, ComEd provided comprehensive documentation explaining the repetitive nature of this work, why it is necessary, how costs are derived, approved and managed, and how much ComEd has spent in recent years. This information was provided in the form of reports prepared by an outside engineering expert, PDR&C. (ComEd Ex. 59.0 at 5-6, 9-10). Regarding outside Chicago New Connections, during the periods January 1, 2009 through June 30, 2009 and January 1, 2010 through June 30, 2010, ComEd connected 5,998 and 4,950 new customers, respectively. ComEd plans to install 5,286 services under this program by June 30, 2011. (ComEd Ex. 58.0 Rev. at 33). With respect to inside Chicago New Connections, during the periods January 1, 2009 through June 30, 2009 and January 1, 2010 through June 30, 2010, ComEd connected 2,734 and 2,332 new customers, respectively, and, it plans to install 2,375 new services between January and June 2011. (ComEd Ex. 58.0 Rev. at 33; ComEd Initial Brief at 13-14). ComEd further asserts that work planned to meet its legal obligations to connect new customers is, by definition, known and reasonably certain to occur as planned. ComEd argues that it can not be simultaneously obligated to perform new business work but unable to recover the costs for that work. (ComEd Initial Brief at 21).

ComEd states that the most significant work that it plans for in the corrective maintenance category are cable faults and overhead defect repairs. This work is managed through four blanket projects: 1) Emergency Cable Fault Replacements (ITN no. 20543); Emergency Cable Fault Repairs (ITN no. 10623); 3) Overhead Distribution Defect Repairs (ITN 10622); and 4) Storm Restoration (ITN no. 10628). (ComEd Exs. 32.0 Rev. at 34-37; 58.0 Rev. at 28–29; ComEd Initial Brief at 14-15).

ComEd argues that Staff's position is based on an incorrect and unreasonable reading of the *pro forma* rule. It acknowledges that the *pro forma* rule does state that "[a]ny proposed known and measurable <u>adjustment</u> to the test year shall be individually identified and supported in the direct testimony of the utility," citing 83 Ill. Admin. Code 287.40 (emphasis added). ComEd maintains that contrary to Staff's position that individual projects must be identified and supported, the rule limits this obligation to the proposed *pro forma* "adjustment" but not every single one of its component parts or projects. It states that Staff's recommendation to accept all planned *pro forma* investments for November and December of 2010, including investments for emergent

work under blanket programs, does not raise this concern or apply this standard. The "data" and information that supports investments based on emergent work for the first and second quarters of 2011 is not distinguishable from the "data" and information that supports such investments for November and December of 2010. ComEd further asserts that the Commission's rules specifically provide that the "standard information requirements do not bind the Commission to a decision based solely on data provided pursuant to this Part" citing 83 Ill. Admin. Code 285.110(b). (ComEd Initial Brief at 16-17).

According to ComEd, Staff's assertion that emergent work is unexpected, and therefore cannot be known, is contrary to the record. ComEd's witness Mr. Donohue explained "emergent" work as follows:

> The need for some of the relatively small, short duration jobs may be identified on the day in which the addition is placed into service or during the preceding few days. That type of work can be reasonably planned. It is work such as repairing or replacing damaged or failed underground or overhead equipment that is needed to restore reliable electric service to customers.
>
> The quantity of emergent work can be reasonably planned while the exact location may not be known in advance. The quantity of that work is driven by the needs of the electric distribution system size, design, age, exposure, and other factors that do not materially change year to year. With the aid of trend analyses and reviews of internal and external factors that may affect those trends, ComEd is able to plan for this small and short duration type of work and costs with reasonable certainty. Of course, particularly in categories where the work is comprised of hundreds of small jobs and dominated by emergent tasks or tasks driven by relatively immediate events or customers' requests, the specific work cannot be completely identified.
>
> ComEd cannot predict exactly where or when a storm will strike or when a particular transformer or cable will fail. But, it is routine and required for prudent management of the distribution infrastructure to plan for such work. ComEd also has a service obligation to plan resources for that work. ComEd knows with a high degree of certainty that emergent work will occur, and can plan for both the scope and costs of that work with reasonable certainty.
>
> (ComEd Ex. 35.0 Rev. at 17-18).

The AG's Position

AG/CUB witness Mr. Effron proposed eliminating all plant additions after March 31, 2011 because, in his opinion, those additions cannot reasonably be characterized as known and measurable with any reasonable degree of certainty. (AG/CUB Exs. 2.0 at 4-8; 8.0 at 1-5). In the AG's opinion, ComEd's proposal to calculate rates in a manner that includes recovery for plant additions through June 30, 2011 does not comport with the Commission's rule on *pro forma* adjustments. The applicable

regulation, the AG continues, (83 Ill. Adm. Code 287.40) requires that such adjustments reflect "known and measurable" forecasts, and not mere expectations of capital investment. Yet, the AG states, ComEd's plant additions proposal includes budgeted numbers which are not only not "known and measurable," but which, as Staff witness Ms. Ebrey states, were not produced in time to be properly reviewed in this proceeding. (AG Initial Brief at 8).

The AG argues that the Commission has explicitly recognized its duty under Section 9-211 of the Public Utilities Act to ensure that a utility's approved rate base does not exceed the value of the assets that the utility actually uses to provide service, citing *AmerenCILCO, et al., Proposed general Increase in electric delivery service rates docket* No. 09-0306, Order of April 29, 2010, at 31. It concludes that therefore, the Commission should not rely upon budget projections for plant additions which have not been verified as realistic. To do so, it opines, risks overstating rate base by permitting recovery of investment in utility plant that may never be used to serve customers because it was never actually made. (AG Initial Brief at 9).

In contrast, the AG continues, its witness Mr. Effron's proposal to include in rate base only those plant additions, for which, what the AG contends is actual figures is consistent with the "known and measurable" standard of Part 287.40. It is also, according to the AG, identical with the method adopted by the Commission in ComEd's last rate case. AG/CUB witness Mr. Effron recommended that ComEd's rate base exclude any plant additions occurring subsequent to March 31, 2011, not because he believes that no growth in plant will take place after that date, but because "…the extent to which plant additions will exceed concomitant growth in the depreciation reserve and ADIT in the second quarter of 2011 cannot reasonably be characterized as known and measurable with any reasonable degree of certainty." (AG/CUB Ex. 8.0 at 2; AG Initial Brief at 9).

The AG avers that Staff witness Ms. Ebrey expressed similar concerns that ComEd's budgeted numbers were problematic, in terms of providing reliable information upon which, to make an accurate determination of utility plant-in-service. She noted on cross-examination that not only had she not had the opportunity to review ComEd's latest budget for plant additions for December 2010, she also noted that ComEd's budget forecast information "keeps changing" and that its updated forecast on surrebuttal was "something over $9 million" lower than its rebuttal budget forecast. (Tr. 730-31).

It argues that its witness Mr. Effron's proposal to use actual plant-in-service figures to the extent possible in calculating rates is not an unorthodox approach, at least not as far as the Commission is concerned. Staff witness Ms. Ebrey allegedly acknowledged the Commission's decision in the company's last rate case (docket 07-0566) to require ComEd to report the latest actual plant-in-service amounts for the purposes of calculating rates as a "true-up" of budget projections. In that case, ComEd was required to adjust its reported plant-in-service before the Commission's decision to reflect the difference between ComEd's projected *pro forma* capital additions ending on June 30, 2008 and the actual plant in service as of that same date. (Tr. 737-38; AG Cross Ex. 6 and AG Cross Ex. 7 at 3).

The AG states that the Commission then relied on these actual plant-in-service amounts to determine rates. (AG Initial Brief at 9). It asserts that the Commission should rely upon the same methodology here as it did in ComEd's 2007 rate case, when determining the amount of *pro forma* plant additions to be included in the company's jurisdictional plant-in-service. The AG contends that ComEd should be required to provide a late-filed exhibit which supplies the Commission with a true-up representing the difference between its budgeted amounts for capital additions as of March 30, 2011 and its actual plant-in-service as of that date. (AG Initial Brief at 9-10).

In its Reply Brief, the AG states that ComEd's assertion that AG/CUB supports the inclusion of the first 12 months of these *pro forma* capital additions as an adjustment to its test year rate base is untrue and contradicted by record evidence. The AG states that although ComEd's Initial Brief alleges that AG/CUB "accepts every dollar of investment that ComEd projected to place in service through December 31, 2010," the evidence does not indicate any such support. In fact, AG/CUB explicitly challenged ComEd's *pro forma* capital additions for December 2010 as disproportionately large compared to its average monthly capital additions for the previous 11 months of the test year. ComEd's forecast of plant additions of $100.8 million for December 2010 is nearly twice the level of actual monthly plant additions for the first eleven months of 2010. (AG Reply Brief at 5).

The AG avers that, as was pointed out in both AG and Staff Initial Briefs, ComEd's forecasts of plant additions have not been reliable. Staff witness Ms. Ebrey observed that the Company's forecast of $100.8 million of plant additions in December 2010 as "probably not reasonable." (Tr. 730-31). The AG concludes that whether the adjustment for *pro forma* plant additions is cut off as December 31, 2010 (as proposed by Staff) or as of March 31, 2011 (as proposed by the Attorney General), ComEd's forecast of plant additions must be trued up to the actual balance of plant additions. (AG Initial Brief at 5-6).

The AG also maintains that ComEd has mischaracterizes the AG's testimony on this issue. According to ComEd, Mr. Effron argues that the forecast of plant additions planned for the second quarter cannot be characterized as "known" and "measurable" with any reasonable degree of certainty. What Mr. Effron actually argued is that "the extent to which plant additions will exceed concomitant growth in the depreciation reserve and ADIT in the second quarter of quarter of 2011 cannot reasonably be characterized as known and measurable with any reasonable degree of certainty." In support, the AG cites AG/CUB Ex. 8.0 at 2. (AG Initial Brief at 6).

CUB's Position

CUB contends that ComEd'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. CUB agrees with Staff witness Ebrey's opinion that ComEd's forecasts through June 2011 have changed significantly through the course of this case. CUB states that changes of the magnitude described by Ms. Ebrey have previously resulted in disallowance by the Commission, and signify that the expenses, for which, ComEd seeks recovery are not known and measurable at this time. AG/CUB witness Mr. Effron proposes to eliminate

all plant additions after March 31, 2011, and then true them up to match actual expenditures through that date before the final order in this case. CUB notes that no party in the case suggests that ComEd will not make expenditures between March 31 and June 30; however, CUB continues, it 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 its forecast. Also, ComEd reduced its 2010 forecasted plant additions by $52 million from direct to rebuttal testimony in this case. (AG/CUB Ex. 2.0 at 4-5; 10-11; CUB Initial Brief at 9-10).

CUB states that additionally, ComEd'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. 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, CUB opines, in light of the ComEd's actual vs. forecasted spending in its last case, as well as its decreased forecast in this case. CUB argues that 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 are relied upon. CUB asserts that, to remove ComEd'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. (CUB Initial Brief at 10).

Analysis and Conclusions

The Public Utilities Act requires the Commission to establish just and reasonable rates. (220 ILCS 5/9-101). A utility's rate base may include only the value of such investment which is both prudently-incurred and used and useful. (220 ILCS 5/9-211). Part 287 defines the test year options available to a utility. In this vein, this Commission must determine that the cost of a new plant, or, additions to an existing plant are reasonable. (*Business and Professional People v. Ill. Commerce Comm. ("BPI II"),* 146 Ill. 2d 175, 196, 585 N.E.2d 1032 ((1991)).

A utility may propose a future test year, which is: "Any consecutive 12-month period of forecasted data beginning no earlier than the date new tariffs are filed and ending no later than 24 months after tariffs are filed." (83 Ill. Adm. Code 287.20(b)). A historical test year, on the other hand, is "Any consecutive 12 month period, beginning no more than 24 months prior to the date of the utility's filing, for which actual data are available at the time of filing new tariffs. (83 Ill. Adm. Code 287.20(a)). The purpose of the test-year rule is to prevent a utility from overstating its revenue requirement by mismatching evidence of low revenue with high expenses from a different year. (*BPI II,* 146 Ill. 2d at 238).

Here, ComEd chose an historical test year. The Commission's regulations regarding historic test years provide that:

> A utility may propose pro forma adjustments (estimated or calculated adjustments made in the same context and format in which the affected information was provided) to the selected historical test year for all known

> and measurable changes in the operating results of the test year. These adjustments shall reflect changes affecting the ratepayers in plant investment, operating revenues, expenses, and cost of capital where such changes occurred during the selected historical test year or are reasonably certain to occur subsequent to the historical test year within 12 months after the filing date of the tariffs and where the amounts of the changes are determinable. Attrition or inflation factors shall not be substituted for a specific study of individual capital, revenue, and expense components. *Any proposed known and measurable adjustment to the test year shall be individually identified and supported in the direct testimony of the utility. Each adjustment shall be submitted according to the standard information requirement schedules prescribed in 83 Ill. Adm. Code 285.*
>
> (83. Ill. Adm. Code 287.40; emphasis added).

In construing this regulation, we are bound by its plain meaning. (*Commonwealth Edison Co. v. Ill. Commerce Comm.,* 398 Ill. App. 3d 510, 535, 944 N.E.2d 1065 (2nd Dist. 2009)). This regulation requires that any proposed known and measurable adjustment to the test year must be individually identified, and, also supported, on an evidentiary basis, in a utility's direct testimony. This language clearly means that a utility, which has the burden of proof, must provide specific evidence, in its direct testimony, supporting its *pro forma* capital adjustments. General statements as to what these adjustments are, as a matter of law, cannot satisfy this requirement. This is true because the language requiring individual identification of a *pro forma* capital adjustments and the factual support for those projects would be rendered meaningless, if a utility could merely, in a historical test year, state generally what these adjustments are.

We further disagree with ComEd's definition of the word "adjustment" in the regulation to solely mean "change." *Pro forma* capital adjustments are actual expenditures, or expenditures to be made. They are not just changes to capital projects.

Additionally, we note that ComEd's construction of this regulation would render the differentiation between historical test years and future test years in the pertinent regulations to be meaningless. While the regulatory evidentiary burdens between historical and future test years differ, we note that ComEd chose to proceed here with a historical test year. Therefore, ComEd, like any other utility, must adhere to the laws regarding historical test year requirements.

We note that the record indicates ComEd failed to establish, in its direct testimony, specific plans for many of its post-test year *pro forma* plant additions. It also failed to "cure" this defect in its evidentiary proof requirement (we make no determination herein as to whether this initial evidentiary burden required by 83 Ill. Adm. Code 287.40 *can* be cured) with its subsequent filings. This fact is abundantly clear from Staff's, and the AG CUB testimony, arguments and cross-examination. We also note that ComEd has not provided any facts, in its arguments or testimony, indicating that Staff's averments in this regard are not correct.

ComEd, in fact, merely argues, generally, that its ever-changing list of projects and expenses for these projects, satisfies the historical test year rules. ComEd has failed to meet its legal requirement, and, it has proffered not legal reason for its failure to do so. Specifically, ComEd has failed to proffer any reason indicating that the language in the regulation regarding historical test year rules do no apply here. In so ruling, we again note that the choice of a historic test year was solely the choice of ComEd.

ComEd is also incorrect in stating that in Ameren's last rate case, docket 09-0306, the evidence that Ameren used to substantiate its *pro forma* capital additions was merely a "summary spreadsheet." In that case, in fact, the spreadsheet was one bit of evidence, amongst many other pieces of evidence. Also, in that case, Staff proposed a similar cut-off to the one it proposes here and Ameren agreed to that cut-off date. (See, e.g., docket 09-0306, Ameren Ex. 43.0, Staff Ex. 16.0 at 3-4).

We additionally note that ComEd's evidence only bolster the positions of Staff and others that many of ComEd's *pro forma* plant additions are not known and measurable. For example, Mr. Donnelly testified that, where changes are made to project plans, they occur because specific changes affecting ComEd's system have altered investment priorities, and ComEd has responded by investing in the work that is of a higher-priority. According to Mr. Donnelly, changes in work orders are driven by need. (ComEd. Ex. 32.0 at 19-20). This testimony establishes that ComEd plans for system upgrades and other items, but, reaction to weather conditions, new customers, and other unforeseen events requires ComEd to re-evaluate the priority of, and re-determine the cost of, the post-test year projects at issue. These projects may be known, but they are not measurable. This is true because, if a project can be re-prioritized, or if its cost estimate seriously "misses the mark" it cannot be said to be measurable.

However, after a thorough evaluation of the evidence that ComEd did present, certain "New Business" projects are reasonably likely to be in place before June 30, 2011. They are:

Finkl Steel (ITN # 22782)	$13,068,408
O'Hare Runway (ITN # 13507)	$ 1,008,615
2520 N. Lakeview (ITN No. 34054)	$ 866,756
Silver Cross Hospital (ITN # 41817)	$ 3,470,721
Anderson Schumaker (ITN # 43696)	$ 953,074
Inside Chicago Baseline (ITN # 5968)	$11,444,947
Outside Chicago Baseline (ITN # 5972)	$30,428,649
CE Transformers (ITN # 24143)	$ 5,610,100
Total:	$66,851,270

(*See,* Staff Initial Brief, Appendix B; ComEd Ex. 32.2 2nd Cor. Confidential).

After a review of the evidence regarding the projects listed above, we conclude that work planned to meet ComEd's obligations to new customers is likely to be

completed within the time period prescribed by the regulation. The projects above are "known and measurable," albeit with imperfect evidence. Therefore we conclude that Staff's proposed adjustment is adopted, with an adjustment upward of $66,851,270 to reflect the addition of the projects above.

The AG/CUB Proposal

We decline to adopt AG/CUB witness Mr. Effron's proposal. Merely filing a "late-filed" exhibit as some sort of "true-up" does not satisfy the rules of evidence, or the test year rule previously cited herein. There is also no assurance of accuracy or completeness.

While we agree with Staff that no true-up of ComEd's *pro forma* plant additions occurred in ComEd's last rate case, we caution all of the parties to state matters in legal terms. It is unclear what Mr. Effron really meant when using the term "true-up. To a lawyer, a true-up means presenting evidence that satisfies the legal burden of proof, such as, in the case of what is required in establishing the amount of a default judgment. This may not mean the same thing to Mr. Effron, who is not a lawyer. In any case, merely filing a late-filed exhibit does not "true-up" with actual facts.

We also would be reluctant to encourage utilities to satisfy their burden of proof after trial, especially in a rate case, with an 11-month deadline. There is no point in having an evidentiary hearing, if a party can merely late-file a document that can be highly-controverted, without that document being subject to discovery and cross-examination. Such a position runs counter to basic principles of due process.

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

Staff's Position

Staff proposed adjustments to "roll forward" Accumulated Depreciation on Embedded Plant as of December 31, 2009 to correspond to the date, to which, gross plant in service has been restated. This is necessary, Staff states, in order to reflect the correct value of plant investment. With regard to ADIT, (Accumulated Deferred Income Taxes) Staff proposes the companion adjustment to ADIT reflect the adjustment to Accumulated Depreciation on Embedded Plant as of December 31, 2009. (Staff Exs. 1.0 at 10-15; 16.0 at 21-25; Staff Memo at 1). Staff states that recognizing increases in rate base, without recognizing the contemporaneous offsetting decreases in the value of existing investment, overstates ComEd's rate base. In other words, allowing ComEd to raise rates based on anticipated new plant, but not giving ratepayers the benefit of decreasing rate base on existing plant due to depreciation of existing plant for that same period of time, results in an overstatement of rate base, and an overstatement of rates. (Staff. Ex. 1.0 at 10-11).

Staff also cites the recent appellate decision regarding ComEd's last rate case, in which, the Appellate Court stated that:

> We conclude that the Commission miscalculated the value of the plant investment by recognizing increases in rate base investment value due to post-test-year additions without recognizing contemporaneous offsetting

> decreases in the value of that investment attributable to ongoing depreciation. Section 9-211 (of the Public Utilities Act) essentially requires the Commission to ensure that a utility's approved rate base does not exceed the investment value that the utility actually uses to provide service. The measure of the amount of investment so dedicated must account for both increases and the decreases over a consistent period. Under section 9-211, contemporaneous increases and decreases to rate base are not severable items that can be given disparate treatments. The utility's plant in service, and net plant are opposing sides of the coin. The Commission approved a rate base that exceeds the investment value ComEd actually dedicates to utility services. The approval of excess rate base violates section 9-211 by overstating ComEd's revenue requirement.

(*Commonwealth Edison Co. v. Illinois Commerce Comm.* 405 Ill App. 3d 389, 937 N.E.2d 685, 701-03 (2nd Dist. 2010)).

Staff opines that a proposed adjustment to the accumulated depreciation reserve should be evaluated in light of the facts and circumstances in each individual case. A determination must be made regarding whether a particular proposal will overstate rate base. (Staff Ex. 1.0 at 14). Staff further avers that, when considering *pro forma* plant additions, the Commission should consider the extent, to which, the post-test year additions are effectively "rolling forward" the gross plant balance and the corresponding *pro forma* adjustments that are required to balance the regulatory lag with the matching principle.

Staff witness Ms. Ebrey averred that, because she is accepting all of the plant additions placed into service as of December 31, 2010, the comparison adjustments to accumulated depreciation and ADIT should therefore be reflected here. She stated that, if the Commission does not adopt her limitation on *pro forma* plant additions, the Accumulated Depreciation and associated ADIT should be adjusted to reflect whatever date is used to measure *pro forma* plant additions in order to achieve a correct valuation of net plant. (Staff Ex. 16.0 at 23-25; Staff Initial Brief at 10-11).

ComEd's Position

ComEd witness Ms. Houtsma testified that, on September 30, 2010, the Illinois Appellate Court issued an opinion in the appeal of ComEd's 2007 rate case, docket 07-0566, that addresses this issue. ComEd filed a petition seeking leave to appeal (the "PLA") to the Illinois Supreme Court of the Appellate Court's ruling. ComEd stated that the mandate of the Appellate Court has not yet issued, and it will not issue, until the PLA is acted upon by the Illinois Supreme Court. (ComEd Initial Brief at 24). Ms. Houtsma also stated that, given the status of the appeal and the factors discussed in her direct and rebuttal testimony, she believes that the approach applied in the direct case, which is contrary to what the appellate court ruled, is appropriate. Thus, she opined that a *pro forma* adjustment to roll forward the Depreciation Reserve is not warranted. (ComEd Ex. 6.0 at 10-15). ComEd urges this Commission to follow what was done in its last rate case, ICC Docket No. 07-0566, the propriety of which, was reversed by the Appellate Court. (ComEd Initial Brief at 23-24).

The Commercial Group's Position

The Commercial Group contends that the Illinois Appellate Court held, on appeal of ComEd's 2007 rate case that "[t]he utility's plant in service and net plant are opposing sides of a coin" and it is reversible error for the Commission to "recogniz[e] increases in rate base investment value due to post-test-year additions without recognizing contemporaneous offsetting decreases in the value of that investment attributable to ongoing depreciation." The Commercial Group proffers that the proper match of costs and revenues in a rate year is a bedrock principle of utility law. Also, the Commission came to a similar conclusion in a recent Ameren rate case order. *Ameren CILCO et al.*, Docket No. 09-0306. April 29, 2010 Order at 30-31; *affirmed on rehearing* (November 4, 2010).

The Commercial Group states that, notwithstanding the Appellate Court decision and the Ameren rate case, ComEd proposes to increase the value of its rate base on one side of the coin by over $1 billion through post-test year additions, without offsetting such amounts on the other side of the coin with the corresponding decrease in value of its rate base (during the same period) from accumulated depreciation and amortization. The Commercial Group supports the adjustments of Staff, AG/CUB and IIEC, as they have been updated throughout this proceeding. (Commercial Group Initial Brief at 2-3).

The IIEC's Position

The IIEC states that in accordance with the Commission's most recent decisions on this issue, and the Illinois Appellate Court decision, a correction must be made to any adjustment for post-test year changes in test year plant investment to recognize the build-up of accumulated depreciation reserve over the same time period of the time period for any Commission-approved approved plant additions. It cites *AmerenCILCO, d*ocket 09-0306, Order of April 29, 2010, at 30-31, and the Order on Rehearing in that case, which issued on November 4, 2010. The IIEC additionally cites the recent Appellate Court opinion on this issue, which concerned ComEd's last rate case, *Commonwealth Edison Co v. Illinois Commerce Comm.,* 405 Ill App. 3d 389, 937 N.E.2d 685, 701-703 (2nd Dist. 2010). Based on the period of the planned plant additions that were included in ComEd's proposed post-test year adjustment, IIEC witness Mr. Gorman recommended a $582.7 million correction to ComEd's proposed adjustment for plant additions over a period of 18 months. (IIEC Ex. 1.0 at 71-73).

IIEC witness Mr. Gorman opined that ComEd 's proposal to include in rate base anticipated plant additions over a period of 18 months after the historical test year results in a mismatch of the historical test year gross plant, and the historical test year balance of accumulated depreciation reserve that has not been similarly augmented. The result, he continued, is a complete distortion of the impact on historical test year net plant in service by the post-test year plant additions adjustment. In effect, this is a rate base that reflects gross plant balance 18 months after the end of the test year, but reflects an accumulated depreciation reserve balance at the end of the test year, which was adjusted only minimally for some plant additions. (IIEC Ex. 1.0 at 69-70).

He further testified that the build-up in accumulated depreciation reserve for the 18-month post-test year period that is defined by ComEd's plant additions will result in an increase in the accumulated depreciation reserve of $582.7 million, and also a buildup of accumulated deferred income taxes of $49.7 million. (*Id.* at 71-72).

With regard to Accumulated Deferred Income Taxes, (ADIT) the IIEC maintains that the Commission has recognized that adjustments to include post-test year increases to the test year rate base require recognition of contemporaneous post-test year decreases to the rate base, citing *AmerenCILCO,* docket 09-0306, Order on Rehearing, November 4, 2010 at 49). In this respect, the IIEC contends that the post-test year change in Accumulated Deferred Income Taxes ("ADIT") is a companion to the offsetting adjustment for accumulated depreciation. The IIEC recommends a corresponding offsetting correction to ComEd's proposed post-test year plant investment adjustment of $49.7 million for ADIT. (IIEC Ex. 1.0 at 71-73). The combined effect of these offsets reduces ComEd's proposed revenue requirement by $70.9 million, if an 18-month period for *pro forma* capital investments is approved herein. (IIEC Exs. 1.20; 1.0; 4.0).

The IIEC also asserts that ComEd's petition for leave to appeal to the Illinois Supreme Court does not delay or diminish the effectiveness of the Appellate Court decision, which became effective when it was entered on September 30, 2010, citing *PSL Realty Co. v. Granite Investment Co.*, 86 Ill. 2d 291, 304-305 (1981); *Long v. City of New Boston*, 91 Ill. 2d 456, 462 (1982). It avers that ComEd's reliance on a prior Commission decision that was reversed provides no basis for any lawful Commission action.

The IIEC further contends that ComEd has relied upon distorted calculations and inapt comparisons prepared by ComEd witness Ms. Houtsma as its evidentiary support for several immaterial contentions. ComEd argues that Ms. Houtsma's calculations show that despite having its rates set using the adjustment that was declared unlawful by the Appellate Court, ComEd did not earn more than its authorized return on equity, suggesting that the Commission can accept the same adjustment here. (IIEC Reply Brief at 3-5).

The AG's Position

The AG maintains that ComEd has asked the Commission to abandon its own rules. Correct application of the test year rules, the AG continues, has now been endorsed by the Illinois Appellate Court. It states that ComEd's final rate base amount of $7,349,227,000 does not reflect an accounting for the accumulated depreciation on existing plant. (AG Initial Brief at 11).

The AG states that this Commission believes that accounting for all accumulated depreciation on existing plant is not a discretionary act; it is a statutory requirement. This is done, the AG continues, to account for all changes to utility plant in determining rates, as the Commission's decision in the Ameren rate case docket states:

> Section 9-211 essentially requires the Commission to ensure that a utility's approved rate base does not exceed the investment value the utility actually uses to provide service. The measure of the amount of

> investment so dedicated must account for both increases and decreases (over a consistent period) at any point in time. Under Section 9-211, contemporaneous increases and decreases to rate base are not severable items that can be given disparate treatments. They are opposing sides of a coin, the utility's plant in service and net plant. . ..
>
> However, a reading of the rule which excludes accumulated depreciation for the pro forma period incents the utility to always seek upward pro forma adjustments regardless of any decline in actual net plant—and for an amount that ignores accompanying depreciation accumulating over the same period. This interpretation results in consistently and unavoidably inflated rate base and an inescapably inaccurate picture of the utility's finances. This reading is also plainly inconsistent with the Commission's treatment of plant investment should the utility adopt a future test year under Section 287.20(b), plainly inconsistent with basic matching principles, and inconsistent with the approach taken in at least six other states.
>
> To avoid confusion respecting proposals in future rate cases, the Commission finds that if a utility has recovered in rates the cost of an asset through depreciation expense, the associated amount of accumulated depreciation should be deducted from rate base.

(See, AmerenCILCO, docket 09-0306, Final Order at 31; AG Initial Brief at 11-12). Upon rehearing of the depreciation issue at Ameren's request in the same case, the Commission pointed out that its treatment of the issue, as well as its interpretation of the statute and rules, was consistent with that of the Appellate Court in its recent decision on the appeal of the Commission's order in docket No. 07-0566, which is, *Commonwealth Edison Co. v. Illinois Commerce Comm.,* 405 Ill. App. 3d 389, 937 N.E.2d 685 701-703 (2d Dist. 2010). (*See, AmerenCILCO,* docket 09-0306, Order on Rehearing, November 4, 2010, at 27). The AG concludes that the appropriate adjustment to rate base to properly determine net plant-in-service is $490,108,000, based upon the AG's proposed March 31, 2011, cut-off date for *pro forma* capital additions. (AG Initial Brief at 13).

With regard to ADIT, the AG states that in the same way as it "insists" on accounting only for depreciation associated with post-test year plant additions when calculating its depreciation on plant-in-service, ComEd only recognized the incremental accumulated deferred income taxes ("ADIT") associated with those same plant additions. According to the AG, ComEd did not acknowledge the source of funds that will be provided by the growth in ADIT related to plant-in-service as of December 31, 2009. According to the AG/CUB witness Mr. Effron, as ComEd continues to record tax depreciation in excess of book depreciation on plant in service, that excess depreciation will reduce income taxes currently payable, thereby providing ComEd with cash to finance its post-test year additions to plant. The AG concludes that not acknowledging that a portion of post-test year plant additions will be financed with customer-supplied, zero-cost capital supplied through the growth in ADIT is inconsistent with the inclusion of those post-test year plant additions in rate base. (AG/CUB Ex. 2.0 at 13). AG/CUB witness Mr. Effron proposed to increase ADIT in order to reflect the growth that will be

available to finance the growth in plant balances following the test year. He calculated an adjustment to this rate base of $39,209,000, based upon the AG's proposed March 31, 2011, cut-off date for *pro forma* capital additions. (AG/CUB Ex. 8.0 at 8; Schedule DJE-1.4; AG Initial Brief at 14).

According to the AG, ComEd witness Ms. Houtsma admitted that ComEd's own forecasts show that its net plant in service in 2011 will be $440 million less than the *pro forma* test year net plant in service that it is proposing in this case. (Tr. 2360). The AG asserts that ComEd's admission that its *pro forma* test year net plant in service is greater that ComEd's forecasted net plant in service for 2011 undermines its request for *pro forma* additions. In support, the AG maintains that the available evidence demonstrates that the plant additions in 2011 will not exceed concomitant growth in the depreciation reserve and ADIT, as ComEd witness Ms. Houtsma confirmed that ComEd has been adding plant in service at rate of approximately $50 million per month. (*See,* AG Cross Ex. 25; Tr. 2397-98). The AG avers that Ms. Houtsma also confirmed that the reserve for accumulated depreciation has been growing at a rate of approximately $35 million per month. (*See,* AG Cross Ex. 26; Tr. 2400). The AG also states that under cross-examination, she agreed that tax deductions that are associated with *pro forma* plant additions were accelerated under the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010; thus, ComEd can deduct 100% of capital additions for income tax purposes. (Tr. 2401).

The AG concludes that, with the 2011 plant additions qualifying for 100% bonus depreciation, the growth in ADIT would be approximately $20 million (39.745% tax rate x $50 million) per month. It also concludes that therefore, if the plant additions in 2011 continue at a rate of $50 million per month, the growth of plant in service will be less than the combined monthly growth in depreciation reserve of $35 million and ADIT of approximately $20 million ($35 million + $20 million = $55 million). (AG Reply Brief at 7-8).

CUB's Position

CUB asserts that, when including 18 months of *pro forma* plant additions after the test year, but, failing to reflect the corresponding growth in accumulated depreciation on existing plant through that time period, ComEd chose to ignore the directive of the Illinois Appellate Court, which requires this Commission to adjust the depreciation reserve to the same date as *pro forma* plant additions are included in rate base. CUB states that, while ComEd has averred that it is appealing that decision, 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. Also, according to CUB, ComEd did not cite any precedent (absent a stay, which has not been granted in this case) for ignoring an Appellate Court decision on the relevant issue, simply because one or more parties sought leave to appeal to the Illinois Supreme Court. (CUB Initial Brief at 10).

CUB additionally avers that *pro forma* adjustments are allowed by the Public Utilities Act only if "all known and measurable changes" are taken into account, citing *Commonwealth Edison Co.*, 937 N.E.2d at 704; 83 Ill. Adm. Code Secs. 287.20, 287.40. CUB maintains that ComEd 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. Depreciation on embedded test year plant in service is a known and measurable change that must be taken into account. CUB concludes that ComEd has selectively chosen which factors it would prefer to include in post-test year calculations, which, it argues, is both poor policy and is inconsistent with the law. (AG/CUB Ex. 2.0 at 12).

CUB further contends that the recent Appellate Court decision regarding ComEd's last rate case dictates that the date, from which, the ADIT reserve is calculated must also match the date to which post-test-year additions are allowed. ComEd, CUB continues, has recognized the incremental ADIT that would be generated by *pro forma* adjustment to post-test-year additions to plant in service, but it has not recognized the growth in ADIT that is related to embedded plant, as of the end of the test year. CUB concludes that, by failing to properly calculate ADIT, ComEd 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. In accordance with his proposal to include adjustments through March 31, 2011, AG/CUB witness Mr. Effron proposed to increase ADIT by $39,209,000. (AG/CUB Ex. 8.0 at 7-8; AG/CUB Ex. 7.1, Schedule B-3; CUB Initial Brief at 10-12).

Analysis and Conclusions

As many parties have pointed out, ComEd ignores the effect of the recent Appellate Court decision regarding ComEd's last rate case, *Commonwealth Edison Co, v. Illinois Commerce Comm.,* 405 Ill. App. 3d 389, 937 N.E.2d 685, 701-703 (2nd Dist. 2010). In that case, the Appellate Court specifically found that a utility's accumulated depreciation must match, in terms of the time period involved, its *pro forma* plant additions. It also made this ruling in the context of ComEd's last rate case. (*See, Commonwealth Edison Co,* 937 N.E.2d at 701-704). In so ruling, it reversed this Commission. We also note that it is not controverted that, if accumulated depreciation must match *pro forma* plant additions, ADIT must also correspond in this manner.

Merely filing a petition seeking leave to appeal to the Illinois Supreme Court has no effect on the Appellate decision. As such, we are required to follow it. We note that the Appellate decision in question is currently the law of the land. Also, there is no indication that ComEd sought a stay of this appellate decision. Further, we decline to ignore the Appellate Court decision until when the mandate issues. As the IIEC has alluded to, the appellate court mandate merely concerns what this Commission is required to do on remand, if anything. It does not concern the effect of the Appellate Court decision else wise. In the Appellate Court decision at issue, this Commission was reversed on a legal basis; the Appellate Court did not conclude further fact-finding on the part of the Commission is necessary. (*Id.* at 701-704). Therefore, when the mandate issues, is not relevant here.

We therefore find that ComEd shall adjust accumulated depreciation plant and ADIT in a manner that corresponds with the correct amount of *pro forma* plant additions that are previously set forth herein. ComEd shall also inform this Commission, and, all parties in this proceeding, as to any development in its Petition for Leave to Appeal to

the Illinois Supreme Court, within three business days from the time when it receives notice regarding any decision or ruling made by the Illinois Supreme Court regarding ComEd's Petition for Leave to Appeal. We further caution all parties to refrain, in the future, from arguments that merely urge this Commission not to follow the law.

2. Accumulated Deferred Income Taxes (ADIT)

See Section IV C 1 b herein, entitled "Accumulated Provisions for Depreciation and Amortization-Related Provisions for Accumulated Depreciation."

3. Construction Work in Progress

ComEd seeks to include $12.6 million in rate base for CWIP. The AG seeks to disallow this entire amount.

ComEd's Position

ComEd seeks to include $12.6 million in CWIP for its short-term investments that are not eligible for AFUDC (Allowance for Funds Used During Construction) in its revenue requirement. ComEd's witness Ms. Houtsma stated that the contention that CWIP should be excluded from rate base because it is "vendor financed," disregards the very short-term interim nature of accounts payable as a source of funds. According to ComEd, it also disregards the results of ComEd's cash working capital analysis because Staff witness Mr. McNally's capital structure conclusions were based on assumptions about financing for CWIP. (ComEd Exs. 29.0 at 42-43; 55.0 at 33-34). ComEd also contends that its rate base already accounts for the effects of vendor financing thorough its cash working capital position. (ComEd Initial Brief at 25-27).

Also, Ms. Houtsma testified that the items that were included in ComEd's short-term CWIP will be used and useful within weeks from the time when the rates that are set in this docket will take place. (ComEd Ex. 55.02nd Rev at 33). Specifically, she stated that the items that will be included in ComEd's represents estimated CWIP as of the end of the *pro forma* period, and therefore, they will, in all likelihood, go into service within 30 days thereafter. She concluded that these projects will be used and useful, and also providing service for, the vast majority of the period that rates pursuant to this docket will be in effect. (*Id.* at 33).

ComEd additionally argues that Section 9-214(e) of the Public Utilities Act specifically allows inclusion of CWIP here, as the investments in question will be placed in service within 12 months from the date of the final order in this case. Ms. Houtsma stated that there will probably always be open accounts payable CWIP-related accounts, however, on a going-forward basis, the new CWIP-related accounts payable will be related to new CWIP, which is not included in rate base here. (ComEd Ex. 55.0 at 33).

The AG's Position

AG/CUB witness Mr. Brosch recommended removing ComEd's CWIP from rate base. (AG/CUB Exs. 1.0 at 16-21; 7.0 at 26-28). His analysis results in a disallowance of $12,591,000. (AG/CUB Ex. 7.1, Schedule B-7; CUB Memo at 4; AG Memo at 4).

Mr. Brosch pointed out that CWIP is an asset account that contains the amount of money that is invested in projects that are under construction before completion and before placement in service. These assets, he stated, are not in service and are therefore not used and useful or providing any benefit to rate base. (AG/CUB Ex. 1.0 at 16-17). According to Mr. Brosch, traditionally, CWIP investment is generally not included in rate base; instead it is given a capitalized return in the form of Allowance for Funds Used During Construction ("AFUDC"). However, ComEd's witness Ms. Houtsma testified that ComEd is not seeking to include specific projects that were recorded in CWIP as of the end of 2009. Rather, according to Ms. Houtsma, only the overall level of CWIP that does not accrue AFUDC as of December 31, 2009, is included.

ComEd witness Ms. Hotsma stated that ComEd's CWIP is a reasonable proxy for the amounts that are expected to be incurred in future periods. (AG/CUB Ex. 1.0 at 17; ComEd Ex. 6.0 Rev. at 26). It is this vague statement, with which, the AG takes issue. The AG avers that this vague reference to a "reasonable proxy" provides the Commission with no evidence or assurance that these unnamed projects are or will be in service. (AG Initial Brief at 15). The AG also maintains that the record evidence and Section 9-211 of the Public Utilities Act, which allows only plant that is used and useful and prudently incurred to be included in customer rates, support adoption of Mr. Brosch's adjustment.

Mr. Brosch stated that ComEd's CWIP assets fall into two broad categories. For all CWIP projects with a total expected expenditure of greater than $25,000 and an expected construction period of greater than 30 days, ComEd capitalizes AFUDC and is therefore not seeking any rate base inclusion. (AG/CUB Ex. 1.0 at 15-16). The other type of CWIP asset, which ComEd does seek to include in rate base, is smaller construction projects that are charged to "blanket work orders" and that have a construction completion period that is shorter than 30 days. (*See,* ComEd response to Data Request No. AG 7.08). This is ComEd's short-term CWIP. While these projects are not eligible for AFUDC, Mr. Brosch averred that a large percentage of ComEd's recorded short-term CWIP has probably not been paid for in cash and therefore it need not be allowed a rate base return. (AG/CUB Ex. 1.0 at 18).

Mr. Brosch further testified that ComEd's short-term CWIP projects that do not earn AFUDC have not been fully paid for in cash because ComEd's financial books are maintained on the accrual basis of accounting, recognizing transactions as charges to CWIP when costs are incurred, as opposed to when they are paid. This means, he continued, that charges to CWIP projects are recorded before the time when contractors, materials suppliers and employees must actually be paid for the goods and services that were incurred and added into the CWIP balances. The cash payments for such goods and services generally occur in arrears. For example, Mr. Brosch stated, ComEd's study of the timing of cash flows has concluded that the cost of base payroll and withholdings for Company employees is actually paid an average of 14.64 days after labor costs are incurred. Miscellaneous cash voucher payments to vendors occur even more slowly; they are estimated to experience a 64.34 day delay according to ComEd's lead/lag study. These facts, according to the AG, establish that ComEd is seeking rate base inclusion for a type of short-term CWIP asset where it will have little or no actual cash investment that requires any return from customers. (*Id.* at 17).

The AG additionally contends that ComEd has a vehicle to revise its AFUDC calculations to be more inclusive of short-term projects and to directly account for project costs that are not yet paid for in cash, should the Commission exclude all CWIP in determining ComEd's rate base. It asserts that the Electric Plant Instructions in the FERC Uniform System of Accounts at *Components of Construction Cost* allows AFUDC including, "…the net cost for the period of construction of borrowed funds used for construction purposes and a reasonable rate on other funds when so used, not to exceed, without prior approval of the Commission, allowances computed in accordance with the formula prescribed in paragraph (a) of this subparagraph." In support, the AG cites 18 CFR 101, Electric Plant Instructions 3(A)(17). (AG Initial Brief at 18-19).

The AG further asserts that Section 9-214 of the Act leaves the decision as to whether to include CWIP to the Commission; it is not a mandatory grant. It thus surmises that a utility has the burden of demonstrating that the plant at issue will be used and useful and prudently incurred. Additionally, according to the AG, CWIP investment is, by definition, investment for work where construction is "in progress," where the assets are not completed and placed into service. When CWIP is ultimately completed and placed into service, the amount invested is transferred into the Plant in Service account and depreciation accruals commenced. The AG argues that, if the Commission elects to include in rate base only assets that are used and useful and providing benefits to customers, then, short-term CWIP cannot be included. (AG Initial Brief at 19).

The AG acknowledges that short-term CWIP was allowed into rate base in ComEd's last rate case, docket No. 07-0566, Order of September 10, 2008, at 15. However, in that case, ComEd's proposed level of test-year CWIP not accruing AFUDC was uncontested and was therefore approved. Here, however, the notion that ComEd has proven the appropriateness of adding these CWIP projects to rate base has been challenged. (*Id.* at 20).

The AG also contends that ComEd witness Ms. Houtsma is erroneous in asserting that adjustments to capitalization made by Staff witness Mr. McNally require the Commission to include short-term CWIP in rate base. The AG argues that Mr. McNally's adjustments are to align the capital balances with the capital sourcing assumptions employed within the AFUDC formula. According to the AG, Staff made reductions to capital balances in order to not double-count the assignment of certain capital that is assumed to be supportive of long-term CWIP and that is allowed to accrue an AFUDC return. According to the AG, none of these adjustments concern short-term CWIP that does not earn AFUDC. In fact, according to the AG, it is the absence of AFUDC that is its basis for including any CWIP in rate base. (AG Initial Brief at 21; AG/CUB Ex. 7.0 at 28).

Finally, the AG disputes the correctness of Ms. Houtsma's assertion that recording AFUDC on the small projects would delay inclusion of the small projects in rate base, but would also modestly increase the value of those projects when they do go into rate base. She asserted that, with all else equal, customers should be economically indifferent as a result. (*See,* ComEd Ex. 29.0 at lines 919-926). Mr. Brosch opined that including short-term CWIP in rate base, as proposed by ComEd,

immediately increases the revenue requirement. He also opined that, if ComEd accrues AFUDC on such balances instead of including the costs in rate base, ratepayers will be better off because ComEd's incremental cost of capital is generally lower than ratepayers' marginal cost of capital. He stated that this is because CWIP is presumed to be financed first with available short-term debt. The cost of ComEd's short-term debt in Schedule D-1 (ComEd Ex. 30.1) is only 0.39%. If the short-term CWIP balances are reduced for vendor-provided working capital (accounts payable), there may be no significant remaining balances that would accrue any AFUDC at all. (AG Initial Brief at 21-22).

CUB's Position

CUB states that 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. According to CUB, ComEd also seeks recovery of "short-term CWIP," which is not eligible for AFUDC because it has a shorter construction period. AG/CUB witness Mr. Brosch recommended disallowing 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. He concluded that the vendors who perform the work finance the project during this delay because by the time payment is made, the work is complete. (AG/CUB Ex. 1.0 at 18-19).

CUB avers that ComEd witness Ms. Houtsma has mischaracterizes Mr. Brosch's disallowance by making it appear that his recommendation is contrary to the Public Utilities Act. In fact, CUB continues, Mr. Brosch did not take issue with ComEd's AFUDC, which accounts for construction work in progress. Rather, Mr. Brosch opines that all CWIP could and should be included in rate base in this manner. CUB contends that therefore, ComEd chooses to count short-term CWIP separately from AFUDC. In Mr. Brosch's opinion, this is probably 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. Removing short-term CWIP from rate base results in a disallowance of $12,591,000. (AG/CUB 7.0 at 27-28; CUB Initial Brief at 13-14).

Analysis and Conclusions

We decline to apply Section 9-211 of the Public Utilities Act here because Section 9-241 of the Act specifically concerns CWIP. Section 9-214 provides, in pertinent part, that:

> Notwithstanding the provisions of paragraphs (b) and (d) of this Section, the Commission may include in the rate base of a public utility an amount for CWIP for a public utility's investment which is scheduled to be placed in service within 12 months of the date of the rate determination. . . .

(220 ILCS 5/9-214(e)).[1] As long as there is a preponderance of evidence that the projects that are being funded by CWIP will be placed in service within 12 months from May of 2011, inclusion in rate base of CWIP-funded projects is proper. We therefore disagree with the AG's argument that short-term CWIP should not be included in rate base. In fact, as the AG acknowledges, CWIP that has a longer-term duration is subject to AFUDC, rendering longer-term CWIP projects ineligible for CWIP treatment.

We note that this standard is not unduly burdensome on a utility. It merely requires a utility to supply evidence establishing the truly short-term nature of the CWIP that it seeks to include in rate base. Additionally, at all times, ComEd has the burden to establish the validity of the rates it proposes.

Yet, ComEd has provided evidence establishing that the projects to be funded through its proposed CWIP will be placed in service by April of 2012 are non-specific. ComEd's sole basis for this fact is the testimony of its employee, Ms. Houtsma, who concluded that ComEd's short-term CWIP will be used and useful within weeks from the time when rates are set in this docket. (*See,* ComEd Ex. 55.02 2nd Rev at 33). It appears that there was no attempt on the part of ComEd to determine what, if any, of these smaller projects are funded by the lag between the time when they are booked and when the bills for these items/payment to employees or contractors are actually paid. As the AG and CUB point out, many of these items can be temporarily financed by time. Additionally, the AG asserts that ComEd's lead/lag study does not include CWIP-related items and ComEd's evidence provides no specifics indicating that the AG or Mr. Brosch are wrong in this regard.

While Ms. Houtsma's testimony in this regard is vague, we cannot conclude that it is inadmissible as a matter of law. (*See, e.g., Fraley v. City of Elgin,* 251 Ill. App. 3d 72, 76-77, 621 N.E.2d 276 (2nd Dist. 1993), discussing when factual conclusions are totally unsupported factually, and therefore may be disregarded, as a matter of law). $12.6 million is at issue, and it concerns many, many, small projects that can be completed quickly. We also cannot state, within a reasonable degree of certainty, that all of these projects are vendor-financed. We appreciate the fact that accrual-based accounting records record items that will become due and owing in the future, as opposed to when the bills for those projects become due and owing. We also appreciate the fact that there can be a lag between when work is performed and when the bill for that work is paid. However, without evidence indicating that these two lags allow ComEd to pay for its CWIP-related projects, we cannot state, within a reasonable degree of certainty, that ComEd's CWIP-related projects are financed by these two lags.

However, in ComEd's next rate case, any lead/lag study shall include the effect of accrual accounting on payment for its smaller CWIP-related payments (the payments that are at issue here and that are not accounted for with AFUDC). Failure to do so could result in a determination that ComEd did not meet its burden of proof, or, that

[1] ComEd cites *Citizens for a Better Environment v. Illinois Commerce Commission,* 103 Ill. App. 3d 133, 430 N.E.2d 684 (4th Dist. 1981). (*See,* ComEd's Initial Brief at 26). While this case contains an analysis of CWIP and the "used and useful" standard, it did not discuss Section 9-214 of the Public Utilities Act. Because Section 9-214 of the Act specifically concerns CWIP, we decline to apply this 1981 case here.

ComEd failed to comply with a Commission Order, with all of the penalties that are provided for such failure in the Public Utilities Act.

We note for the record that at issue is $12.6 million in very short-term projects. It therefore appears unlikely that these projects will not be completed by the statutory completion date. However, we cannot state, based on the record, and within a reasonable degree of certainty, that ComEd's very short-term expenditures that are at issue here will not be in service, and, therefore, used and useful, within 12 months from the statutory deadline, which is 12 months from the time when a final order issues in this docket. In so ruling, we note that these items are, by their very nature, very short-term projects. We therefore decline to adopt the AG's adjustment. Because we make this determination based upon the evidence presented, we decline to determine whether any FERC rule aids ComEd.

4. Specific Plant Investments

a. West Loop Project Repair Disallowances

Staff's Position

Staff proposes to disallow ComEd's proffered $4,065,248 cost to repair a high-pressure fluid filled (HPFF) 138kV cable that failed after ComEd initially placed it in service as part of ComEd's West Loop Project. Staff states that ComEd's HPFF 138,000 volt cable at issue here failed approximately two years after ComEd placed it in service as part of its $10 million West Loop Project. The HPFF 138,000 volt cable that failed used pressurized oil as an insulating fluid. The failure occurred due to the depletion of insulating fluid from the pipe that held the cable. (Staff Ex. 6.0 at. 7-8) It is Staff's opinion that Section 9-211 of the Public Utilities Act permits the Commission to allow only prudently-incurred investments in a utility's rate base. (*Id.* at 5). Staff bases this recommendation upon its conclusion that ComEd's management could and should have taken steps to prevent the cable failure from occurring, and that ComEd's cost for the cable repair was therefore not prudently incurred. (Staff Ex. 21.0 at 3). Staff interprets Section 9-211 of the Public Utilities Act to require the Commission to allow only prudently-incurred investments in a utility's rate base. (Staff Memo at 2).

ComEd's Position

ComEd witness Mr. McMahan testified that the initial event that sparked this cable failure resulted from human error. He testified that the contractors involved were properly qualified and selected and ComEd had proper procedures and practices in place for constructing and operating such cable. Mr. McMahan testified that there was no fault in ComEd's practices or on the part of its management. (ComEd Exs. 33.0 at 1; 60.0 at 2-14).

Analysis and Conclusions

We agree with Staff's conclusion that ComEd's management could have and should have been more diligent in preventing this tragic and costly cable failure. However not every bad decision, or set of bad decisions is imprudence. (*See, e.g., Business & Professional People for the Public Interest v. Ill Commerce Comm.,* 279 Ill. App. 3d 824, 831-33, 665 N.E.2d 553 (1st Dist. 1996)). We caution all utilities to act with the utmost care with regard to safety issues. But we cannot state here within a

reasonable degree of certainty that failure to detect the problems with the cable in question was imprudence. We therefore decline to adopt Staff's recommended disallowance.

1. Plymouth Court Feeders

In direct testimony, Staff witness Ms. Elsaid questioned the prudence and used and usefulness of the Plymouth Court Feeders Project, but, following provision of additional detail and explanation in ComEd's rebuttal testimony, Ms. Elsaid concluded that the project was prudent and used and useful. (Staff Ex. 22.0:at 4).

2. Underground Cable

Staff's Position

Staff proposes that ComEd's costs for underground cable repairs, which was disallowed in ComEd's last rate case, docket No. 07-0566, are not appropriate for reconsideration in the current case and should not be included in rate base. (Staff Exs. 1.0 at 16; 16.0 at 26; Staff Memo at 2).

The AG/CUB Position

AG/CUB witness Mr. Effron proposed adjusting ComEd's plant in service to remove the cost of underground cable which was disallowed by the Commission in ComEd's last rate case, docket 07-0566. Mr. Effron stated that nothing in the Final Order in docket 07-0566 stated that the exclusion was for only that case. (AG/CUB Ex. 2.0 at 10). In rebuttal, he opined that, if the $18.7 million disallowance was only for the purpose of ComEd's last rate case, ComEd has not explained why it wrote those assets off from its books of account. This fact led him to conclude that ComEd viewed this adjustment as one that was permanent. (AG/CUB Ex. 8.0 at 7-8).His total adjustment reduces ComEd's rate base by $15,222,000. (AG/CUB Ex. 7.1, Schedule B-2; CUB Memo at 4; AG Memo at 4).

ComEd's Position

ComEd witness Ms. Houtsma testified that the Final Order in docket 07-0566 and the evidence in this proceeding do not support this adjustment. According to ComEd, nothing in the Final Order in Docket No. 07-0566 provided that the $18.7 million of underground cable costs that was excluded therein would be excluded from ComEd's rate base in future proceedings. Instead, ComEd states, the ruling in docket 07-0566 was based on lack of evidence .

Ms. Houtsma testified that the evidence in this proceeding demonstrates that the $15.2 million of underground cable costs that are at issue here were prudently-incurred and reasonable. The difference between the 2005-2006 costs incurred and the average unit costs in the 2000-2004 period was attributable to a change in capitalization policy with respect to underground cable fault repairs. This change, which occurred in 2004, resulted in the capitalization of certain costs to Account 366 that had been recorded as expense in the prior years. When the effect of the change in capitalization policy is removed from the calculation of the $18.7 million adjustment, the 2005-2006 average unit costs are lower than the 2001-2004 inflation adjusted costs. (See, CE Ex. 29.4). In other words, ComEd states, there was no increase in costs. Because no cost increase

occurred and because that was the sole basis for the argument in docket 07-0566 that an adjustment to rate base was appropriate, ComEd concludes that there is no basis for any adjustment in this proceeding. (ComEd Exs. 29.0 at 11-12, 55.0 at 32).

Analysis and Conclusions

The sole basis asserted by Staff for disallowing this item is that it was disallowed in ComEd's last rate case, docket 07-0566. In fact, in that case, the Final Order of September 10, 2008, at 32-47, concluded that $18.7 million should be disallowed due to lack of evidence on this issue. Therefore, ComEd is correct that this Order did not set a precedent disallowing underground cable in general. However, it appears that the actual reason for dispute here stems from a change in accounting procedures on the part of ComEd. It is disconcerting that this change was not communicated to Staff or other parties. While we decline to adopt this disallowance, we strongly encourage parties to disclose relevant facts early on in proceedings.

3. Whether to Include PORCB (Purchase of Receivables and Consolidated Billing Service) Costs Here

Staff's Position

Staff proposed that the costs that are identified as PORCB costs should not be recovered here, in ComEd's rate case. Staff states that this is consistent with the Commission's final Order in Docket No. 10-0138, the docket in which this Commission approved ComEd's statutorily-required PORCB program. (*See*, 220 ILCS 5/16-118). Staff contends that, because ComEd has already included these same costs under its UCB and POR-related Rider for the PORCB program, those costs cannot also be included for recovery here. Staff avers that, while no evaluation of the specific PORCB costs to be recovered will occur until a reconciliation proceeding (pursuant to ComEd's PORCB tariff) there is no way, at present, to determine whether the PORCB costs at issue are allowable under ComEd's PORCB-related Rider. (Staff Ex. 1.0 at 15-16).

Additionally, Staff does not agree with testimony offered by Dominion witness Mr. Christ or ICEA witness Mr. Fein (*see* below) which is, that the costs that are identified as PORCB-related are recoverable in base rates. Staff opines that the appropriate case for evaluation of PORCB costs is in the Rider reconciliation proceedings that are provided for in the Rider for PORCB services. (Staff Exs. 1.0 at 10-15; 16.0 at. 21-25; Staff Memo at 2).

Dominion's Position

Dominion's witness Mr. Crist's testimony addressed treatment of ComEd's startup costs of implementing POR. He recommended that all of the costs associated with ComEd's IT upgrades that were needed to offer POR should be included in rate base here, as opposed to being collected from POR or UCB customers through ComEd's PORCB Rider. He opined that all of ComEd's retail customers that are eligible for retail electric supplier service should share the burden of the PORCB upgrades that ComEd incurred. (*See,* Dominion Ex. 3.0 at 8).

He also opined that ComEd should not be allowed to recover the full amount of its IT improvement-related costs. He testified that those costs are extraordinarily high,

in relation to what other utilities have spent for similar upgrades. There has been no audit of those costs in this proceeding by the Staff or any other party. At the very least, he continued, the Commission should make it clear that there has yet to be a determination as to whether those costs were/are prudently incurred and that prudence reviews will be conducted in the reconciliation proceedings regarding those costs. (Dominion Ex. 3.0 at 8).

Dominion additionally asserts that ComEd only spent a small portion of those costs for POR upgrades. The bulk of those costs, according to Dominion, are for general upgrades to ComEd's IT systems that were needed to serve retail electric supplier customers, in general, and/or provide consolidated billing service. Mr. Crist recommended that, if ComEd must recover its upgrade costs from POR customers, ComEd should only be allowed to recover $2 million of costs, which is approximately what the Ameren utilities and ComEd's affiliate PECO spent to upgrade their systems to provide POR charges. In Dominion Ex. 3.0, Mr. Crist went through each of the elements of the IT upgrades that Mr. Marquez testified were performed by ComEd. According to Dominion, Mr. Crist demonstrated that virtually all of those upgrades were necessitated not by POR, but by changes necessary to provide service to an expected increase in retail electric suppliers' customers and to provide consolidated billing (UCB services). (Dominion Memo at 1-2).

ICEA's Position

ICEA avers that the costs associated with changes that are new and specific to PORCB service alone are theoretically appropriate for inclusion for recovery in PORCB, if those charges were approved in the appropriate docket, after having been found to be just and reasonable. It further maintains that, to the extent that the changes or upgrades were made that are not specific to PORCB service itself, or that they benefit ComEd and its customers in other ways, the costs are more appropriate for rate base recovery. (ICEA Exs. 1.0 at. 6-7; 2.0 at 14-15).

ComEd's Position

ComEd's witness Mr. Marquez testified that, while ComEd agrees with Mr. Fein that the Commission should determine what, if any portion of these costs should be included in rate base, Mr. Crist is incorrect that any portion of the costs should be disallowed. Mr. Marquez averred that the fundamental and extensive changes to ComEd's billing systems that were necessary to implement PORCB were prudent and reasonable. (ComEd Exs. 10.0 at 27-29; 36.0 at 3-20). According to Mr. Marquez, if not for the legal obligation to offer PORCB services, ComEd would not have incurred these costs. (*Id.* at 8-9).

In its Reply Brief, ComEd avers that the drivers of the PORCB costs are in Mr. Marquez' Rebuttal testimony, and, those drivers are as follows:

1. $2,474,211 of the capital costs ($2,192,151 jurisdictional) were to implement POR service;

2. $6,402,789 of the capital costs ($5,672,871 jurisdictional) and $1,915,000 of the deferred O&M expenses (all jurisdictional) were for other work that supports the provision of PORCB service (including $1,007,017 for bill redesign necessitated by provision of POR service) and was needed in order to be able to process the increased switching expected to result from the provision of PORCB service; and

3. $6,842,012 of the capital costs ($6,062,000 jurisdictional) and $780,000 of the deferred O&M expenses (all jurisdictional) were for work on the Customer Data Warehouse and Retail Office applications, due to increased "data" volumes required to provide PORCB service and to house other "data, which would not have been performed, absent the statutory requirement to provide PORCB service.

(ComEd Ex 36.0 Rev. at 5–18; ComEd Reply Brief at 44-45). Also, according to ComEd, Staff has incorrectly asserted that the support lacking for the PORCB costs is still not been presented here. (ComEd Reply Brief at 45). Additionally, ComEd avers that the PORCB costs are now "used and useful;" thus, it concludes that all ratepayers should pay for this program, irrespective of whether they use POR or UCB services. Finally, ComEd argues that the Order in the PORCB docket, docket 10-0138 "just adopted Staff proposal to limit the amount recovered. . . to the original estimate of $12,596,000." (*Id.* at 45-46).

According to ComEd, Staff's proposal guarantees that it will be denied recovery of some of these costs. This is because, ComEd states, Staff does not provide any mechanism for ComEd ever to recover the $4,066,000 difference between the cap imposed in the PORCB docket ($12,596,000) and what ComEd contends is now its actual PORCB costs ($16,622,000). Also, ComEd continues, Staff's proposal places at risk ComEd's recovery of additional portions of these costs because, if, in 2014, (when the first PORCB-related reconciliation will occur, pursuant to ComEd's Rider regarding PORCB) the Commission decides some of these costs do not meet the requirements for rider recovery under Section 16-118 of the Public Utilities Act, (the statute that requires ComEd to have POR and UCB services) ComEd's recovery of those costs is at risk, because it could be required to issue refunds with no mechanism to recapture these costs. (ComEd Reply Brief at 47).

However, ComEd acknowledges that Staff has advocated that ComEd can file a new tariff regarding POR and UCB costs. (*See,* ComEd Reply Brief at 48-49). ComEd, in fact, recommends as an option for this Commission here, that it could find that all PORCB costs could be recovered through a revised Rider that ComEd would file regarding Rider RCA, which concerns ComEd's PORCB program. (*See,* ComEd Reply Brief at 48).

Analysis and Conclusions

Dominion's argument that all ratepayers should pay for the cost of ComEd's PORCB program has been thoroughly examined and rejected in the final Order in

docket 10-0138. (*See, e.g.,* docket 10-0138, final order of December 15, 2010, at 26-27). We decline, therefore, to entertain this argument here.

We further decline to entertain arguments that PORCB-related costs should be included in general rates, or, whether only POR-related costs are recoverable. We note that, with regard to POR services, the enabling statute provides, in pertinent part, that:

> The tariff filed pursuant to this subsection (c) shall permit the electric utility to recover from retail customers any uncollected receivables that may arise as a result of the purchase of receivables under this subsection (c), may also include other just and reasonable terms and conditions, and shall provide for the prudently incurred costs associated with the provision of this service pursuant to this subsection (c).

(220 ILCS 5/16-118(c)). Regarding UCB services, this same statute provides that:

> The tariff filed pursuant to this subsection (d) . . . shall provide for the recovery of prudently incurred costs associated with the provision of service pursuant to this subsection (d). The costs associated with the provision of service pursuant to this Section shall be subject to periodic Commission review.

(220 ILCS 5/16-118(d)). Clearly, the General Assembly meant to allow recovery for both POR and UCB services through separate tariff(s), not through general rates. There would be no point in requiring a separate tariff recovery mechanism that is subject to separate periodic reviews, if the costs at issue could be recovered in general rates. We agree with Staff witness Ms. Ebrey that there is no legal authority for recovery of these costs here.

We acknowledge that Dominion asserts that many of the costs that ComEd states were attributable to its PORCB program were not prudently-incurred in order to provide UCB or POR services. According to Dominion's witness Mr. Crist, many of these costs were incurred to accommodate retail electric supplier services in general, and not just those retail electric suppliers who offer PORCB services. However, if those costs were not prudently-incurred for UCB or POR services, they will be disallowed in the statutorily-mandated prudence reviews.

For the reasons stated above, we conclude that all of the costs that ComEd has attributed to its PORCB program are disallowed. In so ruling, we note that ComEd witness Mr. Marquez has testified that all of the expenses that are at issue here were incurred as a result of ComEd's legal requirement to provide UCB and POR services. Because the General Assembly intended recovery of those costs to occur through a separate tariff(s), from those imposed in general rates, they cannot be included here.

In its Reply Brief, ComEd vaguely asserts that Staff has never suggested, and the final Order in the PORCB docket, docket 10-0138, has never stated, that ComEd is free to file a new tariff (Rider) that encompasses the totality of the costs that ComEd has experienced related to this program, but which, ComEd failed to provide any evidence substantiating, in the PORCB docket. These allegations are simply incorrect. Staff, in fact, pointed out that ComEd can file a new tariff. (*See, e.g.,* docket 10-0138,

Amendatory Order of February 9, 2011, at 37). And, in fact, the final Order in that docket noted that ComEd can file a new Rider that encompasses its newly-found expenses. (*See, id.* at 39). We therefore reiterate, for the sake of clarity, that ComEd is free to file a new Rider that encompasses the PORCB-related expenses that ComEd did not substantiate in the PORCB docket, docket 10-1038.

However, it is counter to basic cost-causation principles to include PORCB-related costs in rates that include every ComEd customer, when some customers will not or do not take these services. While ComEd has argued that these costs are "used and useful" and "known and measurable," they simply are not "used and useful" or "known and measurable" for all of ComEd's customers. Moreover, as the final Order in the PORCB docket makes abundantly clear, the General Assembly intended for recovery of the POR and UCB services to be included in the charges that are assessed pursuant to that program. We will not impose those charges upon all ratepayers here.

4. Allocation of G & I Plant

Staff's Position

Staff states that ComEd currently functionalizes its General Plant (FERC Accounts 389-399) and Intangible Plant (FERC Accounts 301-303) ("G&I") using a combination of generic functional allocators and direct assignment approved by the Commission in Dockets Nos. 08-0532, 07-0566 and 05-0597. For certain G&I accounts, ComEd now proposes to switch from a set of generic functional allocators to a single generic functional allocator of Wages and Salaries ("W&S"). For other G&I accounts, ComEd now proposes to replace the previously-approved direct assignment methodology with a general W&S allocator. (Staff Ex. 12.0, p. 9) Staff opposes these changes. According to Staff, ComEd failed to present a reasonable justification for these proposals.

Staff posits that ComEd's only justification for the proposed changes is a statement by ComEd witness Ms. Houtsma that the proposed methodology aligns with the method employed in ComEd's Transmission Formula Rate, thus assuring that ComEd will not over or under recover G&I costs in either jurisdiction. (ComEd Ex. 6.0 Rev. at 24).

It is Staff's position that Ms. Houtsma's explanation is inadequate. Staff contends that cost allocation should be based upon the principle of cost-causation, not achieving consistency with the functionalization of transmission costs. Staff asserts that ComEd did not present any compelling reason demonstrating why the current approach that has been approved by the Commission is not cost-based and should be revised. Staff states that, given the strong support that ComEd has expressed for direct assignment in the past, it is incumbent on ComEd to explain why it is moving towards more general allocators for these costs. Staff recommends rejecting ComEd's proposed G&I changes. This results in an adjustment to ComEd's proposed revenue requirement as presented in Schedule 16.12 which was filed on December 23, 2010 with the rebuttal testimony of Staff witness Ebrey. (Staff Ex. 16.0; Staff Initial Brief at 107-108).

ComEd's Position

ComEd argues that the Commission should approve including in rate base $1,419,780,000 of General and Intangible ("G&I Plant") that supports the delivery services (distribution and customer service) functions. G&I plant includes costs that are diverse in nature; they support one or more business functions, including telecommunications equipment, land and office buildings, office furniture, transportation equipment, and computer systems. ComEd contends that the Uniform System of Accounts does not record G&I Plant costs by function; they therefore must be functionalized. ComEd seeks approval of its new methodology regarding functionalization of its G&I plant both for purposes of calculating ComEd's rate base and for determining rate design. (ComEd Initial Brief at 40-41).

ComEd states that it has included in rate base the costs recorded in G&I Plant Accounts that support the provision of distribution and customer service. According to ComEd, its direct case provided detailed information regarding how G&I Plant had been functionalized between the Delivery Service and non-Delivery Service functions. (ComEd Exs. 6.0 Rev. at 23; ComEd Ex.6.1, Sched. A-5). ComEd directly assigned the largest G&I Plant Account, Account 397 – Communication Equipment, using the same direct assignment study methodology that was approved for this Account in ComEd's 2007 rate case. (ComEd Ex. 6.0 Rev. at 24). ComEd functionalized the remaining G&I Plant Accounts using the general labor allocator, (also called the "GLA" or the "Wages & Salaries" or "W&S" allocator) rather than using the mix of the general labor allocator and other methods approved in its 2007 rate case, because, according to ComEd, that simplified approach results in better alignment with ComEd's Transmission Formula Rate, thereby avoiding over-recovery or under-recovery of G&I plant costs. (ComEd Initial Brief at 41).

According to ComEd, Staff witness Mr. Rukosuev dismisses "out of hand" Ms. Houtsma's testimony about how use of a general labor allocator better aligns the allocation of costs between FERC and the ICC on the basis that "the objective for cost allocation should be cost causation principles, not achieving consistency with the functionalization of transmission costs." (*See,* Staff Ex. 12.0 at 10). ComEd avers that Mr. Rukosuev simply disregarded Ms. Houtsma's testimony that by this change: "ComEd will not over (or under) recover its associated General and Intangible Plant costs in either jurisdiction." According to ComEd, this is a statement about consistently identifying cost causation between the two jurisdictions, it was not simply a statement about "overlaps or gaps," as Mr. Rukosuev implies. (ComEd Initial Brief at 42).

ComEd also argues that its use of the general labor allocator to allocate the costs in G&I Plant Accounts other than Account 397 has caused the costs to be recovered through ComEd's distribution rates to be approximately the same overall as under the prior methodologies used by ComEd. ComEd asserts that, as shown on ComEd Cross Ex. 14, if the previous methods for functionalizing General and Intangible plant had been used, jurisdictional test year General and Intangible plant would have been only about 1.2% lower than the $1,280,718,000 (gross plant amount) requested in this

proceeding. ComEd concludes that therefore, the simplified methodology is not biased towards assigning more costs to distribution service. (ComEd Initial Brief at 42-43).

Analysis and Conclusions

ComEd contends that use of the new procedure is inconsequential, as if the previous methods for functionalizing General and Intangible plant had been used, it would have only been about 1.2% lower than the $1,280,718,000 gross plant that ComEd seeks here. In fact, however, this 1.2% is still several million dollars. It is $15,368,616, which is not a trivial amount. This contravenes Ms. Houtsma's testimony that ComEd will not over-recover or under-recover using the new methodology. It also belies ComEd's contention that this methodology does not assign more costs to distribution service. We agree with Staff that these proposed changes should be rejected. ComEd proffers no reason that justifies imposing this additional cost upon ratepayers. We do not approve ComEd's proposed new accounting procedures.

5. Cash Working Capital

<u>ComEd's Position</u>

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

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

AG/CUB relies on the testimony of AG/CUB witness Mr. Brosch, who claimed ComEd's lead/lag study was unreliable, but who presented no "corrected" study or counter study and instead urged a 100% disallowance of ComEd's CWC. AG Init. Br., pp. 23-44. The Commission approved lead/lag studies with similar methodologies in the 2009 Ameren Illinois rate cases (*Central Ill. Light Co., et al.*, ICC Docket Nos. 09-0306 Cons. (Order on Rehearing Nov. 4, 2010)), the 2009 North Shore and Peoples Gas rate cases (*North Shore Gas Co., et al.*, ICC Docket No. 09-0166 Cons. (Order Jan. 21. 2010)), and the 2008 Nicor Gas rate case (*Northern Illinois Gas Co*., ICC Docket No. 08-0363 (Order March 25, 2009)). ComEd Ex. 31.0, 2:30-34, 3:52-58, 8:169-9:179 and fn. 1; ComEd Ex. 57.0, 6:131-137 and fn. 10, 7:145-8:154; Tr., 1148:14 – 1150:11.

AG/CUB lacks credibility on CWC, because AG/CUB and Mr. Brosch imply that it was determined in ComEd's 2007 rate case that ComEd had no CWC requirement, but ComEd did not perform a lead/lag study, nor request CWC, in its 2007 rate case. ComEd Ex. 31.0, 25:508-510.

AG/CUB's main criticism of ComEd's lead/lag study relates to the calculation of the collections revenue lag, yet it ignores that its witness misunderstood ComEd's policy for when customer receivables are written off. ComEd writes off customer receivables after the amount owed remains unpaid for 90 days after the account is "finaled" (service has been terminated), not 90 days after the amount initially became due. ComEd Ex. 10.0, 24:487 – 25:494; *see also* Brosch Tr. 1545:3 – 1548:3. AG/CUB's criticisms of the study's use of midpoints for receivables aging intervals, after the initial period(s) in which customers have "grace periods" to pay their bills, to weight ComEd's revenue collections lag boil down to the AG's speculation that it is possible, within any given receivables aging period after the initial period(s), that customers pay more, earlier, within the period, such that the receivables should be weighted at an amount that is less than the result of the midpoints methodology for the period. *See* AG Init. Br., pp. 25-35. AG/CUB largely ignores that the Commission approved a collections lag methodology using midpoints similar to those in ComEd's study in the 2009 Ameren Illinois rate cases, the 2009 North Shore and Peoples Gas rate cases, and the 2008 Nicor Gas rate case, as noted above. Mr. Brosch admitted that he did not even analyze the collections lag or cash working capital results of any of those cases. AG/CUB does not present any calculation that "corrects" for the supposedly flawed midpoints methodology. AG/CUB seems to seek to excuse its failure to present a "corrected" calculation by complaining about ComEd's information systems not having different data that could have supported other methodologies than the midpoints methodology. The data that ComEd used to calculate its revenue collections lag is data from receivables reports that ComEd uses for normal business purposes. AG/CUB's claim that ComEd should have collected other data and used a different methodology also is unfair because ComEd relied on a methodology repeatedly and recently approved by the Commission.

AG/CUB's criticism of including receivables 91 to 365 days old in the collections revenue lag calculation, on the theory that the customers eventually will be disconnected and the amounts they owe will prove to be uncollectible (*e.g.*, AG Init. Br., pp. 28-29), also is without merit. First, the point of the cash working capital requirement is that ComEd should be made whole for the difference in timing of the applicable expenses and revenues. *E.g.*, ComEd Ex. 31.0, 9:186-188. Ignoring receivables older than 90 days is arbitrary, and it is contrary to the very purposes of a lead/lag study and the reason for inclusion of CWC in rate base; the utility still loses the time value of money with older receivables, regardless of whether they eventually are collected. ComEd Ex. 51.0, 9:182 – 11:216.

Staff and ComEd now agree as to the revenue collections lag and employee benefits and FICA taxes (Staff Init. Br., p. 27), but Staff still disagrees with ComEd on three subjects: (1) revenue lags and expense leads for Energy Assistance Charges / Renewable Energy Charge ("EAC/REC") pass-through taxes, (2) revenue lags and expense leads for Gross Receipts / Municipal Utility ("GRT/MUT") pass-through taxes, and (3) the expense lead for intercompany expenses. Staff Init. Br., pp. 22-26.

Staff's positions are based on Staff's interpretation of the relevant statutory language, which refers to "the 20th day of the month following the month in which the charges imposed by the Section were collected…" (305 ILCS 20/13(f)). In addition, Staff's GRT/MUT position is based on Staff's misinterpretation of the law, which is not worded the same as with the EAC/REC; under the law ComEd correctly pays these taxes in the month following activity that occurs in a prior "tax liability" month "during which the tax is collected or is required to be collected" (see Section 3-53-040 of the Municipal Code in ComEd Ex. 31.2). Staff does not and cannot deny the facts regarding when ComEd actually remits payment of these taxes owed by its customers versus when it actually collects payment of these taxes from its customers, *i.e.*, ComEd pays before it collects. ComEd Ex. 31.0, 4:66-73, 15:319 – 19:388 and fn. 7; ComEd Ex. 51.0, 2:55-62, 14:279 – 15:286. Finally, Staff, with respect to intercompany expenses (payment of amounts owed to an affiliate), contends that ComEd has discretion to pay later and proposes to substitute the expense lead for payment of non-intercompany vendors. Staff's incorrectly assumes that ComEd is affording its affiliate inappropriate preferential treatment, which it does not. ComEd Ex. 31.0, 3:61-62, 14:302 – 15:309. Staff's position does not and cannot alter when ComEd actually pays intercompany expenses, which causes its actual CWC requirement. ComEd Ex. 57.0, 2:41 – 3:54, 13:252 – 14:266. The Commission should not adopt Staff's incorrect interpretation, and, even if it did, that would not be a sound reason to ignore ComEd's actual CWC requirement here.

AG/CUB

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. AG/CUB states that 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. Mr. Brosch states that 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.* The most significant flaw about which Mr. Brosch testified is ComEd's choice 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.* Mr. Brosch states that this methodology does not precisely calculate when ComEd actually collects revenues, in part because the ages assigned to those categories are mid-points, not averages. *Id*. AG/CUB avers that it is possible that 90% of receivables 31-60 days old are actually 31-35 days old, causing a mid-point (rather than an average) to be inaccurate. *See Id.* at 28-29.

AG/CUB also indicates that the results of ComEd's lead/lag 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. AG/CUB avers that although ComEd 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.* AG/CUB believes that it is entirely likely that many if not most receivables older than 90 days are uncollectible, and therefore that a negative CWC is appropriate. 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, AG/CUB did not advocate 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. ComEd complains that no party put forth an alternative lead/lag study for the Commission to consider; AG/CUB notes that no party could perform an accurate analysis of receivables aging data because ComEd cited information technology limitations as preventing them from providing more precise information. Tr. at 1080, 1085, 1086, 1088, 1092, 1102, 1106, 1107, 1120.

AG/CUB notes that ComEd 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, AG/CUB argues that 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. AG/CUB avers that such a proper study is not possible without more detailed information from ComEd, and 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.

Staff

ComEd, at the surrebuttal stage, requested a CWC requirement of $67.741M (ComEd Ex. 55.1, Sched. B-1 Revised, p. 1, line 9). This amount is based on the results of a lead/lag study prepared by ComEd witness Subbakrishna (ComEd Exs. 57.0, 57.1, 57.2 and 57.3) and reflects updates from ComEd's final revenue requirement (ComEd Ex. 55.1, Sched. B-8). Both ComEd and Staff agree that the final CWC requirement will be based on the revenue requirement that is ultimately approved by the Commission in this proceeding. (Staff Ex. 3.0R, pp. 37-38; ComEd Ex. 31.0, p. 5)

However, a few issues concerning the lead/lag study remain contested between ComEd and Staff. Those issues include lead/lag days associated with certain pass-through taxes and expense lead days associated with intercompany expenses, as more fully described below:

1) Energy Assistance Charges/Renewable Energy pass-through tax ("EAC/REC") for which Staff proposes 0 revenue lag days and 35.21 expense lead days as opposed to ComEd's proposed 42.11 revenue lag days and 26.11 expense lead days;

2) Gross Receipts/Municipal Utility pass-through Tax ("GRT/MUT") for which Staff proposes 0 revenue lag days and 44.21 expense lead days as opposed to ComEd's proposed 42.11 revenue lag days and 26.11 expense lead days; and

3) Intercompany expenses for which Staff proposes 45.35 expense lead days as opposed to ComEd's proposed 30.35 expense lead days. (ComEd Ex. 57.0, pp. 2-3)

Revenue Lag and Expense Lead Days for Pass-through Taxes

ComEd asserts in its Initial Brief that Staff's proposal to change the revenue lags and expense leads for certain taxes does not match the reality of when these amounts are required to be and are paid by ComEd to the taxing authorities versus when they are collected from customers. However, the evidence clearly demonstrates that it is ComEd's position that is inconsistent with the requirements of the underlying statutes that impose the taxes. The Commission should accept Staff's position, which is based on a plain reading of the statutes, as more fully explained below.

Revenue Lag and Expense Lead Days for EAC/REC Pass-through Taxes

Staff's adjustment to the expense lead days associated with EAC/REC pass-through taxes is based on language contained in the statute governing the Energy Assistance Charge ("EAC") (305 ILCS 20/13) which provides that a public utility engaged in the delivery of electricity shall assess each of its customer accounts a monthly charge. (Staff IB, pp. 22 – 24) The utility shall remit all moneys received as payment to the Illinois Department of Revenue by the 20th day of the month *following the month of collection*. The statute requires ComEd to remit these pass-through taxes after they have been collected from customers. Therefore, there is no revenue lag associated with these collections. However, there is an expense lead because ComEd has the use of these monies until they are remitted to the State of Illinois. Staff calculated an expense lead time of 35.21 days based on the assumption that revenues (including the collection of pass-through taxes) would occur on average, at the midpoint of a given month, 15.21 days, as calculated by ComEd's witness Subbakrishna (ComEd Ex. 7.0, page 14) and accepted by Staff, plus the number of days in the month prior to remittance, 20 days. The sum total of which is 35.21 days. (Staff Ex. 3.0R, p. 40)

ComEd opposed Staff's calculation of expense lead days and instead argues that it remits the EAC/REC pass-through taxes 16 days before it collects them (revenue lag of 42.11 days minus expense lead of 26.11 days produces a net revenue lag of 16 days). ComEd produces this counter-intuitive result by starting the clock at the end of the month for which the tax relates, regardless of when those taxes are collected from customers. (ComEd Ex. 31.0, p. 16) In so doing, Mr. Subbakrishna essentially utilized accrual basis accounting to derive a cash basis impact. (Staff Ex. 18.0, p. 33). This result is counter-intuitive based on a plain reading of the statute. Regardless of the methodology used by Mr. Subbakrishna, the language in the law clearly states that these pass-through taxes are not due until after they are collected from ratepayers. Therefore, Staff urges the Commission to accept Staff's calculation of zero revenue lag days and 35.21 expense lead days for EAC/REC pass-through taxes, which is consistent with both the statute and the reality of the cash flows.

Revenue Lag and Expense Lead Days for GRT/MUT Pass-through Taxes

As described in testimony and Staff's Initial Brief (Staff IB, pp. 24-25), Staff adjusted the GRT/MUT pass-through taxes based on the language contained in the City of Chicago's ordinance. This ordinance requires ComEd to file a monthly tax return to accompany the remittance of such taxes, due by the last day of the month following the month during which such tax is *collected*. The ordinance requires ComEd to remit these pass-through taxes after they have been collected from customers. Accordingly, there is no revenue lag associated with such collections. Moreover, there is an expense lead arising from the fact that the Company is not required to remit these taxes until after they are collected, thereby having the use of these monies until such time as they are remitted to the City of Chicago or other municipality. Staff calculated an expense lead time of 44.21 days based on the assumption that revenues (including the collection of pass-through taxes) would occur on average, at the midpoint of a given month, 15.21 days, as calculated by ComEd's witness Subbakrishna (ComEd Ex. 7.0, p. 14) and accepted by Staff, plus a full 29 days prior to remittance in the month after collection. The sum of which is 44.21 days.

Because Mr. Subbakrishna made the same arguments against Staff's calculation of GRT/MUT as he made against Staff's calculation of EAC/REC, Staff will not repeat its EAC/REC arguments here and Staff urges the Commission to conclude that the CWC calculation for GRT/MUT pass-through taxes should reflect zero revenue lag days and 44.21 expense lead days, as supported by Staff.

Expense Lead Days Associated with Intercompany Expenses

ComEd asserts in its that Staff's proposal to change the expense leads for intercompany billings is arbitrary and does not match the reality of when these amounts are paid by ComEd. (ComEd IB, p. 44). The Commission should accept Staff's proposed adjustment to increase the number of expense lead days for intercompany expenses from 30.35 to 45.35. These payments to affiliates are within the Company's discretion and a higher CWC charge for early payment represents a form of cross subsidization that is generally prohibited. It would be improper to charge ratepayers a higher CWC requirement in order to compensate ComEd for paying its affiliates earlier than non-affiliated vendors are paid. Initially, Staff proposed to increase the intercompany expense lead days to 64.34 days to be consistent with the expense lead days for nonaffiliated vendors utilized for other O&M expenses in the Company's CWC calculation. However, Staff reduced it to 45.35 days to recognize that non-affiliated vendors are paid later than affiliated vendors. (Staff Ex. 18.0, pp. 30-31) Staff's final proposal utilizes the midpoint of the service month, 15.35 days, and adds 30 days for payment. This length of time more closely approaches the expense lead time for non-affiliates, while recognizing that affiliates invoice charges for their services promptly and on a monthly basis. (Staff Ex. 18.0, p. 31). Accordingly, Staff urges the Commission to accept Staff's proposed number of expense lead days, 45.35, based on the fact that such payments are within the Company's discretion and allowing a higher CWC charge for early payment represents a form of cross subsidization that is generally prohibited in affiliated interest agreements.

Commission Analysis and Conclusion

ComEd's lead/lag study for the most part was prepared in an appropriate manner and its methodologies are similar to those of studies approved by the Commission in other recent rate cases. Both ComEd and Staff agree that the final CWC requirement will be based on the revenue requirement that is ultimately approved by the Commission in this proceeding. Staff and ComEd now agree as to the revenue collections lag and employee benefits and FICA taxes.

With respect to AG/CUB's criticisms of ComEd's lead/lag study's calculation of the revenue collections lag, the Commission finds the criticisms as to both the weighting of different aging periods of receivables and the criticisms relating to inclusion of receivables 91 to 365 days old are not well-founded and are inconsistent.

AG/CUB's challenges to ComEd's lead/lag study on the subject of pension/OPEB costs, severance costs, and the IEET also lack merit. For example, the first two erroneously try to treat cash items as non-cash, and once again disregard that ComEd actually understated its loss of the time value of money. The IEET criticism also was shown to be erroneous. Finally, AG/CUB's attempt to raise concern with respect to Rider PE is speculative and incorrect.

The Commission agrees with Staff's interpretation as to the EAC/REC and GRT/MUT tax issues. For the EAC/REC tax, the utility shall remit all moneys received as payment to the Illinois Department of Revenue by the 20th day of the month *following the month of collection.* Under the GRT/MUT tax, this ordinance requires ComEd to file a monthly tax return to accompany the remittance of such taxes, due by the last day of the month following the month during which such tax is *collected*. Both the statute and ordinance requires ComEd to remit these pass-through taxes after they have been collected from customers. ComEd stated in its briefs that the Company correctly pays these taxes in the month following activity that occurs in a prior "tax liability" month. The Commission concludes that the CWC calculation for GRT/MUT pass-through taxes should reflect zero revenue lag days and 44.21 expense lead days and zero revenue lag days and 35.21 expense lead days for EAC/REC pass-through taxes as supported by Staff.

Finally, with respect to payments of intercompany obligations, ComEd has not shown the need to reject Staff's adjustments in this area. According to the Company's initial brief, ComEd's affiliate invoices it on a monthly basis, on time, and the invoices require payments on or around the 15th of the month following the provision of service. Staff's adjustment is based on this statement. There was no mention of an affiliate agreement to the contrary. Therefore, the Commission accepts Staff's proposed number of expense lead days of 45.35, based on the fact that such payments are within the Company's discretion.

6. 2009 Pension Trust Contribution

ComEd's Position

The defined benefit pension plan covering ComEd employees experienced significantly lower than expected performance over the last few years. As a result, by December 31, 2008 the plan was approximately 40% underfunded. Houtsma Reb.,

ComEd Ex. 29.0 at 17. In response to the increase in the unfunded status of the plan, ComEd made an additional $152 million contribution to the plan in 2009. ComEd seeks to include the $92.5 million ICC-jurisdictional rate base effect of this contribution in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev. at 28. ComEd's $152 million pension contribution was prudent and ComEd should be allowed to earn a return on the remainder of the pension asset resulting from its contribution equal to its weighted average cost of capital. Houtsma Reb., ComEd Ex. 29.0 at 25.

AG/CUB

AG/CUB witness Mr. Effron indicates that 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. Mr. Effron notes that from 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, even in light of the economic downturn. AG/CUB Ex. 8.0 at 9. ComEd argues that the effect on ComEd's rate base would have been roughly the same whether the necessary contributions were made over several years or all in 2009. However, Mr. Effron testifies that 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. AG/CUB Ex. 2.0 at 15.

AG/CUB disagreed with the Company's argument that the entire amount of its contribution should be allowed simply because making the contribution "was the right thing to do." ComEd Ex. 4.0 at 23. 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. AG/CUB avers that 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.

AG/CUB's 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.

STAFF

ComEd included as an addition to rate base a deferred debit of $92.591M, which it calls a pension asset. This deferred debit represents the jurisdictional portion of a discretionary cash contribution by ComEd to the Exelon pension plan that covers ComEd employees. (Staff Ex. 3.0R, p. 4) Staff opposed the Company's treatment of the 2009 pension contribution as an addition to rate base. Instead, Staff proposed to allow cost recovery associated with the contribution only to the extent there is a corresponding ratepayer benefit. Staff's proposal, which is in the spirit of the Commission's Order in Docket No. 05-0597, would limit recovery through the operating statement to an amount of costs up to (but not greater than) the amount of the

corresponding savings (i.e., ratepayer benefit) that is reflected in the 2009 test year. (Staff Ex. 3.0R, pp. 3-15; Staff Ex. 18.0, pp. 4-9)

The Company argued that Staff's alternative proposal would disallow a significant portion of the costs based on a novel and unsupported limitation. Specifically, the Company asserted that limiting the recoverable costs to the amount by which pension expense is immediately lowered would result in a $1.4M reduction to the revenue requirement. (ComEd IB, p. 46)

Staff opposes the Company's treatment of the discretionary 2009 pension contribution as an increase to rate base because that would cost ratepayers an amount equal to the approved rate of return multiplied by the $68.750M net pension asset ($92.591M discretionary 2009 contribution minus accumulated deferred income taxes of $23.841M), without regard to the amount of benefit to ratepayers. (Staff Ex. 18.0, Schedule 18.01) The expected benefit that the 2009 pension contribution may have on 2010 pension expense and rate base shows that there is an incremental cost to ratepayers using the treatment proposed by the Company. The cost is calculated to be $851,000 ($7,899,000 - $7,048,000) using Staff's proposed rate of return under the analysis provided by ComEd witness Houtsma. (ComEd Ex. 29.6, p. 1) Accordingly, to the extent that ratepayers benefit from the prepayment in the determination of rates in this case, a cost that equals the ratepayer benefit of the prepayment in the test year should be allowed for recovery. (Staff Ex. 18.0, p. 8) Staff's proposal would not be inconsistent with the treatment allowed by the Commission in Docket No. 05-0597. (Order on Rehearing, December 20, 2006, p. 28) Therefore, it does not constitute a novel approach. Moreover, even if the Commission agrees that such a prepayment is prudent, the cost to ratepayers must also be reasonable. Staff's proposal ensures the reasonableness of the cost by limiting recovery to the amount of ratepayer benefits.

Commission Analysis and Conclusion

ComEd is requesting to include $92.5 million ICC-jurisdictional rate base effect of its pension contribution in its rate base.

Staff contends that ComEd would be adequately compensated for its contribution by providing for a regulatory return equal to the jurisdictional portion of the reduced pension expense resulting from the discretionary contribution. Pearce Reb., Staff Ex. 18.0 at 8-9. We agree with ComEd, however, that Staff's methodology for arriving at its recovery amount - working backward from an estimated reduced cost to customers - bears no relationship to the economic cost to ComEd of its pension contribution. A customer benefits test has been applied only in the context of incentive compensation payments and should not be expanded into other areas. It would be impossible to match costs and customer benefits on a system-wide basis. We therefore reject Staff's proposal.

AG/CUB contend that ComEd should be denied recovery of the cost of the $92.5 million pension asset because, according to AG/CUB, the underfunding should have been addressed through larger contributions in 2006 through 2008. Effron Dir., AG/CUB Ex. 2.0 at 15; Effron Reb., AG/CUB Ex. 8.0 at 9. However, , ComEd's 2009 pension contribution was necessitated by the substantial investment losses experienced by Exelon's pension fund in 2008 as a result of the recession and it was thus

unnecessary to have made larger contributions in prior years. We reject AG/CUB's proposed disallowance.

The Company's 2009 pension contribution was a reasonable response to the decline in the funded status of the pension plan. By making the contribution in 2009, ComEd properly avoided the compounding effect of continued underfunding and as a result of earnings on the contribution, reduced the pension expense component of the revenue requirement in this proceeding. We agree that not allowing ComEd to include its pension contribution in its revenue requirement may encourage utilities to divert capital resources to other investments that would produce a full return, rather than properly fund pension plans. Therefore, the Commission approves the 92.5 million ICC-jurisdictional rate base effect of its pension contribution in its rate base.

7. Capitalized Incentive Compensation

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

8. Customer Deposits

ComEd's Position

ComEd maintains that its rate base should be reduced by $44,705,000 to account for customer deposits. ComEd also argues that an average balance should be used to calculate the amount of customer deposits reflected in the rate base calculation and that only delivery-related customer deposits should be accounted for in that calculation. (ComEd Ex. 29.0 at 37-38).

ComEd asserts that the evidence refutes AG/CUB's and Staff's proposals to determine customer deposits using a year-end balances. ComEd argues that the use of an average, rather than a year-end, balance smoothes out seasonal variations, providing a more accurate reflection of customer deposit amounts. (ComEd Ex. 6.0 Rev. at 37). In addition, ComEd argues that no party has presented any evidence showing that the "increasing trend" posited by Staff and AG/CUB either exists or is likely to continue in the future. Therefore, ComEd concludes that it is not "appropriate" for the Commission to use a year-end balance, particularly when the Commission has 12 months of test year data that the Commission can use to set the level of customer deposits. ComEd points out in its Reply Brief that the growth in this area from January 2006 through December 2009 is predominantly in 2009 itself. (ComEd Reply at 68). To illustrate this point, ComEd notes that the increase in customer deposits from January 2006 to January 2009 was approximately 2.3% per year on average. ComEd explains that if this "trend" were applied to 2009, the year-end balance would be more than $8 million less than the actual year-end 2009 balance and about the same as the average balance ComEd used. ComEd further asserts that in 2009, by contrast, the growth was slightly over 9% for that year alone. Thus, ComEd concludes, using an average for 2009 more than fully captures the "growth" in customer deposit balances that Staff and AG/CUB identified. (*Id*. at 69).

ComEd also avers that the year-end 2009 balance that AG/CUB prefers is not representative of the time period that AG/CUB analyzed because it is the highest

balance during that period, and nearly 10% higher than any monthly balance during 2006 through 2008. (*Id*.). It states that AG/CUB failed to cite any evidence that suggests that customer deposit balances will continue to grow in 2010 or 2011, or at anywhere near the rate experienced in any of the years from 2006 through 2009. Similarly, ComEd avers, the record contains no evidence that new business will be accompanied by increased customer deposits. ComEd asserts that therefore, the use of a 2009 average, as ComEd proposes, is far more representative of the test year amount of balances than the year-end 2009 figure. (ComEd Ex. 29.0 at 37).

ComEd also argues that it correctly reduced its rate base by customer deposits in an amount that reflects the deposits on its delivery service charges, as opposed to the total amount of customer deposits, as proposed by Staff and AG/CUB. (ComEd Reply Brief at 50). ComEd avers that Staff and AG/CUB do not consider that the total amount of customer deposits includes not only charges based on delivery, but also charges based on supply. (ComEd Ex. 55.0 2nd Rev. at 26). According to ComEd, they also ignore the fact that FERC ratemaking is different and the fact that the transmission rate does not explicitly include customer deposits is not determinative of the appropriate treatment in this proceeding. ComEd also maintains that not all customer deposits relate to transmission or delivery. (ComEd Reply Brief at 70). ComEd acknowledges that the amount of a customer deposit is generally based on the entire amount of the customer's expected total bill for service, which includes not only charges for delivery services but also charges for energy. It asserts, however, that the outcome of a delivery rate service case should not be affected by inclusion of what ComEd calls "non-jurisdictional amounts." (ComEd Ex. 55.0 2nd Rev. at 25-27).

ComEd posits that in essence, Staff is proposing to treat the delivery services rate as a residual or catch-all rate for revenue or cost components that are not assigned or collected elsewhere. ComEd argues this is inconsistent with Staff's position concerning the allocation of late payment charges. (ComEd Ex. 55.0 2nd Rev. at 26) ComEd states that the Commission's practice has been to reflect items that are a function of revenues in delivery service rates based on a revenue allocator, and customer deposits should be treated in the same manner. (*Id*.).

ComEd contends that contrary to Staff's and AG/CUB's assertions, the matter of customer deposits is not governed by any delivery services tariff, but instead by ComEd's General Terms and Conditions on file with the Commission and which apply to all of ComEd's tariffs, including but not limited to, the delivery services tariff. ComEd argues that, even if customer deposits were collected solely pursuant to Commission-approved tariffs, that alone would not be dispositive of whether those revenues are related to delivery and therefore jurisdictional in nature. (ComEd Reply Brief at 68-69). ComEd argues that the Commission has regulatory jurisdiction over many services and costs that are recovered through tariffs that are outside the scope of this proceeding. (ComEd Ex. 55.0 2nd Rev. at 25). According to ComEd, "non-jurisdictional" costs or revenues, such as the portion of customer deposits at issue, are those components that are not related to delivery services and should not be included in rate base. (ComEd Reply Brief at 69).

Staff's Position

Staff is proposing use of a 2009 year-end balance to calculate the amount of customer deposits reflected in ComEd's rate base calculation, rather than an average balance, due to a consistent upward trend from 2006 through 2009. Staff is also proposing to reduce ComEd's rate base by the total amount of customer deposits, instead of a jurisdictional amount as proposed by ComEd. Staff recommends an adjustment to ComEd's rate base in the amount of $85,962,000. (Staff Ex. 4.0 at 4; Staff Ex. 19.0 at 4-6).

Staff contends that a 2009 year-end balance should be used for customer deposits because ComEd's customer deposit balance reflects a consistently increasing trend from 2006 and 2009. This upward trend of balances, coupled with ComEd's projection of growth, necessitates the use of a year-end balance according the Staff, since it is a more representative balance for determining the appropriate rate base than an average balance. (Staff Initial Brief at 30). Staff also argues that ComEd bears the burden of proof and ComEd has presented no evidence that the increasing trend that Staff asserts exists will not continue in the future. (Staff Reply Brief at 25).

Staff also avers that ComEd's total amount of customer deposits should be used because ComEd should not be allowed to recover the costs that are associated with customer deposits related to energy and supply through its delivery service tariffs. It is Staff's position that the delivery service tariffs govern ComEd's ability to collect customer deposits. Thus, according to Staff, all deposits collected pursuant to those delivery service tariffs should be considered in the determination of tariffed delivery service rates. (Staff Initial Brief at 30).

The AG/CUB Position

AG/CUB concur with Staff. They maintain that the 2009 year-end balance should be used to calculate ComEd's customer deposits and ComEd's total customer deposit balance should be used to reduce rate base, resulting in an adjustment to ComEd's rate base in the amount of $85,962,000. (AG/CUB Ex. 7.1, Schedule B-8).

AG/CUB argue that ComEd made several errors in calculating customer deposits which resulted in underestimation and increased rate base. AG/CUB maintain that the balances of customer deposits have been consistently growing since 2006 and throughout 2009. Therefore, they conclude that using a 2009 average underestimates the amount of customer deposits. AG/CUB state that the "seasonality" that ComEd uses to justify using this average does not explain this consistent, year-over-year growth. They also disagree with ComEd's assertion that this trend will not continue. AG/CUB aver that, while ComEd is correct that the majority of growth happened in 2009, growth was consistent in previous years as well. (AG/CUB Ex. 1.0 at 37). They note that ComEd did not contest this fact.

AG/CUB also maintain that ComEd's claims that only a portion of its total collected customer deposits are jurisdictional should be rejected. (ComEd Ex. 29.0 at 37). They aver that all of the customer deposits that have been collected by ComEd have been collected in Illinois, and none have been used to reduce FERC rate base.

(*Id.* at 37-38). ComEd's comparison of customer deposits to jurisdictional plant is a straw man argument, according to AG/CUB. 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. AG/CUB maintain that customer deposits neither relate to transmission nor are used to reduce FERC rate base. AG/CUB state that both in testimony, and when asked in a "data request," ComEd failed to identify to what other jurisdiction customer deposits are attributable to. (AG/CUB Ex. 7.0 at 29-30). AG/CUB state that 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*.). They conclude that the total amount of customer deposits should be attributed to retail delivery services and calculated as a reduction to rate base. (AG/CUB 1.0 at 38).

Analysis and Conclusions

We reject Staff's and AG/CUB's proposal to use a 2009 year-end balance, instead of an average balance, to calculate customer deposits. The evidence shows there were insignificant increases in customer deposit balances from 2006 through 2008 and significant increases in 2009. The use of an average balance, as proposed by ComEd, more accurately reflects the test year balance, as it is accounts for the fluctuations in the monthly balances during the test year. We additionally note that it also more fully captures any growth in customer deposits.

With regard to the amount of the deposits, that is, whether to use the total amount or only an amount that reflects delivery service, we note that ComEd acknowledges that deposits reflect the entire amount of a customer's expected bill, including the cost of the energy delivered. This is because, if a customer does not pay a bill, ComEd will be at a loss both for the delivery service provided and also the cost of the energy it paid for when providing delivery service. Conversely, it is the total deposit, not just the delivery-service portion of the deposit that is a source of revenue for ComEd. We also note that if there were no electricity to deliver, there would be no delivery service. Also, as the AG and CUB point out, while ComEd states that this service is non-jurisdictional, it provides no proof of what other jurisdiction would be involved in this service. Therefore, ComEd's reference to the portion of the deposit that is not for delivery service as "non-jurisdictional" is misleading. It is the total deposit amount that should be the amount used to reduce rate based here. This is consistent with our conclusion regarding Late Payment Charge Revenue. The amount of customer deposits reducing rate base is therefore, $$85,962,000. (ComEd Ex. 29.1 Sched. B-13).

9. Material and Supplies Inventories

<u>ComEd's Position</u>

ComEd seeks to include a material and supplies inventory balance of $26,586,000 in its revenue requirement. (ComEd Ex. 6.0 at 28; ComEd Ex. 6.1, Sched.B-1, l.11) ComEd argues that Staff's proposal to reduce the materials and supplies balance included in rate base by the associated accounts payable should be rejected. According to ComEd, accounts payable balances relating to inventories are simply a form of cash working capital, which is measured through the lead-lag study,

making a further reduction in this area unnecessary and duplicative. (ComEd Ex. 29.0 at 42; ComEd Ex. 55.0 2nd Rev. at 30) ComEd explains that, if Staff's proposal to reduce the materials and supplies balance by associated accounts payable were to be accepted, consistency would require that the thirteen month average of accounts payable (rather than the year end balances proposed by Staff) be used. (ComEd Ex. 55.0 2nd Rev. at 31).

ComEd observes that it is ironic that Staff opposes its position that a thirteen month average should be used if accounts payable are deducted. (ComEd Reply Brief at 73). ComEd explains Staff's position is ironic since Staff cited large fluctuations in the level of materials and supplies inventory as justification for its original position that a thirteen month average balance should be used to determine the inventory balance, but simultaneously argued that fluctuations in accounts payable monthly balances supported discarding them in favor of an average that relied on the beginning and ending balances of the test year which happen to be two of the four highest balances in the thirteen-month period. (*Id*.) ComEd also contends that the Commission should not accept Staff's argument that ComEd's proposal to use an average of monthly balances should be rejected because ComEd produced the balances in surrebuttal testimony and Staff finds the balances "questionable." It is ComEd's position that the fact that evidence was accepted into the record on surrebuttal is irrelevant and if the balances are actually "questionable" as Staff asserts without evidence, Staff had opportunity for both discovery and cross examination to resolve any questions it had regarding the balances. (*Id.)*

Staff's Position

Staff is proposing an adjustment to reduce the materials and supplies balance included in rate base by the associated accounts payable. Staff contends that the accounts payable balance should be calculated based on an average of the beginning and ending balances in the test year. Staff's adjustment would result in a reduction to rate base of $5,064,000. (Staff Reply Brief at 27).

Staff argues that an adjustment to reduce the materials and supplies balance by the associated accounts payable is necessary since the accounts payable represent vendor financing and not an investment by the Company's shareholders. Thus, Staff maintains that the appropriate ratemaking treatment is to reduce rate base by these payables. (Staff Ex. 4.0 at 3-4; Staff Ex. 19.0 at 3-4) Staff asserts that the Company's statement that the benefit of the accounts payables associated with materials and supplies is already captured in the cash working capital allowance is a false assumption. (Staff Initial Brief at 31) Staff argues that the Company's position fails to distinguish between the materials and supplies still on hand in inventory and those that are no longer in inventory because they have been used up and charged to operating expense. (*Id*.) When calculating its cash working capital allowance, the Company applied the lead and lag days only to the materials and supplies dollars that have been used up and charged to operating expense. (*Id*.) Staff explains that the Company did not apply the lead and lag days to the materials and supplies dollars that remain in inventory and that are included in rate base. Therefore, according to Staff, the cash working capital calculation, as proposed by the Company, does not account for the balance sheet

portion of materials and supplies and does not capture the payment lag of the associated accounts payable. (*Id*.)

Staff also takes issue with the Company's argument that, should an adjustment be made to reduce inventory by the associated accounts payable, an average of thirteen monthly balances of accounts payable should be used instead of an average based on the beginning and ending balances of the test year. (Staff Initial Brief at 32; Staff Reply Brief at 27) Staff asserts that at first glance the Company's point sounds appealing. However, the balances proposed by the Company are questionable and have not been fully supported according to Staff. Staff argues that the month end accounts payable balances which were not provided by the Company until surrebuttal testimony include debit balances from August through November of 2009. Accounts payable debit balances are not customary and indicate that the supplier owed ComEd money. Staff maintains that the Company should have explained these unusual balances especially considering that the Company did not propose this alternative until surrebuttal testimony. Moreover, Staff notes that ComEd argued in its initial brief, in its discussion concerning its proposal which is no longer contested to use a year end balance to determine the materials and supplies balance, that there is a need for consistency when determining the appropriate accounts payable balance associated with materials and supplies. Staff states that it agrees with ComEd's statement that consistency is needed and accordingly maintains that the average accounts payable balances should be calculated using the year end balances. (Staff Reply Brief at 27)

Analysis and Conclusion

We accept Staff's proposed adjustment to reduce the materials and supplies inventory balance included in ComEd's rate base by the associated accounts payable. We agree with Staff's position that ComEd's vendors are financing the materials and supplies inventory until the corresponding accounts payable are paid. Moreover, since the vendor is in effect financing these purchases until they are paid, the Company's shareholders have no investment in the related materials and supplies and accordingly, the Company should not earn a return on the investment for the inventory until the inventory has been funded by the Company's shareholders.

We concur with ComEd that an average of thirteen monthly balances of accounts payable should be used instead of an average based on the beginning and ending balances of the test year. Based on our review of the record, it is more appropriate to use an average of the monthly balances because the year end balances recommended by Staff reflect very high variations which do not provide an accurate reflection of the accounts payable balance during the time at issue. ComEd's proposal to calculate the accounts payable using an average of thirteen monthly balances will provide a more representative balance. For these reasons, we adopt ComEd's proposal to use an average of thirteen monthly balances.

10. Severance Cost - Regulatory Debit

See Section IV.C.3.h

D. Rate Base (Total)

Based on the electric utility delivery services rate base as originally proposed by ComEd along with the conclusions supra, the utility rate base for ComEd approved for purposes of this proceeding is $6,629,441,000. The rate base may be summarized as follows:

Approved Rate Base
(In Thousands)

Gross Utility Plant	$14,423,422
Accumulated Provision for Depreciation and Amortization	- 5,694,017
Net Plant	8,729,405
Additions to Rate Base	
Materials and Supplies	26,109
Construction Work in Progress	12,591
Regulatory Assets	11,040
Deferred Debits	95,741
Cash Working Capital	79,807
Deductions From Rate Base	
Accumulated Deferred Income Taxes	-1,821,174
Accumulated Misc. Operating Provisions	-306,818
Asset Retirement Obligation	-18,750
Other Deferred Credits	-11,665
Customer Advances	-42,273
Customer Deposits	-124,572
Rate Base	$6,629,441

The development of the overall electric utility delivery services rate base adopted for purposes of this proceeding is shown in Appendix A to this Order.

Commission Analysis and Conclusion

IV. Operating Expenses

A. Overview

ComEd's Position

ComEd's delivery services operating expenses comprised three main categories: (1) expenses recorded in Operating and Maintenance ("O&M") Accounts under the USOA that are functionalized to the distribution function; (2) the portion of expenses recorded in other O&M Accounts that are customer-related and that are appropriately

assigned or allocated to the delivery services function; and (3) the portion of expenses recorded in other FERC Accounts that are appropriately assigned or allocated to the delivery services function. Houtsma Dir., ComEd Ex. 6.0 Rev. at 35. The last category includes items such as Administrative and General ("A&G") Expenses, Depreciation and Amortization Expenses, and Taxes. *Id*.

Despite the major cost reduction efforts ComEd has undertaken, which decreased overall operating expenses before *pro forma* adjustments by $10 million when compared to the amount allowed in ComEd's last rate proceeding, ComEd has incurred many additional cost increases that are beyond its control. Trpik Dir., ComEd Ex. 4.0 Rev. at 4; *see also* Guerra Dir., ComEd Ex. 1.0 2nd Rev. at 3, 6. ComEd, has experienced significant increased costs since its last rate case, attributable to investment in plant ($116 million), depreciation expense ($63 million), pension and retiree health care costs ($55 million), bad debt expense ($22 million), cost of capital ($95 million) and other items. Trpik Dir., ComEd Ex. 4.0 Rev. at 4; Trpik Sur., ComEd Ex. 54.0 at 2-3.

B. Potentially Uncontested Issues

1. 2009 Amortization Adjustment of Existing Regulatory Assets

ComEd has accepted the proposal by Staff witness Ms. Hathhorn to reduce the unamortized balances of six regulatory assets to their May 2011 levels to be recovered over a three-year period. (ComEd Ex. 30 at 7 Staff Memo at 4). This proposal is reasonable and it is hereby approved.

2. Outside Professional Services – Jacobs Consultancy

ComEd accepted the proposal by Staff witness Tolsdorf to remove the jurisdictional portion ($200,000) of costs related to Jacobs Consultancy from the revenue requirement. (ComEd Ex. 30.0; Staff Memo at 4). This proposal is reasonable and it is hereby approved.

3. Advertising Expense

ComEd has accepted the proposal by Staff witness Mr. Tolsdorf to remove $51,538 of advertising expenses from the revenue requirement. (ComEd Ex. 30.0 at 10). This proposal is reasonable and it is hereby approved.

4. Investment Tax Credit Amortization

ComEd agreed to the proposal by AG-CUB witness Effron to reduce income tax by $113,000 by including the amortization of proceeds from the sale of investment tax credits in ComEd's income tax expense. (ComEd Ex. 30.0 at 13). This proposal is reasonable and it is hereby approved.

C. Contested Issues

1. Incentive Compensation Cost and Expenses

ComEd seeks to include a total of $27.562 million of incentive compensation costs in its jurisdictional operating expenses, broken down as follows: $23.281 million for Annual Incentive Program ("AIP") expense, $2.158 million for Long-Term Incentive Plan ("LTIP") expense, and $2.123 million for Exelon 2009 Key Manager Restricted

Stock Award. (*See,* AG/CUB Ex. 3.2 PUBLIC, at 2-5). AG/CUB witness Mr. Smith proposes to disallow 50% of ComEd's 2009 AIP expense. Staff recommends a disallowance of about $2.7 million of the LTIP costs and AG/CUB witness Smith seeks to disallow any LTIP cost recovery. Both Staff and AG/CUB seek to disallow 100% of the costs of the Exelon 2009 Key Manager Restricted Stock Award. (ComEd Initial Brief at 55).

ComEd's Position

ComEd states that it sets employee compensation at levels necessary to remain competitive in the marketplace. The total compensation ComEd pays its employees is the amount needed to attract and retain qualified personnel. ComEd uses a "pay at risk" approach under which all employees are at risk of receiving less than competitive compensation, if plan goals are not attained. (ComEd Exs. 4.0 Rev. at 24; 28.0 at 1).

ComEd has two basic incentive compensation programs: the Annual Incentive Program ("AIP") and the Long-Term Incentive Program ("LTIP"). One of the issues the Commission has had with ComEd's incentive plans in previous cases has been that some of the plan "metrics" are thought to primarily benefit shareholders, not customers. ComEd contends that it has been mindful of those issues, and has revised its plans to accommodate those concerns. According to ComEd, the terms of both the AIP and the LTIP have been established specifically to comply with the Commission's standards for incentive compensation cost recovery as set forth most recently in the Order in docket 07-0566. For the 2009 test year, ComEd revised the AIP to eliminate the net income metric that the Commission disapproved in docket 07-0566, and, therefore, all of the costs incurred under the AIP during the 2009 test year are attributable to meeting operational goals of the type approved by the Commission in that case. Similarly, ComEd addressed the concerns identified in Docket No. 07-0566 with the LTIP metrics by eliminating the net income and legislative/regulatory goals from the plan for 2010, thereby insuring that all LTIP costs ComEd will incur in the future meet the Commission's cost recovery standards. (ComEd Initial Brief at 55-56).

ComEd states that the importance of assuring cost recovery for incentive compensation expense is underscored by the testimony of Mr. Apple, President of IBEW Local 15, who testified that ComEd employees represented by IBEW rely on incentive compensation as part of their pay and proposals to disallow recovery of those costs threaten the interests of IBEW employees in this component of their compensation.

ComEd asserts that AG/CUB witness Smith's proposal to disallow 50% of ComEd's 2009 AIP expense should be rejected. According to ComEd, this disallowance is inappropriate because the extraordinary one-time limitations ComEd imposed on the 2010 incentive compensation plan were intended to reduce expenses below the reasonable levels reflected in the 2009 test year. ComEd states that the expected reduction in 2010 incentive compensation does not reflect the reasonable, ongoing costs that ComEd will incur. ComEd points out that Staff witness Pearce

initially proposed significant reductions in AIP cost recovery, but has withdrawn those proposals in light of information provided by ComEd in its rebuttal testimony. (ComEd Initial Brief at 56-57; Staff Ex. 18.0 at 18).

ComEd avers that in its last rate case the Commission disallowed two-thirds of the costs of the LTIP, reasoning that two of the three metrics governing benefits under the plan – setting net income and legislative/regulatory goals – did not benefit customers and therefore shareholders should bear the associated costs. (*See,* docket 07-0566, Final Order at 61). In this case, ComEd witness Trpik noted that for years 2010 and following, ComEd has eliminated these net income and regulatory goals. (ComEd Ex. 4.0 Rev. at 26-27).

Staff witness Ms. Pearce observed that a new goal related to Exelon had become part of the 2010 LTIP, a goal within which, two of the three milestones are either not related to delivery services or have not been approved for recovery in delivery services rates. Accordingly, Staff recommends a disallowance of two-thirds of this 25% weighted goal, or about 17% of the LTIP costs. *Id.,* 19:437-48. This disallowance has a value of about $2.7 million. (ComEd Initial Brief at 57-58). According to ComEd, however, Staff's modified disallowance should be rejected. Mr. Trpik testified that the two milestones found objectionable by Staff - - specific emissions targets and Smart Grid - - are specific operational metrics of the type the Commission has repeatedly approved as appropriate bases for recoverable incentive compensation expenses. ComEd further argues that both metrics provide benefits to customers and are appropriate goals for a delivery services company to aspire to achieve. (ComEd Initial Brief at 57-58).

ComEd states that AG/CUB witness Mr. Smith is misguided when opposing any LTIP cost recovery on the grounds that no customer benefits are provided at all. According to ComEd, this position is out of step with the Commission decision in Docket No. 07-0566 which found at least one of the three metrics to produce customer benefit. ComEd also maintains that it is out of step with its actions in changing the 2010 LTIP to eliminate the two metrics the Commission found not to provide customer benefits; and Staff's position that only 17% of the LTIP costs are questionable.

In response to the recommendation that both Staff and AG/CUB made to disallow 100% of the costs of the Exelon 2009 Key Manager Restricted Stock Award, ComEd states that the basis for this argument is that the objective of the Award is to further the financial and operational success of Exelon, not ComEd, and that the Award provides no direct benefit to customers. However, ComEd continues, the evidence shows, by contrast, that this long-term incentive program for ComEd's Key Managers provides the same sort of benefits as the LTIP, as it "incentivizes" managers to remain focused on the long-term health of the business. (*Id.* at 59).

ComEd disagrees with CUB's contention that incentive compensation is no longer necessary at the level that ComEd pays because of the high unemployment rate. ComEd states that it makes a portion of each employee's pay subject to achievement of

operational metrics specified in incentive compensation plans. To assure that the combination of base pay and incentive compensation is set at market rates, the annual incentive compensation levels are reviewed on a periodic basis by Towers Watson. Towers Watson examines the structure of the plan and the compensation payouts resulting from it. (ComEd Reply Brief 75-76).

CUB's Position

According to CUB, it is well-established by the Commission that a utility can recover those incentive compensation costs that are reasonable, related to utility services, and of benefit to ratepayers or utility service. (*See,* docket 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. In CUB's opinion, ComEd has failed to identify tangible benefits to ratepayers in its incentive compensation plans, and each should be adjusted accordingly. (CUB Initial Brief at 21).

CUB also states that ComEd 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. (*Id.* at 22).

CUB states that in its materials regarding AIP, ComEd has made it clear to employees and shareholders that the AIP is subject to reduction. In December 2009, Exelon announced significant changes that will affect the AIP, effectively cutting AIP payouts in half for 2010. However, CUB avers, ComEd 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. CUB contends that it is also simply appropriate for shareholders to bear some or all of the incentive plan costs, specifically, the 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, CUB continues, ComEd redesigned its AIP in an attempt to circumvent the sharing of such costs between ratepayers and shareholders. CUB states the ComEd'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. CUB asserts that 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, CUB Initial Brief at 22-24).

CUB further avers that ComEd's executive LTIP pays out to executives who meet certain operational and cost controls over time. 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. However, according to CUB, the performance goals under the plan continue to driven by financial and legislative goals that benefit shareholders. For example, CUB continues, Exelon's 10-K, in its description of the executive LTIP specifically names avoidance of adverse legislation as one of the

metrics considered. The Company is well aware that lobbying is typically disallowed for ratemaking purposes. The 10-K also names financial goals, such as a certain return on equity. (AG/CUB Ex. 3.0 at 17-20). CUB further states that ComEd has requested inclusion of 100% of executive LTIP in rates, but has failed to demonstrate tangible benefits to ratepayers for any part of LTIP. CUB concludes that 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).

With regard to ComEd's Key Manager Restricted Stock program, CUB states that it is limited primarily to directors and managers, who are awarded shares of Exelon stock. CUB maintains that this program is designed to improve ComEd and Exelon performance for the benefit of shareholders. CUB concludes that it provides no tangible benefit to ratepayers, as the objectives of maximizing shareholder value are generally opposed to the objectives of minimizing costs to ratepayers. CUB concludes that this program is obviously tied solely to shareholder interests and it must be disallowed. This results in a reduction of $2.123 million. (AG/CUB Ex. 7.1 Schedule C-10; CUB Initial Brief at 24-25).

Staff's Position

Staff witness Ms. Pearce maintains that two of three goals (within a metric that is weighted at 25 percent) are not recoverable in delivery services rates; therefore, she proposes to disallow 17 percent of costs (i.e., two-thirds of 25 percent) related to the LTIP – Cash in the 2009 test year. The specific goals, for which, Ms. Pearce proposes to disallow related costs are: achievement of specific emissions targets and Smart Grid. Staff witness Pearce contends that achievement of specific emissions targets is a goal not related to delivery services. She further contends that the Commission has not approved Smart Grid costs for recovery in base delivery services rates; therefore, the cost of achieving this goal is not recoverable either. (Staff Ex. 18.0 at 19; Staff Reply Brief at 29-30).

Staff strongly disagrees with ComEd witness Mr. Trpik's contention that the two goals at issue are the type of operational metrics the Commission has approved in delivery services rates. According to Staff, an underlying premise for recovery of any cost through delivery service rates is that the cost must relate to the provision of delivery services. Another premise underlying cost recovery is that the cost must be ordinary and necessary, and prudently incurred for the provision of delivery services. Other than Mr. Trpik's bald assertion that the achievement of emissions targets is a worthy goal for a delivery services company, ComEd provides no support for recovery of these costs through delivery service rates. (Staff Reply Brief at 30).

The second goal at issue, Staff continues, related to implementation of Smart Grid, has not yet been approved for recovery in the delivery service rates. According to Staff, ComEd provided no support for recovery of these costs other than the contention of Mr. Trpik. Recoverable costs must be ordinary and necessary, and prudently incurred for the provision of delivery services, as well as used and useful. Staff acknowledges that ComEd has requested permission to recover the cost of Smart Grid in the instant proceeding via the bridge tariff, the Commission has not yet approved

these costs for recovery in base delivery service rates. Staff concludes that ComEd is attempting to use circular reasoning by using its request for recovery of Smart Grid costs in the instant proceeding to support its position that achievement of Smart Grid goals in the incentive compensation plan are ordinary, necessary and prudently incurred costs that are properly recoverable in delivery service rates. (Staff Ex. 18.0, Schedule 18.04; Staff Reply Brief at 30-31).

With regard to the LTIP- Restricted Stock plan, Staff witness Pearce proposed to disallow 100 percent of costs related to the Exelon 2009 Key Manager Restricted Stock Award, referenced herein as the LTIP – Restricted Stock Plan. Staff makes this recommendation because the objectives of the plan are to further the financial and operational success of Exelon, not ComEd. Staff asserts that this plan provided no benefits to ComEd ratepayers.

Staff disagrees with ComEd's assertion that the LTIP – Restricted Stock Plan provides the same benefits as the LTIP – Cash because compensation in the form of restricted stock incentivizes managers to stay focused on the long-term health of the business. Staff responds that the "business" referred to by the Company would be that of Exelon, not ComEd, since managers receive shares of Exelon restricted stock, not ComEd. Staff notes that the financial success of Exelon is favorably impacted by ComEd rate increases. Additionally, Staff maintains, ComEd made no showing that Exelon's financial and operational success directly benefits ComEd ratepayers. (Staff Ex. 18.0 at. 20; Staff Reply Brief at 31-32).

Finally, Staff disagrees with ComEd's argument that denial of 100% of the cost of the Key Manager Compensation Program would require ComEd to adjust this program to provide an alternative form of compensation but would lose the linkage to long-term performance. Staff notes that ComEd could modify its plan to align the interest of management and ratepayers, as Mr. Trpik asserts has been done with the AIP for Senior Vice Presidents and higher level executives. Staff concludes that based on the evidence presented, it is clear that this program is designed to align the interests of ComEd's key managers with those of Exelon shareholders. Staff proposes a disallowance of 100 percent of the costs related to this program. (Staff Reply Brief at 32).

Analysis and Conclusions

We disagree with CUB's argument regarding the AIP Program. This Commission has a long-standing policy of allowing Incentive Compensation costs when those costs benefit ratepayers. We fail to see how a high unemployment rate factors into the benefits for ratepayers. Additionally, cuts that ComEd may make to this program outside the test year are not germane. Also, as ComEd points out, according to ComEd witness Mr. Trpik, in 2010, ComEd paid out 100% of the costs submitted in its rate filing. (ComEd Reply Brief at 77; ComEd Ex. 28.0 at 4). Staff witness Ms. Pearce reviewed the AIP Program, and concluded that except for two metrics, the program, in fact, benefits ratepayers. The actual documents defining the program as opposed to Exelon's 10-K statement, is the best evidence regarding its application and parameters. We decline to adopt CUB's proffered adjustment regarding the AIP Program. Therefore, 100% of the cost of this program is approved.

However, we also disagree with Staff's recommended disallowance regarding the LTIP program. Emission reduction and Smart Grid benefit ratepayers. Smart Grid in general increases the efficiency of the grid, which ultimately reduces the costs that delivery service customers bear. Additionally, emission reduction is an important goal for the quality of ratepayers' well-being. We therefore decline to adopt Staff's proffered adjustment regarding the LTIP Program. 100% of the cost of this program is approved.

This leaves the Exelon 2009 Key Manager Restricted Stock Award Program. Both Staff and CUB witness Mr. Smith recommend disallowing 100% of this program. Both Ms. Pearce and Mr. Smith opine that this program benefits Exelon, not ratepayers. The sole basis proffered by ComEd for including this expense in rates is that it "incentivizes" management. (See, ComEd Initial Brief at 59). However, the same can be said for any incentive compensation program. ComEd has failed to prove that this program benefits ratepayers. Indeed, according to Staff witness Ms. Pearce, the purpose of this plan is to further the financial and operational success of Exelon. ComEd has not presented any evidence indicating that this is incorrect, or, that Exelon's financial success benefits ratepayers. 100% of the cost of this program is therefore disallowed.

2. Rate Case Expenses

Rate Case Expenses of the Instant Case

Background

ComEd seeks to recover $8.5 million in expenses that it states were necessary in order for it to bring this rate case and also, for its alternative regulation case to be amortized over three years. It has accordingly included a $2.833 million amortization amount in its revenue requirement. (ComEd Initial Brief at 59).

The AG avers here that ComEd proposes to amortize this $8.5 million in attorney's fees and expert witness costs, as well as related costs over three years, resulting in an annual expense to ratepayers of $2.833 million. In ComEd's last rate case, docket 07-0566, ComEd identified $10.5 million as rate case expense. The AG asserts that the Order in that docket shows that ComEd originally asked for $11.5 million, amortized over three years, but it accepted a $1 million reduction to $10.5 million. (*See,* docket 07-0566, Order of September 10, 2008, at 52-53). There were no contested rate case expense adjustments in that case. Also, the the Order did not include a specific assessment of the fees making up the total expense.

In 2009, after the Order in docket 07-0566 (ComEd's last rate case) was entered, the General Assembly amended the Public Utilities Act to require the Commission to closely review rate case expense.[2] Now, Section 9-229 of the Public Utilities Act provides:

[2] This statute became effective on July 10, 2009.

Consideration of attorney and expert compensation as an expense.

> The Commission shall specifically assess the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. This issue shall be expressly addressed in the Commission's final order.

(220 ILCS 5/9-229). Before enactment of this statute, there really were no statutory or regulatory requirements regarding rate case expense.

Whether to Treat Rate Case Expense as a Regulatory Asset or a "Normal" Expense

The AG's Position

The AG states that, in addition to the $8.5 million in rate case expense for this case, ComEd originally sought to include in this docket $7.1 million in rates, for the amortization of its: (1) rate case costs from its last rate case; (2) its last rate case costs on rehearing; (3) amortization of rate case costs from docket 05-0597; (ComEd's more previous rate case) and also (4) costs for ComEd's original cost audit, on the grounds that these items are expenses in the 2009 test year. Both Staff witness Ms. Hathhorn and AG/CUB witness Mr. Smith testified that most of these costs would be recovered by the time that the rates in this case are implemented. They surmised, therefore, that it was unjust and unreasonable to include these costs in rates, even though they were 2009 test year expenses. (*See,* Staff Ex. 2 at 3-6; AG/CUB Ex. 3.0 at 38-42). ComEd accepted these adjustments and they are no longer contested. These adjustments remove $6.6 million of the original $7.1 million request for previous rate case expense expenditures. (AG Initial Brief at 50-51).

The AG opines that, although the costs involved for a rate case are incurred the year that the rates are set, the new rates remain in effect until the next rate case is resolved. The AG points out that, in order to match the cost with the benefit, rate case expense is spread over a period of time that is expected to correspond to the time period between rate cases. Rate case expense, the AG argues, is no different from any other expense that is incurred in a single year, but, it has a longer effective period. (AG/CUB Ex. 3.0 at 47).

The AG avers that therefore, rate case expense should not be treated as a regulatory asset that is entitled to dollar-for-dollar assured recovery. Rather, it continues, a new rate case should result in a new rate case expense that replaces, but does not add to, previous rate case expense. The AG asserts that when rate case expense is treated as a regulatory asset, consumers pay for more than one rate case expense in the same set of rates. The AG views this as an "inappropriate" way to treat an expense that is essentially an operating expense. It argues that the amortization approach to rate case expense that ComEd proffers here is unfair to consumers and it is inconsistent with the fundamental legal principles underlying the regulatory bargain, which is premised on the fact that a utility controls its costs between rate cases. (AG Initial Brief at 51-52). The AG opines that its proposal provides a utility with the

incentive to efficiently manage its operations and stretch the period between rate cases, so that it can retain the benefit of the rate case expense amortization over a longer period. In support, the AG cites a West Virginia Public Service Commission decision, West Virginia PSC docket 08-0900-W-42T. (AG Initial Brief at 53).

CUB's Position

CUB also argues that rate case expenses should be normalized over three years rather than amortized, as ComEd has proposed. CUB concludes that ratepayers are at risk for over-paying for a utility's rate case expense, if too short of a period for amortization is used. 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, ComEd continued to recover on that expense which has already been fully reimbursed. CUB concludes that this same risk is present here. If a three-year amortization period 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. CUB asserts that moving to a normalization approach for rate case expense, such as that which is used for O&M expense, helps to mitigate that risk. (CUB Initial Brief at 27).

Staff's Position

Staff recommends rejecting this recommendation. Staff states that AG/CUB witness Mr. Smith discussed implementing the change prospectively, but he proposed no normalized amount. Staff disagrees with the AG/CUB recommendation because this argument could apply not only to rate case expense, but also to any regulatory asset. If adopted, Staff opines that this recommendation could lead to the unintended consequence of denying amortizations of all future regulatory assets in favor of only normalized expenses. (Staff Initial Brief at 42-43).

ComEd's Position

According to ComEd, the AG's and CUB's articulated concern about "overpayment" is simply another variant of their consistent effort to have the Commission decide individual issues in an incorrect and inconsistent manner in an attempt to drive down ComEd's revenue requirement. ComEd avers that the focus on costs that might be continue to be reflected in rates after they have been "recovered" ignores the possibility that a great number and variety of new costs that arise after a rate order is entered will not be reflected in rates set in this or any other rate case. ComEd also contends that this proposal is vague. It also points out that such "normalization" has not been the practice in Illinois. (ComEd Reply Brief at 79-80).

Analysis and Conclusions

We decline to "normalize" ComEd's rate case expense. We note that this proposal is vague. As such, it is not workable. Also, the term "normalize" is one that is traditionally associated with the expenditures for day-to-day operations, like office supplies. Rate case expense is not a day-to-day operational cost; it is an extraordinary cost that occurs sporadically.

However, AG/CUB witness Mr. Smith's point, which is that when rate case expense is treated as a regulatory asset, consumers can be paying, and often are

paying, for more than one rate case expense in the same set of rates, is not without merit. Rate case expense is amortized over a number of years because that number of years is an approximation of the time between rate cases. Increasingly, a number of utilities, including ComEd, have filed for rate increases once every two years (approximately). In such a situation, the rate case expense for the previous rate case is often still being amortized while a utility seeks rate case expense for the new rate case. As shall be set forth below, a rulemaking shall be opened regarding rate case expense. This issue shall be examined during the rulemaking process.

Legal Costs Related to Dr. Hewings' and Dr. Andrade's Testimony

Staff's Position

Staff proposes disallowing $15,000 and $10,000 in consultant and external legal fees, respectively, for the preparation of Dr. Hewings' testimony, ComEd Ex. 2.0. Staff also proposes to disallow $13,000 and $8,000 in consultant and external legal fees, respectively, for the preparation of Dr. Andrade's testimony, ComEd Ex. 3.0, for a total disallowance on this issue of $36,000. Staff notes that in a September 17, 2010 ruling, the Administrative Law Judges ("ALJs") granted a Motion to Strike Dr. Hewings' testimony and stated that his testimony was irrelevant. Because Dr. Hewings' testimony is not relevant and not related to whether ComEd should receive a rate increase or related rate-related issues, Staff concludes that it is not reasonable to include the costs for preparation and review of irrelevant testimony in rate case expense. In the ALJ ruling that struck ComEd's witness Dr. Hewings' testimony, the ALJs also struck Dr. Andrade's testimony concerning whether ComEd has been "a good corporate citizen" or whether its employees have been involved in charitable activities. In the ruling, the ALJs ordered ComEd to file revised testimony. (Staff Ex. Initial Brief at 40-41).

ComEd's Position

ComEd argues that the cost of the testimony in question was incurred in good faith, and states the disallowance can only be done with the benefit of hindsight review. (ComEd Ex. 30.0 at. 15). ComEd also points out that the testimony of both Dr. Andrade and Dr. Hewings has been admitted into evidence as rebuttal and surrebuttal testimony, thus, this dispute should be moot. (ComEd Initial Brief at 60-61).

The AG's Position

The AG also asserts that the cost of Dr. Hewings' and Dr. Andrade's testimony should not be allowed. The AG acknowledges that this testimony was admitted into evidence, but states that while ComEd is free to present this testimony, it should not expect ratepayers to pay for it. (AG Initial Brief at 57-59).

CUB's Position

CUB also assets that this evidence, as well as other evidence related to economic development, should be disallowed. (*See,* CUB Initial Brief at 26-27).

Analysis and Conclusions

The legal process has a variety of tools available to parties who view evidence as irrelevant. They include motions to strike, motions *in limine* and objections to the

admission of evidence while the case is being tried. As ComEd correctly points out, the testimony of Drs. Andrade and Hewings were admitted into evidence, without objection. While this testimony was previously stricken as irrelevant, it still was later admitted without objection. We cannot now disallow the cost of this testimony based on the fact that it is irrelevant. Presumably, if this testimony were irrelevant, a party would have objected to its admission on that basis. Indeed, it is the parties' responsibility to ensure that the evidence submitted conforms with the rules of evidence. We encourage all parties to use the legal tools available to them in the future.

However, there is no evidence that the costs charged by these two witnesses are reasonable. These two witness' testimony is unlike the situation with attorney's fees or certain types of expert witnesses, where the parties at least have the charges incurred in other cases or in previous cases as a guideline to determine the reasonableness of the charges. That is not the case with these two witnesses. Also, they prepared short pieces testimony with few facts therein. Therefore, the charges for these two witnesses ($25,000 for Dr. Hewings and $21,000 for Dr. Andrade) are not just and reasonable. They are reduced therefore by half. ($12,500 for Dr. Hewings and $10,500 for Dr. Andrade).

Other Economic Development Evidence

The AG's Position

The AG contends that the testimony of ComEd witnesses Drs. Andrade and Hewings were only a small portion of the economic development and job creation related expenses that ComEd included in its rate case expense. ComEd seeks to recover a total of $225,000 for experts and witnesses concerning "Economic Development/Job Creation." (*See,* AG/CUB Ex. 9.0 at 21). The AG avers that ComEd Exhibit 56.3, page 2, shows at line 12 that ComEd has been billed $101,030 in charges by "Chicago Partners" for "Economic Dev/Jobs Creation and Retention." The invoice for "Chicago Partners," admitted as AG Cross Exhibit 18, demonstrates that it billed ComEd hourly rates ranging from $225 to $980 per hour, with more than 100 hours billed at $580 per hour in May of 2010 alone. (*See,* AG/CUB Ex. 9.0 at 22; AG Cross Ex. 18 at CRC0035555, at CRC0035558, at CRC003555560; AG Initial Brief at 55).

The AG argues that the billing in question establishes that the services provided were not related to the costs that ComEd incurs to serve customers. Instead, the AG avers, this testimony addresses general economic conditions. For example, the consultants "reviewed papers and articles" and "reviewed literature on unemployment," and "Examined CPS data." (*See, id*. at CRC0035552, 04/01/10 and 04/02/10). The AG points out that, although the billing indicates the consultants "worked on econometric model and analysis," they offered no testimony. Also, Dr. Hewings, the ComEd witness on this issue, did not refer to anything done by the "Chicago Partners." Instead, he presented a model that was developed by the Regional Economics Applications Laboratory at the University of Illinois-Chicago. (*See*, ComEd Ex. 43.0 at 1 and 43.1). According to the AG, there is no evidence suggesting that any of this work was used in the rate case or related to ComEd's cost of service. The AG concludes that therefore, the bills for the "Chicago Partners" should be entirely excluded from rate case expense. The AG additionally asserts that the hourly rates that ratepayers are expected to pay for

this work is extremely high. The AG concludes that it is unreasonable and unjust to expect ratepayers to pay for services unrelated to ratemaking at rates that were up to $980 per hour. (AG Initial Brief at 55-56).

CUB's Position

CUB states that ComEd improperly included expenses for consultants who provide no testimony regarding rate analysis, but nevertheless billed at rates ranging from l $225 to $980 per hour, with no more detail than "services rendered in the month of April" to justify some amounts. CUB concludes that $980 an hour to a consultant who presents no testimony, with no description of services, is "outlandish" to ask ratepayers to pay. (CUB Initial Brief at 26).

ComEd's Position

In response to the adjustments recommended by AG/CUB witness Mr. Smith, ComEd cites to the testimony of its witness Mr. Fruehe, who stated that:

> In preparation for this rate case, ComEd sought the opinion and assistance of several consultants, one of which was Chicago Partners. Although ComEd ultimately chose to present the testimony of Dr. Hewings and Dr. Andrade in regards to the issue of Economic Development and Jobs Creation, it does not diminish the upfront investigation of the issue. . .
>
> (ComEd Ex. 56.0 Rev. at 14; ComEd Initial Brief at 60-61).

In its Reply Brief, ComEd states that AG/CUB attempt to make much of the fact that ComEd has paid hourly rates of "almost $1,000 per hour" to certain consultants at a single firm. However, it states, only six hours of time was billed at $980 per hour, while the average hourly rate billed by the firm was about $440. ComEd concludes that the rhetorical value of the point far outweighs its "miniscule" financial significance. (ComEd Reply Brief at 78-79).

Analysis and Conclusions

There is no evidence here indicating what the "Chicago Partners" did for ComEd. As the AG points out, it appears that there was no testimony proffered by this entity and ComEd has not presented any indication that the "Chicago Partners" otherwise proffered or assisted with the preparation of evidence. We further note that Mr. Fruehe's testimony, cited above, indicates that ComEd may have, in fact, chosen not to use whatever the "Chicago Partners" prepared for ComEd. ComEd proffers no explanation for what appears to be ComEd's decision to "go forward" with the expenses involved regarding the "Chicago Partners" at a point in time when it appears that ComEd was not certain whether to use whatever that entity provided to ComEd in this docket. Further, because ComEd has not established what the "Chicago Partners" did for it, we cannot state that hourly rates of $980 and $440 are just and reasonable. The fees for the "Chicago Partners are disallowed, in their entirety.

Multiple Cost of Capital, ROE (Return on Equity) and Financial Witnesses

The AG's Position

The AG argues that the costs that ComEd seeks to recover from ratepayers regarding ComEd's cost of capital should be closely assessed. It points out that ComEd offered four non-Company witnesses who testified in support of the 11.5% return on equity that ComEd requested. Those witnesses are:

Susan Abbott/Steven Fetter, ComEd Exhibits 5.0, 45.0, 63

Samuel Hadaway, ComEd Exhibits 11.0, 37.0, 62
Carl Seligson, ComEd Exhibits 12.0, 38.0

Susan Tierney, ComEd Exhibits 13.0, 39.0, 64

ComEd has included $360,000 for cost of capital witnesses. In addition, ComEd proffered (employee) witnesses Mr. Guerra, ComEd Ex. 1.0 at 18, 25.0 at 15-16; Mr. Trpik, ComEd Ex. 4.0 at 21; Mr. Fruehe, ComEd Ex. 30 at 25-28 all address the cost of capital. (AG Initial Brief at 59-60).

The AG avers that ComEd estimated that its cost of capital witness and ROE witnesses costs to be $200,000; its Financial Witness costs to be $60,000, and the testimony of Susan Tierney of the Analysis Group, would be an additional $100,000. The AG argues that this is an extraordinary number of witnesses testifying in support of a cost of equity number, in comparison to other cases before the Commission and to the testimony offered by Staff and intervening parties. The AG posits that ComEd offered the ROE testimony of two witness (Seligson and Hadaway), who testified about rating agencies (Abbott and Fetter), and also, a witness who argued that the ROE recommended by ComEd should be increased beyond that which was recommended by the other two ROE witnesses, and finally, a rebuttal witness who testified about investor confidence in the regulatory process (O'Connor). Finally, the AG asserts that ComEd paid a sixth expert, Paul Moul, to provide a cost of capital analysis, in addition to that which was actually presented in testimony. (Tr. 2475-76; AG Initial Brief at 60).

By contrast, the AG continues, the ICC Staff presented the testimony of Michael McNally on the cost of capital and he responded to ComEd witnesses Freuhe, Seligson and Hadaway. (Staff Exs. 5, 20). Staff also presented the testimony of Mr. Brightwell who responded specifically to Ms. Tierney's testimony to increase the return on equity to account for lost revenues. (Staff Exs. 8, 23). The IIEC presented one witness, Mr. Gorman, regarding all cost of capital issues. (IIEC Exs. 1.0, 4.0). The AG and CUB offered a single cost of capital witness, Mr. Thomas, who responded to all ComEd cost of capital witnesses, including Ms. Tierney. The AG concludes that ComEd did not explain why it was necessary to offer the testimony of so many outside witnesses in connection with this issue. The AG also posits that having so many witnesses testify regarding these limited matters places an unreasonable burden on other parties, who limited their expenditures to the usual, single cost of equity witness.

The AG additionally asserts that the Commission should not approve a charge of more than $100,000 for cost of equity testimony because the analysis that goes into

cost of equity determinations is well-settled. Although ComEd is free to spend as much as it pleases to find the cost of equity recommendation it prefers, the AG opines that there is no justification for requiring ratepayers to cover twice the customary cost to bring in more than one expert. The AG recommends reducing the cost of equity charge included in rate case expense to no more than $100,000. (AG Initial Brief at 61).

The AG further maintains that the Commission should specifically assess whether it is just and reasonable for consumers to pay for testimony about how rating agencies view the actions of the Commission. The AG points out that Ms. Abbott, Mr. Fetter, and Mr. O'Connor did not testify regarding the costs that ComEd incurred. Instead, they testified that the Commission should tailor its decisions in accordance with how the rating agencies view the Commission. The AG maintains, however, that Commission decisions must be made based on Illinois law and on the record presented for decision, not on the opinions of credit rating agencies about whether a Commission in general, or particular Commission decision, supports utilities. (See, *e.g.* Tr. at 193-194). The AG concludes that the specific expert testimony offered by Ms. Abbott, Mr. Fetter, and Mr. O'Connor is not relevant to the Commission's decision in this docket, and it is not just and reasonable for consumers to pay for this testimony. (AG Initial Brief at 61-62).

The AG maintains that ComEd also seeks to charge consumers another $100,000 to pay Ms. Tierney for testimony, in which, she states that the Commission should increase an otherwise justified return on equity by 40 basis points to compensate ComEd for what ComEd is required to do by statute. The AG contends that the Public Utilities Act provides specific direction as to how energy efficiency obligations and costs are to be treated. It specifically authorizes dollar-for-dollar recovery of energy efficient costs through an "automatic adjustment clause tariff," which limits ComEd's annual energy efficiency obligations, so that the cost of those efforts is less than 2.015% of rates, citing 220 ILCS 5/8-103(d) and (e). According to the AG, these statutory provisions are inconsistent with ComEd's proposal to increase its ROE by 40 basis points due to energy efficiency. The AG also asserts that, as Staff witness Mr. Brightwell testified, the 40 basis point "adder" does not promote energy efficiency. In assessing whether it is just and reasonable to ask ratepayers to pay for this testimony, the AG asserts that consideration should be made regarding whether the expert testimony that ratepayers are expected to pay for is contrary to the legislative scheme to promote energy efficiency, and whether Ms. Tierney's proposal achieves either the result that ComEd seeks or, a result that is consistent with the law. (AG Initial Brief at 62).

Finally, according to the AG, the bills for Ms. Tierney raise additional questions. Although ComEd estimated her testimony to cost $100,000, as of November 30, 2010, she had billed $213,608.74, more than twice the estimate amount. (*See,* ComEd Ex. 56.3, page 2, line 20. Her hourly rate is $655. (*See,* Tr. 1823). The AG argues that Commission approval is not warranted when the charges are this high. (AG Initial Brief at 63).

CUB's Position

CUB also posits that the cost of equity charges in rate case expense should be reduced by $260,000. (*See, e.g.,* CUB Initial Brief at 26-27).

Staff's Position

Staff adopts AG/CUB's recommendation to reduce the cost of equity charge to $100,000 for a single ROE witness, as is set forth in the testimony of AG/CUB witness Mr. Smith. (*See,* AG/CUB Ex. 9.0 at 26). Staff concurs with Mr. Smith's observation that it is rare for any company to proffer more than one cost of common equity consultant. Here, Staff continues, ComEd seeks to recover the costs for several such outside consultants, which are in addition to Company witnesses Trpik, Fruehe, and Houtsma, who also "weighed in" on ComEd's cost of capital. Staff concludes that customers should not be required to pay for utility's choice to hire an excessive number of consultants, who may or may not even present testimony. (Staff Initial Brief at 41).

ComEd's Position

ComEd is of the opinion that capping the costs associated with its cost of capital witnesses at $100,000 is not "proper." It is not the case, it continues, that all four witnesses provided cost of equity calculations and testimony. According to ComEd, only Dr. Hadaway and Mr. Seligson provided testimony regarding the calculation of ComEd's "base" cost of equity. Additionally, according to ComEd, Dr. Tierney testified about the propriety of ComEd's proposed 40 basis point "adder" to the base cost of equity in order to account for revenue loss due to the Illinois' "aggressive" energy efficiency requirements, as well as regarding the prudence of ComEd's 2009 pension contribution. Ms. Abbott, whose direct testimony was adopted by Mr. Fetter after her death during this proceeding, explained the relationship between this case and credit ratings. ComEd additionally states that AG/CUB witness Mr. Smith's proposed disallowance for the work of P. Moul and Associates is incorrect because, as Mr. Fruehe described in his rebuttal testimony, Mr. Moul provided additional insight to the critically important cost of equity issue, an issue that accounts for nearly $100 million of the difference between ComEd's revenue request and Staff's recommendation. (ComEd Initial Brief at 61).

Analysis and Conclusions

We note at the outset that Section 9-229 of the Public Utilities Act now requires the Commission to specifically assess the justness and reasonableness of the expert witness fees in rate case expense. (220 ILCS 5/9-229). We agree with ComEd that the amount of witnesses on a topic is not necessarily indicative of the fact that these experts were not necessary. We also agree with Staff's and the AG/CUB's argument that, at some point, the deck "is stacked" against them (as they have limited funds) merely due to the volume of experts that a utility proffers with seemingly unlimited funds coming from rate case expense, which the general public pays for in rates. As shall be set forth more fully below, this type of issue is one that has been confronted by the

federal and Illinois courts for decades when entertaining fee petitions in a variety of settings, including Title VII, petitions filed pursuant to 42 U.S.C. Sec. 1988, the Ill. Freedom of Information Act, the Ill. Human Rights Act, the Ill. Nursing Home Care Act and myriad other laws. This issue is illustrative of the necessity for a rulemaking regarding how to apply the new law, (220 ILCS 5/9-229) and the need to assess what a well-established body of law regarding fee petitions can aid in this regard.

However, while we make no assessment as to the correct number of witnesses regarding return on equity, the AG has demonstrated that $360,000 for many witnesses is not something that is just and reasonable for the ratepayers to bear, when the usual amount of expert witnesses on this issue is but one. We also disagree with ComEd's assertion that ComEd only presented two, not four return on equity witnesses. Only two of those witnesses may have been "base ROE" but the fact remains that Ms. Tierney and Mr. Fetter presented return on equity evidence; they just presented evidence regarding discreet portions of return on equity. (ROE).

We also disagree with the AG's argument that the testimony of Mr. Fetter, Ms. Abbott and Mr. O'Connor should be disallowed because it is irrelevant. As was the case with Drs. Andrade and Hewing, we note that this evidence was admitted into evidence without objection. If the AG is of the opinion that evidence is irrelevant, it should have objected to admission of this evidence. It did not.

However, one component of justness and reasonableness for rate case expense is necessity. ComEd has proffered no facts indicating that all of this testimony was necessary. While reducing $360,000 to $100,00 seems to be extreme, it does appear, based on a review of the evidence that ComEd proffered, that a reduction of $120,000 for a total amount of $240,000 reflects what could have easily proffered in terms of return on equity. We also note that much of the evidence on these issues was duplicative. Therefore, ComEd's rate case expense is reduced by $120,000.

Sullivan & Associates

The AG/CUB Position

AG Cross Exhibit 21 is a copy of Sullivan & Associates' invoices that were produced in discovery. When reviewing the invoices provided by ComEd to justify the rate case expense, AG/CUB witness Mr. Smith was not able to discern what services Sullivan & Associates provided. The AG asserts that the record is devoid of evidence about this vendor or what services it provided other than "consulting services on ComEd's 2010 Distribution Rate Filing under contract # 00127919." ComEd listed Sullivan & Associates as "consultants" for "rate case support" for $150,000 on ComEd Ex. 56.3, page 2.

The AG asserts that Sullivan & Associates' work was not explained until the Surrebuttal Testimony of ComEd witness Fruehe, who described Mr. Sullivan as "an accounting and financial contractor" who "assists in the preparation of the voluminous Part 285 filing requirement schedules and in responding to discovery." (*See,* ComEd Ex. 56.0 at 16). Mr. Fruehe did not state how Sullivan & Associates' work differed from or added to the $250,000 and $50,000 to "Prepare Data Room" and for its "Discovery Contractor." The AG concludes that, given the lack of information about what these

services entail, the Commission should decline to include the $150,000 attributable to Sullivan & Associates in rate case expense. (AG Initial Brief at 63-64; CUB Initial Brief at 26-27).

ComEd's Position

Citing no record evidence, ComEd asserts that Mr. Smith's proposed disallowance for the work of Sullivan and Associates should be rejected because, Mr. Sullivan is an accounting and financial contractor who provides a necessary and cost effective augment to ComEd's regulatory staff during rate case preparation. ComEd states that because the heavy work load associated with rate cases is intermittent, ComEd does not staff for the peak work load. ComEd avers that, in addition to having provided assistance with the voluminous Part 285 filing requirements, Mr. Sullivan assisted with the response to over 1,550 individual data requests (with their numerous subparts). According to ComEd, Mr. Sullivan was instrumental in allowing it to meet the stringent time deadlines imposed in this case for data request responses. (ComEd Initial Brief at 62).

Analysis and Conclusions

We note at the outset that the "stringent time deadlines" in this docket were necessary, in large part, due to ComEd's failure to make a complete initial rate case filing in accordance with what was mandated in the *Rate Design Investigation* Order regarding ComEd, docket 08-0532. Filing essential evidence that was required to be initially, weeks afterward, placed all entities in a bind regarding time. ComEd could have, but chose not to, remedy this situation by merely complying with the Commission's final Order in the *Rate Design Investigation* docket. Also, ComEd cites no evidence indicating that what Sullivan and Associates did to gain $150,000. If, as ComEd states, this entity was truly involved in discovery and ComEd's initial Part 285 filing, it would have been a simple matter to submit evidence setting forth what Sullivan & Associates did for ComEd or its lawyers. (*See, e.g., Raintree Health Care Center v. Ill. Human Rights Comm.,* 173 Ill. 2d 469, 494-96, 672 N.E.2d 1136 (1996)). ComEd has proffered no such evidence in support of its argument. In fact, ComEd has proffered no evidence in its briefs to substantiate this expense. Further, while ComEd avers that Sullivan & Associates assisted it with its tariff filing, that tariff filing initiated this docket. Normally, lawyers prepare whatever is necessary to initiate legal proceedings. It is clear that Sullivan & Associates is not a law firm.

We further note that even if the invoices for Sullivan & Associates did provide the evidentiary support for its inclusion in rate case expense, it was ComEd's choice to file for a rate case without all of the evidence that the decision that was required of it in the final Order in the *Rate Design Investigation* docket, docket 08-0532. Ratepayers should not have to pay for the onus on ComEd that the "stringent deadlines" that ComEd imposed on itself, as well as the parties and Commission Staff, by failing to comply with the final Order in the *Rate Design Investigation* docket.

Because ComEd has failed to substantiate what work Sullivan & Associates actually did, it cannot be said that payment to this entity is just and reasonable. The $150,000 that ComEd paid to this entity is therefore disallowed.

AG/CUB Witness Mr. Smith's General Reduction for Rate Case Expense due to Overestimations

The AG's Position

The AG states that in its Schedule C-10, ComEd included an itemized estimate of its rate case expense in four categories, which are:

- Consultants $1,770,000
- Expert Witnesses – Direct Case $ 840,000
- Post-Direct Testimony – Witnesses $ 890,000
- External Legal $5,000,000

However, the AG continues, the accounting of the amounts actually spent provided in discovery and in ComEd Exhibit 56.3 Rev. page 2, demonstrate that ComEd over-estimated its rate case costs. In assessing the rate case costs, the AG continues, it is useful to remember that ComEd filed its Direct Case on June 30, 2010 and August 9, 2010 (rate design). It then filed its non-rate design Rebuttal Testimony on November 22, 2010. ComEd Exhibit 56.3 Rev. shows ComEd's incurred or paid costs through November 30, 2010. (AG Initial Brief at 64-65).

The AG contends that it is clear, from reviewing ComEd Exhibit 56.3 Rev., page 2, that all of the non-legal costs incurred as of November 30, 2010 were assigned to either "Consultants" or "Expert Witnesses – Direct Case." Not one penny, according to the AG, was assigned to the $890,000 claimed for Post-Direct Testimony Witnesses. Also, the AG avers, none of the $890,000 cost that ComEd claims was itemized or identified. Further, the AG states, after removing the estimates and costs for Alternative Regulation, (see below) ComEd spent only 76.4% of the total claimed amount through November 30th, 2010. The AG maintains that, although ComEd presented its costs and estimates differently from the way in which Mr. Smith analyzed them, the result is not much different from Mr. Smith's conclusion that ComEd had used only 64.42% of the amount that ComEd claimed for allowed Consultants and Expert Witnesses – Direct Case as of the time of his review, which included information for one month less (through October 31, 2010) than what is contained in ComEd Ex. 56.3, page 2. (*See,* AG/CUB Ex. 9.0 at 29; AG Initial Brief at 65).

AG/CUB witness Mr. Smith recommended removing the same percentage from consultant and witness costs for Direct from the amounts that ComEd has asserted for its Post-Direct Testimony Witnesses, and apply the same 64.42% percentage of incurred cost to actual cost that he calculated up to October 31, 2010 to the $890,000 to account for the over-estimation of costs reflected in Schedule C-10. (*See,* AG/CUB Ex. 9.0 at 30-31). This results in a $661,000 reduction to the post-Direct Witnesses cost. (AG Initial Brief at 65-66).

In total, (including fees for the issues discussed above and fees for the alternative regulation docket, as well as the fees discussed in the next subsection, regarding high legal fees) Mr. Smith recommends a $2,201,340 reduction to the consultant and witness portion of the rate case expense. The AG maintains that included is $100,000 for cost overruns for the Cash Working Capital witness. ComEd

Exhibit 56.3, page 2 shows that the estimate for that entry was somewhat higher than Mr. Smith indicated on his schedule, reducing the adjustment to $61,988. This reduces his adjustment to the consultant and witness portion of the rate case expense to $2,163,328, leaving a total expert and consultant expense of $1,337,000.

The AG asserts that ComEd Ex. 56.3 Rev. page 2, shows ComEd's costs through November 30, 2010, the major portion of its Rebuttal case (non-rate design rebuttal testimony was filed on November 22, 2010). The AG argues that an increase of incurred costs to 76.4% "clearly covers" costs that should be included in the $890,000 Post-Direct Testimony expenses. However, the AG states, without an itemization, it is impossible to determine what costs are for post-Direct Testimony services. The AG argues that therefore, neither ComEd Ex. 56.3 nor Mr. Fruehe's testimony attributes any costs to Post-Direct Testimony, preventing the Commission from complying with Section 9-229 of the Public Utilities Act, which now requires this Commission to "specifically assess the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. The AG avers that therefore, ComEd has failed to meet its burden of proof to justify the expenditure of any of the $890,000 it seeks to include in the rate case expense for third-party Post-Direct Testimony. (AG Initial Brief at 66-67).

Finally, the AG asserts that a specific assessment of rate case costs requires that the Commission protect consumers from excessive rate case costs. Although the courts have recognized rate case expense as a valid test year expense, multiple entries for similar service and over-estimates of costs are not "just and reasonable," as is require by Section 9-229 of the Public Utilities Act. (AG Reply Brief at 29).

The AG states that a large portion of ComEd's claimed rate case expense is for legal fees. Of the $8.5 million requested for rate case expense, $5.0 million is for legal services, and of that, $4.025 million is for two fixed fee contracts. (*See,* Tr. 2470). However, the AG continues, due to the limited billing information provided for these two contracts, the Commission cannot use invoices to "specifically assess the justness and reasonableness of the charges, " citing 220 ILCS 5/9-229. In furtherance, the AG avers that AG Cross Exhibits 31 and 32 are copies of two invoices that ComEd produced in discovery for legal expenses. For the two fixed fee contracts, no hourly billing or description of services is included, although expenses are itemized. (*See,* Tr. 2468-70; AG Cross Ex. 31, CRC 0035415-16, CRC 0035428-29; AG Cross Ex. 32, CRC 0035790-92, CRC 0035797-99). According to the AG, only the invoices of one firm appears to be comprehensive, which are the bills for the law firm of Sidley and Austin. (AG Initial Brief at 67).

Given the large portion of legal services covered by fixed fee contracts, the AG avers that the amounts that were actually paid by ComEd do not provide the information that is necessary to assess whether the fees are "just and reasonable" at the claimed level. For example, the AG continues, the September and October invoices presented in AG Cross Exhibits 31 and 32 show that the fixed fee contracts cost ComEd $245,000 per month, while the hourly attorneys billed $37,922 (Sidley and Austin) and $45,407 and $44,283 per month (Jenner and Block). Irrespective of the work done, $245,000

per month is the equivalent of 432 hours at the top Exelon attorney rate of $566 per hour, or more than 10 weeks of senior attorney time for a single month. In the alternative, $245,000 is the equivalent of 1,025 hours of associate time at $239 per hour, or 25 weeks of attorney time in a single month. Paralegals and other support staff would be billed at lower rates. The AG contends that this Commission must assess whether it is reasonable to believe that the two fixed fee firms devoted this amount of time, in the absence of any documentation showing the number of hours performed, or, the work that was actually performed. (AG Initial Brief at 67-68).

The AG argues that therefore, in the absence of detail for these firms, the Commission, through the ALJs, is left in the position of either disallowing the costs in their entirety or trying to assess the reasonableness of the fees another way. For example, the AG continues, the Administrative Law Judges can assess the presence of legal staff at hearings or on motions, taking into account the attorneys from the fixed fee firms, the hourly firms, or from Exelon Business Services or ComEd employees, whose costs are not included in the rate case expense. The Commission can also compare the costs other utilities have requested. In the last Ameren rate case (docket 09-0306) Ameren requested a total of $4,662,000 for outside experts and legal services; the Illinois-American Water Company rate case, docket 09-0319, included a total rate case expense of $2,339,496 for a company with five different districts, rates, and revenue requirements. By contrast, the AG asserts, ComEd requests $5 million, including $4.025 million in fixed fee contracts, for legal services alone. (AG Initial Brief at 68-70).

ComEd's Position

ComEd argues that this Commission should reject Mr. Smith's proposed disallowance of the "overrun" associated with ComEd's Cash Working Capital study. This recommendation follows from AG/CUB witness Brosch's characterization of that study as "severely flawed and unreliable." ComEd asserts that Mr. Smith did not contest that ComEd spent what it claims on this study; he simply stated that it was "too much." It should go without saying, ComEd avers, that the allowance of rate case expenses for a particular piece of testimony should not depend upon whether an intervenor witness, or even ultimately the Commission itself, finds that testimony to be persuasive. ComEd further avers that this study was performed by an eminently qualified expert, Mr. Subbakrishna of Navigant Consulting, using methods that are consistent with studies accepted by the Commission in numerous recent cases involving Illinois utilities. (ComEd Initial Brief at 62).

ComEd also contends that its witness Mr. Fruehe rebuts Mr. Smith's point that, even after all of the individual expenses that he finds objectionable are eliminated, ComEd has still "over-estimated" its rate case costs, and thus another $555,000 as part of the direct case and $661,000 as part of the post-direct case should be disallowed. Mr. Fruehe testified that "data" through the end of November 2010 show that the amount ComEd has paid to consultants and expert witnesses for the direct case is relatively close to its estimate.

ComEd further argues that it is not at all surprising that its post-direct case is likely to cost more than its direct case, because its post-direct case necessarily includes the preparation and filing of both rebuttal and surrebuttal testimony, preparation of

hundreds of "data request" Responses, preparation and presentation of the witnesses for trial, preparation for and cross-examination of Staff and intervenor witnesses and preparation and filing of four rounds of post-trial briefs, as well as a proposed order and pretrial memorandum. ComEd asserts that its witness Mr. Fruehe showed that five months after the filing of its last rate case, ComEd incurred $7.1 million of rate case expenses, or about 68% of the total $10.5 million that was allowed in that case. Over the same time period in this case, ComEd has incurred just over $5 million, or about 59% of its estimated $8.5 million. This shows, according to ComEd, not only that ComEd's actual costs so far have been reduced by about $2 million, compared to its last rate case, but also that ComEd is "on track" to incur the estimated $8.5 million. (ComEd Initial Brief at 63).

Analysis and Conclusions

ComEd correctly asserts that often, more work has to be done in rebuttal in a Commission case than in the direct case is, unfortunately, often the case at this Commission. This can be especially the case in a rate proceeding, where often, there are no pleadings to guide the parties and the Administrative Law Judges. Also, ComEd has the burden of proof here, which usually entails more work than that which is done by other parties. Also, ComEd was required to prepare its witnesses for cross examination and prepare its lawyers for the cross-examination of non-ComEd witnesses. It does not appear that Mr. Smith took these tasks, which can be laborious, into account. We additionally note that there is no evidence that Mr. Smith, when calculating his percentages, took the totality of the circumstances that the practice of law, and especially practice at the Commission incurs. We therefore decline to reduce the attorney's fees in the manner proffered by the AG.

We additionally note that the AG's argument that multiple entries for similar services and over-estimates of costs are not "just and reasonable," is not persuasive. This is because the AG cited no specific example of over-estimate or multiple entries for similar services.

We also decline to reduce the fees incurred for preparation of the lead-lag study. As ComEd points out, there is no evidence that the amount billed was excessive or unreasonable.

We further decline to determine ComEd's rate case expense based upon what other utilities do, or, what was approved in other utilities' rate cases. We note that ComEd is the largest utility in Illinois and its lawyers are in the third-largest city in the United States (Chicago). It does not appear to be unreasonable, therefore, for ComEd to incur costs that are above and beyond what downstate utilities incur, or, what other, smaller, utilities incur. Additionally, we note that Sidley & Austin's participation in this docket appears to be relatively marginal. Therefore, while we agree with the AG that the level of factual specificity provided by this firm is preferable over what other firms provided, what Sidley & Austin billed for cannot provide any meaningful guidepost in terms of the amount of work that lawyers at other law firms did.

Also, on the one hand, the AG argues that it is impossible to verify the reasonableness of the attorney's fees in question, but on the other hand, it contends that an assessment of the reasonableness of these fees can be made by comparing

these fees to fees incurred in other rate cases, or, the hourly rates of other lawyers. While the AG breaks down the fixed-fee contracts, it does not state how many lawyers were provided by these contracts. Therefore, we cannot reach the conclusions that the AG reaches as to the hourly rates charged therein. While we conclude that there is nothing that is obviously unreasonable about the legal fees in this case, which are considerably less than those incurred in ComEd's last rate case, we note that no party has really addressed what impact the recent enactment of Section 9-229 of the Public Utilities Act has here. Before this statute was enacted, there was no standard regarding rate case expense. ComEd has proceeded here as though that were still the case. It is not. All utilities would be advised to provide, at the very least, an explanation of what services were performed, the amount of time involved in performing those services and, the need for whatever service was performed, in order to justify rate case expense.

We additionally note that even for large companies in Chicago, the issue of just and reasonable attorney's fees, and expert witness fees, has been examined by the federal and Illinois courts for decades, regarding fee petitions for prevailing parties in many settings, including such matter as Title VII, 42 U.S.C. Sec. 1988, the Freedom of Information Act, the Administrative Procedure Act, the ADA, the Ill. Consumer Fraud Act, the Ill. Nursing Home Care Act, and the Ill. Human Rights Act, to name a few. (*See, e.g., Rackow v. Ill. Human Rights Commission,* 152 Ill. App. 3d 1046, 1061, 504 N.E.2d 1344 (2nd Dist. 1987); *Harris Trust & Savings Bank v. American National Bank & Trust Co.,* 230 Ill. App. 3d 591, 594 N.E.2d 1308 (1st Dist. 1992); *Estate of Price v. Universal Casualty Co.,* 334 Ill. App. 3d 1010, 779 N.E. 2d 384 (1st Dist. 2002)).

The wiser course of action, for all parties concerned, including the general public, as well as ComEd and other utilities, is to open a rulemaking for the purpose of determining what must be included in rate case expense, the level of specificity involved in that inclusion, and the documentation involved. This shall include an analysis of any of the issues that are specified above for inclusion, as well as an analysis of how to incorporate well-established law on this issue regarding fee petitions into any rule that results from this rulemaking. In this way, all parties will be on notice as to what defines an expense that is categorized as a rate case expense. Also, all parties will have the benefit of knowing what is required of a utility regarding the evidence it must have in order to support attorney's fees and expert witness fees, (and like fees, such as those for support staff). We additionally assert that Section 9-229 of the Public Utilities Act is relatively new; it appears to be untested, or at least unasserted by any party in a rate case, until now.

3. Alternative Regulation (Alt. Reg.) Case Costs

Staff's Position

Staff proposes to disallow $250,000 and $496,000[3] in Alt. Reg. consultant and external legal fees, respectively. Staff avers that the costs for ComEd's Alt. Reg. docket

[3] Only one-third of these amounts are included in the total disallowance of $263,000 due to the three-year amortization period proposed by ComEd. The supporting documents for Staff's disallowance are contained in Staff Group Cross Ex. 1, pp.182-183 and 285 Public.

are costs for a separate proceeding from this rate case. They also were not incurred during the test year. (Staff Ex. 2.0 at 9 and Sch. 17.01). (*See,* ComEd Ex. 30.0 at 14). Staff disagrees with ComEd's assertion that it was able to negotiate with the R3 law firm (Rooney, Rippie and Ratnaswamy, LLP) a competitive flat rate for the delivery of legal services for the rate case, and no additional charge would be imposed for its work associated with the Alt. Reg. docket. Staff opines that the statement that a law firm would provide services at the same price for two cases as for one case alone strains credulity. It argues that the Commission should find that is unreasonable to include the Alt. Reg. costs and fees in this case. (Staff Initial Brief at 43-44).

ComEd's Position

Both Staff witness Ms. Hathhorn and AG/CUB witness Mr. Smith recommend disallowances from the $8.5 million of rate case expenses (a $2.833 million amortized amount) that they claim are related to the Alt. Reg. case. The Staff disallowance includes $496,000 for attorneys' fees attributable to two law firms and another $250,000 for consultants. Mr. Smith adopts each of these disallowances, but, according to ComEd, he relies on a withdrawn Staff recommendation to support his $2.5 million Alt. Reg. legal fee disallowance.

Although ComEd has estimated that through October 2010, the Alt. Reg. legal costs were about 11% of total legal costs, it states that virtually all of these costs would have been incurred even in the absence of the Alt. Reg. proceeding because one of ComEd's outside law firms, Rooney, Rippie & Ratnaswamy ("R3") agreed to a flat rate for all of the work on the rate case, with no additional charge imposed for whatever work the firm did on the Alt. Reg. matter. (ComEd Ex. 30. at 14). ComEd also states that that the overall (total amount that ComEd seeks for rate case expense) $8.5 million figure is reasonable because it is 20% lower than what ComEd incurred in its last rate case. (ComEd Initial Brief at 64-65).

CUB's Position

CUB states that ComEd has included Alt. Reg. litigation expenses in its request for recovery, though the Public Utilities Act allows recovery only for fees incurred as part of a "general rate case filing," citing 220 ILCS 5/9-229. According to CUB, ComEd has refused to specify exactly what amounts, for which, it seeks recovery are actually related to the Alt. Reg. litigation for every attorney and witness involved in both cases. At the very least, CUB continues, ComEd 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, CUB continues, ComEd has taken the unbelievable position that R3 law firm charged nothing extra to take on the Alt. Reg. docket. (CUB Initial Brief at 28).

According to CUB, ComEd attempted to estimate its alternative regulation costs at 11%. However, CUB opines, as shown by the testimony of Mr. Smith and Ms. Hathhorn, this estimate is grossly understated. It recommends adopting Mr. Smith's recommendation to reduce the legal fees for attorneys working on both cases by half, as, according to CUB, the attorneys' work has been split between two cases. This results in a $250,000 disallowance. (CUB Reply Brief at 18).

The AG's Position

The AG's proposed total rate case adjustment includes adjustments to remove both the cost of Alt. Reg. consultants and legal services associated with Alt. Reg. (as is subsumed in its 50% disallowance). It states that the Commission should not allow a rate case expense of more than $3,798,660, amortized over three years. This results in a test year adjustment of $1,567,000. (AG/CUB Ex. 9.0 at 31; AG Initial Brief at 73-74).

The non-legal portion of the rate case expense also included costs for the Alt. Reg. proceedings. Staff witness Ms. Hathhorn and AG/CUB witness Mr. Smith recommended removing the $250,000 that ComEd included in its rate case expense for Alt. Reg. consultants. (*See* ComEd Sch. C-10, Line 3. Staff Ex. 17.01 and AG/CUB Ex. 9.0 at 27.

The AG states that ComEd included in its rate case expense the legal costs for ComEd's Alt. Reg. case that ComEd filed while this case was pending. (docket 10-0527). Staff witness Ms. Hathhorn initially recommended that ComEd's legal expense should be cut in half to remove these services because both the rate case and the Alt. Reg. case were included in the estimate of legal costs and there was insufficient detail regarding the legal invoices involved which would verify the costs associated with each proceeding. (Staff Ex. 2.0 at 10; AG Initial Brief at 70).

AG/CUB witness Mr. Smith agreed with the asserting in Staff's Direct Testimony that legal services fees should be cut in half. Notwithstanding Staff witness Hathhorn's reduction in her adjustment to $496,000, Mr. Smith maintained that in "light of the lack of detail in ComEd's legal invoices, it is reasonable for the Commission to adopt Ms. Hathhorn's adjustment to remove 50% of ComEd's requested attorneys' fees related to Alt. Reg. and to the rate case." (AG/CUB Ex. 9.0 at 28). According to the AG, the evidence demonstrates that Ms. Hathhorn relied on ComEd's information, which underestimates the amount of legal services for Alt. Reg. case. The AG concludes that Ms. Hathhorn's adjustment in her Rebuttal testimony is too low to remove the costs of the Alt. Reg. case from the rate case expense. (AG Initial Brief at 70). In response to data requests, ComEd initially stated that it incurred approximately $270K to date that are related to Alt. Reg. legal expenses. It later updated that response to explain that the number "was based upon counsels' estimate *in the absence of specific daily time breakdowns*." (Staff Group Ex. 1, DLH 19.01 (italics added)). ComEd averred that it asked the R3 law firm, which receives $145,000 per month under a fixed fee contract, "to separately track the total hours spend working" on each docket for September and October (of 2010). *Id*. However, the AG opines, the nature of the work performed in the Alt. Reg. case in September and October, shows that this estimate is low. (AG Initial Brief at 71).

The AG avers that each case has a pattern of initial testimony, discovery, direct testimony by Staff and Intervenors, rebuttal testimony by the petitioner and Staff and Intervenors, and the petitioner's surrebuttal testimony. In both the rate case and the Alt. Reg. case, hearings for cross-examination follow, along with briefing. However, the AG continues, the period of time which ComEd measured its attorney fees (September and October) corresponded with a particularly quiet time in the Alt. Reg. case, and a

relatively quiet time in the instant rate case. In September and October, there was no Staff or Intervenor testimony to review in the Alt. Reg. docket, and testimony in the rate case was not filed until close to the end of October. (Tr. 2473). The AG concludes that therefore, the time period, during which, the legal time was estimated is not representative of the amount of time that is reasonably attributed to the Alt. Reg. case. (AG Initial Brief at 71-72).

The AG also maintains that there was no itemization of Alt. Reg. legal services. If ComEd's attorneys did track their time, the AG states that there is no documentation of that effort. Given the lack of time records produced for the R3 law firm, and the "extensive" redaction of the Jenner & Block and Foley & Lardner invoices, (*See,* AG Cross Ex. 31, CRC 0035420-27; AG Cross Ex. 32, CRC 0035793-96) the AG opines that it is impossible to verify the accuracy of ComEd's designation of Alt. Reg. legal services.

The AG contends that the Commission should reduce the $5 million that ComEd claims for legal services to $2.5 million. While this is still a sizable charge, and it is more than the total rate case expense in docket 09-0319, (for another utility) the AG states that it brings the legal expenses to a more reasonable level. It also, according to the AG, recognizes that extraneous services are included in the legal expense figure. It recognizes that the redactions and lack of itemized billing for 80% of this charge makes a specific assessment of this cost essentially impossible. It maintains that, to the extent that the Commission's decisions are not arbitrary or capricious and are rooted in credibility determinations, it "has wide latitude to use its business judgment to reach pragmatic solutions by filling gaps in the record;" citing *Commonwealth Edison v. Illinois Commerce Comm.,* 405 Ill. App. 3d 389, 937 N.E.2d 685, 701 (2nd Dist. 2010). (AG Initial Brief at 73).

The AG avers that it is difficult to discern what portion of a charge is attributable to which services, yet it is not credible to expect a firm to accept the same fee for a rate case plus a novel petition for alternative regulation, involving an untested statute and unique cost recovery methods. If the fee is high enough for the firm to "throw in" an alternative regulation petition, the AG concludes that the fee must be too high for a rate case, making an adjustment necessary. (AG Reply Brief at 30).

When assessing the level of attorney's fees in fee-shifting civil litigation, the AG maintains that Illinois courts have required the production of time records, to guard against the risks of overstatement of costs, citing *Fiorito v. Jones*, 72 Ill. 2d 73, 90-91 (1978). It concludes that, in this docket, the Commission needs more detail than a fixed fee contract to serve as a "check," in the same way that a Court requires itemized billing in a fee-shifting, class action setting. The AG additionally states that Illinois Courts have been clear that the reasonableness of fees "cannot be determined on the basis of conjecture or on the opinion or conclusions of the attorney seeking the fees," citing *LaHood v. Couri*, 236 Ill. App. 3d 641, 648 (1992), where the Appellate Court reversed a trial court order to pay the plaintiff's attorney's fee because the plaintiff did not provide sufficient records to demonstrate that its fees were reasonable.

The AG asserts that Illinois Courts regularly discuss attorney fee petitions in their orders, including the hourly rates and charges of attorneys. (AG Reply Brief at 30-31).

In a fee-shifting situation, the AG continues, the ordinary incentives applicable to the parties who pay out of their own pocket are either absent or not as strong because someone else is ultimately responsible for the bill. The need to assess the reasonableness of costs for services that one party (the utility) obtains, but another party (ratepayers) pays, requires that all relevant details must be provided. Under such circumstances, the AG continues, courts require that the party seeking fees demonstrate the reasonableness of these fees by producing "detailed information concerning the nature of the actual time expended in each of the legal tasks performed, the identity of who performed them, how they related to the litigation and whether they were necessarily required," citing *Mars v. Priester*, 205 Ill. App. 3d 1060, 1065 (1st Dist. 1990). The AG avers that, although more detail has been produced in connection with the unredacted portion of the remaining $975,000 in attorneys' fees, the bulk of the legal services charges are essentially a "black box." (AG Reply Brief at 31).

The AG further maintains that Section 9-229 of the Public Utilities Act requires a specific assessment of legal expenses. It concludes that the lack of specificity to support the legal expense makes it impossible for the Commission to conduct the assessment that this statute requires. (AG Reply Brief at 32).

Analysis and Conclusions

Section 9-229 of the Public Utilities Act, which became effective only recently, (on July 10, 2009) provides that:

> Consideration of attorney and expert compensation as an expense. The Commission shall specifically assess the justness and reasonableness of any amount expended by a public utility *to compensate attorneys or technical experts to prepare and litigate a general rate case filing*. This issue shall be expressly addressed in the Commission's final order.

(220 ILCS 5/9-229; emphasis added). Therefore, attorney's fees and expert witness fees are only recoverable here if they concern this docket. The costs incurred for ComEd's Alt. Reg. Docket do not fit within this statutory requisite. Therefore, the legal fees and expert witness fees that ComEd incurred regarding the Alt. Reg. docket cannot be included here. (*See,* docket 10-0527, generally). Because we find that this statute mandates exclusion of Alt. Reg. rate case expense, we need not address Staff's test year argument.

We also agree with Staff, the AG and CUB, that it is not credible that the Alt. Reg. docket was a "freebie," that lawyers agree to litigate, at no cost, above and beyond this docket, at no cost. We note that, to date, the Alt. Reg. docket was litigated rather extensively, (*See,* docket 10-0527, generally). This is not the sort of work that a reasonable person would agree to do at no cost.

We further agree with the AG and CUB that now, after enactment of Section 9-229 of the Public Utilities Act, recovery of rate case expense must be substantiated with specific documentation stating the work performed, the need for the work performed and justifying the reasonableness of any rate charged for that work. Otherwise, the language in that statute requiring that this Commission "shall specifically assess the justness and reasonableness of any amount expended by a public utility to compensate

attorneys or technical experts"; and the language requiring that "this issue shall be expressly addressed in the Commission's final order" are meaningless. (*See,* 220 ILCS 5/9-229). That clearly was not done here. As the AG points out, because this was not done, it is difficult to determine what work is related to the Alt. Reg. docket.

After a preliminary analysis of the e-docket in the Alt. Reg. docket, (*See,* docket 10-0527, generally) we disagree with the AG and CUB's contention that half of ComEd's attorney's fees are attributable to the Alt. Reg. docket. We note that the trial in that docket lasted three days, while the trial in this docket lasted seven days. Additionally, of those seven days, most were spent on a rigid schedule, lasting into the evening, with few breaks. Also, there are fewer parties to the Alt. Reg. docket. Further, Staff's Initial Brief in that docket contains many less issues than Staff's Initial Brief in this docket. In fact, Staff's Brief in that docket is less than half the size of Staff's Initial Brief in this docket. ComEd's Initial Brief in the Alt. Reg. docket is about a third of the size of its Initial Brief in the instant docket. The evidence filed in the Alt. Reg. docket is not nearly as extensive as the evidence in this docket. Finally, there was extensive motion practice in this docket; there does not appear that the Alt. Reg. docket had much in the way of motion practice. All of this leads us to conclude that ComEd's lawyers did not spend 50% of their time on the Alt. Reg. docket.

Staff's recommendation was determined based on a sampling of the work performed by ComEd's lawyers during a two-month period. While this evidence is imperfect, there is no evidence here that it is not accurate. While the AG argues that the two-month period in question was a "quiet time" in this proceeding and in the Alt. Reg. docket, merely because nothing was not required of an attorney at any given time does not mean that work was not performed by that attorney. This would assume that ComEd's attorneys waited until the last minute to perform the voluminous tasks that are involved in a rate case, and that are involved in a rather heavily-litigated Alt. Reg. docket. We find no evidence that this was the case. We further note that there is a strict eleven-month deadline in a rate case, which was heightened due to ComEd's failure to comply with the Commission's *Rate Design Investigation* Order in a timely fashion. We therefore decline to assume, in the absence of evidence demonstrating otherwise, that this two-month period was just a "lull" in the litigation of these two dockets.

Staff's disallowance for Alt. Reg. attorney's fees, which is approximately 18.33% of the total R3 fixed fee contract, is also more in line with what was observed in the paragraph above, which is, that ComEd's attorneys spent much less time on the Alt. Reg. docket than they spent here. We therefore adopt Staff's recommended disallowances, which are stated above, in their totality.

4. Administrative and General (A&G) Expenses

a. Exelon Way Severance Amortization

<u>ComEd's Position</u>

In the 2005 rate case, the Commission approved recovery of the Exelon Way severance costs by amortizing them over a 7 ½ year period. *Commonwealth Edison Co.*, ICC Docket No. 05-0597, Final Order (July 26, 2006) at 86-90; *Commonwealth*

Edison Co., Docket No. 05-0597, Corrected Order on Rehearing (Dec. 20, 2006) at 4. The costs were approved again by the Commission in the 2007 rate case as appropriate and necessary. *Commonwealth Edison Co.*, ICC Docket No. 07-0566, Final Order (Sept. 10, 2008) at 66. Accordingly, ComEd should continue to be allowed to recover these severance costs.

CUB's Position

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, AG/CUB Mr. Effron notes that 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.* According to Mr. Effron, 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, says Mr. Effron. AG/CUB Ex. 8.0 at 16.

ComEd argues that Mr. Effron's recommendation would disallow recovery of 40% of the costs incurred by the Company. ComEd Init. Br. at 65. This is simply not true, as the Company already recovered, by way of savings, that entire amount. *Id*. at 15-16. Therefore, CUB believes that 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, Mr. Effron testifies that 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. CUB demonstrates that the Company has fully recovered this expense, and it should now be removed. This results in an adjustment of $18,665,000. AG/CUB Ex. 7.1 Schedule C-4.

Commission Analysis and Conclusion

The Commission ordered amortization of these costs in the Order in Docket No. 05-0597. Moreover, this cost recovery was reaffirmed in Docket No. 07-0566. Moreover, this cost recovery was reaffirmed in Docket No. 07-0566. ComEd could not have recorded this as a regulatory asset and begun to amortize it in 2003 or 2004 because it was not authorized by this Commission.

AG/CUB propose that the Commission terminate any further recovery of the Exelon Way severance costs thus reducing ComEd's jurisdictional revenues by approximately $18.8 million. The Commission rejects this proposal.

b. Accounts 920-923

See Section IV.C.3.j.

c. Pension Costs

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

ComEd's Position

ComEd seeks to include $65,536,000 in actuarially determined 2010 pension costs in its revenue requirement. ComEd Ex. 6.1, Sched. C-2.2, line 3, column (F). These costs should be allowed.

To determine its pension costs, ComEd retained Towers Watson to prepare a pension valuation report that is used to determine pension costs based on the funded status of the pension plan. Towers Watson prepared a report in March 2010, and ComEd relied upon Towers Watson's work when establishing pension costs for approval in this proceeding, because use of an actuarial report of this type is standard practice in rate cases. ComEd explained that in both their 2005 and 2007 rate case proceedings, the reports used were comparable to the March 2010 report and were accepted as providing known and measureable verification of ComEd's pension and post-retirement benefit costs. Houtsma Reb., ComEd Ex. 29.0 at 31-36. Staff concurs that ComEd's adjustment based on the Towers Watson report is appropriate. Pearce Reb., Staff Ex. 18.0 at 40.

The evidence also shows that Mr. Smith's recommendation of a separate reduction of $2.424 million to remove the costs of ComEd's Supplemental Executive Retirement Plan ("SERP") should also be rejected. Smith Dir., AG/CUB Ex. 3.0 Corr. at 35. Mr. Smith did not deny that ComEd actually incurred this cost, but nonetheless deemed the expense to be one that is unreasonable and stated that if ComEd wants to provide these benefits it should do so at the expense of its shareholders. *Id.* at 34-35. Nowhere in his testimony did Mr. Smith assert that ComEd's SERP costs result in the beneficiaries of this program receiving benefits above or out of proportion to benefits received by similarly situated executives at other comparable companies. ComEd asserted in its Reply Brief that, contrary to CUB's position, IRS regulations do not purport to set a "just and reasonable" rate or have anything to do with such a rate. ComEd Reply Br. at 81. ComEd notes that the ICC previously has rejected a claim to disallow supplemental pension plan expense when, as here, total compensation was not shown to be excessive. *Id.* at 81.

AG/CUB's Position

Mr. Smith indicates that 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. Mr. Smith showed that 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. CUB maintains that using this abnormally high amount is inappropriate.

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, Mr. Smith testifies that 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, Mr. Smith found that 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.*

Mr. Smith contends that 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. Mr. Smith also recommends that the cost of the Supplemental Executive Retirement Plan ("SERP") 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. Mr. Smith explains that SERPs provide retirement benefits to executives in excess of the limits placed by the IRS regulations on pension plan calculations. *Id.* at 34. Therefore, concludes Mr. Smith, 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.* AG/CUB avers that 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.

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.

Commission Analysis and Conclusion

ComEd requests approval to include $65,536,000 in actuarially-determined 2010 pension costs in its revenue requirement. ComEd Ex. 6.1, Sched. C-2.2, line 3, column (F). AG/CUB propose determining the actual 2009 amount using an average of 2006-2008 costs and rejecting the *pro forma* adjustment based on the actuarial report issued in March 2010. Smith Dir., AG/CUB Ex. 3.0 Corr. at 32. AG/CUB's adjustments reduce ComEd's pension expense by $37.4 million. Houtsma Reb., ComEd Ex. 29.0 at 34.

The Commission approves ComEd's actuarially determined amount relating to its 2010 pension cost in its entirety and rejects the adjustments proposed by AG/CUB. The record shows that ComEd relied on actuarial reports in Docket Nos. 07-0566 and 05-0597 that were comparable to the March 2010 report and were accepted as providing

known and measureable verification of ComEd's pension and post-retirement benefit costs. No evidence has been presented that the Towers Watson report contained any errors.

ComEd requests approval to include $65,536,000 in actuarially-determined 2010 pension costs in its revenue requirement. ComEd Ex. 6.1, Sched. C-2.2, line 3, column (F). AG/CUB propose determining the actual 2009 amount using an average of 2006-2008 costs and rejecting the *pro forma* adjustment based on the actuarial report issued in March 2010. Smith Dir., AG/CUB Ex. 3.0 Corr. at 32. AG/CUB's adjustments reduce ComEd's pension expense by $37.4 million. Houtsma Reb., ComEd Ex. 29.0 at 34.

The Commission approves ComEd's actuarially determined amount relating to its 2010 pension cost in its entirety and rejects the adjustments proposed by AG/CUB. The record shows that ComEd relied on actuarial reports in Docket Nos. 07-0566 and 05-0597 that were comparable to the March 2010 report and were accepted as providing known and measureable verification of ComEd's pension and post-retirement benefit costs. No evidence has been presented that the Towers Watson report contained any errors.

(ii) 2005 Pension Funding Cost Recovery

ComEd's Position

The Commission should continue to allow ComEd to recover its $803 million pension contribution in ComEd's rates. In 2005, ComEd made an $803 million pension fund contribution for which the Commission, in Docket No. 05-0597, authorized recovery at the rate of $25.5 million per year, a return equal to the cost that ComEd would have incurred had ComEd issued debt to fund the contribution. Houtsma Reb., ComEd Ex. 29.0 at 13-14; *Commonwealth Edison Co.*, ICC Docket No. 05-0597, Corrected Order on Rehearing (Dec. 20, 2006) at 28. This return is lower than would have resulted from application of ComEd's overall return, as ComEd had claimed was appropriate. The amount was also included, without any challenge, in ComEd's approved revenue requirement in Docket No. 07-0566. In accordance with the Commission's orders in those cases, the $25.5 million is included in ComEd's revenue requirement in this case.

Staff contends that the $25.5 million cost recovery authorized in Docket No. 05-0597 should be reduced by $6.329 million to reflect the supposed diminished value of the $803 million contribution due to the passage of time. Pearce Dir., Staff Ex. 3.0 Rev. at 16; Pearce Reb., Staff Ex. 18.0 at 9. The evidence shows, however, that the presumption of diminishing value is incorrect. First, ComEd's long term debt does not amortize down over time. Of the $5.6 billion of ComEd's long-term debt, only $40 million (0.7%) is amortizing debt. Houtsma, Sur. ComEd Ex. 55.0 2nd Rev. at 13. Instead, ComEd pays interest periodically and the principal balance remains outstanding in its entirety until the maturity date. *Id.*

Staff argues that Alternative 3, under which recovery of this pension contribution was allowed in the Commission's Rehearing Order in Docket 05-0597, was based on the issuance of 5, 10, and 30 year bonds and that by the time the rates in this case go into effect, "the 5 year bond series reflected in Alternative 3 could be assumed to be

paid off around the end of 2011." Therefore "it appears improper to reflect the entire cost of these 5 year bonds in the 2009 test year." Staff Init. Br. at 47.

ComEd explained in its Reply Brief however, that nothing in the Order in Docket 05-0597 relating to Alternative 3 as the basis for cost recovery mentioned 5, 10 or 30 year debt. ComEd Reply Br. at 82. ComEd further explained that the Commission did not intimate in 05-0597 that in future cases it would pretend further that ComEd "retired" these hypothetical "bonds" because to do so would have denied ComEd even debt rate recovery. *Id.* at 82-83.

ComEd acknowledged that the pension asset resulting from the 2005 contribution will not last in perpetuity. Rather, it will decrease each year by an amount equal to that year's pension accruals. Houtsma, Sur. ComEd Ex. 55.0 2nd Rev. at 14. However, ComEd explained that it has used the pension accruals to diminish the pension asset not accounted for by the $803 million contribution because that part of the asset should receive a greater return (weighted average cost of capital), thereby resulting in a lower overall revenue requirement. *Id.*

ComEd recommends that the Commission should continue to reflect the $803 million pension contribution in ComEd's rates in the same manner as it did in Docket Nos. 05-0597 and 07-0566.

Staff

The Commission should accept Staff's adjustment to reduce the amount of recovery for the 2005 pension contribution due to the passage of time. (Staff Ex. 3.0R, pp. 16-18; Staff Ex. 18.0, pp. 9-12) The Company's proposal effectively treats this as a permanent investment that will never decline, even though the Company itself acknowledges that the contribution does not exist in perpetuity and will decrease over time. (ComEd Ex. 55.0, p. 14)

The Order on Rehearing in Docket No. 05-0597 allowed ComEd to recover an imputed debt return of 4.75% on the 2005 jurisdictional pension contribution in an annual amount of $25.3M in operating expenses. Although the Order on Rehearing in Docket No. 05-0597 permitted the recovery of these costs, it did not specify how long the Commission intended such costs to be reflected in utility rates. (Order on Rehearing, Docket No. 05-0597, December 20, 2006, p. 28) Accordingly, Staff proposed to reduce the amount of cost reflected in the 2009 test year for recovery of the 2005 pension contribution. Staff reduced the recovery related to the pension contribution based on the principle that the underlying debt (as more fully described in "Alternative 3" of the Order on Rehearing in Docket No. 05-0597) balance will decline over time and with it, the related interest thereon.

The Company asserts that Staff's presumption of diminishing debt is both unsupported and unrealistic. (ComEd IB, p. 69) To support this assertion, the Company addresses the actual debt that is issued and outstanding by the Company today, in complete disregard for Alternative 3 that was selected by the Commission as the basis on which the original $25.3M of cost recovery was calculated in Docket No. 05-0597 (Order on Rehearing, p. 28). The Company's argument misses the point because it focuses on actual debt issuances rather than the imputed cost of the contribution itself.

By disregarding the hypothetical Alternative 3, which is the only basis for any amount of cost recovery (allowed by the Commission in Docket No. 05-0597 in its Order on Rehearing), the Company can ignore the fact that the amount of cost recovery will diminish over time, as the underlying 5-, 10- and 30-year bonds mature. Staff's calculation estimates the average outstanding term of the hypothetical underlying bonds with maturities of 5, 10, and 30 years, as more fully described in the hypothetical scenario selected under Alternative 3. (Docket No. 05-0597, ComEd Ex. 52.15) Based on this calculation, Staff estimates that approximately 25% of the average term of debt assumed to finance the 2005 pension contribution would have been recovered between the effective date of the rates established in Docket No. 05-0597 (January 2007) and the effective date of rates established in the instant proceeding (June 2011). Accordingly, in test year 2009 Staff proposes to reflect 75% of the original $25.078M cost approved in the Order on Rehearing in Docket No. 05-0597, or approximately $18.749M. (Staff Ex. 18.0, Schedule 18.02).

The Company further asserts that the Company often refinances its debt at maturity. (ComEd IB, p. 69) This too is irrelevant because there is no basis under the scenario selected by the Commission in Docket No. 05-0597, to assume that any of the debt described in Alternative 3 would be refinanced. Staff simply acknowledges that the entire balance of debt would not be outstanding for a full 30-year period under Alternative 3. Accordingly, Staff's adjustment seeks to calculate a reasonable amount of cost that would be incurred by the Company in the 2009 test year, based on the information contained in Alternative 3.

Finally, the Company mischaracterizes the issue raised by Staff, instead describing the treatment of pension assets. (ComEd IB, p. 69) Again, this argument is irrelevant to the issue raised by Staff. The issue does not concern treatment of the 2005 pension contribution itself, but rather the amount of cost recovery associated with the 2005 contribution in the 2009 test year, to the extent permitted by Alternative 3. As the Commission is well aware, the Company's request to include the 2005 pension contribution as a pension asset in rate base was denied. Instead, the Commission utilized Alternative 3 as the cost recovery mechanism that was ultimately approved in Docket No. 05-0597. (Order on Rehearing, December 20, 2006, p. 28) The resulting amount, $25.1M, was also reflected in the Company's operating statement in its next rate case, Docket No. 07-0566 and approved by the Commission, possibly because no witness challenged this treatment. (Tr., January 20, 2011, pp. 2557-2558) In the current proceeding, Staff witness Pearce has challenged the Company's inclusion of the full amount that was approved in Docket No. 05-0597. The issue now before the Commission concerns the application of Alternative 3 to the 2009 test year.

The proposal put forth in Staff Ex. 18.0, Schedule 18.02 recognizes that the basis for cost recovery of the 2005 pension contribution under Alternative 3 was a series of 5, 10, and 30 year bonds. Given that five years have passed since the Commission approved recovery of 2005 pension contribution costs, it is necessary to address the application of Alternative 3 to the 2009 test year. Accordingly, Staff urges the Commission to accept Staff's proposal to reduce the amount of cost recovery associated with the 2005 pension contribution.

Commission Analysis and Conclusion

ComEd requests approval to continue to recover its $803 million pension contribution in ComEd's rates in the annual amount of $25.5 million that the Commission authorized in Docket No. 05-0597. Staff contends that the $25.5 million annual cost recovery authorized in Docket No. 05-0597 should be reduced by $6.329 million to reflect what it believes to be a diminished value of the $803 million contribution due to the passage of time

ComEd has presented sufficient evidence to show that this pension asset has not diminished, that additional accruals were applied first to the remaining pension asset and this has benefited customers by reducing the revenue requirement. Further, Staff's attempt to use ComEd's Rehearing Order in 05-0597 to support its position misapprehends what the Commission held in that Order. Therefore, the Commission approves ComEd's recovery of its pension contribution in the amount of $25.5 million annually and rejects Staff's proposed adjustment.

d. Wages and Salaries *Pro Forma* Adjustment

Staff's Position

Staff proposed an adjustment of $2,605,000 to reduce the amount of ComEd's *pro forma* 2010 wages and salaries. This reflects a decrease in the overall forecast 2010 payroll expense, offset by the IBEW Local 15 increase for 2011. (Staff Ex. 3.0R at 24-25; Staff Ex. 18.0 at 13-14). Staff states that ComEd's response to Staff Data Request BAP-23.01, Attachment 1, reflects a decrease in overall wages and salaries for 2010, even after giving effect to increases for overtime and fringe benefits. Staff recognized the amount of 2011 increase based on the Memorandum of Agreement with IBEW Local 15, offset by the decline in overall 2010 wages and salaries expense that was reflected in the most recent forecast that ComEd provided. (Staff Ex. 18.0, Schedule 18.03; Staff Reply Brief at 38).

Staff initially proposed to revise ComEd's *pro forma* adjustment for 2010 wages and salaries increases (Staff Ex. 3.0R, Schedule 3.03) on grounds that the amount of 2010 wages and salaries expense was not known and measurable. Based on updated information that ComEd provided in response to a "data request," Staff witness Pearce revised her proposal in rebuttal testimony to allow recovery of the IBEW Local 15 increase for 2011, reduced by the overall decline in 2010 forecast payroll expense. Staff strongly disagrees with ComEd's argument that an increase in 2010 wages and salaries is a known and measurable change. To the contrary, Staff states, ComEd's response to Staff "data request" BAP-23.01, Attachment 1, reflects a decrease in overall wages and salaries for 2010. (Staff Ex. 18.0 at 14). Staff recognized the amount of 2011 increase based on the Memorandum of Agreement with IBEW Local 15, offset by the decline in overall 2010 wages and salaries expense that was reflected in the most recent forecast that ComEd provided. (Staff Ex. 18.0, Schedule 18.03; Staff Initial Brief at 49-50).

CUB's Position

CUB avers that the number of ComEd employees has steadily declined from early 2009 through August 2010, including a sharp drop from June to July of 2009 that is related to ComEd's 2009 severance program. CUB avers that the *pro forma* adjustment recognized by ComEd was of only 108 employees; however, the actual number of employees had decreased by 300 from January 2009 through August 2010. Mr. Effron determined that the decrease in payroll for those employees significantly exceeded the increase in overtime. Based on ComEd's requested *pro forma* adjustment, CUB states that payroll expense in 2010 should actually be about $5.1 million higher than in 2009. CUB maintains that in actuality, ComEd anticipates that payroll costs will actually be $286,829 lower than 2009. AG/CUB witness Mr. Effron recommended 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. 7.1, Schedule C-3; CUB Initial Brief at 31-32).

The AG's Position

The AG maintains that its witness Mr. Effron's adjustment is based on ComEd having 5,712 employees as of October 31, 2010. This represents a reduction of 147 employees from the 2009 test year level. By comparison, the AG continues, ComEd only removed the costs that are associated with 63 employees in its *pro forma* adjustment. (AG/CUB Ex. 8.0 at Sch. DJE-2.2a) AG Cross Exhibit 27 shows that between October 31, 2010 and December 31, 2010, ComEd continued to reduce the number of employees to 5,692, which is 20 positions fewer than Mr. Effron recognized in his adjustment. (AG Initial Brief at 77).

According to the AG, ComEd misstates the purpose of the AG/CUB adjustment, which is to reflect reductions to the number of employees *beyond* the reduction that was already recognized by ComEd. The AG further argues that ComEd's assertion that "the proposed disallowance overlooks offsetting increases in overtime and fringe benefits" is without merit because Mr. Effron's proposed adjustment explicitly takes into account offsetting increase in overtime. It also incorporates changes in fringe benefits in the quantification of the proposed adjustment. (*See,* AG/CUB Ex. 8.0. Sch. DJE-2.2a; AG Reply Brief at 34-35).

ComEd's Position

ComEd seeks to include $8.809 million in *pro forma* wages and salaries expense in its revenue requirement. (ComEd Ex. 6.1, Sched. C-2.1). AG/CUB witness Effron and Staff witness Pearce propose to cut ComEd's *pro forma* wage and salary expense by $4.15 million and $6.2 million, respectively. ComEd witness Mr. Fruehe stated that the amount of the 2010 wages and salaries increase is known and measureable, being based on an agreement with the union effective April 1, 2010, and a non-union wage increase that went into effect on March 1, 2010. (ComEd Ex. 30.0 Public at 18). Mr. Fruehe averred that the AG/CUB and Staff recommendations should be rejected because ComEd's proposed revenue requirement already takes into account $3.69

million in what ComEd has already determined are sustainable savings from the reductions. (ComEd Ex. 56.0 3rd Rev. at 5). According to ComEd witness Mr. Fruehe, the proposed disallowances overlook offsetting increases in overtime and fringe benefits. (ComEd Ex. 30.0 Public at 5-6; 18-19; ComEd Initial Brief at 69-70).

Analysis and Conclusions

We decline to adopt the AG/CUB adjustment on this issue. A decrease in the number of employees is not the same as a decrease in the overall amount paid in salaries and wages. Different employees are paid different amounts. Even assuming that the number of ComEd employees continues to decline, without more, this does not mean that the amount of money that ComEd pays for wages and salaries will decline.

However, ComEd proffered no evidence indicating that the overall amount that it pays its workforce has not decline. While Mr. Freuhe testified that ComEd's overall revenue requirement already takes $3.69 million in sustainable savings resulting from the reductions, his statement is devoid of any evidentiary factual foundation. We therefore did not consider it. Additionally, Mr. Freuhe's statement that the proposed disallowances overlook overtime and fringe benefits is incorrect. The amount proposed by Staff takes into account the decline in wages and salaries that ComEd is experiencing. It is reasonable and it is approved.

e. Directors' Fees and Expenses

Staff's Position

Staff proposes to reduce, by half, the amount of Directors' Fees and Expenses reflected in the test year. Staff reasons that some of the Board of Directors' duties benefits shareholders, not ratepayers. (Staff Exs. 3.0R at 36; 18.0 at 26-27; Staff Memo at 5).

ComEd's Position

ComEd's witness Mr. Fruehe testified that Staff's proposal to reduce directors' fees and expenses by 50% should be rejected because a utility is required by law to have a board of directors to govern the affairs of the corporations. Mr. Freuhe stated that some of the Board's duties include a.) overseeing the provision of safe and reliable electric service at just and reasonable rates; b.) monitoring ComEd's operating and financial performance; c.) staffing, executive compensation and employee benefits; d.) capital investment; e.) operating budgets; f.) financing business activity; g.)approval of material commercial contracts; h.) review of collective bargaining matters; i.) corporate policy and strategy; j.) recovery of costs to conduct the business; k.) legislative and public affairs; compliance with legal and ethical requirements; and l.) corporate citizenship and diversity initiatives. (ComEd Ex. 30.0 at 17-18, 56.0 at 20).

Analysis and Conclusions

While we do not dispute the accuracy of Staff's reasoning that ComEd's directors engage in many activities that solely benefit shareholders, and not ratepayers, there is no evidence here as to what percentage of time those directors engage in activities that are solely for the benefit of its shareholders. Without that evidence, we are reluctant to

apply Staff's 50% reduction, or any reduction, at this time. We therefore decline to do so.

f. Corporate Aircraft Costs (Now Uncontested)

Staff witness Pearce and AG/CUB witness Mr. Brosch proposed disallowance of 100% and 50% respectively of ComEd's corporate aircraft costs. To limit the issues in dispute, ComEd has agreed to reduce aircraft expense by 50% or $384,000. (ComEd Ex. 30.0 at 6). Staff and the AG/CUB accepted this adjustment; this matter is no longer at issue. (*See, e.g.,* Staff Memo at 5; AG Memo at 8). This adjustment is reasonable. It is therefore approved.

g. Perquisites and Awards

ComEd's Position

ComEd seeks to recover $3.495 million in perquisites and awards. ComEd witness Mr. Trpik testified that the disallowances proposed by Staff and the AG/CUB should be rejected because perquisites and awards are reasonable business expenses that benefit customers. He stated that the majority of the expenses represent retention awards, special recognition performance awards and meter reader performance awards, which are designed to improve accuracy and completeness of meter reads. The retention awards are intended to insure that employees in critical roles within the organization continue in those roles by providing a long-term financial incentive. Mr. Trpik testified that disallowing such expenses discourages the very type of performance that most benefits customers. (ComEd Initial Brief at 72-73).

CUB's Position

AG/CUB witness Mr. Smith recommends that retention awards of $566,000 ($501,000 jurisdictional) that were not already removed by ComEd should be removed. 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. Company policy is clear that management retains the right to modify or revoke its retention bonus policy at any time, but it chose not to do so during this tumultuous time. CUB asserts that ComEd 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 54-56; CUB Initial Brief at 32).

CUB also contends that a "normalized" amount is more appropriate than use of the extraordinarily high payout of retention awards in 2009. AG/CUB witness Mr. Brosch proposed a four-year average, which provides for an annual allowance of $688,000. This results in an adjustment of $737,000 ($519,000 jurisdictional). AG/CUB witness 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. Awards under this policy include cash awards up to $5,000, gift certificates, and other non-cash spot awards. (*Id.* at 56). This results in an adjustment of $419,000 ($372,000

jurisdictional). CUB's total adjustment for perquisites and awards is $1.392 million (jurisdictional). (AG/CUB Exs. 3.0 at 54-56; 7.1 Schedule C-13; CUB Initial Brief at 33).

Staff's Position

In direct testimony, Staff witness Ms. Pearce proposed a disallowance of $3,568,000 of perquisites and awards expense on the ground that these costs were not necessary for the provision of utility service and did not provide direct ratepayer benefits. Ms. Pearce modified her position in rebuttal testimony. After having been provided with more information, Ms. Pearce concluded therein that some of the items in this expense provides ratepayers with benefits because they are tied to job performance and safety. (Staff Ex. 18.0 at 19-24). Ms. Pearce averred, however, that stock awards and executive perquisites are not necessary for the provision of service and, essentially, there is no evidence that they provide direct ratepayer benefits. She proposes a disallowance of $501,000 of operating expenses and $62,000 of rate base (Staff Ex. 18.0, Sched. 18.05) of perquisites and awards on the ground that these costs (principally stock awards or executive perquisites) were not necessary for the provision of utility service and did not provide direct ratepayer benefits. (Staff Ex. 18.0 at 24; Staff Memo at 5).

The AG's Position

The AG states that ComEd seeks to include various stock awards and other executive perquisites in its jurisdictional operating expenses. AG/CUB witness Mr. Smith pointed out that ComEd seeks $566,000 for "other stock awards and executive perquisites" that include amounts allocated from affiliates and that are in addition to the annual incentive compensation plans. The AG further avers that ComEd has a separate incentive compensation plan for its employees. The AG argues that therefore, it is unreasonable to expect consumers to pay this added amount to account for such payments. Also, the AG continues, ComEd included $1.425 million in its 2009 test year for "retention awards." However, the AG state, this amount is higher than the previous three years of retention awards combined. The AG contends that the Commission should not include such an abnormal expense in rates. To bring the charge to a more normal and representative level, Mr. Smith recommended a $519,000 disallowance to ComEd's jurisdictional operating expense, leaving a normalized annual expense of $688,000. (AG/CUB Ex. 3.0 at 54-5; AG Initial Brief at 78).

The AG further contends that the Commission should reduce a third award amount that ComEd included in its operating expenses. ComEd included $837,000 of performance-based awards based on an Exelon Reward and Recognition Policy. This award is discretionary, and consists of small cash and other payments ranging from $5 gift cards to payments of $5,000. This program is "designed to reward significant employee contributions to Exelon's success." The AG argues that consumers should not pay more than 50% of this cost, given the vague standard applicable to these awards, the wide discretion retained by management in both amount and also whether to make awards, and the existence of other incentive programs. The AG reasons that disallowance of $372,000 on a jurisdictional basis is required. (AG/CUB Ex. 3.0 at 56). The total disallowance for these three items is $1,392 on a jurisdictional basis. (AG Initial Brief at 79).

Analysis and Conclusions

We note at the outset that no party informed this Commission as to what the Uniform System of Accounts, or, pertinent law, may require. We urge all parties to so state in the future.

However, we do agree with the AG and CUB on this issue. The amount of the perquisites and awards here, during the test year, is more than the total amount for the previous three years. If we did not amortize these discretionary costs of the period of time proffered by the AG/CUB, we create the incentive for utilities to "shove" discretionary costs into the test year, in order to make it appear that the utility has less funds available than it really has. Also, while some of these awards may benefit consumers, they also undoubted benefit shareholders, as they reward improvements in job performance. Therefore, the AG/CUB proposals to amortize these expenses over four years, and to decrease the amount for perquisites and awards by half, is adopted. We note that ComEd has articulated no facts indicating that shareholders do not benefit from these "perks."

Finally, the AG/CUB, and Staff proffered slightly different amounts to be totally disallowed. It appears that the AG/CUB witness Mr. Smith analyzed the different items involved in this issue in a very thorough manner. We therefore, adopt the AG/CUB's adjustment on the issue of what is entirely disallowed. In summation, we adopt the AG/CUB recommendation in its totality.

h. Severance Expenses

<u>ComEd's Position</u>

ComEd incurs expenses for employee severance related to cost cutting initiatives. ComEd incurred $12.8 million in jurisdictional severance costs in the test year, and proposed to amortize that amount over a three-year period, including $4.277 million in its revenue requirement. Houtsma Dir., ComEd Ex. 6.0 Rev. at 48-49; ComEd Ex. 6.1, Sched. C-2.5, C-22; Houtsma Reb., ComEd Ex. 29.0 at 44. ComEd explained that the costs are attributable to an initiative that is expected to save more than $6 million annually (on a jurisdictional basis) and which has been fully reflected in ComEd's rate filing. Houtsma Reb., ComEd Ex. 29.0 at 44. ComEd noted that the Commission authorized recovery of similar severance costs in Docket No. 05-0597 (those related to the "Exelon Way" severance program) and reached a similar conclusion in Ameren's rate case Docket No. 09-0306 *et al*, providing for amortization of the costs in both situations. *Id.* at 45. The recovery of severance costs would also be consistent with the intent of the Section 285.3125 filing requirements for rate cases (allowing utilities to request recovery of cost savings programs with savings of $1,000,000 or more). *Id.*

<u>AG/CUB</u>

CUB recommends an adjustment to remove 2009 severance costs from the Company's revenue requirement, which the Company seeks to recover and amortize. AG/CUB Ex. 2.0 at 24. Mr. Effron shows that 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.* CUB avers that 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.*

Alternatively, CUB recommends that 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. According to Mr. Effron, the amortization period must be extended to better match the realization of benefits of the program. *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 suggests is the basis of Mr. Effron's argument is that the savings won't be realized until those 7.5 years have passed. ComEd Init. Br. at 76. CUB avers that this is not accurate. Mr. Effron notes that savings from the program will continue at least another 7.5 years, therefore Mr. Effron proposes that if such costs are included in rate base, the amortization period for those costs should match that time.

According to CUB, ComEd's argument that disallowing these costs is single-issue ratemaking (ComEd Ex. 55.0 at 29) is a straw man argument. CUB states that while 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.

STAFF

Staff witness Tolsdorf proposed an adjustment (Staff Ex. 4.0, p. 8; Staff Ex. 19.0, pp. 9-11) to reduce the severance cost-regulatory debit associated with the termination of 108 management employees in 2009. Staff's adjustment offsets the cost of severance incurred by the Company with the annual savings achieved by the Company in the form of reduced payroll expense. The Company incurred approximately $12.8 million in severance costs which resulted in approximately $6.3 million in annual savings. Those annual savings to the Company will total $11.6 million by the time new rates from this proceeding go into effect. (Staff Ex. 19.0, Schedule 19.04, p. 2) The Company's proposed regulatory debit would lead to a $24.4 million dollar windfall for the Company ($11.6 million in savings + $12.8 million in cost recovery). Staff maintains its position that the expense incurred should be offset by the savings achieved and that only the difference should be amortized over three years.

The Company argues that Staff's position is single-issue ratemaking and cites to the Commission's Order in Docket No. 08-0312. (ComEd IB, p. 75) However, the facts of the two cases are distinguishable. In Docket No. 08-0312, the Commission rejected an adjustment that attempted to defer savings resulting from an event that occurred in between rate cases in a year prior to the test year. In the current case, Staff witness Tolsdorf calculated the net regulatory asset that would result from an event that occurred in the test year, where all the elements of the revenue requirement are

considered together, considering when the new rates will go into effect. (Order, Docket No. 08-0312, January 12, 2010, p. 3)

Commission Analysis and Conclusion

ComEd incurred $12.8 million in jurisdictional severance costs in the test year, and proposes to amortize that amount over a three-year period, including $4.277 million in its revenue requirement. Staff proposes adjustments that would reduce ComEd's jurisdictional severance expense to about $1.1 million or $370,000 annually, for an annual disallowance of $3.867 million. . AG/CUB seeks to disallow all recovery.

The evidence shows that Staff's adjustment is improper and must be rejected because it would reduce ComEd's jurisdictional severance costs on the assumption that those costs would be recovered through savings and thus create the risk that reasonable and prudent costs would not be recovered at all. Moreover, Mr. Tolsdorf admitted that "he is not aware of any Commission decision in which the Commission reduced the amount of an otherwise proper regulatory asset on grounds that the underlying expense was being recovered by cost savings." Staff Group Cross Ex. 1 (Staff Response to ComEd Data Request ComEd-Staff 12.01 (Public)).

AG/CUB's proposals must also be rejected. AG/CUB's proposed 7.5 year amortization period is inconsistent with its claim that the severance costs will be recovered in the two years between the time the costs were incurred and the time this rate case is concluded.

The Commission approves ComEd's proposal to amortize $12.8 million in jurisdictional severance costs over a three-year period, including $4.277 million in its revenue requirement.

i. Charitable Contributions

ComEd's Position

ComEd seeks to include $6.3 million (before removal of non-jurisdictional portion) in charitable contributions in its revenue requirement. (ComEd Ex. 30.0 at 8) ComEd notes that inclusion of charitable contributions in the revenue requirement is provided for in Section 9-227 of the Act.

ComEd contends that the proposal by Staff and AG/CUB to disallow portions of ComEd's charitable contributions should be rejected. According to the Company, the disallowances are contrary to the facts and the law, specifically, Section 9-227 of the Act. (ComEd Initial Brief at 77) ComEd argues that neither Staff nor AG/CUB asserted that the recipients of the amount in question are not *bona fide* charitable organizations, or even that the overall contributions are excessive.

ComEd asserts that the contributions are reasonable, are lower than the $6.8 million of contributions approved in Docket No. 07-0566, support well-established civic or charitable organizations and should be approved. (ComEd Ex. 30.0 at 7-9, ComEd Ex. 56.0 at 6-8) The Company argues that the contributions made by Exelon on behalf of ComEd in conjunction with large contributions made on behalf of ComEd affiliates are functionally equivalent to the donations made by ComEd in its own name. ComEd contends that it is nearly certain that had it made those donations directly, no question

would have been raised about the propriety of those contributions (to such organizations as the United Way of Metropolitan Chicago, the Kellogg School of Management, the Chicago 2016 Committee and the Field Museum). (Staff Ex. 4.0 at 78, Sched. 4.03 at 2, 3) ComEd explains that the average contribution level of 23 utility companies in 2008 was approximately $8.5 million, more than one third higher than the amount for which ComEd seeks recovery in the 2009 test year. (ComEd Ex. 30.0 at 8) The Company posits that the fact that it may receive some unintended positive recognition for its contribution is no reason to characterize the contribution, to an admittedly *bona fide* charity as "promotional" or "goodwill" in nature. ComEd points out, such contributions are quite different from, for example, a promotional billboard at U.S. Cellular Field. (*Id.* at 9)

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

Staff's Position

Staff is proposing an adjustment to disallow the following charitable contributions: (1) contributions made by Exelon that have been allocated to ComEd; (2) contributions to organization's outside of ComEd's service territory; and (3) contributions that represent promotional or goodwill advertising. (Staff Ex. 4.0 at 4-8; Staff Ex. 19.0 at 6-9) Staff's adjustment would result in a reduction to rate base of $2,281,000. (Staff Ex. 4.0, Schedule 4.03)

Staff asserts that ComEd's customers should not be responsible for the charitable contributions made by Exelon that have been allocated to ComEd because Exelon is performing an unnecessary duplicative function. (Staff Ex. 19.0 at 6-7) Staff argues that ComEd has demonstrated that it is capable of making its own charitable donations and funding another entity's charitable donations is an unnecessary expense for providing safe, reliable electric service to customers. In addition, Staff disagrees with ComEd's assertion that these contributions are functionally equivalent to the donations made by ComEd in its own name. Staff argues the issue is not the charitable contributions themselves but rather the reasonableness of charging ratepayers for both ComEd's and Exelon's charitable contributions, which are sometimes to the same organization. (Staff Reply Brief at 42)

Staff argues that ratepayers should not be responsible for charitable donations to organizations in Philadelphia Electric Company's ("PECO") service territory. (Staff Ex. 4.0 at 5-6, Staff Ex. 19.0 at 7-8) Staff notes that Section 9-227 of the Act allows the Commission to consider as an operating expense only those donations which are reasonable. Staff argues that it is not reasonable to expect ComEd customers to pay for these expenses which were incurred for the benefit of PECO's customers.

Staff also argues that certain donations made by ComEd represent goodwill or promotional advertising which are not recoverable under the Act. (Staff Ex. 4.0 at 6-8, Staff Ex. 19.0 at 8-9) Staff notes that Section 9-225 of the Act specifically denies the recovery of any advertising which is designed primarily to bring the utility's name before the general public in such a way as to improve the image of the utility. Staff believes the Company's argument that the primary reason for the donations is for the furtherance of the organizations' missions is an issue of form over substance. (Staff Initial Brief at 54) Staff argues that in effect the Company is attempting to circumvent the intent of Section 9-225 and recover those otherwise unrecoverable costs for promotional or goodwill advertising through Section 9-227. (*Id*.) It is Staff's position that by making charitable contributions and instructing those organizations on how to publicly recognize ComEd, the Company is receiving a benefit in the form of goodwill advertising which the Act specifically states can not be recovered.

Staff does not support AG/CUB's proposal of equal sharing of charitable contributions between ratepayers and shareholders. (Staff Initial Brief at 52). It is Staff's understanding that the AG/CUB proposal violates Section 9-227 of the Act.

The AG/CUB's Position

AG/CUB is proposing that the cost of test year charitable contributions incurred in the test year should be shared on an equal basis between ratepayers and shareholders primarily because they are discretionary expenditures that are not necessary, and have no bearing on the provision of safe and reliable service for customers. (AG/CUB Ex. 1.0 at 45-47, AG/CUB Ex. 7.0 at 31-32) The total reduction to rate base proposed by AG/CUB is $2,803,000. (AG/CUB Ex. 7.1, Schedule C-17)

AG/CUB argues that the "sharing" approach would better reflect the fact that charitable contributions are discretionary costs that ComEd should be expected to moderate during times of financial hardship. (AG/CUB Ex. 1.0 at 47) AG/CUB states that sharing those costs would provide ComEd with incentive to carefully prioritize its funding. (*Id*.) According to AG/CUB, ComEd seeks costs-plus, full recovery regulatory treatment of its charitable contributions. (*Id*.) AG/CUB explains that 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) AG/CUB avers that 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) In addition, 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*.)

AG/CUB witness 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, AG/CUB propose

that ComEd may recover 50% from ratepayers; which AG/CUB argues is generous. (*Id*.)

It is AG/CUB's position that ComEd'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, CUB Initial Brief at 35)

Analysis and Conclusion

We concur with Staff's proposal to disallow charitable contributions made by ComEd to organizations outside of the Company's service territory. There is no evidence that these contributions provide any benefit to ratepayers in ComEd's service territory. We agree with Staff that it is not reasonable to require ComEd ratepayers to bear the cost of such contributions. Accordingly, Staff's adjustment is adopted.

We, however, decline to adopt Staff's proposed disallowances for contributions made by Exelon on behalf of ComEd and contributions characterized by Staff as promotional and goodwill advertising. There is no reason we should disallow recovery of donations made to well-established civic and charitable organizations that provide a benefit to the public in ComEd's service territory simply because the donations were made indirectly by Exelon on ComEd's behalf. In addition, we conclude that ComEd has established that the contributions that it made directly, which Staff views as essentially promotional and goodwill advertising were reasonable in amount and prudently incurred in furtherance of a legitimate charitable purpose. The fact that ComEd received recognition for these donations and provided impute regarding the manner in which the recognition was given, namely its corporate policies concerning the use of its logo, does not diminish the charitable nature of the contributions or make them unrecoverable under Section 9-227 of the Act. If we used Staff's rationale to review charitable contributions, the majority of contributions would be automatically disallowed since it is customary for charitable and civic organizations to publicly recognize donors in some way. A blanket exclusion of such donations would be a clear violation of Section 9-227 which states in part,

> In determining the reasonableness of such donations, the Commission may not establish, by rule, a presumption that any particular portion of an otherwise reasonable amount may not be considered as an operating expense. The Commission shall be prohibited from disallowing by rule, as an operating expense, any portion of a reasonable donation for public welfare or charitable purposes. (220 ILCS 5/9-227).

We find that both categories of contributions are recoverable and Staff's proposed disallowances are rejected.

AG/CUB's proposal that the cost of ComEd's charitable contributions should be shared on an equal basis between ratepayers and shareholders is also rejected. This approach blatantly violates Section 9-227 of the Act by indiscriminately disallowing 50% of the contributions without analyzing the contributions to determine if they meet the requirements of the Act. These expenses are by their nature within the purview of

Section 9-227 and they should be carefully considered in accordance with the statute. For these reasons, AG/CUB's sharing approach is not adopted.

j. Legal Fees – IRS Dispute

ComEd's Position

ComEd witness Mr. Fruehe testified that AG//CUB witness Mr. Effron's proposal to reduce ComEd's jurisdictional operating expenses by $2.187 million for legal costs related to an IRS dispute associated with the gain on the sale of the fossil generating units should be rejected because these costs are "likely to" relate to both the transmission and distribution functions. He concluded that these costs are properly allocable to the appropriate function by use of a general allocator that applies to the thousands of charges in ComEd's Uniform System of Accounts Account 923. Specifically, Mr. Fruehe states that Account 923 includes thousands of different charges, most of which, cannot be allocated to a single function. He concludes that reviewing each line item for appropriateness is therefore not a reasonable task. (ComEd Ex. 56.0, 8-9).

The AG/CUB Position

AG/CUB witness Mr. Effron recommends eliminating the legal fees that are related to this IRS dispute, which is regarding the tax treatment of the gain on the sale of fossil-generating units in 1999. In his opinion, the tax treatment of the gain on the sale of fossil-generation is not a jurisdictional amount. (AG/CUB Exs. 2.0 at 21-22; 8.0 at 13-14). This results in a reduction of jurisdictional operations and maintenance expenses by $2,187,000. (AG/CUB Ex. 7.1 Schedule C-6. CUB Memo at 10; AG Memo at 10).

Specifically, Mr. Effron stated that, in response to AG Data Request 6.26, ComEd stated that the tax at issue is one that is being deferred because it "relates to the gain incurred on the sale of fossil generating stations that were "previously owned by ComEd, thus it is non-jurisdictional." Mr. Effron opines that, if the tax deferral being claimed by ComEd is non-jurisdiction, so are the legal fees associated with that deferral. (AG/CUB Ex. 2.0 at 21).

Staff's Position

Staff recommended adopting AG/CUB witness Mr. Effron's adjustment regarding legal fees because it appears, to Staff, that the fees in question are not jurisdictional in nature. (AG/CUB Ex. 2.0 at 21-22; AG/CUB Ex. 2.1, Sch. 2.2b). Staff states that ComEd does not dispute the nature of the fees as ones that originate from tax dispute regarding fossil plant, but, instead, ComEd argues that because the fees at issue were recorded to Account 923, a general allocator should be used. (*See,* ComEd Ex. 30.0 at 10-11). Staff states that, while it is reasonable to sometimes allocate costs to delivery services when the nature of the cost is not 100% related to the delivery service function, it is never reasonable to include a cost in the delivery service revenue requirement when it is definitively known that the cost here is not related to providing delivery services. Staff's revenue requirement reflects the inclusion of the AG's disallowance on this issue. (Staff Ex. 17.0 at 11-12).

Analysis and Conclusions

ComEd has proffered no reason to explain why rate base should include legal fees that are clearly related to non-jurisdictional matters--fossil fuel generation, for a company that cannot generate electricity. ComEd states that this matter was include in account 923. However, merely because matters were included in account 923 does not change the issue. Rather, the issue here is whether these fees should have been included in rate base in the first place. The AG/CUB adjustment, which Commission Staff agrees to, reducing jurisdictional operations and maintenance expenses by $2,187,000, is approved.

k. Professional Sporting Activity Expenses

ComEd's Position

ComEd argues that it should be allowed to include in its revenue requirement $64,000 in operations and maintenance expense and $8,000 in rate base for the costs associated with professional sporting activities. ComEd explains that the proposals by Staff and AG/CUB to remove costs associated with professional sporting activities should be rejected because these are reasonable business expenses for employee recognition, team building and development of business relationships with key customers. (ComEd Ex. 30.0 at 11; ComEd Ex. 56.0 3rd Rev. at 9) ComEd notes that ComEd witness Mr. Fruehe clarified during his cross examination at the hearing, that ComEd's initial request to include $511,000 in its revenue requirement was an error. Mr. Fruehe testified that the vast majority of that amount, all but $64,000 plus $8,000 allocated to a capital account, was reclassified "below the line." As a result, ComEd's proposed revenue requirement contains, for this category of expense, only $64,000 in operations and maintenance expense and $8,000 in rate base. (Tr. 2445-47; ComEd Initial Brief at 79-80)

In addition, ComEd asserts that the AG's argument in its Initial Brief that the Commission should disallow recovery of these expenses to "conform its rate treatment to the FERC treatment" should be rejected. (ComEd Reply Brief at 88) ComEd contends that the Commission should reject this recommendation because the AG has no citation of authority as to how FERC might decide this issue, or why the Commission ought to follow FERC precedent on this single issue. (*Id.*)

Staff's Position

Staff is proposing an adjustment to disallow the costs of individual game tickets and luxury box catering expenses for professional sporting events. Staff argues that these expenses are extravagances that are not necessary costs for providing safe, reliable electric service to customers. (Staff Ex. 4.0 at 12; Staff Ex. 19.0 at 13-14) Staff notes that the Company has provided corrected figures which reflect the costs associated with professional sporting activities included in the Company's proposed revenue requirement. (Staff Group Cross Ex. 1 at 367) However, Staff maintains its position that all of these costs, which consist of $64,000 in operations and maintenance expense and $8,000 in rate base, should be disallowed. Staff avers that the Company would normally reclassify these expenses as "below the line" and the Company's failure

to reclassify these expenses is an accounting oversight that does not create justification for recovery of these expenses. (Staff Reply Brief at 43)

The AG/CUB Position

AG/CUB recommends denying ComEd's request for recovery of costs of sporting event tickets and catering, such as well appointed skyboxes for professional sporting events because these expenses are discretionary and they are not necessary for the provision of utility service. (AG/CUB Exs. 3.0 at 53-54; 7.1 Schedule C-13) AG/CUB asserts that ComEd is unable to provide sufficient details, such as the amount spent on catering, alcohol, etc., to support its request. (AG/CUB Ex. 3.0 at 54) AG/CUB acknowledges ComEd provided corrected figures for this expense, but argues that ComEd failed to explain why it is appropriate to move any of these expenses from the "below the line" treatment provided in its FERC accounts. (AG Reply Brief at 40) AG/CUB contends that ComEd did not address the reasonableness of its professional sporting activity expenses but simply argued at the hearing that it has classified most of the expense "below the line". (CUB Reply Brief at 25)

Analysis and Conclusions

We agree with the proposal by Staff and AG/CUB to remove all of the costs associated with professional sporting activities from ComEd's proposed revenue requirement. These expenses should not be charged to ratepayers as they are not necessary for the provision of safe and reliable electric service. Accordingly, the adjustment proposed by Staff and AG/CUB is approved.

I. Workforce Expense Reduction

See Section V.C.3.d. of this Order.

5. AMI Pilot Expenses

Staff's Position

Staff proposed reducing the amount of *pro forma* AMI Pilot expenses for expenses to be incurred from December of 2010 through June of 2011 because these costs are not known and measurable costs that occurred during the test year. Staff recommends a reduction in the amount of $1,108,000. (Staff Memo at 6; Staff Ex. 19.0 at 11-13).

ComEd's Position

ComEd witnesses Mr. Fruehe and Mr. Marquez in surrebuttal testimony testified that ComEd has reduced its AMI Pilot O&M expenses from $2.8 million to $1.306 million. (ComEd Exs. 56.0 at 25-29; 61.0 3rd Rev. at 10-12). Mr. Fruehe testified that the Bridge Tariff regarding AMI Pilot expenses authorizes ComEd to include these otherwise unrecoverable operating expenses in a general rate case when they fall within the test year. He also stated that the Bridge Tariff does not include recovery of the O & M expenses for this project. He points out that excluding these costs from ComEd's revenue requirement would therefore leave ComEd without the ability to recover the costs that it incurs for this project after December of 2010. (ComEd Ex. 56.0 3rd Rev. at 27-29).

Analysis and Conclusions

In docket 09-0263, this Commission approved ComEd's AMI pilot program. In so doing, it approved recovery of the costs of that program through a Rider. Subsequently, however, the Illinois Appellate Court issued a decision in which it found that recovery of the expenses for this program through a rider violated the prohibition against single-issue ratemaking. (*Commonwealth Edison Co v. Illinois Commerce Comm., 937 Ill. App. 3d 389,* 937 N.E.2d 685, 737-42 (2nd Dist. 2010)). While a motion for a stay of this decision has been filed, to date, no stay order has issued. Therefore, Rider recovery of the costs that this Commission approved in docket 09-0263 is no longer a viable option.

While we agree with Mr. Tolsdorf that generally, when a utility uses a historical test year, only the known and measurable costs are recoverable, this Commission has already approved recovery of these costs, after extensive litigation of those costs and other issues, in docket 09-0263. Therefore, the assurances that the known and measurable standard provide are in place, through the litigation of docket 09-0263. Additionally, the AMI pilot program is for a relatively short duration. We therefore approve inclusion of the $1.306 million of AMI pilot program costs.

6. New Business Revenue Credit

See Section VIII.E.

7. Tax Repair Methodology – New IRS procedures

The AG/CUB Position

The AG states that in September 2009, the IRS issued Revenue Procedure 2009-39, clarifying the procedures for taxpayers to obtain consent for changes in the procedure of accounting, for which, expenditures are currently deductible under Internal Revenue Code Section 162 and which expenditures must be capitalized under Internal Revenue Code Section 263. The existing deductibility of such expenditures had been expanded by proposed regulations that issued in March 2008, and Revenue Procedure 2009-39 clarified that consent to implement such changes in accounting would be automatic. (AG/CUB Exhibit 2.0 at 29; AG Initial Brief at 87; *See also* CUB Initial Brief at 37-38).

The AG asserts that the collective effect of the proposed regulations and Revenue Procedure 2009-39 was to greatly enhance the current repair allowance deduction for certain expenditures (including "network assets") that are capitalized for financial reporting purposes. Although the change in accounting would decrease the income taxes currently payable and its authorization is automatic, to date, ComEd has neither requested nor implemented the change in accounting for repairs, and the effect of the tax accounting change is not reflected in the determination of ComEd's revenue requirement. The AG acknowledges that the reason that ComEd has not yet requested this change in tax accounting is because ComEd is concerned that there remains significant uncertainty around the definition of 'unit of property' for purposes of determining a tax-deductible repair expense regarding ComEd's transmission and distribution property. The AG also acknowledges that ComEd asserts that it is collaborating with other utilities through the electric industry group, Edison Electric

Institute, for guidance from the IRS regarding the treatment of the repair allowance for transmission and distribution expenditures. (AG Initial Brief at 88).

However, the AG asserts, many other utilities are implementing changes in order to take advantage of this tax allowance. The AG asserts that an income tax deduction of $342,663,000 would result in additional accumulated deferred income taxes of $136,191,000. At ComEd's currently-requested rate of return, this increase to the balance of ADIT would reduce its revenue requirement by approximately $17.4 million. (AG Initial Brief at 90).

The AG asserts that ComEd's determination of its revenue requirement here does not reflect the impact of the increased income tax deduction for repair allowances. Absent any mechanism to preserve the benefits of the increased tax deductions for ratepayers, the AG concludes the ComEd's shareholder would reap a windfall benefit in the form of immediate, substantial income tax savings, if ComEd decides to make the tax accounting change after the completion of the present rate case. The windfall would result from the Section 481(a) adjustment, plus the going-forward deductions until the time when ComEd files its next rate case. The AG contends that therefore, if ComEd implements this change before the record in this case closes, then its rate base should be adjusted to reflect the additional ADIT related to the incremental deduction. The AG states that otherwise, the Commission should require ComEd to: 1) maintain the effect of 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 deduction from the effective date of the accounting change. The cumulative revenue requirement effect of the change in accounting for repair allowances, with appropriate carrying charges, should then be credited to customers at the time of the Company's next rate case. (AG Initial Brief at 90-91 *See also* CUB Initial Brief at 37-38).

Staff's Position

Staff recommends rejecting AG/CUB witness Mr. Effron's recommendation to adjust rate base and accumulated deferred income taxes, if ComEd changes its method for recording repair allowances for tax purposes prior to the close of this case. Staff states that it is not a known and measurable change to the test year. Staff opines that these separate accounting requirements are already in place from the Uniform System of Accounts, and due to the ICC's normalization approach to income taxes, the benefits of any reduced taxes will be reflected as a reduction to rate base in future rate cases. (Staff Ex. 17 at 12-13; Memo at 6).

ComEd's Position

ComEd witness Ms. Houtsma testified that implementation guidelines for the new IRS reporting method have not yet been issued by the IRS. If guidelines for the new method are issued and can be implemented by ComEd, customers will benefit because any resulting cash flows will help finance new plant investment and the cumulative accelerated benefit will be reflected as a reduction to rate base in future rate cases. (ComEd Ex. 29.0 at 38-41).

Analysis and Conclusions

We cannot conclude that ComEd's cautious behavior with the IRS, without more, is an act of imprudence. We also cannot conclude that only ComEd's shareholder will benefit when and if ComEd elects to use this new tax procedure. As Staff points out, when the IRS issues guidelines on this new procedure, and when ComEd avails itself of this procedure, (providing it proves to be beneficial) ratepayers will benefit in the future. Additionally, ComEd used a historic test year. As Staff points out, any change regarding the IRS will not occur during the test year. We therefore decline to adjust ComEd's rate base in the manner that Mr. Effron recommends.

8. Depreciation of Intangible Plant

ComEd's Position

ComEd seeks include over $70 million in its revenue requirement for costs related to the depreciation of general and intangible plant. While AG/CUB's witness Mr. Effron opines that the amortization expense should be adjusted for plant additions and fully-amortized intangible plants should be disallowed, ComEd states that AG/CUB is attempting to create single issue ratemaking. (ComEd Initial Brief at 84). ComEd contends that, even though a plant item may be retired before the end of the *pro forma* period, newly-placed projects will offset the depreciation that was not taken on the retired plants. ComEd argues that full consistency, as AG requests, also would require it to recognize depreciation of projects put in place in December 2009. (ComEd Reply Brief at 89).

The AG's Position

The AG argues that ComEd is inconsistent in its practice because it adjusts amortization expense for its post-test year additions to intangible plant items, but, it does not recognize the reductions to amortization due to the retirements of intangible plant items, or an intangible plant item becoming fully-amortized after the end of the test year. The AG opines that there must be a subsequent reduction to amortization, when ComEd recognizes an addition to intangible plant at the end of the test year. The AG states that this offset could be significant. (AG Initial Brief at 91). Recognizing both sides of this coin is what is consistent, and it is exactly what ComEd does with the depreciation of distribution plant. The AG argues that therefore, the same should take place with the intangible plant. (AG Reply Brief at 43).

CUB's Position

CUB asserts that there must be a matching adjustment to recognize reductions to intangible plant from those items that have become fully-amortized by March 31, 2011. CUB states that some intangible plant items, which began their amortization period in 2002, will be fully-amortized by March 31, 2011. CUB avers that ComEd's only argument against removing those fully-amortized assets from rate base is that ComEd made other investments in late 2009, which should balance out the amortized assets. CUB avers that ComEd has 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" does not justify keeping fully-amortized assets in rate base. According to CUB, allowing ComEd to do this results in recovery that is well-beyond ComEd's actual expense for these assets. (CUB Initial Brief at 38).

CUB further states that disallowing continued amortization of 2002 intangible plant, reducing *pro forma* amortization expense by $4,721,000, and eliminating the amortization of 2005 intangible plant, reduces *pro forma* amortization expense by $908,000. This would result in a total reduction to amortization expense of $5,629,000. 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; CUB Initial Brief at 39).

Analysis and Conclusions

We initially note that no party has articulated what the Uniform System of Accounts or any law requires in this regard. Further, we are at a loss as to how contesting one item, in a full-blown general rate case, constitutes "single-issue ratemaking." We urge all parties to refrain from making arguments that are obviously incorrect.

We further note that the adjustment that the AG and CUB proffer is based on a March 31, 2011, cut-off date. This appears to be, although it is not articulated by any party, based upon the AG/CUB proffered cut-off date for adjustments to *pro forma* capital additions. As is stated herein, we have declined to adopt this cut-off date.

However, ComEd has articulated no fact or law indicating that it should not be required to record depreciation of intangible plant when it actually occurs. At a minimum, it is inaccurate bookkeeping not to remove fully-amortized assets simply on the basis, essentially, that other assets "should balance out" with the fully-amortized assets. We adopt the AG/CUB's recommendation, but, we recognize that the dollar amount of the AG/CUB adjustment may change, due to the fact that the AG and CUB appear to have assumed a March 31, 2011, cut-off date and we impose a different cut-off date herein. The exact adjustment consistent with the conclusions above shall be the subject of a post-record data request. It shall require a determination as what assets are at issue, based on the cut-off date articulated herein for *pro forma* capital additions, (and depreciation and ADIT adjustments thereto) as well as the correct adjustment amount based upon that cut-off date.

9. Late Repayment Charge Reclassification

*S*ee Section VIII. D. of this Order.

10. Illinois Electric Distribution Taxes ("IEDT")

<u>ComEd's Position</u>

Illinois Electric Distribution Taxes are taxes on the quantity of electricity delivered in the state of Illinois. *See generally* 35 ILCS 620. The Public Utilities Revenue Act requires that they be calculated and collected based on a percentage of kilowatt hours used. *Id.* ComEd properly calculated its Illinois Electric Distribution Taxes (IEDT) liability using a weather-normalized tax and an off-setting credit based on a six-year average of credits. Fruehe Reb., ComEd Ex. 30.0 Public at 12.

AG/CUB

ComEd has requested amortization on additions to post-test year intangible plant during the *pro forma* period. The Company agrees with CUB that certain assets, which began their amortization period in 2002, will be fully amortized by the end of the *pro forma* period. ComEd Init. Br. at 84., ComEd Ex. 55.0 2nd Rev. at 34. CUB avers that, under the matching principle, as with other *pro forma* calculations, if *pro forma* amortization is included in rates then assets becoming fully-amortized during the *pro forma* period must correspondingly reduce rates. 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's 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.* CUB argues that the end of 2009 was a part of the test year, and the Company included all 2009 investments in rate base, so 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. CUB maintains that allowing such would result in recovery well beyond the Company's actual expense for these assets.

CUB calculations show that 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

STAFF

Staff recommends the Commission reject the AG/CUB proposal to revise ComEd's normalization of the IEDT pro forma adjustment for updated 2009 usage and estimated credit information since the AG/CUB methodology does not reflect the reality that the credits lag the taxes paid by several years, and that 2009 was an abnormally low kilowatt-hour use year. (Staff Ex. 17.0, pp. 10-11; AG/CUB Ex. 1.0, pp. 51-51; AG/CUB Ex. 1.3, Schedule C-19) Therefore, a normalized credit as ComEd proposed should be adopted.

Commission Analysis and Conclusion

ComEd contends that it properly calculated its IEDT liability using a weather-normalized tax and an off-setting credit based on a six-year average of credits. AG/CUB proposes to reduce ComEd's revenue requirement through an alternative methodology for determining IEDT by using the actual tax paid in 2009 and an estimated credit for 2009.

The Commission agrees with Staff and ComEd that calculating IEDT using a weather–normalized credit is appropriate because a normalized credit smoothes out year to year fluctuations. Moreover, we agree that AG/CUB's proposal must be rejected because AG/CUB's methodology underestimated the net amount of the IEDT that ComEd will pay on an on-going basis and it does not account for the fact that the IDET credit ComEd receives lags ComEd's payment by three years.

11. Depreciation and Amortization Expenses (Derivative and Direct)

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

ComEd's Position

ComEd seeks to include $3,104,000 in operating expenses for the amortization of costs associated with loss of the Medicare Part D subsidy. ComEd's witness Ms. Houtsma testified that the March 2010 federal health care reform legislation changed the tax-free status of cash subsidies paid to employers who provide prescription drug coverage to retirees. Absent the subsidy, there was concern in Congress that, after the adoption of Medicare prescription drug benefits in 2003, employers might cancel their coverage and have retirees become Medicare Part D participants. The tax-free subsidy, together with the deductibility of the prescription drug coverage costs, provided an incentive for employers to continue their programs. (ComEd Ex. 29.0 at 26-31; ComEd Initial Brief at 86).

According to Ms. Houtsma, the lengthy amortization period proposed by the AG will probably place ComEd with insufficient funds to make required tax payments when they become due. She explained that Mr. Effron's amortization period might be appropriate, if ComEd had passed on to customers only the actual cash subsidies that ComEd received, instead of the full amount that ComEd expected to receive. But in fact, she continued, customers have already enjoyed the full amount of the subsidy, even though ComEd has received only a fraction of the subsidy (in the aggregate 13%) from the government. (*See,* ComEd Ex. 29.0 at 27). ComEd contends that it is asking for symmetrical treatment: because it has passed on to customers each year the full benefit of the subsidy, as if it will receive the full amount of the subsidy from the government, ComEd should be allowed to recover the full amount of the taxes to be paid on the subsidies, as if ComEd will receive the full amount of the subsidy each year. ComEd states that the three-year amortization period that ComEd proposes allows this outcome to be achieved. (ComEd Initial Brief at 87-88).

Staff's Position

Staff no longer contests this issue. (Staff Memo at 7).

The AG's Position

The AG states that before the 2010 health reform legislation, in its calculation of the deferred tax asset, ComEd had assumed that the tax-free nature of the subsidy would continue in the future. As a result of that legislation, the deferred tax asset had to be "written down" to recognize that the subsidy would be subject to income taxes after 2012. ComEd now seeks authority to establish a regulatory asset for the write-down, to amortize the regulatory asset over three years, and to include the annual amortization in its revenue requirement. The AG asserts that the lost tax benefits, on which, the deferral is based would have been realized over many years. For example, the AG continues, the accrued subsidy as of December 2009 was $36.6 million, but the actual subsidies to be received in the years 2010 through 2012 are estimated to average about $3.4 million annually. From this fact, the AG contends that one can imply that the accrued subsidy as

of the end of 2009 would be realized over approximately eleven years. (AG Initial Brief at 94).

According to the AG, ComEd witness Ms. Houtsma was unable to support its proffered three year time period, or specify the time by which the full amount of the tax due needs to be paid, other than to say that it will not be due before January 1, 2013, and that "The exact timing of when the tax is due is dependent on when the federal government remits the cash subsidies to ComEd." The AG argues that therefore, Ms. Houtsma does not appear to know specifically when the tax will need to be paid. It concludes that therefore, it is unclear how she knows that the necessary amounts will not have been collected from customers by that time. In contrast, the AG continues, AG/CUB witness Mr. Effron's proposed ten-year amortization period is intended to be consistent with when the federal government remits the cash subsidies to ComEd.

The AG recommends amortizing this deferral over a period of at least ten years, resulting in annual amortization expense of $931,000. This is $2,173,000 less than the annual amortization expense of $3,104,000 calculated by ComEd. Thus, the *pro forma* amortization expense would be reduced by $2,173,000. (AG Initial Brief at 94-95).

Analysis and Conclusions

We agree with ComEd that no adjustment is necessary. Merely because the exact timing as to when the tax is due is not known does not mean that payment is not imminent. Also, as ComEd points out, it has already has passed on to customers each year the full benefit of the subsidy as if it will receive the full amount of the subsidy from the government. ComEd should therefore be permitted to recover the full amount of the taxes to be paid on the subsidies, as if ComEd will receive the full amount of the subsidy each year.

13. Taxes Other than Income Taxes (Derivative Adjustments)

14. Income Taxes (Derivative Adjustments)

ComEd states that while the evidentiary hearing in this docket was pending, the Illinois state corporate income tax rate changed from 7.3% to 9.5% and new federal tax provisions were enacted which accelerated the tax deductions that are applicable to the 2010 and 2011 *pro forma* plant additions. (Tr. 2410-11). Both of these new provisions should be incorporated into the revenue calculations. Because of the derivative nature of income taxes, the ultimate impact of these changes will vary, depending on the final revenue requirement. Staff Cross Ex. 15, which is DLH 21.01 Revised, reflects the mechanics of making this change and provides the impact to Staff's rebuttal position. *Id.* The schedules that are attached to DLH 21.01 reflect where the tax increase adjustment has been made. (ComEd Initial Brief at 88). This issue is not contested. ComEd's proposed methodology is reasonable and it is hereby approved.

15. Photovoltaic Pilot Costs

In order to narrow the issues in this proceeding, ComEd accepted Mr. Tolsdorf's proposed disallowance of the $10,251 in costs related to the Photovoltaic Pilot program. (ComEd Ex. 55.0 2nd Rev. at 34). The Commission approves Staff's proposal.

16. Customer Deposits – Interest Expense Component

Staff and AG/CUB proposed to include the interest expense associated with customer deposits as an operating expense, which increases test year revenue. (Staff Ex. 19.0 at 6; AG/CUB Ex. 7.1, Schedule B-8). ComEd does not dispute this adjustment. (ComEd Ex. 29.0 at 37; AG/CUB Ex 1.0 at 39; AG/CUB Ex 7.0 at 31; Staff Ex. 19.0 at 6). This adjustment is reasonable and is hereby approved.

17. Materials and Supplies Inventories Balance

Staff proposed using a thirteen-month average balance to determine the balance for materials and supplies to be included in rate base, rather than a year-end balance, as proposed by ComEd. In an effort to narrow the issues in this proceeding, and without conceding the validity of ComEd's position, Staff accepted ComEd's proposed year-end balance for materials and supplies as reasonable. (Staff Reply Brief at 26. This adjustment is reasonable and is hereby approved.

18. Operating Expenses (Total)

Based on the electric utility delivery services operating expense statement as originally proposed by ComEd and the adjustments to operating revenues and expenses as summarized above, the total electric utility delivery services operating expenses for ComEd approved for purposes of this proceeding are $1,420,489,000. The operating expense statement may be summarized as follows:

Approved Operating Expense Statement

(In Thousands)

Operating Revenues	$2,109,616
Other Revenues	103,792
Total Operating Revenue	2,213,408
Uncollectibles Expense	32,139
Distribution	309,199
Customer Accounts	157,744
Customer Services and Informational Services	8,803
Sales	0
Administrative and General	339,624
Depreciation and Amortization	387,104
Taxes Other Than Income	147,041
Regulatory Debits	38,835
Total Operating Expense Before Income Taxes	1,420,489

State Income Tax	8,932
Federal Income Tax	-42,761
Deferred Taxes and ITCs Net	262,584
Total Operating Expenses	1,649,244
Net Operating Income	$ 564,164

The development of the overall electric utility delivery services operating expense statement adopted for purposes of this proceeding is shown in Appendix A to this Order.

V. Rate of Return

A. Overview

ComEd's Position

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

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

B. Capital Structure

ComEd's Position

ComEd proposes to use its actual capital structure adjusted as in past proceedings to remove goodwill. This is a reasonable capital structure, appropriate for ratemaking, and if coupled with an appropriate rate of return, will allow ComEd to compete in the capital markets as necessary for its operations. Trpik Dir., ComEd Ex. 4.0 Rev. at 20-21. With the exception of a small issue concerning the balance of short-term debt discussed in the next section, the witnesses addressing capital structure issues agree on the components and percentage weights used in ComEd's capital structure.

C. Cost of Short-Term Debt

ComEd's Position

The Commission should approve ComEd's proposed short-term debt balance of $15,870,000 which ComEd calculated using the thirteen month average balance of short term debt ending March 31, 2010. Fruehe Reb., ComEd Ex. 30.0 at 26.

Staff proposes a short-term debt balance of $49,344,124. McNally Dir. Staff Ex. 5.0 at 4. Staff calculated the short-term debt balance using the thirteen month average balance ending September 2010. *Id*. at 3. ComEd explained that while either calculation method could be used, using the end date March 31, 2010 provides a better indication of cost and balance of short-term debt over the historical year period because more of the 2009 test year is used to calculate the average and it aligns with the other components of capital structure, which are also measured as of March 31, 2010. Fruehe Reb., ComEd Ex. 56.0 3rd Rev. at 25. IIEC and AG/CUB also used the March 31, 2010 period in their direct testimony, before Staff proposed using the September 2010 period. Gorman Dir., IIEC Ex. 1.0-C at 12-13; Thomas Dir., AG/CUB Ex. 4.0 Rev. at 37. The Commission should therefore approve ComEd's short term debt balance amount using the thirteen month period ending March 31, 2010.

Staff

Staff proposes a short-term debt balance of $49,344,124. McNally Dir. Staff Ex. 5.0 at 4. Staff calculated the short-term debt balance using the thirteen month average balance ending September 2010.

The primary issue with regard to the capital structure is whether short-term debt should be measured over a thirteen month period ending March 31, 2010, as the Company recommends, or a thirteen month period centered on March 31, 2010, as Staff recommends. Staff demonstrated that the use of a period centered on March 31, 2010 better aligns the measurement period for short-term debt with that of the long-term capital components. Under the Company's proposal, 78 months are misaligned; Staff's proposal cuts the number of misaligned months almost in half (42 months). (Staff Ex. 20.0, p. 3) Moreover, not only is the adoption of that approach consistent with Commission precedent, but that consistency removes the opportunity for parties to manipulate the cost of capital by arbitrarily proposing whichever method produces the results they may desire. (Staff Ex. 5.0 pp. 3-4; Staff Ex. 20.0 pp. 2-3) Indeed, the Commission has explicitly acknowledged this potential for bias and found consistency to be the solution. (Order, Docket Nos. 06-0070/06-0071/06-0072 (Cons.), November 21, 2006, p. 104)

Likewise, in this proceeding the Commission should adopt Staff's proposal to use a short-term debt measurement period centered on the measurement date of the other capital structure components.

Commission Analysis and Conclusion

ComEd proposes a short term debt balance in the amount of $15,870,000. Fruehe Reb., ComEd Ex. 30.0 at 26. Staff proposes a short term debt balance of

$49,344,124. McNally Dir. Staff Ex. 5.0 at 4. We believe ComEd's calculation method is preferable because it captures more of the 2009 test year and aligns with how other components of ComEd's capital structure were measured. Therefore, the Commission approves ComEd's proposed short term debt balance in the amount of $15,870,000.

D. Cost of Long-Term Debt (Potentially Uncontested)

ComEd's Position

ComEd's cost of long-term debt is 6.52%. That value is based on Staff's slightly-revised version of ComEd's original 6.53% calculation, which ComEd accepts. *See* McNally Dir., Staff Ex. 5.0 at 9. IIEC and AG/CUB accepted ComEd's 6.53% cost of long term debt and do not dispute the small adjustment that ComEd and Staff have concluded is appropriate. No contested issues remain.

Therefore, the Commission adopts ComEd's cost of short term debt is 6.52%.

E. Cost of Common Equity

ComEd's Position

ComEd requests that the Commission approve its reasonable and appropriate proposed total cost of common equity (or "ROE") of 11.30%. ComEd Init. Br. at 89. ComEd's proposed base cost of equity derives from the independent expert assessments performed by ComEd witnesses Dr. Hadaway and Dr. Seligson.

Dr. Hadaway estimates ComEd's cost of equity using basic discounted cash flow ("DCF") models and tested the reasonableness of his findings with bond-yield plus equity-risk premium analysis. Hadaway Dir., ComEd Ex. 11.0 at 1. He explains that the DCF model estimate of ROE is the sum of expected dividend yield plus expected long-term growth or price appreciation. *Id.* at 11. The risk premium method is based on the current interest rates on government or corporate bonds with an added increment to account for the additional risk faced by equity investors. *Id*.

Dr. Hadaway applies three alternative versions of the DCF model to 31 investment grade electric utilities and 4 gas local distribution companies ("LDC"s). *Id.* at 2-3. In the first version of the DCF model, Dr. Hadaway uses the constant growth format with long-term expected growth based on analysts' estimates of five-year utility earnings per share growth. *Id.* at 31. In the second version, for the estimated constant long-term growth rate, he uses the estimated growth rate for long-term GDP. *Id*. In the third version of the model, he applies a three-stage growth rate approach similar to models the ICC Staff has used in recent cases. *Id.* He explains that he restricted his comparable group to investment grade companies with senior secured bond ratings of at least BBB from Standard & Poor's (S&P) or Baa from Moody's and who obtained at least 70 percent of their revenues from domestic regulated utility sales. *Id.* at 2. For his risk premium analysis he uses *Moody's* average public utility bond yields and recent and projected triple-B utility bond interest rates. *Id.* at 3.

The results of Dr. Hadaway's updated DCF analysis yield an estimated ROE range of 10.3%-10.9%. Hadaway Reb., ComEd Ex. 37.0 at 2. Also, Dr. Hadaway discounts the results of his risk premium analysis because they were negatively skewed by the artificially low interest rates resulting from the government's expansionary money

policies. *Id.* Dr. Hadaway noted that due to the recent market turmoil and the continuing effects on capital market conditions, use of a lower DCF range likely understates the cost of equity. Hadaway Dir., ComEd Ex. 11.0. at 37-38. He also demonstrates that the relatively lower prices for utilities shares indicate that the cost of capital for utilities is higher. *Id.* at 25-26. For these reasons, Dr. Hadaway's estimates ROE is reasonable.

ComEd's other expert, Dr. Seligson, uses a risk premium method and a comparable earnings method to determine ComEd's cost of common equity. Seligson Dir., ComEd Ex. 12.0 Rev. at 7. To determine the cost of common equity using the comparable earnings method, Dr. Seligson examines the earning levels of utility operating companies. *Id.* at 9. This method yields a median return of 11.4%. *Id.* To determine the cost of equity using the risk premium method, Dr. Seligson uses the estimated yield for 2011 of United States bond returns as the basis for calculating risk premiums attributable to alternative investments. *Id*. at 9-10. The resultant return on common equity under the risk premium method was 12.6%. *Id.* at 10. Dr. Seligson determined that the middle ground between the two methods, 12.0%, represents a reasonable return on common equity for ComEd. *Id.*

Dr. Seligson observes that investors are concerned about regulatory risk and seek assurances that the allowed return on equity and resulting earnings will be sufficient to attract new capital. *Id.* at 11. He notes that investor representatives viewed the Commission's low allowed returns in the *Ameren* case as a negative order and concludes that the Commission should attempt to reverse the negative opinions of investor representatives so that ComEd may compete in the marketplace for funds necessary to further capital expenditures and provide a fair and reasonable return to its shareholders. *Id.* at 11-12. Dr. Seligson reasons that the higher risks facing utilities for major construction initiatives; the mounting need for external financing; increasing costs for medical, post-retirement, and pension benefits, and other factors warrant higher allowed returns on equity for utilities than have been authorized in many jurisdictions in the recent past. Seligson Dir., ComEd Ex. 38.0 at 2.

The Commission should reject the estimated ROEs proposed by Staff, AG/CUB, and IIEC. Staff witness Mr. McNally proposes a return on equity of 10.0% (McNally Dir., Staff Ex. 5.0 at 33), IIEC witness Gorman submits an estimate resulting in a 9.6% return on equity (Gorman Dir., IIEC Ex. 1.0 at 38) and AG/CUB witness Thomas proposes an even lower return on equity of 8.94% (Thomas Dir., AG/CUB Ex. 4.0 Rev. at 37) with the possibility of an adjustment if the SFV rate design is adopted (*id.* at 14-15).

The evidence shows that the parties' recommendations are below ComEd's cost of equity capital. ComEd explains that the other parties fail to consider the ongoing effects of the recent financial crisis and offer recommendations more aligned with the artificially low, government policy-induced interest rates than with the market cost of equity capital. Hadaway Reb., ComEd Ex. 37.0 at 3. ComEd further explains that the other parties' conclusion that the cost of equity has dropped in lockstep with falling interest rates is incorrect and that their traditional rate of return models should have been tempered with consideration for the widened equity risk premiums that result from heightened equity market risk aversion. *Id*. ComEd also observes that the other parties' ROE recommendations are well below the rate of return authorized by other state utility Commission's throughout the country. *Id.* at 9-10. Moreover, ComEd

demonstrates that Staff's, AG/CUB's and IIEC's contentions that Dr. Hadaway's and Dr. Seligson's base common cost of equity analyses are incorrect are flawed and unsupported by the record.

Response to Mr. McNally Regarding Base Cost of Equity

Concerning the ROE proposed by Staff witness Mr. McNally, ComEd demonstrates that Mr. McNally's comparable company selections contained companies that are not comparable at all to ComEd. *Id.* at 11; McNally Dir., Staff Ex. 5.0 at 10-21. ComEd also disagrees with Mr. McNally's DCF analysis because he employs a low growth rate for GDP to average down his analysts' growth rate estimates. *Id.*

ComEd explains that Mr. McNally's sample group includes two natural gas companies that receive a major portion of their revenues from unregulated activities. Tr. at 1872-1874; Hadaway Reb., ComEd Ex. 37.0 at 13. As detailed in ComEd's Initial Brief, the influence of these non-comparable companies is exaggerated because Mr. McNally's sample is relatively small (he uses 12 companies, while Dr. Hadaway uses 31). ComEd Init. Br. at 97. These non-comparable gas companies thus account for 16.6% of Mr. McNally's DCF sample and its results. *Id.* at 97-98. Removing these two non-comparable companies – and retaining all of the major regulated distributors – would raise Staff's DCF results by 25 to 40 basis points. *Id*.; McNally, Tr. at 1873. Moreover, as ComEd stated in its Reply Brief, Staff's criticism of Dr. Hadaway's failure to use size as a comparable company criterion is not supported. ComEd Reply Br. at 99; Staff Br. at 74. While Dr. Hadaway's states comparable company criteria do not include a size filter and his 35-company group did contain a few relatively small utilities, not one of those companies is as small as either of Mr. McNally's New Jersey companies in terms of net plant investment. *Id.*

ComEd also explains that Staff's argument, that if the cost of equity of the Comparable Sample would decrease by 19 basis points Southern Union was to be removed from Mr. McNally's sample, (Staff Br. at 72-73) is irrelevant. *Id.* at 100. Although inclusion of Southern Union (along with AGL Resources) is "questionable," (Hadaway Reb., ComEd Ex. 37.0 at 14) Dr. Hadaway did not recommend that either be excluded. *Id.* ComEd states that Dr. Hadaway's point is that the two New Jersey gas utilities are not comparable to ComEd in a meaningful way from an investors' perspective notwithstanding any statistical analysis (Hadaway Reb., ComEd Ex. 37.0 at 14) and their removal is therefore appropriate. *Id.*

ComEd also details how Mr. McNally's GDP growth rate forecast is incorrect because it is based on erroneous assumptions that are inconsistent with actual historical growth for the U.S. economy. Hadaway Reb., ComEd Ex. 37.0 at 15. For example, Mr. McNally's 2.4% inflation rate compares to historical GDP inflation rates that have averaged 3.5% and his real GDP growth rate of 2.5% is much lower than the actual historical growth rate of 3.4%. *Id.* at 16; *See* McNally Dir., ComEd Ex. 5.0 at 17-19. ComEd concludes that it is reasonable to believe that future real growth and inflation will both be 3% and therefore a 6% growth rate is a more reasonable proxy for investor's long-term expectations. Hadaway Reb., ComEd Ex. 37.0 at 15. Use of the 6% growth rate, combined with correction of Staff's comparable sample, increases Mr. McNally's multi-stage DCF results to 10.44% and an average DCF (non-constant and

constant growth) of 10.29%. *Id.* at 16. This is 60 basis points higher than the average of Mr. McNally's constant and non-constant growth DCF results. *Id. at 11*.

Also, as ComEd explains in its Initial Brief, Mr. McNally's CAPM analysis placed sole reliance on a risk free rate (30 year Treasury bonds) that he chose to measure on September 22, 2010. ComEd Init. Br. at 96. The Commission has recently rejected use of such a pure "spot date" approach in its *North Shore* decision (Thomas, Tr. at 1783) and notes the problems that can result from using such data. *Id.*; *See North Shore Gas Co., et al,* ICC Docket Nos. 07-0241/07-0242 (Cons.), Final Order (Feb. 5, 2008) at 92, 125-6. Mr. McNally's choice of a September 22 spot date was unfair to ComEd because the 3.77% rate measured on that date is not only nearly an all-time low (McNally Dir., Staff Ex. 5.0 at 25; Tr. at 1879-1880), but is fully 67 basis points below the rate on December 29, 2010 and well below the risk-free rate investors demand generally throughout the entire year (Hadaway Sur., ComEd Ex. 62.0 at 9 n.1; Tr. at 1784-1785; ComEd Cross Ex. 20); ComEd Init. Br. at 96-97). ComEd believes that it is inappropriate and unfair to set ComEd's delivery rates – rates that must recover its costs going forward – based on a short-lived blip in bond interest that the data shows to have been strikingly anomalous. *Id.* ComEd asserts that if Mr. McNally's CAPM were adjusted upward by those 67 basis points alone, the results of his CAPM model would have been 10.99%, not 10.32%. *Id.*; *See also,* McNally Dir., Staff Ex. 5.0 at 43 (Table 3). That result would, in turn, significantly increase his total recommended cost of equity. *Id.*

In addition, the record shows that the Commission has rejected the "b times r" sustainable growth argument Mr. McNally's employs in an effort to demonstrate that Mr. Hadaway's average analyst growth rate is not sustainable. Hadaway Reb., ComEd Ex. 37.0 at 17-18; *See* McNally Dir., Staff Ex. 5.0 at 45-48. As Dr. Hadaway explains, "b times r" calculations bear little relationship to the numerous factors that affect investors' long-term growth rate expectations. Hadaway Reb., ComEd Ex. 37.0 at 18. ComEd also states that Mr. McNally's comments about Dr. Hadaway's bond-yield plus equity-risk premium analysis were irrelevant because Dr. Hadaway only offers that analysis for general perspective and would now discount those results. *Id.* at 17; *See* McNally Dir., Staff Ex. 5.0 at 48-50. Mr. McNally's comments about Dr. Hadaway's endorsement of the upper end of the DCF range were also misplaced. Hadaway Reb., ComEd Ex. 37.0 at 18; McNally Dir., Staff Ex. 5.0 at 50-51.

In response to Mr. McNally's criticism of Dr. Seligson's ROE estimates, ComEd states that all securities analysts covering utilities and reporting to investors use the return on book value and it therefore is an appropriate measure of current investor required rate of return. Seligson Reb., ComEd Ex. 38.0 at 2. Dr. Seligson also explains that an analysis on a security specific basis is not the only approach that is useful to the Commission in arriving at a fair and reasonable return on equity and that the Commission should look to the risk premium method for instruction and information. Many in the market look to the risk premium method in deciding which firms will get scarce funding. *Id.* at 2-3. ComEd also explains that the Commission should consider the risk premium approach because it takes into account the severe effects of the capital markets on regulated electric utilities. *Id.* at 6. The evidence also shows that Dr. Seligson's comparable earnings approach is reasonable as reflected in a recent survey

where 25% of the utility commissions surveyed stated they employed the comparable earnings approach. *Id.* at 3. Moreover, Dr. Seligson notes that the comparable earnings approach is no more prone to distortion by accounting practices than any other method. *Id.* at 4.

Response to Mr. Gorman Regarding Base Cost of Equity

Concerning IIEC witness Mr. Gorman's proposed ROE estimate, ComEd presents evidence that his estimated ROE for ComEd is too low because his model inputs are negatively biased. Hadaway Reb., ComEd Ex. 37.0 at 19. ComEd explains that under current market conditions, Mr. Gorman's version of the CAPM is not reasonable. *Id.* at 20. Specifically, ComEd explains that Mr. Gorman excluded data in one of his constant growth DCF models that would increase his results and summarize the data in a way that skews the results downward. *Id.* In his multi-stage DCF model, while agreeing with Dr. Hadaway's use of GDP growth for the long-term growth rate, Mr. Gorman uses a short-term estimate of GDP growth. Such an approach was not consistent with DCF model requirements. *Id.*; *see* Gorman Dir., IIEC Ex. 1.0 at 24. Moreover, ComEd further notes that Mr. Gorman's GDP growth rate estimate is entirely dominated by recently low inflation rates. Hadaway Reb., ComEd Ex. 37.0 at 20; Gorman Dir., IIEC Ex. 1.0 at 47-48. Also, ComEd notes that the inflation rate in Mr. Gorman's GDP forecast is almost a full percentage point lower than long-term historical averages and that the approach is inconsistent with the long-term requirements of the DCF model. Hadaway Reb., ComEd Ex. 37.0 at 20; Gorman Dir., IIEC Ex. 1.0 at 47-48. ComEd also demonstrates that Mr. Gorman's CAPM estimate is too low because he mismatches the CAPM inputs for the risk-free rate and the market risk premium. Hadaway Reb., ComEd Ex. 37.0 at 20. ComEd explains that as a result of this mismatch, Mr. Gorman "cherry picks" the CAPM approach to produce a low estimate of ROE, and therefore his CAPM estimate should be disregarded. *Id.* at 23; *see* Gorman, Dir., IIEC Ex. 1.0 at 37-38; IIEC Ex. 1.16.

Concerning Mr. Gorman's criticism of Dr. Hadaway's estimates, ComEd explains that Mr. Gorman's comments are based on the mistaken view that the cost of equity for utilities has declined as much as interest rates. Hadaway Reb., ComEd Ex. 37.0 at 25. Dr. Hadaway states that a comparison to allowed rates of return for other utilities demonstrates that Mr. Gorman's characterization of his GDP growth forecast is misplaced and that his contention that equity costs have declined significantly is incorrect. *Id.* Specifically, Dr. Hadaway notes that the GDP growth rate he employs is not based on historical GDP data as Mr. Gorman suggests, but instead, is based on general economic conditions that investors may expect for utilities in the very long run, as is required in the DCF model. *Id.* Dr. Hadaway also notes that Mr. Gorman's objections to his equity risk premium analysis are misplaced primarily because Dr. Hadaway has already discounted those results. *Id*. at 26.

Dr. Seligson explains that Mr. Gorman's contention that his risk premium analysis was flawed, because of the Morningstar market risk premium and Treasury bond interest rate he employed, is incorrect. Seligson Reb., ComEd Ex. 38.0 at 4. In support, he notes that the 12.6% cost of equity produced by those factors is lower than the 12.74% weighted average expected market rate of return calculated by Mr. McNally.

Id. Dr. Seligson also demonstrates that Mr. Gorman's contention that utilities are below market risk companies that do not require reasonable rates of return is partly responsible for the extremely low authorized returns on equity that utilizes have received. *Id.* at 5. Dr. Seligson explains that maintaining low rates of return on the theory that utilities are below market risk is the wrong course of action in the current difficult economic times and that the risks faced by utilities requiring outside financing to pay for required capital expenditures must be considered in setting fair and reasonable rates that will provide an appropriate return on common equity. *Id*.

Response to Mr. Thomas Regarding Base Cost of Equity

Concerning AG/CUB witness Mr. Thomas' proposed ROE estimate, ComEd presents evidence that his estimated ROE for ComEd is well below the reasonable range. Hadaway Reb., ComEd Ex. 37.0 at 28. Dr. Hadaway explains that Mr. Thomas' ROE is too low because he uses only "b times r" internal growth rates in his constant growth DCF analysis then combines these low growth rates with a similarly low 20-year historical average of GDP growth in the third stage of his multi-stage model. *Id.* at 27; *see* Thomas Dir., AG/CUB Ex. 4.0 Rev. at 24-29. Dr. Hadaway further explains that Mr. Thomas' GDP growth rate is low because it is from the most recent 20 years of data, which are entirely dominated by historically low inflation rates and negatively influenced by the financial crisis' effects on economic growth. Hadaway Reb., ComEd Ex. 37.0 at 27. ComEd noted that Mr. Thomas' methods are not consistent with the Commission's preferred approaches and that his 8.94% recommendation is much lower than ROEs recently allow for other electric utilities in Illinois or around the country. *Id.* at 28. Also, Mr. Thomas' analysis of recent utility stock performance and utility risk profiles is incorrect. *Id.* ComEd supports and details not only how Mr. Thomas' analysis includes several mistakes, inaccurate data input and averaging methods, but also how he compares utility stock prices adjusted for cash dividends to the S&P 500 index which was not similarly adjusted. *Id*. at 28-30; *see* Thomas Dir., AG/CUB Ex. 4.0 Rev. at 10-11. His conclusion, therefore, that utility stock prices have increased relative to their highest levels in 2007 is incorrect. Hadaway Reb., ComEd Ex. 37.0 at 28-30.

The evidence also shows that contrary to Mr. Thomas' claims, Dr. Hadaway's, DCF growth rates are sustainable. *Id.* at 30-31. ComEd explains that Mr. Thomas' assertions are based on his employment of the improper "b times r" growth approach and that he ignores readily available survey of analysts' growth forecasts. *Id.*; *see* Thomas Dir., AG/CUB Ex. 4.0 Rev. at 24-25. Mr. Thomas' criticisms of Dr. Seligson's analysis echo those presented by Staff and IIEC, and they fail for the same reasons. Seligson Reb., ComEd Ex. 38.0 at 5-6.

For all of the above reasons ComEd concludes that Mr. Thomas' recommendations should be discounted and should not influence the Commission's ROE decision.

Response Regarding Proposed 40-Basis-Point Adder

The record shows that the Commission should reject the arguments posed by Mr. Gorman, Mr. McNally, Dr. Brightwell and Mr. Thomas in opposition to ComEd's proposed 40 basis-point adder because none of the witnesses address the combined

effects of risk and revenue erosion attributable to the impacts of energy efficiency programs in ComEd's service territory. Tierney Reb., ComEd Ex. 39.0 at 2.

First, ComEd explains that Mr. Gorman's contentions regarding the proposed adder should be rejected because he mischaracterizes the testimony of Dr. Tierney when he states that she acknowledged that regulatory mechanisms provided a high level of assurance of full cost recovery. *Id.* at 2-3; *see* Gorman Dir., IIEC Ex. 1.0 at 53-54. In truth, Dr. Tierney emphasizes in her testimony that the law was silent on the implication of energy efficiency programs for other rate making issues and that recovery of direct costs was not the only way the programs could impact a utility's revenues and financial condition. Tierney Reb., ComEd Ex. 39.0 at 3. In addition, ComEd notes that Mr. Gorman provided no support for a number of his statements. *Id.* In particular, ComEd explains, Mr. Gorman provided no support for his statement implying that the proposed 40 basis-point adder would offset energy efficiency gains and economic benefits created on customers' behalf by the demand response and energy efficiency programs. *Id.* at 4; *see* Gorman Dir., IIEC Ex. 1.0 at 54. The record shows that through the testimony of ComEd witness Mr. Jensen, ComEd demonstrates that the lifetime net benefit of the programs implemented through ComEd's 2008-2010 Energy Efficiency and Demand Response Plan alone is $155 million contrasted with the estimated annual 40-basis-point adder of approximate $30.8 million proposed in this rate case. Tierney Reb., ComEd Ex. 39.0 at 4; *see* Jensen Dir., ComEd Ex. 17.0 Rev. at 5.

In addition, ComEd explains that Mr. Gorman's position that using a forecasted test year could permit ComEd to set rates in an efficient manner by reflecting sales level impacted by energy efficiency and demand response programs should also be set aside. Tierney Reb., ComEd Ex. 39.0 at 4-5; *see* Gorman Dir., IIEC Ex. 1.0 at 54. A future test year was not selected for this rate case, and a future test year would not address the various other risk elements ComEd faces. Tierney Reb., ComEd Ex. 39.0 at 4-5. ComEd further explains that Mr. Thomas' position that the impact of energy efficiency and demand response programs are better addressed using a future test year fails for the same reasons. *Id.* at 5; *see* Thomas Dir., AG/CUB Ex. 4.0 Rev. at 36.

Also, Mr. McNally asserted, without basis or support, that adding a risk premium to the cost of common equity estimates for Dr. Hadaway's and Dr. Seligson's comparable company samples would not be warranted if the companies in the samples already reflect the risks described in Dr. Tierney's testimony. Tierney Reb., ComEd Ex. 39.0 at 8; *see* McNally Dir., Staff Ex. 5.0 at 55. Unlike Mr. McNally, however, Dr. Tierney analyzed the groups of companies used by Dr. Hadaway and Mr. Seligson in their cost of equity studies to determine whether the included companies were subject to energy efficiency requirement risks comparable to those confronting ComEd in Illinois. Tierney Reb., ComEd Ex. 39.0 at 8-11. Her analysis shows that the vast majority of companies in the groups do not reflect the combination of aggressive energy efficiency targets and absence of compensating ratemaking mechanisms that face ComEd. *Id.* No witness presented any contrary evidence. Tierney Sur., ComEd Ex. 64.0 at 1. Because the energy efficiency risks and revenue erosion to which ComEd is subject are not reflected in the cost of equity estimates presented by Dr. Hadaway and Mr. Seligson, a cost of equity "adder" is warranted to address those risks. For these reasons Mr. McNally's contention should be rejected by the Commission as well.

ComEd also supports and details how Staff witness Dr. Brightwell's analysis of the 40 basis-point adder is flawed and should be rejected by the Commission. ComEd noted that though Dr. Brightwell acknowledges that energy efficiency programs can cause a conflict between the interests of customers and shareholders (Brightwell Dir., Staff Ex. 8.0 at 2-3), he seemed content to ignore this ratemaking problem and fails to offer an alternative to address the problem. Tierney Reb., ComEd Ex. 39.0 at 14. Also, ComEd demonstrates that Dr. Brightwell's contention – because the proposed adder will make efficiency more costly, customer bill increases will result that will erode customer support for the programs – is incorrect. *Id.*; *see* Brightwell Dir., Staff Ex. 8.0 at 4. ComEd explains that the testimony of Mr. Jensen summarizes the lifetime savings that customers will experience resulting from implementation of ComEd's energy efficiency programs and shows that customers will continue to reduce the overall size of their electricity bill through participation in efficiency and demand response programs or actions. *Id.* at 14-15; *see* Jensen Dir., ComEd Ex 17.0 Rev. at 1-2. In addition, ComEd explains that Mr. Brightwell's suggestion that a particular cost should be excluded from a utility's revenue requirement because it will diminish customer acceptance of services associated with this cost is unreasonable. *Id.* at 15. This argument could be applied to any legitimate cost item but would render a revenue requirement entirely unjust and unreasonable because it would fail to reflect the real cost of providing service. *Id.* ComEd further explains that Dr. Brightwell's contention that ComEd is not likely to incur involuntary performance risk penalties for failure to achieve efficiency goals misses ComEd's point that the proposed adder would reduce ComEd's incentive to subject itself to such penalties over the course of the years during which new rates would be in effect. *Id.*; *see* Brightwell Dir., Staff Ex. 8.0 at 4-8.

Staff

Response to CUB

CUB's Initial Brief suggests that Staff's DCF cost of common equity estimate is biased upward due to its reliance on analyst growth rates. CUB argues that the 8.99% cost of common equity Dr. Hadaway calculated for Staff's sample using the "b times r" growth approach confirms Mr. Thomas's 8.94% cost of common equity estimate and highlights the bias in Staff's estimate. CUB further notes the fact that Staff's 5.53% analyst growth rate exceeds 5.0% long-term GDP estimate demonstrates that the current 3-5 year estimates are not sustainable. (CUB IB, pp. 61-62) Staff disagrees with CUB's conclusions. First, while Mr. McNally acknowledges that the continuous sustainability of the Zacks growth rates for the Comparable Sample is questionable, he could not conclusively establish that those growth rates are unsustainable, as CUB suggests. That is precisely why Mr. McNally recommends the use of both a single stage, constant growth DCF analysis and a multi-stage non-constant DCF analysis. (Staff Ex. 5.0, pp. 15-16) Second, Dr. Hadaway's 8.99% cost of common equity calculation both fails to consider the external growth component of the sustainable growth formula and is mathematically incorrect. When those flaws are corrected, the DCF result is 9.60%. (Staff Ex. 20.0, pp. 9-13) The similarity of that result to Staff's 9.69% DCF recommendation corroborates Staff's decision to use a combination of constant growth and a non-constant growth DCF analyses. In fact, that 9.60% result is much closer to Staff's 9.69% DCF recommendation than to CUB's 8.94% DCF

recommendation. Thus, contrary to CUB's assertion, that result validates Staff's recommendation rather than CUB's.

Response to IIEC

IIEC's Initial Brief states that Staff's 12.74% estimated required return on the market is "problematic," noting that it implies a growth rate of over 10%. (IIEC IB, p. 31) However, that growth rate estimate is not provided in the testimony cited and, to Staff's knowledge, is not a part of the record. Thus, it is unclear how IIEC arrived at that number. Regardless, the approach Staff uses to estimate the required return on the market has been adopted numerous times by the Commission, including in the recent Ameren rate case. In that case, IIEC made a similar argument as it makes now. As Staff explained in that proceeding:

> IIEC argues that Staff's market risk premium in its CAPM analysis is overstated, Staff recognizes that some of the growth rates used in Staff's DCF analysis of the S&P 500 are unsustainably high, which produces an upward bias in Staff's market return estimate, and, thus in Staff's CAPM cost of equity estimate. Staff avers that while there is upward bias in Staff's estimate of the market return, there is no way to know the extent of the bias. Staff notes it did not use a non-constant growth DCF to estimate the return on the market because of the extreme difficulty of applying the more elaborate model to 500 companies. Staff states Mr. Gorman's non-constant DCF analysis of the S&P 500 illustrates the difficulty of applying that model to the diverse group of companies that compose that index, as his estimate of the required return of the market is 8.71%, 129 basis points below his 10.00% rate of return on common equity recommendation for AIU. Staff asserts his results imply that the S&P 500 is less risky than AIU, which is not plausible.

(Order, Docket No. 09-0306/0307/0308/0309/0310/0311 (Cons.), April 29, 2010, p. 186 and 214) Furthermore, Mr. Gorman testified that he uses a market risk premium that was "developed in a manner very similar to Staff witness McNally's development of his market risk premium." (IIEC Exhibit 4.0, p. 7) This would suggest that Mr. Gorman's criticism would likely apply to his analysis, too.

Response to ComEd

Staff's CAPM Analysis

The Company laments that Mr. McNally's choice of a September 22, 2010 spot date for his CAPM calculation was "particularly and extraordinarily unfair." Instead, the Company suggests that if the December 29, 2010 30-year U.S. Treasury rate were substituted into Staff's CAPM, the result would be higher. (ComEd IB, p. 97) The Company's distortion of Staff's CAPM analysis is inappropriate for several reasons.

First, as explained earlier, mixing and matching data from different time periods is a corruption of the CAPM that produces a meaningless amalgam of data. Indeed, when Mr. McNally pointed out that the other CAPM inputs, aside from that U.S. Treasury rate, may have changed as well, the Company's attorney agreed and clarified that "I agree, and I am not asking you about a complete CAPM analysis done on any

other date." (Tr., January 18, 2011, pp. 1878-1879) Changing a single input in the CAPM outside of context of the rest of the inputs is nothing more than an abstract exercise that serves no practical purpose. In fact, accepting such an argument would only encourage parties to manipulate cost of common equity results by presenting similar such "analyses" based purely on hypothetical speculation. For example, one could just as accurately argue that if the August 31, 2010 U.S. Treasury rate of 3.52% were utilized, the CAPM result would be *lower*. (ComEd Cross Ex. 20) If, for comparison's sake, a party wishes to provide a second analysis from a different date, that party must perform a complete analysis, rather than just subjectively selecting individual inputs to modify.

Second, the Company's argument suggests that September 22, 2010 was in some way anomalous. However, Mr. McNally testified that September 22, 2010 was a normal day (Tr., January 18, 2011, pp. 1876-1877); the Company offers no evidence to suggest otherwise. Aside from the fact that the U.S. Treasury rates were more favorable to the Company on December 29, 2010, the Company provided no explanation, much less any evidence, as to why that date would be preferable for calculating ComEd's cost of common equity.[4] Moreover, the Company provides no analysis of the other inputs to the CAPM as of December 29, 2010, changes in which may have more than offset any increase in the 30-year U.S. Treasury rate. Without such an examination, the Company cannot decry the normalcy of Staff's CAPM results or speculate whether they would have been higher or lower if performed on any other date.

Finally, although the Company's argument suggests that the Company is extremely concerned about changes in capital costs from September 2010 to December 2010, its counsel adamantly objected when Staff offered to provide an appropriate, complete update of its CAPM analysis. (Tr., January 18, 2011, pp. 1877, 1879, and 1882-1883) It would appear that the Company is more interested in deriving a misleading, improper cost of common equity result than obtaining a legitimate cost of common equity estimate from a different day. This exposes the Company's argument as the disingenuous pretense that it is.

Staff's Comparable Sample

In its Initial Brief, the Company continues its attempt to impugn Staff's Comparable Sample. (ComEd IB, pp. 97-98) The propriety of Staff's sample and the impropriety of the Company's attempt to cherry-pick for removal from that sample only the companies with the lowest cost of equity results, without consideration of the overall risk of the sample, was discussed in Staff's Initial Brief. (Staff IB, pp. 69-74) The Company now suggests that Staff's 12-company sample is too small. However, that suggestion is contrary to recent Commission findings, a vast majority of which adopted costs of common equity based on smaller samples. Indeed, based on those Commission decisions, a sample of 12 companies would be one of the largest samples

[4] Of course, the choice to use a December 29, 2010 measurement date was not an option for Mr. McNally, since both his direct and rebuttal testimonies were due prior to that date. Rather, Mr. McNally's choice of using September 22, 2010 was dictated by the schedule set for this proceeding, which was a function of the filing date the Company chose.

(see table below). Of the rate setting proceedings before the Commission since 2005, the Final Orders in 12 of those cases specify the number of companies in the sample(s) underlying the adopted cost of common equity. A sample with greater than 12 companies was used in only one of those proceedings, while all of the other costs of equity decisions were based on samples with *fewer* than 12 companies (with one having as few as 5 companies). None included as many as 35 companies.

Docket No.	**Company**	**# of Sample Companies**
10-0276	Consumers Gas Company	7
10-0194	Aqua Illinois, Inc	5 and 9
09-0319	Illinois-American Water Company	5
09-0312	MidAmerican Energy Company	9
09-0306-0311	Ameren Illinois	9, 16, and 29
09-0166-0167	Peoples Gas / North Shore Gas	9
08-0549	Sundale Utilities, Inc	8
08-0482	Illinois Gas Company	7
07-0566	Commonwealth Edison Company	9
07-0357	Mt. Carmel Public Utility Company	11
06-0285	Aqua Illinois, Inc	8 and 9
05-0071-0072	Aqua Illinois, Inc	6 and 9

(Order, Docket No. 10-0276, October 6, 2010, pp. 6 and 8; Order, Docket No. 10-0194, December 2, 2010, pp. 16 and 22; Order, Docket No. 09-0319, April 13, 2010, pp. 93 and 112-113; Order, Docket No. 09-0312, March 24, 2010, pp. 12 and 26; Order, Docket Nos. 09-0306/0307/0308/0309/0310/0311 (Cons.), April 29, 2010, pp. 159 and 175; Order, Docket Nos. 09-0166/0167 (Cons.), January 21, 2010, pp. 103 and 123-128; Order, Docket No. 08-0549, April 22, 2009, pp. 8 and 11; Order, Docket No. 08-0482, May 13, 2009, pp. 18-19; Order, Docket No. 07-0566, September 10, 2008, pp. 98-99; Order, Docket No. 07-0357, March 12, 2008, pp. 23-24; Order, Docket No. 06-0285, December 20, 2006, pp. 9 and 11; Order, Docket Nos. 05-0071/0072 (Cons.), November 8, 2005, pp. 52-53) Thus, it is clear that Commission does not agree that a 12-company sample is too small, nor that a 35-company sample is necessary.

As Mr. McNally explains, to derive his sample, he ranked ordered 62 utilities for which the necessary financial and operating ratio data was available and chose the 12 utilities the least distance from, and therefore, <u>the most comparable to</u>, ComEd that met three conditions: (1) they are assigned an investment grade rating from S&P; (2) they have growth rates from Zacks Investment Research, Inc. ("Zacks"); and (3) they have neither pending nor recently completed significant mergers, acquisitions, or divestitures. (Staff Ex. 5.0, pp. 10-12) Using the Company's logic that a 35-company sample is

superior to a 12-company sample due to its relative size, then a 62-company sample would be better still. However, while Mr. McNally could have utilized a sample with as many as 62 companies, each additional company added would be less and less similar to ComEd in risk, making the sample less comparable in risk to ComEd overall. Staff performed rigorous, comprehensive quantitative and qualitative analyses that demonstrated Staff's 12-company sample to be very similar in risk to ComEd. (Staff Ex. 5.0, pp 10-12 and 33-34) In contrast, the Company has presented no such analytical evidence for Dr. Hadaway's 35-company sample. Instead, the Company implores the Commission to simply ignore Staff's analysis and blindly accept the unfounded insinuation that Dr. Hadaway's sample is more similar in risk to ComEd than is Staff's Comparable Sample. The Commission should reject the Company's plea.

AG/CUB Position

AG/CUB characterizes the testimony of the Company as alarmist and states that ComEd is not a relatively risky investment. Furthermore, AG/CUB notes that 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 11.3%, the product of an 10.9% "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 Init. Br. at 89. 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. CUB notes that the Company's request is well above other estimates in this case as well: Staff, 10.0%; IIEC, 9.65%. Staff Ex. 5.0 at 10-35, IIEC Ex. 4.0 at 2.

AG/CUB discusses the importance of the two key decisions on this topic, the first being *Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia,* 262 U.S. 679 (1923) ("*Bluefield*") and the second being the *Federal Power Commission et. al. v. Hope Natural Gas Co.,* 320 US 591 (1944) ("*Hope*"). Together, says AG/CUB, 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. AG/CUB avers that the Commission's decision must be based upon an evaluation of the relative riskiness of the Company. AG/CUB states that the evidence presented in this case shows that investors perceive utilities as less risky than other investments, as demonstrated by the fact that utility equities have not fallen as far as the overall market or have recovered to a greater extent than the market generally. *See* AG/CUB Ex. 4.0 at 12, 31; IIEC Ex. 1.0 at 7-8. According to AG/CUB, this relative stability of utility equity validates intervenors' findings of lower risk and lower cost for utility equity.

AG/CUB states that 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. To make this determination, says AG/CUB, 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.

AG/CUB explains that 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. AG/CUB maintains that 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, AG/CUB contends, 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. However, AG/CUB states that 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.

AG/CUB witness Mr. Thomas explains that 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. He explains that 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 financial sector), and an overall instability in the economy during the last two years. While the economy has begun to recover, Mr. Thomas points out that the Federal Reserve has noted that the recovery is slow and projected to stay that way. Mr. Thomas notes that utility companies have generally fared better than the overall economy. 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 applied by Yahoo Finance and S&P in presenting stock price information and the S&P 500 index, and he presented "corrected" stock prices changes in the following table:

Change in Stock Prices

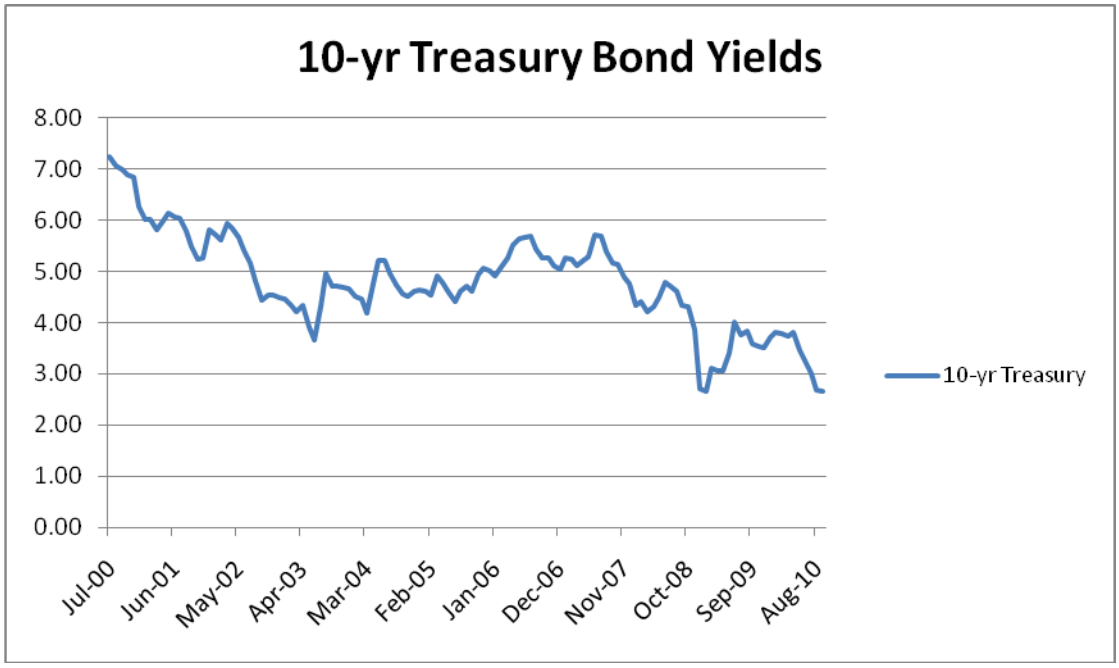
	(1) High Price	(2) Low Price	(3) Present Price	(4) High to Low	(5) Low to Present	(6) High to Present
S&P 500 Index	$1,565.15	$ 676.53	$1,165.15	-56.8%	72.2%	-25.6%
Dow Jones Utility Average	$ 520.89	$ 290.68	$ 403.91	-44.2%	39.0%	-22.5%
Thomas Utility Prices	$1,375.11	$ 837.31	$1,275.25	-39.1%	52.3%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

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.

ComEd Ex. 37.0 at 28, 30.

Mr. Thomas explains that 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, Mr. Thomas finds that the sample utilities were only 7.3% below their collective high. According to AG/CUB, this date shows that investor confidence in public utilities is higher than it is in other firms in the economy.

Mr. Thomas used Treasury bond returns as a comparison. He explains that there has been a distinct downward trend of Treasury bond returns as investors seek to reduce their exposure to risk and invest in low risk securities. Mr. Thomas provided the following chart that demonstrates this phenomenon:



AG/CUB Ex. 4.0 at 12.

AG/CUB agrees that utilities generally spend more of their cash flow on capital expenditures than other industrial firms. However, AG/CUB avers, 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. According to AG/CUB, 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. AG/CUB states that, in the context of a rate case like this one, a utility must show that its investments and expenses are reasonable and prudent and utilities often cite this prudence review as a source of risk. AG/CUB points out the Commission's recent finding that 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. AG/CUB contends that the risk that a utility will not recover its expenses is mitigated by the expectation that the utility will act reasonably.

AG/CUB notes that the regulatory structure in Illinois 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. AG/CUB explains that these rate mechanisms increase utilities' ability to recover expenses and stabilize cash flow. AG/CUB points to the Uncollectibles Rider, 220 ILCS 5/16-111.8, as an example. That rider allows an electric utility like ComEd to recover through an automatic adjustment clause tariff incremental difference in its uncollectible accounts. AG/CUB avers that 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.

AG/CUB notes that 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. ICC Docket No. 09-0306 (cons.) Final Order at 218. Moreover, AG/CUB states, 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, AG/CUB finds that 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.

AG/CUB argues that Mr. Fetter's "diatribe" about the importance of credit ratings should not influence the Commission's decision, as AG/CUB explains that it is impossible, and inherently speculative, to peg an approved rate of return or rate increase to credit rating expectations. AG/CUB states that 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. AG/CUB notes that 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. 09-0306 (cons.), Tr. at 1812. The ratings agencies did not change Ameren's ratings. *Id.*

AG/CUB explains that 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 AG/CUB explains have been previously rejected by this Commission. ComEd Ex. 12. AG/CUB avers that the Commission's analysis in recent cases has relied on combinations of DCF and CAPM analyses. AG/CUB Ex. 4.0 at 17.

AG/CUB argues that the Company's testimony does not justify the Company's proposed rate of return on common equity ("return on equity," or "ROE"). AG/CUB notes that the Company's request is well above the range of estimates put forth by various Staff and Intervenors. 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. Mr. Thomas performed analyses which AG/CUB believes accurately account for the actual potential growth and investor expectations. Mr. Thomas recommends that the Commission adopt an ROE of 8.94%.

1. Discounted Cash Flow Analysis

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 concludes that a non-constant growth DCF analysis would be most appropriate. Mr. Thomas explains that 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. AG/CUB avers that both forecasted and historical growth rate information become highly subjective measures of expected future growth for individual firms. AG/CUB notes that 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).

Mr. Thomas testifies that 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. Mr. Thomas states 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.

Mr. Thomas avers that 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.

In his analysis, Mr. Thomas uses two growth rates. AG/CUB Ex. 4.0 at 25. The first calculates 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 calculates the anticipated internal growth for each sample utility based upon expectations from Value Line. AG/CUB Ex. 4.0 at 26. He then uses 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[5], 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 uses 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 "inappropriate and biased." CUB notes that a 4.86% estimate as being too low, is actually above the published consensus economist estimates of GDP growth. Based on its latest issue, the consensus economists' published GDP 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, CUB argues that Dr. Hadaway's 6% GDP growth estimate is easily the outlier.

[5] 1969-2009.

Mr. Thomas's complete results are summarized below:

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

Based on Mr. Thomas's analysis, CUB finds 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.

Mr. Thomas states that 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. According to Mr. Thomas, 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. When dividend payout ratios decline, Mr. Thomas states, 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. AG/CUB avers that Mr. Thomas's method, because it considers such changes in payout and retention ratios, is more accurate than the Company's. Dr. Hadaway proposed a slightly higher dividend yield than the one used by Mr. Thomas. ComEd Ex. 11.4. CUB states that the Commission should reject his proposal because comparing dividend yields in a vacuum doesn't provide any valuable information. AG/CUB argues that Dr. Hadaway's decision to single out the differences in dividend yields obfuscates the issues in this case. Mr. Thomas notes that 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, AG/CUB avers 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.

The below table compares the results of Mr. Thomas and Dr. Hadaway:

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.

AG/CUB notes that 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 recommendation implies that the "BxR" method used by both Mr. McNally and Mr. Thomas should be rejected. *Id.* AG/CUB contends that 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. AG/CUB points 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. Mr. Thomas stresses that evaluating the Company's internal growth can help the Commission to avoid the type of upward bias produced by the use of analysts' growth estimates.

AG/CUB avers that 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. Mr. Thomas urges that 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, Mr. Thomas argues that 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.

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.

2. CAPM Analysis

Mr. Thomas testifies that the CAPM, like the DCF, 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. AG/CUB notes that 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). AG/CUB avers that while it is not perfect, the CAPM can be useful to verify the results of independently performed DCF analyses, which is what Mr. Thomas did. AG/CUB notes that despite the Commission's traditional reliance on a CAPM analysis, no ComEd witness undertook a CAPM analysis.

AG/CUB avers that 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. 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**

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. Mr. Thomas states that 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 he has proposed in previous 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.*

3. Alternative ROE Analyses

ComEd witness Seligson presented two additional analyses, both of which CUB notes have already been rejected by the Commission in prior cases. CUB cites the Commission decision 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).

AG/CUB avers that the Commission should, as it has in the past, decline the Company's request to use other states' decisions. 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.

<u>IIEC's Position</u>

4. The Parties' Analyses

IIEC argues ComEd's proposed 11.5% return on equity ("ROE") is excessive. IIEC recommends an ROE of 9.6% as reasonable and appropriate under current financial market conditions and adequate to maintain ComEd's investment grade credit ratings. IIEC's says its recommendation is supported by the testimony of Michael Gorman. Mr. Gorman used three variations of the Discounted Cash Flow ("DCF") analysis and a Capital Asset Pricing Model ("CAPM") study to estimate the required market return for ComEd. In addition, Mr. Gorman presented a risk premium ("RP") study, but did not use its result in quantifying his estimate, because of previous Commission decisions rejecting the use of that approach. IIEC says Mr. Gorman identified significant errors in ComEd's ROE-related analyses and showed that they result in an overstatement of the utility's market required return.

IIEC also argues that ComEd supports its recommended ROE with the testimony of several witnesses, a greater number of estimation approaches, and financial commentary from many of its other witnesses. Specifically, IIEC points to the following ComEd testimonies; Seligson, ComEd Ex. 12.0 Rev.(comparable earnings and risk premium estimates); Hadaway, ComEd Ex. 11.0 (DCF [three versions] and risk premium estimates); Fetter, ComEd Ex. 5.0 (credit ratings commentary,); Trpik, ComEd Ex. 4.0 Rev.(access to capital); Tierney, ComEd Ex. 13.0 (ROE adder)). IIEC points out ComEd also proposes a 40 basis point adder to increase whatever market required return is determined by the Commission; ComEd included the effect of the adder in its recommended 11.5% ROE.

IIEC also notes Staff and AG/CUB experts presented their own estimates of ComEd's required return on equity. IIEC says that like Mr. Gorman, these experts used variations of DCF and CAPM analyses. Staff's expert Michael McNally presented two versions of the DCF model: constant growth and multi-stage growth studies. AG/CUB expert Christopher Thomas presented constant growth and multi-stage growth DCF models that used historical and projected internal growth rates.

The following table summarizes the parties' presentations.

WITNESS	OVERALL	DCF	CAPM	RP	COMP. EARNINGS	SOURCE
Seligson (ComEd)	12.0%	----	----	12.6%	11.4%	ComEd. Ex. 12.0 at 10:221-225
Hadaway (ComEd)	10.7% - 11.3% (incl. 40 BP adder)	10.3% - 10.9%	----	[10.24%]	----	ComEd Ex. 37.0 at 31-32:586-601
McNally (Staff)	10.0%	9.69%	10.32%	----	----	ICC Staff Ex. 5.0 at 21:422-426, 32:627-629, and 33:633-634
Gorman (IIEC)	9.6%	9.8%	9.4%	[9.72%]	----	IIEC Ex. 1.0 at 32:734-735 and 38:859-873
Thomas (AG-CUB)	8.94%	8.94%	6.69% - 9.05%	----	----	AG/CUB Ex. 4.0 at 29:592-595, 33:672-676, and 34:690-691

*[Bracketed estimates were not used directly in determining recommendations]

IIEC first discussed the parties' DCF and CAPM Analyses. IIEC says that with the notable exception of ComEd witness Carl Seligson, the ROE experts in this case who estimated ComEd's market required return relied principally on the DCF or CAPM analyses. IIEC says these approaches have been approved by this Commission in its recent decisions. IIEC cites the Commission decisions in the Docket No. 09-0306, et. al. (cons.), Final Order, Apr 29, 2010 at 216 and *Re Commonwealth Edison Company,* Docket No. 07-0566, Order Sept. 10, 2008 at 98.

With respect to the Commission's preferred DCF and CAPM approaches, IIEC says the major sources of the differences in parties' recommended equity returns are (a) the growth rate input to parties' DCF analyses and (b) the estimate of market risk premium component of parties' CAPM analyses. In IIEC's view, ComEd's choices for these inputs have improperly inflated its requested return on equity. For the reasons discussed in greater detail in its briefs, IIEC says those inputs, and the resulting ComEd recommendation, should be rejected. Moreover, IIEC reasons that with an appropriate

determination of the market required return, the further increase of ComEd's proposed 40-basis point adder is unnecessary and excessive. ComEd's proposed adder also should be rejected.

IIEC takes exception to ComEd's Comparable Earnings Estimate. IIEC says ComEd witnesses also presented (and used) the results of two additional approaches that the Commission has traditionally not considered -- Comparable Earnings and Risk Premium methodologies.

IIEC notes that only ComEd witness Mr. Seligson provided a comparable earnings analysis IIEC says that consistent with the Commission's historical rejection of that approach, even ComEd did not use the resulting comparable earnings ROE estimate in quantifying the utility' requested return. IIEC opines that the record provides no reason for the Commission to reverse course to consider the excessive result in any case. In any case, IIEC states its witness, Mr. Gorman found that the "comparable" firms Mr. Seligson used have not been shown to have similar investment risks, types of operations, or accounting practices. Moreover, IIEC reasons earned returns (an accounting metric) are not a measure of the required return for ComEd (a dynamic market measure). ComEd has not provided any evidence that its belief that utilities have risk comparable to the overall market is shared by any market participant or has any validity.

IIEC contends that the only support Mr. Seligson supplied for the suggestion that the Commission should deviate from its consistent policy of rejecting the Comparable earnings approach is a survey of commissions conducted more than a decade ago, wherein only one-quarter of the one-half of commissions that responded used a comparable earnings approach, in some unspecified manner in their estimate of the cost of equity. Therefore IIEC concludes Mr. Seligson's recommended comparable earnings ROE should be discarded.

Next IIEC addresses the Risk Premium Analyses of ComEd witnesses Seligson and Hadaway, noting only Mr. Seligson used his RP result directly in determining his recommendation. IIEC says in prior cases, RP estimates have been rejected by the Commission in determining an appropriate ROE. (Docket No. 09-0306, et. al. (cons.), Final Order Apr. 29, 2010 at 216). IIEC says its witness Gorman detailed defects in those analyses that provide additional reasons those results should not be used. In particular, IIEC pointed out Dr. Hadaway's use of problematic forecasts of Treasury and utility bond yields to determine his equity risk premium and his additional upward adjustment (to effect an assumed relationship between equity risk premiums and interest rates), inflate his RP estimate to an unreasonable level.

IIEC says its witness Mr. Gorman tested Dr. Hadaway's risk premium estimate with a comparison of yield forecasts, current yields, and actual yields for the forecasted period and showed that forecasted yields almost always overstated the yield that ultimately occurred. IIEC says the projections used by Dr. Hadaway are highly problematic, and that his risk premium estimate should be ignored.

IIEC says that Dr. Hadaway has also assumed a simplistic inverse relationship between equity risk premiums and interest rates, and adjusted his RP estimate of a fair equity risk premium in the current marketplace to reflect that assumption. However,

IIEC suggests the actual relationship between those variables is more complicated, changes over time, and is influenced by factors other than nominal interest rates. The foundational assumption of Dr. Hadaway's adjustment is not supported by relevant academic research.

IIEC says that substituting current actual yields for inaccurate adjusted forecasted yields in Dr. Hadaway's estimation equation significantly reduces his ROE estimate to a level near that of Mr. Gorman's recommendation.

IIEC also criticizes ComEd's other RP analysis. IIEC says ComEd witness Mr. Seligson's quantification of ComEd's estimated ROE is at least as flawed as Dr. Hadaway's analysis. Specifically IIEC says Mr. Seligson:

- used a market risk premium more appropriate for the market as a whole, not for a below-market risk distribution utility;
- selected the highest market premium in Morningstar's range of published estimates (5.2% - 6.7%), without explanation or justification; and
- used one of the highest available estimates of Treasury bond yields, selecting 2011 estimates, when a consensus estimate for even the next two years (4.7%) was considerably lower than his 5.9% yield.

(Gorman, IIEC Ex. 1.0 at 59-60:1281-1314).

To provide the Commission with market information from a risk premium analytical perspective, IIEC says its witness Mr. Gorman also presented RP analyses and although Mr. Gorman's analyses avoid the errors he identified in ComEd's RP analyses, IIEC says Mr. Gorman did not use his RP results directly in his estimation of ComEd's ROE. However, according to IIEC, Mr. Gorman's analysis demonstrates the unreasonableness of the RP analyses presented by ComEd's witnesses.

5. ComEd's Commentary Testimony

IIEC notes the commentary on financial and regulatory environments from ComEd witnesses appropriately played no direct role in ComEd's quantification of its market required return. According to IIEC, their opinions on the current state of the financial markets and Illinois regulation do not warrant any modification of ROE estimates determined through the analysis of actual market data.

IIEC explains that conclusions respecting the need for supportive regulation in Illinois (a) are based on risks not faced by ComEd's distribution operations and (b) attempts to compensate ComEd for risks that the utility can manage or eliminate using available regulatory mechanisms. In IIEC's view, ComEd's assessment of Illinois dwells on past legislative issues that are now irrelevant, overlooks the market's improved view of Illinois regulation and ignores regulatory options available to ComEd to manage recovery of its costs of service. Ultimately, IIEC says the objective of ComEd witnesses appears to be replicating other Commission awards and pleasing analysts, rather than determining what the market requires for ComEd.

IIEC says its witness Mr. Gorman testified, on the basis of his own assessment of current conditions, that Illinois regulation provides adequate support to ComEd's access to capital. He supported his assessment by noting, *inter alia*, ComEd's "Excellent" S&P credit rating business profile score and its favorable senior secured bonds ratings from S&P and Moody's.

6. DCF Model Issues – Growth Rates

IIEC says the most significant differences among the DCF analyses and recommended returns in this record can be explained by the various expected growth rates used as DCF model inputs. IIEC identifies two questions respecting those inputs as the most important. The first question is whether short-term growth rate estimates can produce a reasonable constant growth DCF study. To obtain reasonable results from such growth inputs, the three-to five-year earnings growth rate outlooks published by analysts must be reasonable estimates of long-term sustainable growth. To be suitable DCF constant growth inputs, the three-to five-year growth rates cannot exceed the growth rate outlook for the economy in which ComEd must operate over the infinite period used in the DCF model. IIEC argues the Commission has approved the same reasoning in other cases. IIEC cites *Commonwealth Edison Company*, Docket No. 07-0566, Final Order, Sept. 10, 2008 at 97 and Docket No. 09-0306, et. al. (cons.), Final Order, Apr 29, 2010 at 219.

IIEC says that Mr. Gorman and Staff witness Mr. McNally agreed that current three-to five-year growth rates do exceed the expected growth rate of the economy and, therefore, are not reasonable estimates of long-term sustainable growth. Consequently, the constant growth DCF models in this case that use current analysts' projections produce return estimates that are too high. IIEC witness Mr. Gorman acknowledged that flaw in his constant analysts' growth rate DCF model. Staff witness McNally reached the same conclusion with respect to his results from using three- to five-year growth rate projections made by analysts for his sample group. IIEC reasons ComEd witness Dr Hadaway, on the other hand, did not discount his constant growth DCF estimate and embraced that result, even though he used analysts' current, inflated three-to five-year growth rates; but acknowledged that empirical data "support the notion that long-term growth expectations are more closely predicted by broader measures of economic growth than by near-term analysts' estimates."

IIEC states that since there is no reasonable dispute that analysts' short term growth projections are not expected to persist indefinitely, each testifying expert relied to some extent on the rate of growth in the national Gross Domestic Product (GDP) as a surrogate for long term earnings growth. The GDP growth rate used in a constant growth DCF model or as a surrogate for long term growth in a multi-stage DCF model is particularly important according to IIEC. An infinite period of overstated growth has an obvious effect on the resulting estimate. The multi-stage version of the DCF formula recognizes that near term growth rates and transitional growth rates will prevail only for finite, brief periods. However, over the final, infinite period of sustainable growth the DCF model contemplates, the long term growth rate input has the greatest impact on the resulting DCF estimate. In IIEC's view, even small differences in growth rate, applied over an infinite period as required by the DCF formula, can significantly affect ROE estimates.

IIEC says such differences appear in the analyses of the experts in this case. IIEC explained this difference in a table presented in its initial brief. IIEC posits that the relative magnitude of the ROE recommendations of record closely tracks the relative magnitude of the long term growth rate inputs used in the related constant growth and multi-stage, non-constant growth DCF models.

Multi-stage growth DCF analyses were performed by experts for IIEC, Staff, and ComEd. AG/CUB Christopher Thomas used a GDP growth rate of 4.86%. IIEC's Mr. Gorman used a long-term growth rate of the economy of 4.7%. Staff used a long-term growth rate for the economy of 5%. Both IIEC's and Staff's GDP growth outlooks were based on published growth rates available to investors. In contrast, IIEC says ComEd's Dr. Hadaway relied on a GDP growth rate of 6.0%. IIEC notes that growth projection was based on his assessment of historical achieved GDP growth and is unlikely to have affected investors' expectations. IIEC observes ComEd witness Dr. Hadaway's historical GDP estimate was derived specifically for this litigation, is not generally available to investors, and uses a methodology not reviewed by the financial community. IIEC says the Commission should not rest its determination of just and reasonable rates on such parochial inputs.

IIEC says for his sustainable growth rate model Dr. Hadaway set aside analysts growth rates only to select an excessive GDP growth rate estimate, based on his massaging of historical data, that is even higher. In IIEC's opinion, that assessment subjectively weights certain years within the historical period differently. In addition, IIEC says Dr. Hadaway's opinion that GDP growth will return to past levels ignores fundamental changes in national and world economic trends. Further, according to IIEC, as between analysts' estimates of future GDP growth and an average of historical GDP growth rates, Dr. Hadaway chose the higher historical input.

IIEC believes that had Dr. Hadaway used growth rates reflecting published analysts' growth rate outlooks in his multi-stage growth DCF model, those growth rates and the resulting DCF return estimates would have been substantially lower and presented a revision of Dr. Hadaway's DCF estimates using reasonable GDP growth forecasts. In IIEC's opinion, the selection of excessive short term growth projections as long term growth inputs to Dr Hadaway's models accounts for the excessive estimates from his DCF analyses. Further, IIEC says that when using GDP growth as a surrogate for sustainable long term growth, Dr. Hadaway's selection of a GDP growth rate even higher than the short term analysts' growth projections that other experts rejected predictably yields an excessive result.

7. CAPM Analysis Issues -- Market Risk Premium

IIEC finds one aspect of Staff's CAPM ROE estimate troubling. Staff estimated a DCF return on the S&P 500 stocks of 12.74%. Staff did not show the computation of the risk premium estimate used in ICC Staff Exhibit 5.10, but because it was based on a market return of 12.74%, it is IIEC's position that the estimate is at best problematic. Staff's DCF return on the market implies a growth rate of over 10% -- nearly twice the level of growth Staff estimated with its GDP growth rate of 5%. IIEC says Staff simply has not provided any support for the reasonableness of its S&P 500 growth rate estimate of 12.74%.

IIEC says its witness Mr. Gorman presented an alternative approach that did not share this deficiency of Staff's risk premium derivation, but has the reliability of an estimate based on actual market results. However, IIEC concedes that there is some inaccuracy in any estimate of the equity market risk premium. For that reason, Mr. Gorman's analysis recognized that an estimated range of the market risk premium, used in conjunction with other more specific estimates, is a superior approach.

Commission Analysis and Conclusion

ComEd, Staff, AG/CUB, and the IIEC have presented evidence supporting four different values for the cost of common equity. ComEd requests that the Commission approve its proposed total cost of common equity of 11.30%. ComEd Init. Br. at 89. This includes a 40 basis-point cost of equity adder adjustment to ComEd's base cost of equity. Tierney Dir., ComEd Ex. 13.0 at 3. Staff proposes a return on equity of 10.0 % (McNally Dir., Staff Ex. 5.0 at 33), IIEC proposes an estimate resulting in a 9.6% return on equity (Gorman Dir., IIEC Ex. 1.0 at 38) and AG/CUB proposes a return on equity of 8.94% (Thomas Dir., AG/CUB Ex. 4.0 Rev. at 37) with the possibility of an adjustment if SFV rate design is adopted (*id.* at 14-15).

ComEd's proposed base cost of equity is derived from the assessments performed by ComEd witnesses Dr. Hadaway and Dr. Seligson. Dr. Hadaway estimated ComEd's cost of equity using three basic discounted cash flow ("DCF") models and Dr. Seligson used a risk premium and a comparable earnings approach to determine the cost of common equity.

Staff, AG/CUB and IIEC experts presented their own estimates of ComEd's required return on equity. These experts used variations of DCF and CAPM analyses. Staff's expert Michael McNally presented two versions of the DCF model: constant growth and multi-stage growth studies. AG/CUB expert Christopher Thomas presented constant growth and multi-stage growth DCF models that used historical and projected internal growth rates.

ComEd's witness Dr. Seligson used a risk premium and a comparable earnings approach to determine the cost of common equity. Dr. Seligson's quantification of ComEd's estimated ROE is flawed analysis. His numbers are inflated and even the Company is not recommending his final ROE. The only support Dr. Seligson supplied for the suggestion that the Commission should deviate from its consistent policy of rejecting the Comparable earnings approach is a survey of commissions conducted more than a decade ago, wherein only one-quarter of the one-half of commissions that responded used a comparable earnings approach, in some unspecified manner in their estimate of the cost of equity. Therefore, the Commission rejects the risk premium and comparable earnings ROE sponsored by Dr. Seligson.

We agree with ComEd that Mr. McNally's comparable company selections seemed to contain companies that are not that similar to ComEd. It was also noted that his multi-stage DCF analysis was incorrect because he uses a too low growth rate for GDP to average down his analysts' growth rate estimates. Mr. McNally improperly

employs a "spot date" approach in his CAPM analysis as well as a "b times r" sustainable growth argument – both of which this Commission has recently rejected.

Also, as ComEd explains in its Initial Brief, Mr. McNally's CAPM analysis placed sole reliance on a risk free rate (30 year Treasury bonds) that he chose to measure on September 22, 2010. The Commission has recently rejected use of such a pure "spot date" approach in its *North Shore* decision (Thomas, Tr. at 1783) and noted the problems that can result from using such data. *Id.*; *See North Shore Gas Co., et al,* ICC Docket Nos. 07-0241/07-0242 (Cons.), Final Order (Feb. 5, 2008) at 92, 125-6. Mr. McNally's choice of a September 22 spot date was unfair to ComEd because the 3.77% rate measured on that date is not only low, but is fully 67 basis points below the rate on December 29, 2010 and well below the risk-free rate investors demanded generally throughout the entire year. ComEd asserted that if Mr. McNally's CAPM were adjusted upward by those 67 basis points alone, the results of his CAPM model would have been 10.99%, not 10.32%. That result would, in turn, have significantly increased his total recommended cost of equity. *Id.*

The Commission finds that if Mr. McNally's CAPM were adjusted on an average of the 2 risk –free rates and closer to the average rate through out the year or half of the 67 basis points. The result of 33.5 points added to his CAPM model would be in the range of 10.50%. This number would be more in the range of Dr. Hadaway's midpoint of 10.6%.

The Commission finds problems with how Mr. McNally's GDP growth rate forecast is calculated because it is based on assumptions that are inconsistent with actual historical growth for the U.S. economy. For example, Mr. McNally's 2.4% inflation rate compares to historical GDP inflation rates that have averaged 3.5% and his real GDP growth rate of 2.5% is much lower than the actual historical growth rate of 3.4%. It is reasonable to believe that future real growth and inflation will both be 3% and therefore a 6% growth rate is a more reasonable proxy for investor's long-term expectations. Use of the 6% growth rate, combined with correction of Staff's comparable sample, increases Mr. McNally's multi-stage DCF results to 10.44% and an average DCF (non-constant and constant growth) of 10.29%. This is 60 basis points higher than the average of Mr. McNally's constant and non-constant growth DCF results.

A reasonable average between Mr. McNally' CAPM with adjustments and Dr. Hadaway's average is 10.50 %.

We find the testimony of IIEC and AG/CUB relating to ROE also unpersuasive. The evidence shows that Mr. Gorman's estimated ROE is too low because his model inputs are negatively biased and that under current market conditions his CAPM is unreasonable. In addition, we agree with ComEd that Mr. Gorman incorrectly believes that the cost of equity for utilities have declined as much as interest rates.

ComEd demonstrated that Mr. Thomas' estimated ROE is too low because he employs the discredited "b times r" internal growth rate in his constant growth DCF analysis and then combines the low growth rates with a too low 20-year historical average of GDP growth in his multistage model. The Commission has rejected this approach in the past and will not adopt this method in this proceeding.

In addition, like Mr. McNally, the Commission finds Mr. Thomas' improper employment of the "b times r" approach to support his contention that Dr. Hadaway's DCF growth rates are unsustainable to be unpersuasive.

Having reviewed all of the evidence and the arguments of the parties, the Commission finds that a 10.50% cost of common equity for ComEd is reasonable and is hereby adopted in this proceeding.

F. Adjustments to Rate of Return

ComEd's Position

ComEd witness Dr. Tierney recommends adding a 40 basis-point cost of equity adder to ComEd's base cost of equity. Tierney Dir., ComEd Ex. 13.0 at 3. Dr. Tierney stated that the proposed adjustment to ComEd's return on equity is in support of its efforts to promote the adoption of energy efficiency measures by its customers. *Id.* at 1. She explained that the Act set strong targets for utility-sponsored energy efficiency programs and requires that the utilities recover their reasonably and prudently incurred cost. *Id.* at 2. Dr. Tierney noted, however, that the law is silent on the implications of the energy efficiency programs for other ratemaking issues and that the proposed 40 basis-point adjustment to the ROE should be allowed to address the adverse financial implications that will arise from successful implementation of programs required under the Act and other demand-side initiatives. *Id.* at 2-3. Dr. Tierney explained that the inclusion of the basis-point adjustment would compensate ComEd for the incremental risks and lost sales volume imposed by Section 8-103 of the Act and other public policies and initiatives aimed at reducing customers' overall cost of energy through the application of aggressive energy efficiency targets. *Id.* at 19. She observed that the proposed ROE adjustment would send a clear signal to the financial community that Illinois seeks to support both the interests of its customers in implementing cost-effective and aggressive energy efficiency programs as well as ComEd's financial health. *Id*. at 21.

Dr. Tierney also explained that the reasonableness of a 40 basis-point adder is tied to the combined effects of prudency risk, load-related risk, risk of performance penalties, and lost revenues associated with the demand-side programs. *Id.* at 26-27. She stated that assuming a $7.7 billion rate base, a 40 basis-point ROE adjustment would be equivalent to a $30.8 million expense item in ComEd's cost of service. *Id.* at 27. Dr. Tierney noted that the proposed adder would (i) increase the chance that a new rate case would not need to be filed as soon as it otherwise would; (ii) mitigate some of the lost revenues resulting from implementation of the proposed SFV rate design and (iii) help to ensure ComEd's rates are just and reasonable from an economic point of view. *Id.* at 27-28.

The proposed 40 basis-point adjustment when combined with the initial base cost of equity percentage produces a total cost of equity of 11.30%. ComEd's proposed common cost of equity is reasonable and should be approved by the Commission.

IIEC's Position

ComEd has proposed to augment its already over-stated ROE recommendation with a 40 basis point ("BP") adder. The adder would apply to whatever ROE the Commission approves. According to ComEd the adder is necessary "to mitigate the adverse effects on ComEd's revenues that would occur as a result of the combined effects of 'business as usual' ratemaking practices, full compliance with the State's energy efficiency program goals, and the impacts of other demand-side measures on customer loads." IIEC recommends that the Commission reject ComEd's proposed 40 BP adder to the approved ROE.

IIEC explains that the adder is unnecessary, penalizes customers, and reduces the regulatory efficiency. The adder is not needed for ComEd to manage the risks the utility identifies as justification. IIEC says the principal risk identified by ComEd is that energy efficiency and demand response (EE/DR) programs will reduce sales. However, IIEC argues ComEd has adequate means to respond to that risk. IIEC notes ComEd witness Ms. Tierney acknowledges that ComEd can use a future test year to set rates, but suggests that there are risks that a future test year will not eliminate. However, IIEC points out the risks Ms. Tierney identifies are elements of rate setting that have been addressed in the past without ROE adders. IIEC says that simply observing that the Commission's rate setting process has not eliminated every risk of ComEd's operations is not a valid compliant, nor does it satisfy ComEd's burden of proving that a 40 BP adjustment is just and reasonable. IIEC says the test year approach would allow ComEd to incorporate forecasted sales levels and costs of service that take account of its anticipated EE/DR activities. IIEC also reasons a future test year would better align its cost of service with future forecasted billing units. Thus, IIEC concludes ComEd's opportunity to earn its cost of capital is not subject to an unavoidable risk for which it should be compensated. However, rather than address such risk management, IIEC says ComEd's apparent position is that ComEd's choice not to use a future test year in this case ends the discussion, and that ComEd may not be criticized for declining to manage its risks.

IIEC notes that a future test year is not the only regulatory mechanism available to manage that risk. ComEd can mitigate sales loss risk by implementing pricing structures that do not expose ComEd to the same loss of revenue caused by reduced kWh sales. In fact, IIEC contends ComEd has demonstrated both the range of available mechanisms and its ability to manage sales loss risk by simultaneously proposing a straight fixed variable rate design.

Substituting Commission action, in the form of an adder to ComEd's ROE in place of risk management by the utility reduces regulatory efficiency, and it excuses the utility from its responsibility to manage risks. IIEC says ComEd's proposed adder would substitute an inflation of its allowed ROE for more customary and more equitable responses to risk that the utility simply has declined to implement -- *viz.,* using a future test year or more refined forecasts of load changes to set rates.

In any case, IIEC opines that the basis for a 40 basis point adder remains unexplained in this record. ComEd witnesses did not explain why that number is the correct figure or even a just and reasonable figure. IIEC says that in fact, the 40 basis point figure was not even developed by ComEd's principal witness on the adder Ms. Tierney. The number was chosen by ComEd's Chief Financial Officer Joseph Trpik, who did not provide supporting testimony for the adder. Nor did he explain its derivation or objective. IIEC says that even if some basis for imposing an adder existed, there is no record basis for this particular adder.

IIEC concludes that fundamentally, ComEd is asking ratepayers to compensate the utility for risks that it can eliminate or mitigate through its own management actions. ComEd has not explained its decision to simply forego available opportunities to account for the foreseeable changes it offers as justification for the adder. IIEC says it is neither economically efficient nor fair to ratepayers to compensate ComEd for foreseeable, manageable risks. Therefore the proposed adder should be rejected.

CUB

CUB questions Ms. Tierney's characterization of the "significant risk" that the Company will not recover regarding its chances of recovering its authorized return if it is successful in meeting its legislative energy efficiency targets. Though Ms. Tierney acknowledges that 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, the Company has simply stated that it chose differently. ComEd Ex. 39.0 at 5. CUB avers that Ms. Tierney fails to demonstrate why the Commission should adopt her recommendation of an ROE "adder."

CUB notes that Ms. Tierney 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.

CUB maintains that the Commission should reject ComEd's request. As Mr. Thomas notes, 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, CUB notes, 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. CUB agrees with IIEC witness Mr. Gorman's statement that 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. CUB also agrees with Staff that 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.

STAFF

Company witness Tierney recommended that ComEd's cost of common equity be increased by 40 basis points "for energy efficiency" in order to "address the adverse financial implications that will arise from successful implementation of programs required under the Act and other demand side initiatives." Dr. Tierney states that "the reasonableness of a 40 basis point adder is tied to the combined effects of prudency risk, load-related risk, risk of performance penalties, and lost revenues associated with demand-side programs." (ComEd Ex. 13.0, pp. 2 and 19-27)

The 40 basis point ROE adder proposed by Dr. Tierney should be rejected for numerous reasons, as presented in the testimonies of Dr. Brightwell and Mr. McNally. First, the undefined portion of her adder related to reduced sales volume, is single-issue rate making that violates test-year rules. (See *Business and Professional People for the Public Interest v. Illinois Commerce Commission* (1991), 146 Ill. 2d 175, 244-245, "The rule against single-issue ratemaking recognizes that the revenue formula is designed to determine the revenue requirement based on the *aggregate* costs and demand of the utility. Therefore, it would be improper to consider changes to components of the revenue requirement in isolation. Oftentimes a change in one item of the revenue formula is offset by a corresponding change in another component of the formula. For example, an increase in depreciation expense attributable to a new plant *may* be offset by a decrease in the cost of labor due to increased productivity, or by increased demand for electricity.") The Company chose a 2009 test year, but inappropriately seeks compensation for potential sales volume losses in *future* years solely on the basis of one factor (i.e., energy efficiency) that might reduce future sales, without consideration of any other factors that affect sales, including those that might increase future sales, or consideration of other changes to the other components of the revenue requirement. Incredibly, the Company witness sponsoring this adjustment, which is intended, in large part, to offset lost revenues from *falling* sales, still recommends that same ROE adder even though she admits that sales are actually expected to *rise*. (Tr., January 18, 2011, p. 1825) Second, the Company's energy efficiency adder is essentially a back-door attempt to make an inappropriate out-of-test year sales volume adjustment through the cost of equity by referring to it as risk. Notwithstanding the violation of test year rules, the Company has neither demonstrated nor quantified the effect of the risks it claims to be increased by energy efficiency measures. Indeed, the Company witness sponsoring this adjustment did not even calculate the 40 basis point adjustment, but was simply charged with back-filling a rationale for an amount that has no basis in the record. (ComEd Ex. 64.0, p. 9; Tr., January 18, 2011, pp. 1821-1822) Third, the risk adjustments Staff proposes for revenue de-coupling render a separate energy efficiency adder redundant. Finally, contrary to the Company's claims, the

proposed adder does not align the incentives of the Company to improve its energy efficiency performance and actually creates a greater disincentive to perform energy efficiency well. It also charges customers more for the same distribution services they already receive than if there was no energy efficiency program.

Dr. Brightwell testified that the 40 basis point adder does not address the conflict of interests between customers and shareholders that Dr. Tierney testifies exists. (ComEd Ex. 13.0, p. 21) In fact, it exacerbates that conflict of interest because the kilowatt hour charge is higher with a higher ROE than it will be without an ROE adder so that the Company loses even more revenue and profit for each kilowatt hour that is not consumed relative to the case that there is no basis-point adder to ROE. (Staff Ex. 8.0, p. 3)

Dr. Brightwell also testified that Dr. Tierney is incorrect in her assertion that an ROE adder creates support for energy efficiency. Dr. Brightwell reasoned that the key groups needing to support energy efficiency are customers, shareholders, and vendors. Increasing the Company's ROE will cause the total revenue requirement to increase. This means customers will pay even more for distribution service because of energy efficiency programs than they would without the adder. Charging customers even more for electric distribution as a result of energy efficiency does not promote customer acceptance of energy efficiency. (Staff Ex. 8.0, p. 4)

The adder does not provide a proper incentive to shareholders, either. The result of the adder is that the charge per kWh increases relative to a case where there is no adder. This further diminishes the Company's incentive to support energy efficiency, because each kilowatt hour saved reduces the Company's revenue and profit even more than it would without an adder.

Further, the Company's actions are consistent with the risk associated with performance penalties being insignificant. In Year 1, the Company reached its goal and banked 10% of the savings as permitted by the Order in Docket No. 07-0540. In Year 2, it did not spend about $15.7 million that was legislatively permitted in order to achieve its energy efficiency requirements. In the three-year plan filed in Docket No. 10-0570, the Company reports that by the end of the 4th energy efficiency Program-Year it expects to bank 110,000 MWhs of savings in excess of the legislatively mandated requirements. These savings can be credited towards meeting the requirements in future years. The Company's actions and statements make it appear likely that the Company felt there was little risk of being penalized $665,000 for failing to reach the targeted savings in either Year 2 or Year 3. (Staff Ex. 8.0, pp. 5-6)

Additionally, Section 5/8-103(d) of the PUA allows the Company to propose a lower annual energy efficiency savings goal to the Commission if the Company does not believe it could reach the goals set forth in Section 5/8-103(b) within the budget limitations prescribed in subsection (d). ComEd presented no such modification for the plan that includes Years 2 and 3. This further demonstrates that the Company felt the existing standards were achievable. (Staff Ex. 8.0, p. 5)

The final reason Dr. Brightwell concluded that the 40 basis point adder should be rejected is that it is not tied to compliance to the energy efficiency law. That is, the 40 basis point adder would be awarded to the Company regardless of whether the Company actually complies with the energy efficiency law, and the adder provides no additional incentive to comply with the energy efficiency law. In fact, if the Company received this adder and subsequently decided not to comply with the energy efficiency law, it would be about $30.1 million better off than if it failed to comply with no adder.[6] Approving this adder could put the Commission in the position of having to explain to the General Assembly why it rewarded ComEd a $30.1 million annual windfall, should ComEd fail to comply with state law.

Mr. McNally's testimony explained that none of the four "risk" factors Dr. Tierney points to warrant a 40 basis point adder to ComEd's cost of common equity. To begin with, Mr. McNally testified that an adder for prudency risk implies that the prudency risk for ComEd's investment in energy efficiency programs is higher than that of the companies in the samples from which the parties' cost of common equity estimates were derived. That implication is unfounded, as Dr. Tierney provided no quantification of the prudency risk involved. To the contrary, many states, and most of the companies in Mr. McNally's Comparable Sample, have similar such energy efficiency programs, and any prudency risk related to those programs would already be reflected in their cost of equity estimates. Regardless, an adder for prudency risk would only be appropriate if ComEd's energy efficiency program resulted in an increase in ComEd's expenditures that are subject to disallowance or that energy efficiency expenditures were somehow more at risk of disallowance than standard delivery services expenditures. Again, Dr. Tierney presented no evidence that ComEd's budget for capital and operations and maintenance expenditure will increase as a consequence of the its energy efficiency program. (Staff Ex. 5.0, pp. 55-56) In fact, Company witness Houtsma testified that "ComEd has myriad uses for a finite amount of capital." (ComEd Ex. 55.0, p. 17) Similarly, in its recent Purchase of Receivables with Consolidated Billing Rider case, the Company acknowledged that "the monies that ComEd spends to start-up, and administer its PORCB program could have been spent on assets that would be in its rate base." (Order, Docket No. 10-0138, December 15, 2010, pp. 49-50) Both of those statements reveal that ComEd's total expenditure budget caps are determined collectively, so that monies spent on one program (e.g., energy efficiency measures) simply results in that much less that will be spent on some other, lower priority programs; that is, energy efficiency expenditures are not additive to ComEd's expenditures budget and, therefore, do not increase prudency risk. Further, Dr. Tierney has acknowledged that she "has not performed a specific study of the prudency of cost recovery for ComEd's expenditures on energy efficiency and demand response program expenditures relative to ComEd's capital investment or O&M expenditures for

[6] The penalty for failing to reach the savings goal is $665,000. (220 ILCS 5/8-103(i)) According to Dr. Tierney, a 40 basis point adder is equivalent to a $30.8 million expense item on ComEd's cost of service. (ComEd Ex. 13.0, p. 27) Failure to comply with no adder results in a $665,000 loss to the Company. Failure to comply with an adder produces $30.1 million in additional revenues.

electric delivery infrastructure" and is not aware of any basis for assuming the prudency risk associated with energy efficiency measures is any different from that of ComEd's capital expenditures or operations and maintenance expenditures for electric delivery service projects, generally. (Staff Ex. 5.0, p. 56) In fact, Dr. Tierney admits that she is unaware of any disallowances for prudency to date. (Tr., January 18, 2011, p. 1827) In sum, Dr. Tierney has not even studied, let alone verified and quantified, the effects energy efficiency measures would have on ComEd's prudency risk.

Dr. Tierney also points to performance penalty risk as supporting a 40 basis point ROE adder. However, the effect on overall risk of incurring performance penalties related to the failure to meet energy efficiency goals is so minuscule it would have no measurable effect on ComEd's overall risk profile. The maximum penalty ComEd could incur would be $650,000 per year for two years. This amount is very small in relation to a company with assets of $20.697 billion, operating revenues of $5.8 billion, and a $374 million net income in 2009. (Staff Ex. 5.0, p. 57) Indeed, at least seven individual ComEd employees received annual compensation greater than that amount in 2009, with some of them receiving more than four times that amount. (Staff Cross Ex. 14) With a rate base of approximately $6.7 billion, even if ComEd was certain to incur the maximum allowable penalties, full recovery would require less than a single basis point change to ComEd's overall cost of capital. If one also factors in the low probability of ComEd actually incurring any such penalties, as Dr. Brightwell testified, the effect on ComEd's overall risk profile is essentially nil. Moreover, Dr. Tierney admits that the law provides "an out" that would allow ComEd to incur no penalties even if it fails to meet the statutory energy efficiency goals. (Tr., January 18, 2011, p. 1824) Finally, compensating the Company for the risk of incurring penalties would effectively reduce the amount of penalties contemplated in the PUA, thereby undermining the very purpose of the penalties in the first place. (Staff Ex. 5.0, p. 57)

In addition, Dr. Tierney alleges that ComEd will suffer a loss of revenues from implementing a demand-side program. Potential lost revenues due to reduced sales volume stemming from energy efficiency measures are not appropriately recovered via an ROE adder. Simply put, sales volume is a rates issue rather than a finance issue. The Company could have elected to use a future test year, in which case its rates would be set on the basis of expected future sales volume. Instead, the Company apparently felt it would be in ComEd's best interest to employ a historic 2009 test year, which does not allow it to reflect expected future sales volume. While the Company has every right to make that choice, it must accept both the upsides and downsides of that choice. The Company seems to want to both have its cake and eat it, too, but the law does not allow that. Additionally, the Company does not know the effect energy efficiency will have on its sales volume. Even if the effect could be estimated with a reasonable degree of accuracy, it cannot be viewed in isolation. To compensate a company for the downside risk of factors reducing sales without consideration of the upside risk of factors increasing sales would be inappropriate. But Dr. Tierney's proposal fails to consider any other factors that affect sales volume, including those that might have a positive effect. For example, ComEd notes that its net revenues fell by $40 million in 2009 due to the recent economic conditions. (Staff Cross Ex. 14) Obviously, an economic

recovery would raise ComEd's futures sales relative to its 2009 test year, which would offset potential revenue losses from energy efficiency measures. The foregoing arguments notwithstanding, rendering moot all discussion regarding potential lost revenues due to reduced sales volume is the fact that Dr. Tierney testified that overall sales are expected to grow. (Tr., January 18, 2011, p. 1825) Reduced sales volume obviously cannot be used to justify an ROE adder if sales volume is expected to rise. In fact, she also testified that the number of customers is expected to grow. Since both drivers of total revenues, volumetric charges and customer charges, are expected to grow, then total revenue is expected to grow. Thus, it is clear that an upward adjustment to ROE for lost revenues would be inappropriate. Regardless, "lost revenue risk" is a part of sales volume risk generally and thus, is addressed in Staff's proposed cost of common equity adjustments for revenue de-coupling. Accordingly, no further adjustment to the cost of equity would be warranted anyway. (Staff Ex. 5.0, pp. 57-58)

Finally, what is left is load related risk. Ms. Tierney defines "load related risk" as uncertainty in the degrees of efficacy and customer adoption of energy efficiency measures. Once again, an adder for load-related risk would imply that the risk related to unanticipated changes in load due to investment in energy efficiency programs is higher than that of the companies in the samples from which the parties' cost of common equity estimates were derived. Dr. Tierney has presented no analysis to support that implication; even if one could accept that implication, Dr. Tierney provided no quantification of the effect of any load related risk on the cost of common equity in support of her 40 basis point adder. In fact, logic indicates that, all else equal, more efficient appliances and structures would reduce fluctuations in sales volume since, by definition, they consume less electricity per unit of output. Consequently, changes in customer output would result in smaller changes in electricity consumption. Regardless, "load related risk" is a part of sales volume risk generally and, thus, is addressed in cost of common equity adjustments for revenue de-coupling. Thus, no further ROE adjustment, other than the additional eight basis points Staff recommends for revenue de-coupling, is warranted. (Staff Ex. 5.0, pp. 56-57)

Commission Analysis and Conclusion

ComEd has proposed to augment its determined ROE with a 40 basis point adder. According to ComEd, the adder is necessary to reflect the adverse revenue effects of the Commission's ratemaking practices and compliance with EE/DR requirements. Some of the risks ComEd identifies are elements of rate setting that have been addressed in the past without ROE adders. In addition, several parties observed that the Commission's practices allow future test year filings that could take account of any reasonably anticipated effects of EE/DR activities. ComEd has failed to justify the need for this adder as ComEd is not subject to an unavoidable risk for which it should be compensated.

In fact, ComEd's requests for various forms of regulatory relief in this proceeding illustrate an ability to mange the risks associated with the proposed adder. Moreover, the Commission finds that an adder is an inappropriate response to the identified risk. Even if usage reductions never occurred, the proposed adder would still impose higher

rates on customers and yield a higher authorized return for ComEd. Substituting Commission action in the form of an adder to ComEd's ROE in place of risk management by the utility reduces regulatory efficiency and it excuses the utility from its responsibility to manage operational risks. Further, the specific magnitude of the proposed adder has not been explained or justified. Therefore, the Commission rejects ComEd's proposed 40 basis point adder.

G. Staff's Adjustments to Rate of Return

ComEd

The Commission should reject Staff's proposed downward adjustment of between 20 and 32 basis-points to ComEd's return on equity in the event that ComEd's straight fixed variable proposal is adopted. *See* McNally Dir., Staff Ex. 5.0 at 41-42. ComEd explained that Staff witness Mr. McNally's adjustment is based on several problematic premises. Tierney Reb., ComEd Ex. 39.0 at 6.

First, Mr. McNally's calculation is built on his mistaken belief that Ms. Tierney testified that ComEd's 40 basis-point adder equates to the potential revenue loss resulting from energy efficiency and conservation measures. *Id.* In truth, Ms. Tierney stated that the proposed 40-basis-point adjustment reflects the combined effects of increased risks given ComEd's particular circumstances (*i.e.*, prudency risk, load-side risk, performance penalty risk, credit-quality risk, and regulatory risk) as well as the effect of lost revenues associated with energy efficiency targets mandated without compensating ratemaking adjustments for lost revenues. *Id.* ComEd noted that the proposed use of 40 basis-points to adjust ComEd's return on equity is offered in conjunction with a proposal to restructure its rates over a three-year period to move toward a 80/20 fixed/variable rate design and the proposed adjustment would likely have been higher than 40 basis-points had the rate case filing not incorporated this rate design proposal. Therefore, ComEd explained, to use the proposed 40 basis-point adder as a specific proxy for lost revenues would be inaccurate and inappropriate since it would misrepresent the size of lost revenue impacts. *Id*. at 7.

Second, Mr. McNally's suggestion that if the proposed rate design were approved, ComEd's revenues would be less uncertain and that effect would be worth 40 basis-points, is illogical. *Id.* ComEd explained that Mr. McNally's analysis fails to consider that there are categorical differences between the asymmetric risks faced by ComEd for which the proposed 40 basis-point adjustment would provide some compensation, on the one hand, and the potential financial benefits from revenue stability provided by ComEd's ratemaking adjustments. *Id.* at 7-8. ComEd observed that Mr. McNally provided no assessment of the impact of ComEd's ratemaking adjustment on the financial risks the Company faces and his adjustment associated with unrelated financial risks does not offer an appropriate substitute. *Id.* at 8. ComEd stated that Mr. McNally amplified the effect of focusing only on lost revenues rather than other risks when he adjusted the risk profile of the companies in his proxy group. *Id.* at 8.

Staff

Staff maintains that a cost of common equity of 10.00% would be appropriate, assuming the Commission rejects the Company's proposed straight fixed/variable rate design. However, Mr. McNally testified that if the Company's proposal for an 80/20 fixed/variable rate design is adopted, the cost of common equity would need to be further adjusted to reflect the reduction in ComEd's risk that the Company's proposal would produce. As noted above, a downward adjustment of 40 basis points would be reasonable for an 80/20 fixed/variable rate design, all else equal. Thus, Staff would recommend a downward adjustment of 40 basis points, should the Commission adopt an 80/20 fixed/variable-based rate design for ComEd. Similarly, a downward adjustment of 20 basis points would be reasonable for a 60/40 fixed/variable-based rate design, all else equal. Thus, if the Commission should adopt a 60/40 fixed/variable-based rate design, Staff would recommend a downward adjustment of 20 basis points. (Staff Ex. 5.0, pp. 41-42)

Commission Analysis and Conclusion

The Commission rejects Staff's proposed downward adjustment of between 20 and 32 basis-points to ComEd's return on equity resulting from the approval of ComEd's SFV rate design. The Commission agrees that Mr. McNally's reliance on Dr. Tierney's testimony in support of a 40 basis-point adder is misplaced and that using the adder as a proxy for lost revenues is inappropriate because it misrepresents the size of lost revenue impacts. Also, Mr. McNally's analysis does not recognize the difference between the financial benefits arising from the stability that SFV rate design creates and the asymmetric risks ComEd faces for which the proposed 40 basis-point adjustment is intended to provide some compensation.

H. Overall Cost of Capital (Derivative)

Upon incorporation of the conclusions stated above, the Commission finds that ComEd's capital structure and cost of capital, resulting in overall cost of capital of 8.51% may be summarized as follows:

Class of Capital	Proportion	Cost	Weighted Cost
Short-term debt	0.18%	0.39%	0.00%
Long-term debt	52.54%	6.52%	3.43%
Common equity	47.28%	10.50%	4.96%
Credit facility cost	0.00%	0.00%	0.12%
TOTAL	100.00%		8.51%

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

VI. Cost of Service and Allocation Issues

A. Overview

<u>ComEd's Position</u>

ComEd states that cost of service and allocation issues are a revenue neutral exercise for ComEd. Once the revenue requirement is established, the goal is to allocate costs based upon long-standing cost-causation principles, and then establish rates, based on those principles, to recover its approved revenue requirement. ComEd asserts that it has no interest in choosing winners and losers when it comes to issues of cost allocation and rate design.

ComEd argues that it has proposed an Embedded Cost of Service Study ("ECOSS") that reasonably allocates embedded distribution and customer costs among the retail delivery service classes. ComEd further states that its proposed ECOSS utilizes the same methodology used in prior, Commission-approved Embedded Cost of Service Studies. ComEd argues that the Commission should use its proposed ECOSS to set rates in this proceeding, and that the basic structure of the proposed ECOSS is substantially the same as previously approved studies.

ComEd also presented an exemplar ECOSS ("Preferred Exemplar ECOSS") prepared in compliance with the Commission's directives in its Rate Design Investigation Order, Docket No. 08-0532, entered April 21, 2010. In particular, ComEd prepared the Preferred Exemplar ECOSS in response to the Commission's direction in the RD1 Order that required "ComEd to develop and provide in its next rate case … consideration of redefining rate classes on the basis of voltage or equipment usage to better reflect the cost of service." The Preferred Exemplar ECOSS distinguishes between shared (primary and secondary voltage) facilities and secondary voltage facilities, provides for cost allocation to an exemplar primary voltage delivery class, and distinguishes primary voltage transformers. The Preferred Exemplar ECOSS was subsequently revised in rebuttal and surrebuttal testimony to address issues raised by various parties. While ComEd urges the Commission to adopt its proposed ECOSS, if the Commission determines that the creation of a new primary voltage delivery class is appropriate, ComEd recommends that the Commission should approve Preferred Exemplar ECOSS, as set forth in ComEd Ex. 75.2.

B. Potentially Uncontested Issues

C. Potentially Contested Issues

1. Embedded Cost of Service Study Issues

a. Class Definitions

(i) Residential Classes

(ii) Non-residential Classes

b. Primary/Secondary Split

(i) The Appropriate Methodology/Non-Compliance with What the Commission Required in its Final Order in Docket 08-0532

Background

As part of its Final Order in the 2007 ComEd Rate Case, (docket 07-0566, Final Order of September 10, 2008) the Commission initiated the 2008 *Special Investigation* Proceeding, docket No. 08-0532. In the final Order in the *Rate Design Investigation* docket, the Commission concluded that:

> The Company's analysis identified several cost accounts that can be separated into primary and secondary components. REACT indicates that ComEd's analysis fails to explain why other accounts are not similarly divisible. Staff had an initial concern that the list of accounts did not include any transformer costs which were collectively classified as primary only. The Company argued that the assignment of a transformer to primary versus secondary should be determined by the voltage of the source-side of the transformer, not the load-side of the transformer.
>
> Based upon ComEd's tariffs and the description of the system provided to us, we find that ComEd's current method of allocating transformer costs is not appropriate. When the exiting voltage of the transformer is secondary, the transformer can only serve secondary customers and should be allocated as a secondary system cost.

(docket 08-0532, Final Order of April 21, 2010, at 38). The Commission further concluded that:

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

(*Id.* at 40). At issue is whether ComEd did not comply with some of these Commission-mandated directives, thus tainting its cost of service studies that were prepared with this information to comply with these directives. For the reasons stated below, we again conclude that ComEd failed to comply with Commission directives.

(i) Functional Identification of Costs

ComEd's Position

ComEd states that its primary/secondary analysis satisfies the Commission's requirement in the *Rate Design Investigation* Order to provide function-based definitions

of service voltages for facilities other than the line transformers as is revised in ComEd Ex. 49.4. It also avers that this Commission should reject the IIEC's and REACT's proposals to further segment certain primary distribution system costs, noting that Staff agrees that these proposals are unreasonable. (*See,* Staff Ex. 26.0 at 17; ComEd Initial Brief at 110-11).

ComEd maintains that the Commission should reject the IIEC's contention that 24.78% of ComEd's costs for overhead primary voltage conductors, and also 32.82% of its costs for underground primary voltage conductors, should be allocated as secondary costs and only customers that take service from a single-phase circuit should be responsible for those costs. ComEd opines that these proposals are inequitable to other customers, who do not use other parts of ComEd's distribution system. (ComEd Ex. 49.0 Rev. 23-25).

Additionally, according to ComEd, the IIEC's proposal requires a much more complex analysis than the IIEC has presented, as, it is necessary to take into account the parts of ComEd's system that certain customers use more intensively than others, while maintaining equity among customers. ComEd witness Mr. Alongi testified that further segmenting the system as the IIEC and REACT request, would probably be "inappropriate" moments after it is completed, or even while the analyses were in process, because ComEd's primary distribution system is not static. Rather, it is continuously reconfigured and upgraded to meet ever-changing customer needs. (ComEd Ex. 73.0 2nd Rev. at 21; ComEd Initial Brief at 111).

ComEd further asserts that REACT has mischaracterized the *Rate Design Investigation* Order's discussion of the primary/secondary issue. ComEd states that the passage that REACT cites apply only to a general conclusion regarding primary/secondary issues. In support, it cites the *Rate Design Investigation* Order at 40. According to ComEd, the *Rate Design Investigation* Order required ComEd to identify primary facilities and secondary facilities, on a non-customer-specific basis, for purposes of a primary/secondary analysis, and also in order to differentiate primary and secondary costs. ComEd argues that nowhere in *Rate Design Investigation* Order did the Commission direct ComEd to engage in a granular examination. (ComEd Reply Brief at 115-16).

ComEd also argues that segmenting its almost 3.8 million customers based on their usage of specific components of the primary distribution system would be costly, complicated and fraught with assumptions. While one might find that any particular group or class of customers may make disproportionately small use of some components, it is equally plausible that those customers may make disproportionately large use of other components. (ComEd Ex. 73.0 2nd Rev. at 21-22).

Staff's Position

Staff avers that ComEd's proffered rate design and cost of service is based upon its Initial Filing. However, Staff states that ComEd's Supplemental Filing is more

responsive to the Commission's Rate Design Investigation Order in Docket No. 08-0532, (the "08-0532 Order") which rejected two key components of ComEd's analysis. It rejected ComEd's classification of transformers that step down voltages from primary to secondary levels as "primary costs." Also in that case, the Commission rejected ComEd's definition of "primary service" which, according to Staff, was broadly-cast to include customers receiving service at secondary levels. Instead, the Commission decided in the 08-0532 Order that only customers receiving service at 4 kV and higher should be considered to be primary system customers. (Staff Initial Brief at 94-95; Docket No. 08-0532, Order of April 21, 2010, at 38).

Staff opines that the additional revisions to ComEd's analysis recommended by IIEC witness Mr. Stowe are problematic and therefore should not be approved. Mr. Stowe argues against allocating single-phase line costs to primary customers because these lines, for the most part, serve secondary customers. Mr. Stowe contends that single-phase lines are not a viable option to serve primary customers, noting that while household appliances operate on single-phase service, "industrial applications, such as large motors, operate on three phase service." (*See,* IIEC Ex. 3.0 at. 11-12). In dollar terms, Mr. Stowe found that ComEd improperly allocated $2.9 billion of single-phase distribution lines to primary service. (Staff Initial Brief at 96).

According to Staff, Mr. Stowe's proposal is one-sided because he only discusses how this requirement for three-phase service absolves primary customers of responsibility for single-phase line costs. It also, according to Staff, ignores the potential cost increase imposed on ComEd, which could provide the basis for imposing additional distribution costs on primary customers. (Staff Ex. 26.0 at 16-17; Staff Initial Brief at 97).

Staff states that the IIEC asserts a flawed argument when stating that single-phase distribution lines are not a viable option to serve three-phase customers and, if used for this purpose, can lead to localized system load imbalances and voltage instabilities. The problem lies, Staff states, with Mr. Stowe's contention that primary customers cannot be served by single-phase lines because their end-uses require three-phase service. If true, Staff continues, ComEd has no choice but to use three-phase distribution lines to serve primary customers. This contrasts with the flexibility of secondary customers, who can also receive service from single-phase lines. Staff concludes that thus, serving primary voltage customers on a circuit may require ComEd to incur the additional cost of a three-phase line, while a single-phase line might be sufficient to serve secondary loads. Staff contends that Mr. Stowe's argument does not take this potential cost of primary service into account. (Staff Reply Brief at 58).

The IIEC's Position

Line Transformers

The IIEC avers that ComEd has performed two Primary/Secondary (P/S) analyses in this case. The results of ComEd's first P/S analysis, which was presented in ComEd Ex. 16.5, were used in all iterations of ComEd's Proposed ECOS study (ComEd Exs. 15.1; 51.1 and 75.1). Similarly, the results of ComEd's second P/S

analysis, presented in ComEd Ex. 21.5, or a version of this Exhibit, were used in all iterations of ComEd's Preferred Exemplar ECOS study (ComEd Exs. 22.1, 51.2, and 75.2) and its Alternative Exemplar ECOS study (ComEd Exs. 51.3, 75.3). It states that because ComEd's ECOS studies rely on the results of its P/S analyses, errors in the P/S analyses result in errors in all of the associated ECOS studies and the rate designs that resulted from these studies. (IIEC Initial Brief at 43).

The most obvious error found in ComEd's P/S analyses, the IIEC asserts, is that ComEd continues to define facilities as primary or secondary based on the facilities' energized voltage levels, rather than using a functional definition as directed by the Commission. (IIEC Ex. 3.0-C at 11). For example, it states, in its *Rate Design Investigation* Order, the Commission found that: "[T]he cost of line transformers used exclusively to serve customers at secondary voltages should not be allocated to customers taking service at primary voltages." In support, it cites the *Rate Design Investigation* Order at 38. However, ComEd's first P/S analysis did not identify line transformer costs on a functional basis. (ComEd Ex. 16.5). This P/S analysis also did not separate (by function) the costs of single-phase primary facilities from the costs of three-phase facilities used to serve both primary and secondary customers. The IIEC avers that ComEd's second P/S analysis (ComEd Ex. 21.5) does separate line transformer costs as directed by the Commission. However, the IIEC states that therein, ComEd failed to correctly identify single-phase primary facilities. (IIEC Ex. 6.0 at 6-7; IIEC Initial Brief at 44).

The IIEC argues that therefore, the first P/S analysis that ComEd presented here (ComEd Ex. 16.5) does not functionally separate the cost of line transformers. Consequently, the IIEC concludes, ComEd's Proposed ECOS study, (ComEd Ex. 75.1) which is based the results of the analysis presented the P/S analysis in ComEd Ex. 16.5, does not functionally separate these costs, but instead, allocates them to primary and secondary customers. (Tr. 2114-15; IIEC Initial Brief at 44).

Single-Phase Primary Lines

The IIEC avers that similar to line transformers, certain other facilities energized at primary voltages function only to serve customers at secondary voltages. The Commission recognized the importance of function in its *Rate Design Investigation* Order, by directing ComEd to develop and provide, in this rate proceeding, "function based definitions of service voltages for facilities other than the line transformers . . ." (*See, Rate Design Investigation* Order at 40). However, according to the IIEC, ComEd has ignored this directive in both of its P/S analyses. (ComEd Exs. 16.5 and 22.5). The IIEC further argues that ComEd continues to improperly separate distribution costs into primary and secondary sub-functions on the basis of a facility's energized voltage, rather than its function. It avers that often, this function is serving customers at a lower voltage; however, ComEd's failure to provide "function based definitions of service voltages of facilities" was at the heart of ComEd's inappropriate allocation of line transformer costs. That same failure, it continues, affects ComEd's categorization of the costs of other types of facilities. (IIEC Initial Brief at 46).

The IIEC states that ComEd's P/S analyses continue to assign single-phase primary circuits on the basis of voltage level, rather than function. In electrical

distribution systems, the term "phase" simply refers to an energized conductor. Single-phase primary distribution circuits are composed of a single conductor that is energized to a primary voltage level, and a ground or neutral conductor. Three-phase primary distribution circuits consist of three energized conductors and a ground or neutral conductor. (IIEC Ex. 3.0-C at 11). It maintains that because serving a primary voltage customer using single-phase distribution circuits can lead to localized system load imbalances and voltage instabilities, the costs of single-phase primary distribution circuits are incurred predominantly, if not exclusively, to serve secondary voltage customers. (*Id.* at 12; IIEC Initial Brief at 46-47).

The IIEC contends that ComEd has identified the costs of single-phase primary circuits as "shared" costs (costs incurred to serve both primary and secondary customers) because those circuits operate at primary voltage levels. It avers that ComEd's assertion in this regard is despite the fact that single-phase primary circuits are rarely, if ever, used to serve primary customers. (IIEC Ex. 3.0-C at 12). The IIEC argues that therefore, the costs that are associated with the facilities that are used to serve secondary customers, like single-phase components, should be allocated to secondary customers. Both of ComEd's P/S analyses, ComEd Ex. 16.5 and ComEd Ex. 21.5, combine the costs of single-phase and multi-phase circuits and allocate them on the same basis. The IIEC concludes that when the results of ComEd's flawed P/S analysis are reflected in its ECOS studies, single-phase primary circuit costs are misallocated and the cost of distributing electricity to primary customers is overstated. Such a result, it continues, is inconsistent with the Commission's prior orders, and the evidence in this case. It asserts that therefore, ComEd's P/S analysis should be modified as suggested by IIEC. (IIEC Initial Brief at 47-48).

Also, according to the IIEC, ComEd's initial brief misconstrues the IIEC's proposal when stating that:

> IIEC contends that 24.78% of ComEd's costs for overhead primary voltage conductor and 32.82% of ComEd's costs for underground primary voltage conductor should be allocated as secondary costs and only customers that take service from a single-phase circuit should be responsible for those costs.

(See, ComEd Initial Brief at 110, ComEd Ex. 49.0 Rev. at 24). It avers that, in fact, no IIEC witness contended that "<u>only</u> customers that take service from a single-phase circuit should be responsible" for the cost of single-phase facilities, as ComEd alleges. The IIEC reasons that thus, ComEd's "horror stories" about the need to identify each such customer and the difficulty of that task have no basis in the IIEC's proposal. (IIEC Reply Brief at 20-21). Instead, the IIEC states that its witness Mr. Stowe has consistently testified that because single-phase facilities are almost never used to serve primary voltage customers, they should not be allocated the costs of those facilities. As to the allocation among secondary customers, the IIEC has always advocated that the cost of single-phase circuits should be allocated to <u>all</u> of the secondary voltage customers. (IIEC Ex. 6.0 at 10).

The IIEC additionally asserts that allocating single-phase primary circuit costs to secondary customers is not as complicated as ComEd has represented. In fact, it

continues, this separation of costs has already been performed by IIEC witness Mr. Stowe using "data" provided by ComEd. (IIEC Ex. 3.0-C at 13-15 and 26).

The IIEC maintains that ComEd serves only a very few of its primary voltage customers through single-phase circuits. During cross examination, ComEd witness Mr. Alongi testified that ComEd has 936 primary voltage customers. According to Mr. Alongi, ComEd records the usage of only 21 of these 936 primary customers through a single-phase primary voltage meter. (Tr. 2090-91). This means, the IIEC concludes, that only 21 of the 936 primary customers (2.2%) receive single-phase service. However, single-phase service can be supplied by connecting the customers' service to one of the three phases in a three-phase circuit, or by connecting the customer to a single-phase circuit. (ComEd Ex. 49.5). The IIEC states that only eight of ComEd's 936 primary voltage customers were serviced by connecting them to a single-phase circuit. (Tr. 2091; IIEC Reply Brief at 21).

REACT's Position

REACT posits that this Commission should compel ComEd to abide by the terms of the Final Order in the *Rate Design Investigation* proceeding by analyzing the assets that are used to serve the over-10 MW customer classes. The *Rate Design Investigation* Order required, in part, that ComEd develop: "function based definitions of service voltages for facilities other than the line transformers already addressed [and] an analysis of which customer groups are served by which system service components." (*Rate Design Investigation*, docket 08-0532, Final Order of April 21, 2010, at 40).

According REACT, while ComEd Exhibit 21.5 purportedly addressed both of those mandates, ComEd Exhibit 21.5 is nothing more than a first step toward rates reflecting cost causation for ComEd's largest customers, rather than a full accomplishment of that goal. REACT asserts that ComEd itself acknowledges that it was capable of, and did, assign costs, including both direct and shared costs, to a customer class, as; the exemplar "primary class" was based upon actual usage of the facilities. (REACT Initial Brief at 24-25). ComEd conducted an investigation, based on several observation and sampling techniques, into distribution system assets serving primary service points. (*See* ComEd Ex. 21.5.) ComEd's study was not without its flaws, REACT avers, and as other parties have pointed out, there is certainly room for improvement. Nevertheless, REACT witness Mr. Terhune testified that the concepts and basic methodology that ComEd used to create the primary/secondary study demonstrates that ComEd can undertake a similar (although improved) study of distribution system assets serving the over-10 MW customer classes. (REACT Initial Brief at 24-25).

<u>Analysis and Conclusions</u>

Nothing in the *Rate Design Investigation* Order required ComEd to do what the IIEC argues. The IIEC asserts that single-phase primary circuit costs and line transformer costs should be reallocated. However, the Commission did not address this issue in the *Rate Design Investigation* Order. Additionally, while the IIEC has presented its arguments in detail, it has not proffered any evidence to indicate that Staff is incorrect when opining that serving primary voltage customers on a circuit may require

ComEd to incur the additional cost of a three-phase line, while a single-phase line could serve secondary loads. The IIEC has also not presented facts disputing Staff's conclusion that the IIEC's arguments on this issue are one-sided, as, serving primary voltage customers on a circuit may require ComEd to incur the cost of a three-phase line, while, a single-phase line might be sufficient to serve secondary loads. Because, at this time, these costs do not appear to be as neatly (and fairly) segregable as the IIEC asserts, we further conclude that, at this time, ComEd's Primary/Secondary split analysis did not violate the *Rate Design Investigation* Order on this issue. We therefore conclude that, on an evidentiary basis, the IIEC's arguments fail here.

However, as shall be explained below, we do concur with the IIEC's argument that ComEd, generally, has not complied with the Commission's Order in the *Rate Design Investigation* Order in docket 08-0532. We further note that once ComEd finally complies with the requirements in that Order, further segmentation of ComEd's costs may be necessary, depending upon the outcome. REACT's argument is addressed elsewhere herein, in the Section entitled "Investigation of Assets used to Serve Extra Large Load Customers."

c. Direct Observation of ComEd Facilities

Staff's Position

Staff points out that the Commission stated the following concern with ComEd's use of engineering estimates versus direct observation in the *Rate Design Investigation* Order:

> The record shows that when ComEd's engineering estimates were compared to a very small number of system inspections they were found to be very inaccurate. While the Company could not be expected to inspect its entire system, some visual analyses would enable ComEd to conform the engineering assumptions that drive its analysis of primary and secondary costs to reality. We direct ComEd to conform the engineering assumptions that drive its analysis of primary and secondary costs through the implementation of sampling methods for physical inspections to confirm engineering judgments and to provide this supporting documentation in its cost of service testimony in subsequent rate proceedings before this Commission.

(Docket No. 08-0532, Final Order of April 21, 2010 at 38). The Commission's concern was that ComEd's engineering estimates were "very inaccurate," making it incumbent upon ComEd to use all available tools to improve the accuracy of its analysis. Staff opines that clearly, direct observation, which would entail "physical inspections to confirm engineering judgments" is one such tool that should not be dismissed out of hand. (Staff Initial Brief at 97).

Consistent with the Commission's statement above, Staff has explained that direct observation could improve the accuracy of the Company's engineering estimates.

With regard to FERC Account 364, Poles, Towers and Fixtures, ComEd stated that it "does not have data readily available" "to determine the exact number of poles" in its system, with primary and secondary facilities, or either primary or secondary facilities only. (ComEd Ex. 21.5 at 5). However, by directly observing a sample of wooden poles above 50 feet, Staff notes that ComEd's assumption that none of these poles contain secondary facilities could be tested. ComEd could also observe a sample of poles 50 feet or lower to assess the reasonableness of its estimate that 51.6% of those poles contain secondary facilities. (Staff Initial Brief at 98).

Staff also contends that direct observation could be a useful check on the accuracy of ComEd's 50/50 allocation to primary and secondary service for the cost of poles containing both primary and secondary facilities. (*Id.*). ComEd justified this allocation on the basis of "engineering judgment" in docket 08-0532 (*See,* docket 08-0532, ComEd Ex. 1.0 at 18). Staff states that ComEd did not revisit that assumption in the present case. Staff again opines that directly observing a sample of poles could confirm or undermine the reasonableness of this approach. (*See,* Staff Ex. 10.0 at 22-23).

With regard to Account 365, Overhead Conductors and Wires, citing a lack of evidence for estimating the relative shares of weather-resistant wire used for primary and secondary service, ComEd personnel assumed that "the majority of the wire was generally used for wiring transformers and for secondary distribution" and ComEd allocated the associated costs 70% to secondary and 30% to primary. (ComEd Ex. 21.5 at 6). Staff states that direct observation could also be useful to evaluate the accuracy of this estimate. (Staff Ex. 10.0 at 23; Staff Initial Brief at 98-99). Additionally, regarding Account 366, Underground Conduit, ComEd estimated that 1.0% of underground conduit outside the City of Chicago should be considered secondary, based on field and map reviews conducted during the course of docket 08-0532. Staff opines that direct observation could be used to review this estimate. (Staff Ex. 10.0 at 24).

ComEd asserted that it's that direct observation is a review of "manual review and measurement of ComEd maps" to determine the footage of conduit outside the City of Chicago. It cited no other instance of direct observation in its analysis of primary and secondary costs. (*Id.* at 19-20). Staff contends that it strains credulity to equate direct observation with reading a map. Direct observation entails a physical inspection of the system itself in the field, while reading a map involves looking at a document that reflects what the mapmaker considered to be essential information for a physical area. Staff further states that what a mapmaker considers essential for his purposes, may prove insufficient for other purposes, such as the analysis of primary and secondary costs. Staff opines that these are clearly two fundamentally-different activities. Staff opines that ComEd's reliance on maps alone indicates that it did not use direct observation as a tool in its analysis. (*Id.* at 20; Staff Initial Brief at 99).

With regard to the 50/50 pole allocation, ComEd witness Mr. Alongi testified that he does not believe that additional observations "would provide further insight on how to allocate the cost of such shared poles." (*See,* ComEd Ex. 49.0 at 34). However, Staff states, this argument conflicts with the Commission's statement in its 08-0532 Order. The only information provided by Mr. Alongi about these poles is that they carry primary and secondary facilities. The kinds and amount of primary and secondary facilities are not identified. Staff concludes that this lack of information makes it difficult to determine whether a 50/50 allocation is the most reasonable alternative. (Staff Ex. 26.0 at 7-8; Staff Initial Brief at 99-100).

Regarding the allocation of weather-resistant wire between primary and secondary service, Mr. Alongi discounted the usefulness of direct observation, stating that conducting field surveys "of thousands of miles of wire" and examining the wiring for "almost 213,000 overhead transformers" would not produce a more reasonable allocation of these costs. (*See,* ComEd Ex. 49.0 at 35).

However, a Staff state, its position does not require ComEd to conduct field surveys of thousands of miles of wire or examine almost 213,000 transformers. Rather, Staff's position is that ComEd should adhere to the 08-0532 Order by employing direct observation in its analysis of these costs. In contrast to the sweeping field survey indicated by Mr. Alongi, Staff advocates a more limited analysis that entails directly observing a representative set (using a statistically-derived sample) of weather-resistant wire. (Staff Ex. 26.0 at 8-9). Staff further states that direct observation does not mean physical review of <u>all</u> underground conduits outside Chicago; rather, a statistically representative sample could be used to test the assumptions underlying ComEd's analysis. Staff concludes that without these direct observations, ComEd's analysis will continue to reflect unsupported assumptions that may or may not reflect actual costs. (Staff Ex. 26.0 at. 9-10; Staff Initial Brief at 100).

Staff further posits that ComEd itself has found direct observation to be useful for its analysis of primary and secondary costs. ComEd indicates that it relied on "ComEd maps, billing records, and in many instances field reviews" to identify which customers receive service at 4 kV or above. (ComEd Ex. 21.0 Rev. at 18). These field reviews consisted of "a manual review of all 2,800 meter points with PTs." ComEd estimated that "[t]his review would take about two hours to complete per customer account, or 2,800 labor-hours…to complete the entire review." ComEd identified 935 customers receiving service at 4 kV and above, which is a considerably higher figure than the previous estimate of 300 such customers in docket 08-0532. (Staff Ex. 26.0 at. 25-26). Staff avers that these different figures for primary customers show that direct observation can and does play an essential role in testing the accuracy of ComEd's analysis. Staff recommends requiring ComEd to use direct observation in the manner suggested by Staff in its next rate case to ensure that ComEd fully addresses the Commission's directives and concerns that were expressed in its 08-0532 Order. (Staff Initial Brief at 100-101).

Staff also states that it has clearly acknowledged that direct observation may not prove effective in each and every situation. Nevertheless, Staff maintains, ComEd has the responsibility to satisfy the Commission requirement that it directly observe its system and it has failed to do so. That leaves no reasonable alternative to specifically requiring that ComEd use direct observation in the analysis of primary and secondary cost issues to be presented in its next rate filing. (Staff Reply Brief at 58-59).

ComEd's Position

According to ComEd, the term "direct observation" includes both review of ComEd facilities in the field and analysis of ComEd's system maps. ComEd states that experience has shown that ComEd's maps provide a reasonable representation of the facilities that are in the field when the facilities are mapped, making additional analysis of the type proposed by Staff witness Mr. Lazare to be unnecessary. (ComEd Exs. 49.0 Rev. at 32-39).

ComEd further argues that its maps are not subject to the "interpretation" of the mapmaker as Staff suggests. (ComEd Ex. 49.0 Rev. at 20). ComEd's personnel cannot safely operate ComEd's system, unless its maps accurately represent ComEd's distribution wire, poles transformers, switchgear and other facilities necessary to operate a complex, interconnected distribution system. Its maps must also provide a reliable representation of the facilities mapped, as ComEd's personnel depend on this information for its safety. (*Id.* at 33). ComEd concludes that consequently, it has demonstrated why its maps can be relied upon to present an accurate representation of what facilities are in the field.

ComEd acknowledges that Staff does not suggest that it should directly observe all of its facilities in the field. However, Staff also admitted that direct observation does not guarantee useful information for determining the primary and secondary facilities and related costs. ComEd argues that there is no compelling evidence to support "incurring the substantial costs" of conducting direct observations in the manner that Staff suggests. While ComEd will continue to look for ways to improve the accuracy of its estimates, or look for new ways to allocate these costs, ComEd states that its method of conducting direct observations of its system in this proceeding is reasonable, and it results in a fair allocation of primary and secondary costs. (ComEd Initial Brief at 111-13).

Analysis and Conclusions

It is not disputed that the Commission ordered ComEd to use direct observation or sampling and estimation techniques of its system to develop more accurate and transparent differentiation of primary and secondary costs. ComEd defines the term "direct observation" to include review of the system in the field. Yet, no such review took place. ComEd argues, instead, that review of its maps, which are, no doubt, very accurate should suffice. It does not.

Even when using ComEd's definition of "direct observation," some field inspection is necessary. And, ComEd was ordered to use direct observation in the *Rate Design Investigation* Order. Yet, no field inspections occurred.

We additionally note that ComEd's argument that use of its maps should suffice defies common sense. A map cannot provide information like the age or condition of the equipment and other characteristics that a visual inspection of some sample equipment would produce. Direct observation would also determine the accuracy of ComEd's estimates of the kinds and amounts of the equipment at issue. Maps may not have all of the information that could be gleaned by simply viewing some of the equipment. Additionally, ComEd states that its maps provide a reliable portrayal of the systems that are mapped. This language suggests that it is possible that a portion of its system is not mapped, as, there would be no point in adding that the maps prove a reliable portrayal of the systems" that are mapped," if all of the system was mapped. While this language is vague, if some of ComEd's system is not mapped, it only stands to reason that maps will not aid a person regarding the unmapped territory.

Finally, when the Commission issues an Order, it is not for Mr. Alongi, or anyone else at ComEd, to determine the necessity of what is mandated in that order. If ComEd has questions about the meaning of that order, it can file a petition for rehearing regarding that language, or, it can file a motion seeking clarification. It can also file an appeal to the appellate court, if it objects to any language in a Commission Order. None of these legal remedies were pursued. Without use of the legal remedies that are available to ComEd, it is required to comply with Commission Orders. Clearly, ComEd did not comply with the Commission-ordered directive on this issue. ComEd shall work with Staff on this issue to develop a scientifically-significant representative of its direct observations on this issue. It shall also have this representation in its cost of service study/studies in its next rate case. This analysis shall be part of any initial rate case filing that ComEd makes.

d. Sampling

ComEd's Position

ComEd states that the supplemental primary/secondary analysis reflected in the Preferred Exemplar ECOSS responds to the Commission's directive in the *Rate Design Investigation* Order to explore whether sampling techniques could be used "to develop a more accurate and transparent differentiation of primary and secondary costs," and "to explore in any subsequent rate proceeding whether sampling techniques can be used to allocate costs to customer classes for underground circuits operating at primary voltage serving customers only at secondary voltages." ComEd did explore the use of sampling techniques, however, it sampled only four primary circuits, out of approximately 6,400. (*See,* Staff Ex. 10.0 at 26). (ComEd Initial Brief at 113).

ComEd argues that its witness Mr. Alongi explained why examining a larger sample of information was unnecessary. (ComEd Ex. 49.0 Rev. at 37-39). Mr. Alongi presented information regarding all of ComEd's 6,400 circuits. According to ComEd, this shows that its four sample circuits were representative of "the majority of" ComEd's circuits. (*See,* ComEd Ex. 49.6). Comparing that information to what Mr. Alongi

provided in his Supplemental Direct Testimony, ComEd Ex. 21.6, ComEd concludes that ComEd Ex. 49.6 supports the fact that a larger sample of ComEd's circuits and ComEd's customers would be an arbitrary and unnecessarily complicated undertaking. (ComEd Ex. 49.0 Rev. at 38). ComEd's witness Mr. Alongi testified regarding the complexities of examining customer's use of ComEd's 6,400 primary voltage circuits, given ComEd's extensive and integrated distribution system, as well as the costs that are associated with such an undertaking. He also testified that no information suggests that this examination would result in a more precise segmentation of ComEd's distribution system. (*Id.*, at 38-39; ComEd Initial Brief at 114).

Staff's Position

Staff argues that sampling four out of almost 6,400 primary distribution circuits is unacceptably small, but also, ComEd failed to demonstrate that it is representative of the larger number of circuits. Staff concludes that these facts make it difficult to extrapolate conclusions from ComEd's analysis regarding the remaining circuits on the system. Staff concludes that therefore, it is premature to draw a broad conclusion about the breakdown of nearly 6,400 distribution circuits between primary and secondary components based on these four examples. To address this shortcoming, Staff asks this Commission to direct ComEd to examine a larger, representative sample in its analysis and present the results contemporaneously with the initial filing in its next rate case. (Staff Initial Brief at 102).

Staff finds no basis for ComEd's claim that Mr. Alongi has shown these circuits to be representative for purposes of identifying primary and secondary costs. In fact, Staff states, the statement on this issue in ComEd's Initial Brief that these four circuits are "representative of the majority of ComEd's circuits" undermines that claim. Staff maintains that it is not clear what ComEd means by "a majority," in that, it could constitute 51%, 99% or somewhere between the two figures. In addition, Staff continues, for those circuits that are not in the majority, ComEd did not indicate how they diverge from the four circuits in the sample. Staff concludes that ComEd's own arguments raise questions about the value of these four circuits as a representative sample. Staff further states that therefore, it is difficult to draw conclusions concerning the shares of primary and secondary costs on the nearly 6,400 ComEd distribution circuits. (Staff Reply Brief at 59-60).

Analysis and Conclusions

ComEd has failed to explain why sampling 4 out of 6,400 circuits constitutes meaningful sample. We also agree with Staff that for those circuits not in the "majority," ComEd fails to indicate how they diverge from the four circuits in the sample. It is not clear what the non-majority circuits are and ComEd has not explained what the term "majority" means. ComEd, clearly, has made no attempt to comply with this Commission-ordered requirement. Therefore, ComEd shall examine a larger, representative sample in its analysis and present the results contemporaneously with the initial filing in its next rate case. In addition, ComEd shall work with Staff to develop representative samples and to develop a scientifically acceptable sample of these circuits.

We further note that the final Order in docket 08-0532 required direct observation or sampling. (*See,* docket 08-0532, final Order of April 21, 2010, at 40). ComEd did neither one of these two choices, in what could be considered a meaningful way. Additionally ComEd really articulated no legitimate reason for its failure to comply with the Commission's Order in this regard. Instead, ComEd's response was that compliance is not necessary. We again reiterate that there are legal remedies available to any party that does not agree with a Commission Order, or, who has confusion about a Commission Order. Absent the use of the legal options available for parties when they do not agree with Commission Orders, all parties before this Commission shall comply with Commission Orders. ComEd is again advised that the Public Utilities Act provides penalties for failure to comply with Commission Orders.

b. Review of Other Utilities' Treatment of Primary/Secondary Issues

Staff's Position

Staff argues that ComEd should be ordered to provide a full analysis of this issue in its next rate filing. Staff points to the testimony of ComEd witness Mr. Alongi, who stated that ComEd examined 35 other utilities "to consider how they differentiate and allocate primary and secondary systems and costs" and to review their "tariffs, rates and categorizations of customers." (*See,* ComEd Ex. 21.0 Rev. at 31). While presenting a detailed discussion of the rates, tariffs and customer classifications for these utilities, Staff continues, ComEd did not discuss the underlying primary/secondary cost analyses that these utilities prepared. In fact, ComEd witness Mr. Alongi admitted that ComEd's analysis does not identify how these other utilities allocate costs. (ComEd Ex. 49.0 at 41-42). Staff argues that this also is reason enough to establish that ComEd's analysis should be redone. (Staff Initial Brief at 103).

Staff states that another shortcoming is that ComEd did not indicate whether the result of this survey was factored into its analysis of primary and secondary costs. (Staff Ex. 10.0 at 28-29). Staff asserts that this fact presents a problem because this exercise should not just serve to describe the alternative approaches taken, but also determine whether any of the methods adopted by others could improve ComEd's analysis. (*Id.* at 29-30). Staff contends that this issue should also be addressed in the analysis to be presented contemporaneously in the initial filing of ComEd's next rate case. (Staff Initial Brief at 103-04).

Staff maintains that ComEd witness Mr. Alongi's defense of ComEd's review of the primary and secondary systems for other utilities is erroneous, as, Mr. Alongi does not clearly define what he means by primary and secondary systems. Therefore, Staff avers, it is not clear how ComEd has actually satisfied this Commission-ordered mandate. In fact, Staff continues, the primary system consists of the utility plant necessary to deliver electricity at the primary level. Therefore, Staff continues, for primary service at 4 kV and above, the issue concerns what portions of the utility system is necessary to serve customers at that level. As an example, Staff states, ComEd and IIEC disagree as to whether single-phase distribution lines should be

considered to be part of the primary distribution system. Staff opines that this is a fundamentally different topic from the utility tariffs that ComEd analyzed for this case. (Staff Ex. 26.0 at 11; Staff Initial Brief at 104).

Staff further opines that most of the utilities that ComEd examined use a specific voltage to distinguish between primary and secondary customers and many of those use 4 kV as the dividing line between the two groups. ComEd regards these results as affirmation "that the basic approach used by ComEd is consistent with the approach used by other utilities." ComEd also states that it sought to examine how other utilities allocate costs between primary and secondary service, but it could not proceed because the information "was simply unavailable." In support, Staff cites ComEd's Initial Brief at 115. Nevertheless, Staff continues, ComEd insists that it addressed the Commission's directive on this issue.

In response to these averments, Staff contends that ComEd's argument regarding this issue has been refuted by its own statements on the issue. As ComEd notes in its Initial Brief, the Commission directive pertains to "other utilities' methods in differentiating primary and secondary systems and costs." However, Staff continues, ComEd argued that it was unable to examine how "these utilities allocated the costs" between primary and secondary service. (*See, Id.*). Given what Staff views as a fundamental shortcoming, it states that there is no reasonable way that ComEd can conclude that it satisfied this directive. (Staff Reply Brief at 60-61).

ComEd's Position

ComEd avers that the Commission's *Rate Design Investigation* Order directed that ComEd examine "other utilities' methods in differentiating primary and secondary systems and costs." In support, it cites its witness Mr. Alongi, who testified that the Commission's order involved two tasks: examining how utilities distinguish between primary and secondary systems, and how they allocate the costs. (ComEd Ex. 49.0 Rev. at 40). It states that, although Staff was critical of ComEd's examination of how other utilities address the differentiation of primary and secondary costs, its analysis reasonably evaluated the issue. (ComEd Initial Brief at 114).

ComEd contends that it fully-examined how other utilities distinguish between primary and secondary systems by examining the tariffs of 35 unbundled distribution utilities in California, Texas, the Midwest, the Mid-Atlantic, and the Northeast. (ComEd Ex. 49.0 Rev. at 40). Additional information was obtained from utility employees in telephone conversations and through emails. (*Id.*). It concludes that its review showed that most utilities use a specific voltage level to distinguish between primary and secondary systems, and several use 4 kV as that bright line, at which, the primary system is defined. According to ComEd, this confirms that the basic approach that ComEd uses is consistent with the approach used by other utilities. (ComEd Initial Brief at 114).

ComEd also states that it made significant efforts to investigate the second task – how those utilities allocated the costs. However, ComEd concludes that the necessary cost allocation information was simply unavailable. Absent available and reliable information concerning other utilities' cost allocation methods, ComEd could not further refine its primary/secondary analysis. (ComEd Ex. 49.0 at 41-44; ComEd Initial Brief at 114-15).

Analysis and Conclusions

ComEd has failed to establish how examining tariffs, which is the primary method of examination that it used in this regard, satisfies the requirements in the *Rate Design Investigation* Order regarding this issue. ComEd provides no explanation as to why it did not examine the cost of service studies of these other utilities, or, simply consult with the persons or entities that perform these studies. A tariff normally does not provide evidence as to how a utility arrived at the charges that are required therein. And, there is no evidence here that the tariffs that ComEd reviewed contained information regarding how the utilities examined arrived at the charges enunciated in the tariffs.

As Staff notes, ComEd did not provide information indicating that it viewed these other utilities' cost analyses. Finally, and by far, the most troubling aspect here, is the absence of evidence indicating that ComEd factored its analysis of these other utilities into its analysis of its primary and secondary costs. Obviously, the Commission's requirement in docket 08-0532 was meant, solely, to require ComEd to educate itself as to how to apply a meaningful primary/secondary split regarding those costs, after having examined what other utilities in the United States have done. Yet, ComEd has provided no indication that it used any of its analysis of these other utilities here.

In its next initial rate case filing, ComEd shall produce cost of service studies that reflect analysis of what other utilities do regarding this issue in a meaningful manner. ComEd shall also proffer evidence at that time, establishing that it analyzed other these utilities' cost of service studies, and any other evidence that should be readily-available on other state Public Utility Commissions' websites. ComEd is further required to consult with the authors of these studies, as well as any NARUC publications on the issue, and to do any and all other actions that are necessary in order to determine how other utilities in the United States determine this issue. ComEd is also required to work with Staff regarding this issue.

(i) Other Primary/Secondary Split issues

a) **4kv Asset Allocation**

The Position of the CTA

The CTA contends that ComEd's embedded cost of service study incorrectly allocates costs for its 4 kV facilities to the Railroad Class. It avers that both the CTA and Metra exclusively take traction power service at a much higher voltage-12 kV. Thus, it reasons that 4 kV facilities are neither used nor useful for the Railroad Class. The CTA argues that therefore, ComEd should be required, as part of its next rate case, to develop an ECOSS that excludes the 4 kV facilities from being allocated to the Railroad Class.

The CTA states that, when allocating 4kV facilities to the Railroad Class, ComEd has acted in a manner that is contrary to the Public Utilities Act, citing 220 ILCS 5/9-101, which requires that the rates set must be "just and reasonable." Citing *Candlewick Lake Utilities Company v. Illinois Commerce Comm.,* 122 Ill. App. 3d 219, 227 (2d Dist. 1983), the CTA avers that a rate cannot be just or reasonable when it includes costs that do not directly benefit the ratepayer being charged for the costs at issue. (CTA Initial Brief at 7-9).

It asserts that there is no evidence that either the CTA or Metra takes delivery of traction power below 12 kV when they take delivery of electricity at Railroad Class rates. ComEd witness Mr. Alongi alleged that at two Metra traction power facilities, ComEd provides service at 4 kV, which, according to the CTA, erroneously leaves the impression that this service was for railroad-related traction power. However, it continues, the service he spoke of is not traction power service under the Railroad Class; it is service for other facilities that are located in the traction power substation facilities. The CTA asserts that the service he spoke of is not billed under the Railroad Class rate; instead, it is billed under a different rate. (CTA Initial Brief at 8).

CTA witness Mr. Harper reviewed both the CTA and Metra traction power substation diagrams that were referenced by Mr. Alongi. Mr. Harper concluded that: "The only circuits connected to the traction power bus were 12 kV and above. I know that no 4 kV circuit is connected to any CTA traction power bus." (CTA Ex. 4.0 at 3). CTA/Metra Joint witness Mr. Bachman also testified that no 4 kV facilities were connected to any Metra traction power bus. He noted that, as part of the special Railroad Class power flow study of the traction power substations, the characteristics of all traction power substations were reviewed. In no instance was traction power provided via a 4 kV circuit. (CTA/Metra Joint Ex. 2.0 at 5-6).

Mr. Bachman also reviewed the diagrams that Mr. Alongi alleged show that 4 kV circuits provide power to the traction power bus. (CTA/Metra Joint Ex. 2.01 Confidential). He concluded that: "Neither drawing shows 4 kV service connected to the traction power bus,"(non-Railroad Class service) but rather the 4 kV service feeds non-traction power service. (CTA/Metra Joint Ex. 2.0 at 6). And, at trial, ComEd witness Mr. Heinz confirmed that he knew of "no 4kV line that serves the Railroad Delivery Class." (Tr. 703). The CTA additionally asserts that from an engineering point of view, it would be impractical and costly for a 4 kV line to provide service for traction power, as the CTA's witness Mr. Harper testified that: "In essence, all of the 4 kV equipment that would have to be installed inside and upstream of the CTA substations would have to be sized to handle at least three times the electric current that is presently supplied through the existing 12 kV equipment." (CTA Ex. 4.0 at 3; CTA Initial Brief at 8).

The CTA avers that this problem arises because ComEd defines its primary distribution system to include 4 kV. It maintains that the Railroad Class does not create any cost causation for the 4 kV voltage level; nor does it need the 4 kV investment to serve customer classes at that level. By not differentiating the Railroad Class from the other primary distribution system customer classes, (when allocating primary distribution

system costs that include 4 kV voltage level costs) the CTA concludes that ComEd is incorrectly allocating 4 kV costs to the Railroad Class. (CTA Initial Brief at 11-12).

The CTA disagrees with ComEd's argument that it would take too much time and effort to refine its ECOSS to correct this error. The Railroad Class has only two members, who receive service in the same manner. (CTA Initial Brief at 12). Also, in ComEd's last rate case, Docket No. 07-0566, the Commission ordered ComEd to work with the CTA and Metra to conduct a power flow study of the Railroad Class' traction power facilities in order to determine to what extent ComEd uses the Railroad Class' facilities to serve other customers. This study was performed and its results are presented here. To perform the study, ComEd was required to identify each circuit serving each CTA and Metra traction power substation. The CTA maintains that as a result of the study, ComEd can identify each specific circuit and all of the equipment and facilities that are used to deliver power to the Railroad Class traction power substations. In support, the CTA cites ComEd witness Mr. Alongi, who testified, "In order to conduct the power flow, you need to know the circuits involved, the impedence of those circuits, the load on those circuits and where that load is connected." (Tr. 2124-25). This information, the CTA asserts, can be used as the basis for performing a specific cost-allocation for the Railroad Class that would eliminate the incorrect allocations for the 4 kV system to the Railroad Class. The CTA requests that the Final Order in this docket include a requirement for ComEd to develop a new embedded cost of service study for the next rate case that specifically excludes costs for facilities below 12 kV from the Railroad Class allocation. (CTA Initial Brief at 12-13).

The Position of Metra

According to Metra, historically, ComEd's embedded cost of service studies have produced inflated costs of service for the Railroad Class. Metra opines that ComEd's embedded cost of service study in this case also produces inflated costs of service for the Railroad Class.

Metra states that, in the last two ComEd rate cases and in the ComEd *Special Investigation* docket, Metra and the CTA argued that ComEd's embedded cost of service studies produced inflated rates for the Railroad Class and therefore could not be relied upon as a source of cost-based rates, absent substantial refinement and revision. Metra avers that due to revisions that the Commission ordered ComEd to make in the last ComEd rate case, docket 07-0566, and in the *Special Investigation* docket, docket 08-0532, ComEd's calculated cost to serve the Railroad Class decreased significantly. In the 2005 ComEd rate case, ComEd calculated that the cost to serve the Railroad Class to be approximately $8.5 million. (Tr. 2053-54). Metra states that in the 2007 ComEd rate case, it calculated that the cost to serve the Railroad Class was approximately $8.6 million. (Tr. 2056-57). After implementing Commission-ordered refinements, Metra continues, in this docket, ComEd's calculated cost to serve the Railroad Class is less than $6 million in ComEd's two exemplar studies, and is $6.35 million in the other cost of service study proffered. (Tr. 2058, 2060). It asserts that even with those reductions, ComEd's calculated cost to serve the Railroad Class is inflated because the Railroad Class is being assessed costs for 4 kV facilities which are not used to provide service to the Railroad Class.

Metra avers that ComEd delivers electricity to customers using distribution facilities that operate at three principal voltages, 4 kV, 12 kV and 34 kV. (Tr. 2216-17).[7] However, it asserts, the Railroad Class is served uniformly and exclusively at 12 kV. (CTA/Metra Joint Exs. 1.0 at 5-6 and 20-21; 2.0 at 5-9).

Metra disagrees with ComEd's assertion that any further refinement is unwarranted because allocation of individual assets or their costs to individual customers or groups of customers is not useful and would be costly and complicated. Metra contends that the Railroad Class issues do not involve allocation of single phase or three phase facilities within classes, or individual customer cost allocations. Instead, Metra is simply asking the Commission to direct ComEd to work with Metra and the CTA, and ICC Staff if appropriate, to study and delete from the costs assigned to the Railroad Class the 4 kV facilities that are not used to serve the Railroad Class. (Metra Reply Brief at 2-3).

It maintains that ComEd made the same arguments in opposition to the requested delineation of primary and secondary utilities usage and costs, citing ComEd witness Mr. Heinz's testimony. (Tr. 707-08). Metra points out that this argument was unavailing to ComEd, as the Commission "went ahead" and ordered the primary/secondary split, which was one of the two primary refinements in ComEd's cost of service study that reduced the Railroad Class' calculated costs. (*See,* Tr. 2058-2059). Metra maintains that, while there undoubtedly are a number of factors that account for ComEd's $2.6 million, 30 percent reduction, in the calculated cost to serve the Railroad Class, the primary/secondary split and other refinements ordered by the Commission were significant contributors to the 30 percent reduction in the calculated cost to serve the Railroad Class.

Metra further states that it only makes sense to require ComEd to further refine its cost study to eliminate the cost of substantial 4 kV distribution facilities that are not used to serve the Railroad Class. To do otherwise, it continues, potentially subjects the Railroad Class to inflated rates which would impose unwarranted costs on the Railroad Class and the public transportation customers that they serve.

Based upon Mr. Alongi's rebuttal testimony, ComEd has asserted that there are instances in which the Railroad Class uses circuits or facilities that operate at 4 kV. In fact, Metra states, Mr. Alongi testified in a prior case that the Railroad Class cannot be supported by 4 kV lines and facilities. (*See, Special Investigation* docket, 08-0532, Tr. 563; Metra Reply Brief at 5-6).

[7]Metra states that the parties and witness refer interchangeably to 12 kV and 12.5 kV when describing 12.5 facilities and also refer interchangeably to 34 kV and 34.5 kV facilities when describing 34.5 kV facilities.

REACT's Position

REACT states that its witness Mr. Terhune testified in his pre-filed testimony why the use of NCP or CP allocators over-allocate costs to the over-10 MW customer classes. According to REACT, as of the filing date for Staff/ Intervenor Rate Design Rebuttal Testimony, ComEd had refused to provide evidence about the distribution system assets serving the Extra Large Load customer class to confirm Mr. Terhune's argument, citing REACT Ex. 6.0C at 5. However, in its response to data request ALJ-OTR 1, which was served during the evidentiary hearing, ComEd produced some information about the distribution system assets provided to 45 of the 57 Extra Large Load class customers under "Rider NS," which ComEd uses to recover the costs involved with certain distribution system assets that are not covered by Standard Service rate, Rate RDS. REACT avers that ComEd's response to data request ALJ-OTR 1 included information about the non-standard and standard service facilities used to serve those 45 Extra Large Load customers. It also included information about the capacity of all of the listed distribution system assets. (*See* REACT Cross Ex. 25; REACT Initial Brief at 28-29).

REACT argues that ComEd's proposed rates overcharge the Extra Large Load customer class for some categories of system assets that this class uses in a very small amount. (REACT Ex. 6.0C at 21-22). In support, it states that ComEd has acknowledged that it attempts to recover for all distribution system assets allocated to the Extra Large Load class that are in rate base, whether suitable for Standard Service or not, through Rate RDS. (REACT Ex. 6.3; ComEd Response to REACT Data Request 6.10). In fact, it continues, the costs that ComEd recovers through Rate RDS are associated with several types of distribution system assets which are below the capacity that is required to provide Standard Service to the Extra Large Load customer class. (REACT Ex. 6.3; ComEd Responses to REACT Data Requests 6.01, 6.06-07, 6.10, and 6.12; REACT Initial Brief at 36).

Currently, REACT continues, ComEd allocates costs for those distribution system assets, including 12 kV single-/two-phase wires and 4 kV distribution system assets, based on coincident peak, non-coincident peak, or similar allocators applied to Uniform System of Accounts containing those distribution system assets that are "lumped" in with other types of distribution service assets. This is opposed to being based on class usage of distribution system assets. (Tr. 2134, 2146, 2164; 2184-85). According to REACT, the hard evidence in this proceeding undermines the fundamental premise of ComEd's position that applying an NCP or CP-related allocator is the best estimate of each class' usage of those systems. (REACT Initial Brief at 36).

REACT asserts that the information contained in ComEd's response to ALJ-OTR 1 (REACT Cross Ex. 25) demonstrates that ComEd's allocation of entire categories of distribution system assets is far in excess of the Extra Large Load customer class' use of those non-Standard Service distribution system assets. This evidence, it continues, confirmed what REACT witness Mr. Terhune had predicted in his pre-filed testimony. (*See,* REACT Ex. 6.0C at 22-24). The Commission now has evidence, it continues, based on class-specific information provided by ComEd pursuant to a REACT data request, that ComEd is charging non-cost based rates to the Extra Large Load

customer class, because it is charging that class an amount that is far in excess of the proportion of this class' use of the single, two-phase and 4 kV systems. REACT concludes that ComEd's proposed cost allocation and resulting rates fail to comport with the reality of ComEd's service to the Extra Large Load customer class, in violation of the Public Utilities Act. (REACT Initial Brief at 37).

The new information, REACT continues, shows that only 0.7% of the capacity of the distribution system assets serving 45 out of 57 Extra Large Load customers relies on the 4 kV system. (*See* REACT Cross Ex. 25). According to REACT, this completely undermines ComEd's proposed ECOSS-based methodology, which allocates these costs based on allocators related to class CP or NCP. REACT argues that therefore, this Commission should reject ComEd's proposed CP and NCP allocators, and instead assign no more than a system-average increase to the over-10 MW customer classes. (REACT Initial Brief at 29).

Mr. Terhune testified that 4 kV distribution system assets are not used to serve the Extra Large Load class at Standard Service. They would also generally be recovered using Rider NS for non-Standard Service. (*See,* REACT Exs. 3.0C at 17-21; 6.0 at 11-15, 19, and 27). REACT avers that ComEd's response to data request ALJ-OTR 1 corroborates and confirms Mr. Terhune's conclusion that a *de minimis* portion of the 4 kV system is used to serve the Extra Large Load class. (*See* REACT Cross Ex. 25; REACT Initial Brief at 29-30).

ComEd's Position

ComEd asserts that it presented evidence demonstrating that further segmentation of its primary distribution system is not warranted. According to ComEd, it proved that it is not appropriate to exclude all costs for these facilities from these classes because there are instances, in which, such customers use circuits or facilities that operate at 4 kV. In support, it cites its witness Mr. Alongi, ComEd Ex. 49.0 Rev. at 29-30; ComEd Initial Brief a 111). ComEd contends that the CTA, REACT and Metra fail to recognize that ComEd's primary distribution system operates at voltages of 4 kV or higher, as the Commission recognized in its *Rate Design Investigation* Order. In support, it cites the final Order in the ComEd *Rate Design Investigation* Order at 84, finding 4(a).

ComEd further asserts that its contract with CTA provides that ComEd shall provide electricity at 12 kV unless ComEd consents or elects a different voltage. (CTA Ex. 1.02 at 6). ComEd's contract with Metra provides that ComEd shall provide electricity at 12 kV or 4 kV for Metra substations existing at the time of the contract or 12 kV for additional substations unless parties mutually agree to a different voltage. (*See,* Metra Ex. 1.01 at 8-10). ComEd avers that any attempt to segment ComEd's almost 3.8 million customers based on their usage of specific components of the primary distribution system would be costly, complicated and fraught with assumptions. It avers that while one might find that any particular group or class of customers may make disproportionately small use of some components of the primary distribution system, it is equally plausible that those customers may make disproportionately larger use of other components. (ComEd Reply Brief at 115-16).

Analysis and Conclusions

The issue here is whether to allocate the costs that are associated with 4kV lines to the Extra Large Load and Railroad classes. If these customers are paying for service that they do not use, (or use on a *de minimus* basis, in the case of the Extra Large Load customers) they contend that they should not be required to pay for that service.

ComEd argues that the Railroad Class takes service at 4 kV. This is undoubtedly true, however, the evidence overwhelmingly establishes that it does so at a different rate that the Railroad Class rate. While Mr. Alongi testified that the Railroads take service at 4kV, he previously testified, in the *Investigation of Rate Design* docket, 08-0532, that they do not. (*See,* 08-0532, Tr. 563-64). Also, ComEd proffers its contracts with Metra and the CTA (the only members of the Railroad Class) as proof that these two customers take electricity at 4kV. However, a contract merely proves that a party is obligated to do something; it does not establish that Metra and the CTA take Railroad Class service at this level. The two are not the same.

We additionally note that even ComEd's witness Mr. Heintz testified that that he knew of no 4kV line that serves the Railroad Class. In fact, the evidence indicates that if the Railroad class *did* take service at 4kV, it would be impracticable and very costly, as all of the 4 kV equipment that would have to be installed inside and upstream of the CTA substations would have to be sized to handle at least three times the electric current that is presently supplied through the existing 12 kV equipment. (*See*, CTA Ex. 4.0 at 3). Based on the evidence provided, it is clear that the Railroad Class does not, and probably will never, take service at 4kV.

The question then becomes whether this fact justifies requiring ComEd to exclude 4kV costs in a future cost of service study. ComEd argues, essentially, that its customers, in general, must pay a percentage of the whole of its costs, as they have usage of the system as a whole. This contention is not without merit, as, at some point, exclusion of certain asset costs for a particular group of customers could result in a distortion of the price that all customers must pay to benefit from the use of a utility.

However, we need not decide this issue with respect to the Railroad Class. ComEd has had, for many decades, a unique relationship with the CTA and Metra. Proof of this unique relationship can be found in the fact that ComEd has contracts with these two entities. These contracts define the relationship between ComEd and these two entities. This is true because, necessarily, there is no point in entering into a contract, if a tariff governs all of the terms and conditions between the parties. Also, ComEd uses railroad-owned facilities to supply electricity to other customers. In fact, as is set forth elsewhere herein, in some instances, ComEd is dependent upon the railroads' facilities in order to supply electricity to other, non-railroad customers. The Railroad Class is truly a unique class, which has been segregated for decades. It should be segregated here.

We also note that, while ComEd maintains that it would be difficult and costly to segregate-out the 4 kV costs from the Railroad Class, this class has but two customers. And, the load-flow study, presented herein, should guide it. We therefore direct ComEd to work with Metra and the CTA, and Commission Staff if appropriate, to study, define,

and delete from the costs assigned to the Railroad Class the costs that are associated with the 4 kV facilities that are not used to serve the Railroad Class. Pursuant to that effort, ComEd shall develop a new embedded cost of service study for the next rate case that excludes the costs that are associated with facilities below 12kV from the Railroad Class. This study shall be part of ComEd's initial rate case filing. Failure to comply with any portion of this directive could subject ComEd to the penalties provided in the Public Utilities Act for failure to comply with a Commission Order.

As is set forth in the issue below, we conclude that ComEd must perform an investigation of the Extra Large Load customer classes. Included in that study shall be an assessment as to whether these customer use 4 KV service, and if so, to what extent, and also whether the NCP or CP allocator is an accurate allocator for these customers. We acknowledge that, in the past, the Commission has declined to require a study regarding this class of customers. However, that was before REACT presented an engineer who analyzed evidence that ComEd provided to him and concluded that these customers use very little single, two-phase, or 4 KV service, if any. We note that Mr. Terhune analyzed documents regarding 45 of the total of 57 Extra Large Load customers.

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

REACT's Position

REACT seeks a Commission order compelling ComEd to undertake a study of the distribution system assets serving the over-10 MW customer classes. According to REACT, as of the filing date for Staff/Intervenor Rate Design Rebuttal Testimony, ComEd refused to provide evidence about the distribution system assets serving the Extra Large Load customer class to confirm Mr. Terhune's argument, citing REACT Ex. 6.0C at 5. However, in its response to data request ALJ-OTR 1, which was served during the evidentiary hearing, ComEd produced some information about the distribution system assets regarding 45 of the 57 Extra Large Load class customers under "Rider NS," which ComEd uses to recover for certain distribution system assets that are not covered by Standard Service rates (Rate RDS). REACT asserts that ComEd's response to Data Request ALJ-OTR 1 include information about the capacity of all of the listed distribution system assets. (*See,* REACT Cross Ex. 25; REACT Initial Brief at 28-29).

REACT asks the Commission compel ComEd to undertake this task using ComEd's primary/secondary study as a template and starting-point for further investigation. REACT states that ComEd has both the capacity and institutional ability to conduct such a study, as is evinced by ComEd's primary/secondary split study, as well as other information that it has produced in the instant proceeding. Consistent with its rulings in the 2007 Rate Case and the *Special Investigation* Order, REACT concludes that the Commission should compel ComEd to compile the information that is necessary to enable the Commission to establish cost-based rates that reflect the distribution system assets that are used to provide service to the over-10 MW customer classes. (REACT Initial Brief at 31- 32).

REACT witness Mr. Terhune, a former ComEd engineer, testified that each customer class has minimum specifications, at which, the class normally receives Standard Service. As is described in ComEd's Tariff Sheets, the over-10 MW customer classes require, at minimum, nominal 4 kV, three-phase service. (*See,* REACT Ex. 3.0C at 12). REACT asserts that there are certain distribution system assets that are required to provide over-10 MW customer classes' minimum level of service. Also, it is ComEd's practice to use certain types or grades of distribution system assets to serve the classes. (REACT Exs. 3.0C at 15-17; 6.0C at 5, 7-8). Deviations from those minimums, REACT continues, virtually always occur pursuant to Rider NS facilities or facilities provided by ComEd for ComEd's convenience. (REACT Ex. 3.0C at 11).

REACT states that not all customers in the over-10 MW customer classes take Standard Service. According to REACT, most members of the over-10 MW customer classes also take delivery at voltages other than the nominal kV; they require use of the distribution system assets that would be unsuitable for Standard Service to such a customer. (REACT Initial Brief at 34).

REACT maintains that the costs that are associated with many of the non-Standard Service distribution system assets are excluded from rate base because those costs are billed directly to individual customers under Rider NS. (*See,* REACT Ex. 3.0C at 21-22; REACT Cross Ex. 25 (documents reflecting "Rider NS build outs"). Other non-Standard Service distribution system assets, REACT continues, are used by ComEd for its convenience because those distribution system assets' use is less costly to ComEd than installing or connecting to Standard Service distribution system assets. (REACT Exs. 3.0C at 16-17; 6.0C at 6). REACT concludes that, although ComEd nominally has identified the Rider NS-funded distribution system assets serving the Extra Large Load customer class, it has not specifically identified other non-Standard Service distribution system assets that ComEd uses to provide service to these customers. **(**REACT Initial Brief at 34-35). In essence, REACT argues that the information it received (REACT cross Ex. 25) has led it to believe that some Extra Large Load build-outs being billed pursuant to Rider NS are also included in Standard Service charges for these customers resulting in double-billing to these customers.

REACT acknowledges that it is possible that certain distribution system assets that are insufficient to provide Standard Service are not recovered under Rider NS. Also, according to REACT, ComEd has not estimated the impact of excluding those distribution system assets from the Extra Large Load class' base rate. The possible existence of these distribution system assets, REACT posits, "counsels strongly" in favor of approving REACT's request that the Commission compel ComEd to investigate the distribution system assets serving the Extra Large Load customer class. REACT notes that ComEd witness Mr. Alongi conceded that a properly-designed study can potentially pick up these distribution system assets that would otherwise not have been fairly allocated. (*See* Tr. 2208-2209). REACT continues that thus, by examining the required service for the over-10 MW customer classes, and subtracting the non-Standard Service assets that are paid for directly by those customers, it is possible to accurately identify the distribution assets that are used to serve the over-10 MW customer classes. (REACT Initial Brief at 35-36).

REACT agrees with ComEd that any ECOSS that ComEd submits is governed by Part 285 of the Commission's Rules. However, it states, these studies are also governed by the Commission's Orders, which have been highly-critical of ComEd's cost of service studies, as applied to the over-10MW customer classes. In support, it cites docket 07-0566, Final Order of September 10, 2008, at 212-13). REACT posits that Part 285 is a starting point, in that it sets forth the minimal requirements for the presentation of information that a utility must initially provide in a rate case. However, REACT continues, nothing in the language in Part 285, or Commission practice, suggests that compliance with Part 285 irrefutably answers the question of whether the rates that a utility has proposed should be approved. (REACT Reply Brief at 11-12).

REACT also acknowledges that its witness Mr. Terhune never prepared and ECOSS. It points out, however, that Mr. Terhune used his engineering experience and knowledge of ComEd's distribution system, which, ComEd never challenged, to explain the ways, in which, ComEd's ECOSS accounts for the actual engineering system. (*Id.* at 13).

REACT argues that ComEd has attempted to resurrect the "myth" that it now seeks individualized cost of service studies for the members of the Extra Large Load customer class. It states, however, that its proposed study would involve sampling and extrapolation, rather than a "nose count" of individual assets. It also cites the testimony of Mr. Terhune, who stated:

> I made no such recommendation in my direct testimony and I make no such recommendation in this testimony. What I *do* recommend is that the Commission ensures that ComEd's rates are actually cost based. Determining if rates are cost based necessitates understanding what costs underlie the rates -- that is, the cost and related revenue requirements of the assets that serve a given rate *class*.

(REACT Ex. 6.0C at 33; emphasis in original). REACT advocates a study to find the cost basis that the Public Utilities Act requires, rather than simply excluding certain assets from being assigned to those classes altogether. REACT also notes that even in the present rate case, ComEd has adjusted allocators to reflect arguments about distribution system realities that it and other parties have identified. (*See, e.g.*, ComEd Exs. 50.0 at 5; 74.0 at 2, discussing changes to NCP-SEC in Preferred Exemplar ECOSS; REACT Reply Brief at 13-15).

ComEd's Position

According to ComEd, REACT does not recognize that ComEd's ECOSS is prepared in a manner that is consistent with Part 285.5110 of Commission' Rules. Nothing in Part 285.5110, or in any other Commission Rule or Order, ComEd states, requires a utility to conduct a special investigation of the assets that are used to serve any particular customer class to prepare a cost study. (ComEd Initial Brief at 116).

ComEd also posits that REACT witness Mr. Terhune was never principally responsible for preparing an ECOSS or a marginal cost of service study. Also, he does not have knowledge of the Commission's Rules. (Tr. 1629-30, 1635-36). ComEd, on the other hand, presented testimony by witnesses with demonstrated experience in

preparing and relying upon these studies, (Messrs. Heintz and Alongi) such as those used by the Commission in previous ComEd rate cases.

Also, according to ComEd, this Commission should reject REACT's request for an investigation of the assets that are used to serve the Extra Large Load customer class for the same reasons that it rejected similar requests from REACT in prior proceedings. In ComEd's last rate case, the Commission rejected REACT's request for customer-specific cost studies, stating:

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

(Commonwealth Edison Co., docket 07-0566, Order of, Sept. 9, 2008, at 210). ComEd contends that also, in the *Rate Design Investigation* proceeding, the Commission rejected REACT's request to obtain customer-specific information based on a claim that such information would assist in evaluating a prior cost study, citing docket 08-0532, Denial of REACT's Petition for Interlocutory Review (Aug. 25, 2009), wherein Commissioner Elliott stated:

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

(Commission Minutes, Tr. 15:10-16:19).

ComEd further asserts that REACT's request is also at odds with how costs are compiled and allocated in an embedded cost of service study. Like all such studies, ComEd's ECOSS compiles ComEd's costs for providing distribution service and allocates such costs to the appropriate customer classes. (ComEd Ex. 49.0 Rev. at 29). ComEd avers that no ECOSS is conducted by compiling the costs to serve individual customers and then aggregating the costs to serve individual customers into class costs. (ComEd Initial Brief at 117).

Analysis and Conclusions

What REACT contends here is that the Extra Large Load customers have special facilities built for them by ComEd. ComEd bills these customers for these special facilities under Rider NS. Mr. Terhune's analysis of documents regarding 45 out of a total of 57 of the Extra Large Load customers revealed that it is possible that these special Rider NS facilities are also being billed under another Rider. It is also possible, as REACT acknowledges, that the converse is true, in that, other customers may be

paying for Rider NS build-outs. This is a unique situation that warrants further analysis and investigations. REACT also makes it clear that what is seeks involves sampling and class-wide allocation. This is contrary to ComEd's averment that preparing such a cost of service study would entail analyzing the costs on a customer-by-customer basis. While what is built-out and billed pursuant to Rider NS may be somewhat unique amongst these customers, there should be some uniformity regarding the equipment provided and billing for these services. ComEd shall therefore undertake a study of the distribution assets used to serve the Extra Large Load customer class. That study shall be part of any initial filing in its next rate case. However, REACT seeks a study regarding all over 10 MW customers. What it has presented concerns only the Extra Large Load class of customers to the extend that the two are not the same; this study shall be limited to the Extra Large Load customer class.

d. NCP (Noncoindent Peak) vs. CP (Coincident Peak) [8]

IIEC witness Mr. Stowe recommended that ComEd should be required to allocate primary lines and substation costs based on noncoincident peak ("NCP") rather than coincident peak ("CP"). Commercial Group witness Mr. Baudino offers a similar recommendation. In previous Commission Orders, it has required use of CP, rather than NCP, as an allocator.

ComEd's Position

ComEd's ECOSSs allocated primary lines and substation costs using a coincident peak ("CP") allocation method. (See, ComEd Ex. 16.0 3rd Rev. at 29). Consistent with the Commission's direction in the *Rate Design Investigation* Order, ComEd has allocated primary lines and substation costs using a coincident peak ("CP") allocation method. While it remains ComEd's position that the NCP allocation method is the appropriate method for allocating these costs, it is not making that proposal in this proceeding. (ComEd Initial Brief at 118).

Staff's Position

Staff states that the evidence here provides clear and compelling reasons for the Commission to reaffirm the use of the Coincident Peak ("CP") methodology for allocating distribution primary lines and substation costs in ComEd's embedded cost of service study. Staff points out that the CP approach was adopted by the Commission in the recently completed *Rate Design Investigation* docket, docket 08-0532, instead of a non-coincident peak ("NCP") demand allocator, which ComEd previously used. In Staff's opinion, the CP approach correctly recognizes that the size of ComEd's distribution facilities is driven by system peak demands, rather than by the demands of individual rate classes. In support, Staff cites Staff Cross Ex. 28 at 17-20.

[8] The CP method measures the demands for each rate class at the time that demand by the system as a whole is at a peak. The NCP method uses peak demands for all rate classes without regard to how those peaks coincide with the peak demand for the system as a whole. (Staff Ex. 28.0 at 17). Thus, NCP is a type of "worst case scenario."

Staff takes issue with the IIEC witness Mr. Stowe's testimony regarding the demands of the lighting classes, where he stated:

> ComEd has provided data in this case that show the NCP demands of customer classes can vary widely from their system CP demands. For example, the NCP demands of the Fixture Included Lighting and Dawn-to-Dusk lighting classes are nearly 7,300% of, or 73 times, their respective CP demands. When ComEd designs and builds its primary circuits and lines, the NCP loads of the Fixture Included Lighting and Dawn-to-Dusk lighting classes weigh more heavily in that process than the CP demands used to allocate costs.

(*See,* IIEC Exhibit 3.0 at 22). Mr. Stowe also averred that NCP reflects how ComEd designs its system:

> In the Rate Design Investigation docket, ComEd testified that it relies on NCP demands when designing shared circuits and substations, because they combine the peak demands of all of the classes regardless of when those peak demands occur. In other words, the NCP demands reflect the maximum demand that would occur if all of the classes peaked simultaneously.
>
> (*Id.*).

The problem with these arguments, Staff states, is that they are contradicted by ComEd witness Dr. Hemphill's testimony that lighting demands at the time of the peak are more relevant in sizing distribution facilities to meet peak summer loads. (Tr. 306). Also, Staff disagrees with the IIEC's argument that ComEd relies on NCP demands when designing shared circuits and substations. Staff states that this, too, is contradicted by Dr. Hemphill's testimony. Under cross-examination, Dr. Hemphill testified that as a general rule, distribution facilities are sized to meet summer, rather than winter demands. (Tr. 303). He also testified that distribution systems are designed to meet local peak conditions. (Tr. 300-301). Dr. Hemphill further stated that it is the demands that are expected from the customers that are within that area that is served that drives the level of the facility investment. (*Id.* at 301). Additionally, Dr. Hemphill stated that local demands can include the demands of customers from a variety of rate classes, if they all use those local facilities. (*Id.* at 303-304). Dr. Hemphill also averred that ComEd's system peaks in summer usually in the mid-afternoon when street lighting demands are below their nighttime peak. (Tr. 305-306). Regarding the role of summer peak demands in sizing distribution facilities, Dr. Hemphill testified that he considers most distribution facilities to be sized to meet summer, rather than winter demands. (Tr. 303; Staff Initial Brief at 104-105).

According to Staff, these statements clearly indicate that demands for distribution substations and primary lines are more likely to coincide with system peak demands (summer peak demands), than with the demands of individual rate classes, such as lighting customers, which occur during off-peak periods. This, Staff asserts,

undermines Mr. Stowe's claim that ComEd relies on NCP demands when designing shared circuits and substations.

Staff avers that an examination of lighting class demands demonstrates why this is so. Mr. Stowe opined that ComEd considers non-coincident lighting demands more heavily in its planning process. However, Dr. Hemphill indicated that is not true. When asked which are more relevant in sizing distribution facilities designed to meet peak summer loads, lighting demands at the time of the peak or lighting demands at night when they reach their non-coincident peak, Dr. Hemphill replied that lighting demands at the time of system peak are more relevant. Staff concludes that ComEd itself directly contradicts the IIEC's assertions about ComEd's planning process. (Staff Initial Brief at 106; Staff Reply Brief at 62).

Staff contends that thus, despite the IIEC's arguments to the contrary, investments in distribution substations and primary lines are more likely to be shaped by system peak demands (summer peak demands), than the demands of individual rate classes, such as lighting customers, which can occur at other times of the year. Therefore, Staff recommends that the Commission continue to uphold its decision in Docket No. 08-0532 and continue to use the CP method for allocating distribution primary lines and substation costs in ComEd's ECOSS. (Staff Reply Brief at 62-63).

The City of Chicago's Position

The City of Chicago states that, in his rebuttal testimony, City witness Mr. Bodmer responded to Commercial Group witness Mr. Baudino's and the IIEC witness Mr. Stowe's recommendations that the Commission required ComEd to use the NCP allocator to allocate primary distribution facilities. Mr. Bodmer described many reasons why Mr. Baudino's and Mr. Stowe's recommendation should be rejected. However, the City continues, the biggest reason to reject the Commercial Group and IIEC proposal is that the Commission considered this issue in docket 08-0532, the *Rate Design Investigation* docket.

In that case, the Commercial Group, the IIEC, and ComEd advocated use of the NCP allocator. The City and Staff argued for use of the CP allocator. In its Order, the Commission weighed the arguments made by each side and concluded that "We are persuaded that the allocation costs to substations and primary lines should be made on a CP basis." In support, the City cites *Investigation of the Rate Design*, docket 08-0532, Final Order of April 22, 2010, at 55. The City further states that, in Ameren's most recent rate case, docket 09-0306, the Commission rejected arguments to use the NCP allocator and found that primary lines and substations should be allocated on a coincident peak (CP) basis. (*See, In re Central Illinois Light Company,* (the Ameren rate case docket) docket 09-0306, Final Order of April 29, 2010, at 237). The City avers that the Commission was clear in both its *Rate Design Investigation Order* and the Ameren Rate Case Order that utilities should use CP to allocate primary facilities. The City maintains that neither the Commercial Group, nor the IIEC, have provided any reason to shift course and adopt the NCP allocator. (*See*, City Initial Brief at 7-8).

According to the City, Mr. Stowe ignored this distinction and interpreted Mr. Alongi's statement to mean that, because ComEd does not build its system on system-wide coincident peak demand, it must build its system using non-coincident demand. Mr. Bodmer testified that such an implication is not logical. The City also states that it contradicts Mr. Alongi's testimony in previous cases. In a prior ComEd rate case, Mr. Alongi stated that:

> For each of the customer classes, two distribution capacity components were identified, the non-coincident class peak ("NCP") component and the coincident peak component. The NCP component … includes the costs for standard system elements that are likely to be sized to accommodate individual customers' maximum loads. ... The coincident peak component, on the other hand, includes the costs for standard system elements necessary to serve a geographic area or larger group of customers that can be sized with consideration given to diversity between individual customers' loads. … [T]he investment costs of Transmission Distribution Centers ("TDCs"), 34 kV lines, Distribution Centers ("DC"), primary lines, and primary taps were included in the coincident peak component.

The City avers that Mr. Alongi's testimony in Docket 01-0423 is consistent with Dr. Hemphill's testimony in this case. It supports confirming the Commission's decision in the *Rate Design Investigation* docket to use CP to allocate primary lines and substations. (City Reply Brief at 6; City Ex. 2.0 Rev. at 11, *quoting* Docket No. 01-0423, ComEd Ex. 13.0 at 16-17).

The City further asserts that its witness Mr. Bodmer showed that the NARUC Cost manual is not nearly as straightforward as the IIEC and the Commercial Group suggest. Mr. Bodmer testified that the quote from the Cost Manual that Mr. Stowe included in his testimony "is an incomplete and distorted representation of discussion in the NARUC Manual." Mr. Bodmer also pointed out that the Introduction to the NARUC Cost Manual makes clear that "its objectives were to be comprehensive and also 'simple enough to be used as a primer' and to 'be non-judgmental; not advocating any one particular method but trying to include all currently used methods with pros and cons.'" (*See,* City Ex. 2.0 Rev. at 14). The City concludes that therefore, the IIEC's quote from the NARUC Cost Manual does not stand for the simple proposition that IIEC and the Commercial Group assert. Rather, it is filled with conflicting principles and was not intended to be used to advocate any particular allocation method. (City Initial Brief at 10-12).

The City also takes issue with the IIEC's quotation of ComEd witness Mr. Garcia's Rebuttal Testimony from this case. In the quoted testimony, the City states, in fact, Mr. Garcia was quoting ComEd witness Mr. Alongi's testimony from Docket 08-0532, the *Rate Design Investigation* case. (*See,* ComEd Ex. 50.0 at 5-6, *quoting*, Docket 08-0532, ComEd Ex. 10.0 at 27). The City argues that the foundation for IIEC's argument is testimony from the case, in which, the Commission rejected using NCP to allocate primary lines and substations. The City points out that the Commissi

REACT's Position

REACT opines that the Commission should adopt an NCP allocator for ComEd's 12 kV and above primary substations and 12 kV and above, three-phase wire. REACT states that ComEd's NCP-SEC allocator is designed to track use of certain secondary distribution system assets, specifically distribution lines. REACT witness Mr. Terhune testified that because the Extra Large Load customer class uses secondary distribution system assets in a negligible proportion, it would be inappropriate to allocate anything other than a reasonable estimate of the class' *de minimis* impact on the system. (REACT Ex. 6.0C at 17-18). Although ComEd's final ECOSS (surrebuttal versions) do not allocate any costs to the Extra Large Load customer class as part of NCP-SEC, ComEd's original preferred exemplar allocated the class a 0.79% allocation, a result that Mr. Terhune characterized as "absurd." As a result, REACT contends that the Commission should follow the approach set forth in ComEd's surrebuttal testimony, and use the NCP-SEC allocator for secondary lines. (REACT Initial Brief at 41-42).

The IIEC's Position

The IIEC recommends that the Commission direct ComEd to use the NCP for the allocation of primary lines and substations. It states that use of that allocator is consistent with industry practice, cost causation, and the evidence presented in this case. The IIEC avers that in docket 08-0532, the Commission was persuaded that the allocation of costs associated with distribution substations and primary lines should be made on a CP basis because; (1) substations and primary lines were not "sized to meet the demands of any single class, but rather, the collective demands of customers from multiple classes; and (2) lighting classes' demand does not coincide with system peak demands, and therefore, the lighting class plays a lesser role in shaping substation and primary line investments than classes that have demands that are coincident with the system peak. (*See,* IIEC Ex. 3.0-C at 21, quoting from the *Rate Design Investigation Order*). In its view, such an allocation is inconsistent with actual cost-causation on the ComEd system. (IIEC Ex. 3.0-C at 20; IIEC Initial Brief at 48-53). The IIEC maintains that its witness Mr. Stowe has provided un-refuted testimony that the NCP method, like the CP method, reflects the demands of all classes. Mr. Stowe testified that "[t]he difference between the two methods is that the CP method focuses on the load contribution of each class during a particular hour of the year, whereas the NCP method reflects a theoretical or "worst case" estimate of the potential load distributions." (IIEC Ex. 3.0-C at 23).

The IIEC also maintains that Commission's second concern, which is, that lighting class demand does not coincide with the system peak demand is based on the faulty assumption that distribution facilities (as opposed to transmission or generation facilities) are designed to serve the system peak demand. It avers that if utility engineers and planners designed primary distribution circuits and substations to serve customers' load at the time of the system peak, the use of the CP allocation method would be reasonable and appropriate. According to the IIEC, such is not the case, as primary circuits and substations are designed to provide safe and reliable power under

both normal and extraordinary conditions, at any time of the day. (IIEC Initial Brief at 48-53).

The IIEC further cites ComEd witness Mr. McMahan, who is an electrical engineer. He testified that in preparing to construct or enhance distribution facilities, distribution system designers look at the "aggregate" or "area" load that the particular distribution facilities (*e.g.,* particular substations or primary circuits) must serve, not the system loads. (Tr. 501-502). This aggregate load is based on ComEd's "1 in 10-year" planning criteria, which use the highest annual system peak load in the previous 10 years, combined with a projected load forecast for the particular facilities in question. (*Id.* at. 500-501).

The test year CP demands that ComEd used to allocate costs in this case reflect the class loads during a single hour of a summer day in 2009. According to the IIEC, these CP demands have no meaningful relationship to the aggregate or area load estimates used by ComEd engineers to design and construct distribution facilities. NCP demands, however, reflect the maximum potential demand of the customer classes served via the distribution system, regardless of when that demand occurs. In fact, the IIEC continues, the NCP can be viewed as a measure of the potential contribution of each class to cost causation, because the sum of the NCP demands for all customer classes represents the capacity of the distribution system that stands by to serve the electrical demands of all customers at any given time. (Tr. 1199-1200).

The IIEC also cites ComEd witness Mr. Garcia who stated:

> ComEd designs its primary lines and substations based on the non-coincident peak that occurs on those facilities, not the system coincident peak. Likewise, the Commission agreed in its Final Order in ComEd's 2007 Rate Case that the record showed that "[d]istribution facilities must be planned and built to meet customers' maximum loads, regardless of when those may occur." Docket No. 07-0566, Final Order at 217. Consequently, it is reasonable to me that the costs of such facilities would be allocated on the basis of NCP.

(*See,* ComEd Ex. 50.0 at 5-6, quoting from Docket No. 08-0532, therein, ComEd Ex. 10.0 at 27).

According to the IIEC, the testimony of ComEd witnesses Mr. McMahan and Mr. Garcia comport with the testimony of IIEC witness Stowe. Mr. Stowe, an electrical engineer, stated "system designers cannot simply design the primary circuits and substations to distribute the amount of power that flowed through the primary distribution system during a historical system peak hour." Rather, the IIEC states, they must rely on estimates – in particular, 'worst case' estimates – when designing the system for future use. (IIEC Ex. 3.0-C at 21-22; IIEC Initial Brief at 48-53).

Mr. Stowe further testified that it is the CP method, not the NCP method that fails to reflect the combined customer class load that ComEd distribution designers relied upon when they designed ComEd's primary lines and substations. (IIEC Ex. 3.0-C at 22-23). As such, according to the IIEC, the CP method does not allocate costs in

accordance with how those costs were incurred. Mr. Stowe testified that the "NCP demands of the Fixture Included Lighting and Dawn-to-Dusk lighting classes are nearly 7,300% of, or 73 times, their respective CP demands." (*See,* IIEC Ex. 3.0-C at 22). The IIEC concludes that therefore, when ComEd designs, builds, upgrades and maintains its primary lines and substations, incurring investments and expenses to serve the NCP demand of its customers, yet allocates these costs to the classes on the basis of class CP demand, it significantly understates the costs incurred to the lighting classes.

Regarding the cross-examination of ComEd witness Dr. Hemphill, the IIEC states that, on two occasions during his cross examination, Dr. Hemphill clarified that he was neither a facilities planner nor a distribution system engineer. (Tr. 301 and 304). It concludes that, in fact, Dr. Hemphill's testimony makes essentially the same points as that of ComEd witnesses Mr. Alongi and Mr. McMahan, which is, according to the IIEC, that distribution facilities such as substations and primary circuits are designed to meet the highest combined peak demand of the customers connected to them, regardless of when that peak demand occurs. It concludes that Staff is unreasonably assuming that Dr. Hemphill's testimony contradicts the position of ComEd's engineering witnesses, who have already made clear that ComEd does not design these distribution facilities to meet CP demand as Staff assumes. (IIEC Reply Brief at 29-31).

The Commercial Group's Position

The Commercial Group states that distribution substation and primary feeder line costs should be allocated on the basis of class non-coincident peak (NCP). According to the Commercial Group, this is consistent with industry practice, how ComEd designs such systems, how the Commission historically has treated such costs, and with the NARUC cost allocation manual. It further states that the IIEC provided additional information in its direct testimony that showed that ComEd designs these substation and primary line facilities to meet both normal and extraordinary conditions throughout the year (and a given day) and the NCP factor best captures this design reality. (*See,* IIEC Ex. 3.0 at 20-24). Additionally, according to the Commercial Group, ComEd agreed with this approach. In support, it cites ComEd Exs. 50.0 at 2; 74.0 at 61-62. (Commercial Group Initial Brief at 5).

Analysis and Conclusions

In the *Rate Design Investigatio*n docket, docket 08-0532, Final Order of April 22, 2010, at 55; the Commission specifically addressed this issue in relation to the arguments of ComEd, the IIEC and others. This issue was thoroughly explored therein. In that Order, this Commission concluded that CP is the correct factor to use. (*See also, In re Central Illinois Light Company,* docket 09-0306, Final Order of April 29, 2010, at 237). We therefore decline to deviate from these past decisions. We additionally note that essentially, the IIEC and the Commercial Group maintain that these previous decisions were erroneous because the costs that are allocated should mirror engineering concerns for NCP. However, there is no credible evidence that the investments in question, distribution substations and primary lines, correlate to NCP-related investments.

This is true because that there is no indication from the evidence presented here, that NCP, which is a form of "worst case scenario" on a system-wide basis would fairly allocate the costs involved in calculating NCP amongst the customer classes. Generally, what is involved in a "worst case scenario" for an industrial area will be far different from that which is involved in a residential area. It therefore appears that, based on the evidence presented, imposition of NCP costs on this basis could raise the cost of electricity to lower-using customers, (*e.g.,* residences) even though these lower-using customers did not cause much of the NCP-related costs on an overall basis, or to higher (*e.g.,* industrial) users. This is inapposite to the notion of attributing cost-causation to those who incur the costs in questions.

Finally, we find the IIEC's dismissal of Dr. Hemphill's testimony, on the basis that he is not an electrical engineer, not to be persuasive. This issue concerns cost allocation. The IIEC has made no showing establishing that Dr. Hemphill is unqualified to testify regarding cost allocations.

f. Allocation of Primary Lines and Substations

This issue is discussed under the NCP vs. CP heading.

g. Functionalization of General and Intangible Plant

This issue is discussed in Section IV C 3 (e) herein, which is entitled "Allocation of G & I Plant."

h. Street Lighting

This issue is discussed in section VII C g, entitled "Dusk to Dawn Street Lighting"

i. Allocation of Illinois Electricity Distribution Tax

j. Indirect Uncollectible Costs

The City of Chicago's Position

The City of Chicago states that in the docket 07-0566 ComEd rate case Order, and in the *Rate Design Investigatio*n Order, the Commission directed ComEd to change the manner in which it allocated uncollectible costs among the residential sub-classes. Before those Orders, ComEd allocated the costs associated with each sub-class to the members of that sub-class. The Commission agreed with the City in both of those cases that the more fair way to allocate uncollectible costs was to allocate the costs evenly across all of the residential classes.

Here, City witness Mr. Bodmer testified that ComEd complied with the Commission's Orders in Docket 07-0566 and the Rate Design Investigation case. However, he recommended that the indirect costs that are associated with uncollectibles should be allocated in the same manner. Such indirect costs include the costs "of collecting, administering, managing, disconnecting, and reconnecting uncollectible accounts." Given the recent financial crisis, Mr. Bodmer stated that it is likely that indirect uncollectible costs are even greater now. (City Ex. 1.0 at 61-62). Although Mr. Bodmer did not calculate the magnitude of indirect uncollectible costs in this case, he did make the calculation in the *Rate Design Investigation* case and he determined that they were approximately $34 million. (*Id*. at 64).

Mr. Bodmer, in his rebuttal testimony, suggested a method, by which, ComEd could collect indirect uncollectible costs in the same manner as it does uncollectible costs. In particular, Mr. Bodmer said that, to compute the correct number for indirect cost, he would first separate the call center calls related to credit and collections. Some of call center costs could then be assigned to uncollectible costs rather than being assigned on the basis of the number of ratepayers. Next, he would review all of the accounts in account 903 to evaluate which costs are related to credit evaluation, collection activities, the costs of disconnecting consumers, the costs of re-connecting consumers, and any other costs associated with evaluating, collecting or administering costs associated with people who are late in paying their bills. (City Ex. 2.0 Rev. at 36; City Initial Brief at 23).

ComEd's Position

According to ComEd, Mr. Bodmer's proposal should be rejected because he did not produce any evidence or study that identifies or defines what constitutes indirect uncollectible costs. Also, he did not explain why such costs are related to the uncollectible costs themselves. According to ComEd witness Mr. Garcia, there is no clear reason to differentiate the reconnection of service from an initial service connection. (ComEd Ex. 50.0 at 7; ComEd Initial Brief at 121-22).

Analysis and Conclusions

ComEd's argument on this issue circumvents common sense. There are certain costs, such as collection costs, the cost of disconnection for non-payment and the cost of reconnection for non-payment, that are almost always, if not entirely, associated with uncollectible accounts. The cost of reconnection for non-payment involved uncollectible accounts. Initial service connection does not, unless that customer owes ComEd a balance on a previous account. In the future, (in ComEd's next rate case or rate design case) it shall include the segregated indirect uncollectible costs in a cost of service study in the manner that Mr. Bodmer set forth in his rebuttal testimony. This study shall be part of ComEd's initial rate case filing in ComEd's next rate case.

k. Customer Care Cost Allocation

Background

Customer care costs are such items as Field and Meter Services, billing and mail services, the Customer Contact Center, Large Customer Solutions, Revenue Management, payment processing, and customer relations, as well as the costs that are related to back office support of these functions, such as project and support services, Information Technology, Demand Management, Electric Supplier Services, and Market Research. (ComEd Ex. 19.0 Rev. at 5-6). ComEd performed two tests, which are, the "Switching Study" and the "Allocation Study," in order to determine what portion of these customer care costs are properly allocated to delivery service, and are therefore properly passed on to all customers, even those customers that take electricity from retail electric suppliers. REACT, however, advocates use of the Allocation Study when allocating these costs.

Staff's Position

Staff avers that in the ComEd *Rate Design Investigation* Order, the Commission directed ComEd to file an ECOSS for these costs and to also include the results of its avoided cost study. (Order, Docket No. 08-0532, April 21, 2010, at 69). Staff states that the evidence in this proceeding indicates that ComEd's proposed method of accounting for customer care costs, which is, the Switching Study, ("avoided cost study") presents a more reasonable approach than the Allocation Study, ("embedded cost study") that was presented by ComEd and strongly advocated by REACT. Staff maintains that customer care costs support both the distribution and supply functions and the issue in this proceeding concerns how much of these costs should be included in the distribution revenue requirement. The resolution of that allocation issue determines how customer care costs are to be recovered from ComEd customers receiving distribution-only services ("unbundled customers") or both distribution and supply services ("bundled customers"). (Staff Ex. 12.0 at 25; Staff Initial Brief at 108).

Staff avers that ComEd began its analysis of the issue by identifying the amount of customer care costs that were incurred to serve customers. ComEd's review of these costs focused on direct O&M costs pertaining to customer service in excess of $100,000. (Staff Ex. 12.0 at. 27). It then developed two separate methods of allocating these costs between the distribution and supply function. The first method, known as the "Switching Study" (ComEd Ex. 19.1), determines the share of customer care costs that are supply-related, by assessing whether they are sensitive to the number of customers switching to supply service furnished by alternative retail electric suppliers. The second method, known as the Allocation Study, uses the embedded cost approach to allocate customer care costs between the supply and distribution functions. This approach removes a portion of the customer care costs from the distribution revenue requirement for allocation to the supply function. (*Id*. at 26; Staff Initial Brief at 108-09).

The Switching Study, Staff continues, examines the effect of three customer switching scenarios, in which, 1%, 10% and 100% of customers choose alternative suppliers. The degree, to which, customer care costs changed under these three scenarios is ComEd's measure of the relative cost of providing customer care to bundled and unbundled service. (Staff Ex. 12.0 at 28).

According to Staff, the Switching Study suggests that ComEd does not incur significant differences in customer care costs for bundled and unbundled customers. (*Id.* at 30). This result is consistent, Staff continues, with ComEd's contention that, if customer switching were to increase ten-fold from the current level of 1% to 10%, only a few hundred thousand dollars in additional costs would be expended or saved as a result. For example, Staff states, ComEd incurs almost identical billing costs in preparing, sending and processing bills for bundled and unbundled customers. (*See,* ComEd Ex. 19.0 Rev. at 12). In both cases, the meter must be read, the bill prepared and mailed, the payment received and processed. (Staff Ex. 12.0 at 30). Thus, according to Staff, ComEd correctly asserts that increased switching to 10% or even 100% would not produce meaningful savings. (ComEd Ex. 21.0 at. 45) The fact

remains, Staff opines, that virtually all of these costs need to be incurred in order to support ComEd's distribution service. (*Id.* at 36; Staff Initial Brief at 109-110).

Staff opines that the Switching Study correctly recognizes that ComEd, as the default provider, must stand ready to serve customers that have chosen to receive supply service (the actual electricity supplied) from a retail electric supplier. Regardless of the number of customers switching, ComEd must incur the necessary costs to stand ready to serve them again if they switch back to ComEd. The Allocation Study, on the other hand, allocates customer care costs between the supply and distribution functions on an embedded cost basis. (Staff Initial Brief at 110-111).

Staff also maintains that application of the Allocation Study would shift a significant share of customer care costs to the supply function from ComEd's distribution service-related revenue requirement. Under this approach, an unbundled service customer could potentially bypass some customer service costs, assuming that this customer was allocated and charged to only bundled supply customers. (Staff Ex. 12.0 at. 35). As a result, the issue arises concerning how these supply-related customer care costs would be recovered from ComEd ratepayers and it is unclear at this time exactly how that is to be done. (Staff Initial Brief at 111).

Fundamentally, Staff states, the results of the Allocation Study produce a kind of subsidy of the customers that retail electric suppliers serve. Staff contends that this would not foster efficient competition and it does not support the concept of cost-causation. Subsidies, it continues, distort prices, create inefficiencies, and potentially could increase costs to customers. Staff strongly believes that the Commission should not under-price what unbundled customers would pay for customer care costs, thereby overpricing bundled customers. (Staff Ex. 12.0 at 40; Staff Initial Brief at 111-12).

Another consideration Staff made is that ComEd's treatment of customer care costs is similar to the treatment used by other utilities in Illinois. Staff is not aware of any electric or gas utility that has customer care costs allocated on an embedded cost basis between distribution and supply. If the Commission were to accept the Allocation Study instead, this would set an undesirable precedent, not only for other electric utilities in Illinois, but for gas utilities as well, because the same arguments could apply to any utility with significant supply costs relative to distribution costs. (Staff Ex. 12.0 at 31; Staff Initial Brief at 112).

Staff takes issue with REACT's statement that the Switching Study is "guesswork." Staff argues that REACT is incorrect because the Switching Study does, in fact, present a scenario based on current switching levels. The study finds that the current level (*i.e.,* today) of customers switching to retail electric supplier service, which conforms to the 1% switching scenario, has not had an impact upon ComEd's costs that are related to customer services. (Staff Ex. 28.0 at. 13). Staff also states that, for the future 10% or 100% switching scenarios in the study, ComEd estimates that customer services costs will not be reduced in either case, but will actually increase. (Staff Ex. 12.0 at 29). Staff concludes that while switching levels of 10% or 100% are not likely in

the foreseeable future, these scenarios nevertheless show that customer care costs can be expected to rise, even as additional customers switch suppliers. (Staff Initial Brief at 112).

ComEd's Position

ComEd states that customer care costs encompass nearly every aspect of a customer's direct interaction with ComEd. (*See,* ComEd Ex. 19.0 at 5-6). It contends that whether these costs should be recovered in delivery service rates, or functionalized to supply and recovered from supply (and PORCB)[9] customers turns on the sound application of the principle of cost-causation. ComEd avers that it has undertaken a systematic examination of these costs. It also performed two distinct studies of the services that produce these costs. The first study has been denominated the "Switching Study" because it considers the impact on ComEd's costs of customers switching electric suppliers. Costs that are driven by the provision of delivery service should not change when customers switch to an alternative supplier. According to ComEd, the Switching Study identifies these costs. ComEd has also performed a second study, the "Allocation Study," which is aimed at apportioning between the two functions any cost that is properly attributable to both functions and that are thus deemed to be common costs. (ComEd Initial Brief at 122-23).

ComEd asserts that it is not controverted that the Switching Study shows that, both now and in the near future, ComEd realizes virtually no cost savings when its supply customers switch to a retail electric supplier. (*See, e.g.*, ComEd Exs. 19.0 Rev. at 1-2; 19.1). According to ComEd, REACT offered practically no criticism of the Switching Study other than to dismiss its results as "speculative." However, ComEd continues, the Switching Study examined the impact on ComEd of the costs of 1%, 10%, and 100% customer switching to retail electric suppliers for electricity. With 1% of ComEd customers already taking service from a retail electric supplier, there is nothing speculative about the 1% scenario. The other two scenarios, it continues, which come to similar results as the 1% scenario, only confirm that there will probably be no material reduction in ComEd's costs when additional customers switch suppliers. In support, ComEd cites ComEd Exs. 19.0 Rev. at 2; 24.0 at 7-9. ComEd avers that, while the Switching Study shows no change to costs at 1% switching, it does project both increased and decreased costs at levels of 10% and 100%, with the increases offsetting the decreases, resulting in overall cost increases. (ComEd Ex. 19.1).

ComEd further points out that, when evaluating whether to adopt the results of the Switching Study, ComEd, as a delivery service provider, is required to incur the costs of providing delivery service to each of its delivery customers, regardless of from whom the customer obtains its supply of electricity. It concludes that arbitrarily shifting costs to supply that are driven by delivery service understates the true costs of the delivery service.

[9] The term "PORCB" refers to ComEd's Purchase of Receivables and Consolidated Billing program for retail electric suppliers. (*See,* docket 10-0138 generally).

ComEd states that the cost of providing metering services illustrates this point. Each customer receiving delivery service from ComEd is entitled to a meter provided by ComEd. That meter measures the amount of energy delivered by ComEd. It also measures the amount of electric supply that customer uses. ComEd points out that it is undisputed that 100% of the costs of metering are delivery service costs and none of those costs should be functionalized to supply. When a customer taking supply service from ComEd switches to an alternative electric supplier, the costs that ComEd incurs in providing delivery service to this customer, such as the cost of the meter, are not reduced. REACT witness Mr. Merola agreed with the proposition that, even though metering costs are attributable to both supply and distribution, metering costs should be assigned 100% to the delivery function because metering services "are provided by ComEd regardless of whether or not they provide the supply." (*See,* Tr. 2008-09;. ComEd Initial Brief at 125).

ComEd further avers that the Switching Study also comports with the Commission's treatment of customer services costs in the past, as part of delivery services costs. Disregarding this logical approach "in favor of an arbitrary allocation between supply and distribution" would set an undesirable precedent for all Illinois utilities. In support, ComEd cites Staff witness Mr. Rukosuev, Staff Ex. 12.0 at 31.

REACT's Position

REACT witness Mr. Merola testified that ComEd's customer care costs "represent those costs ComEd incurs to provide customer service for its delivery and supply customers." (*See,* REACT Ex. 2.0 at 5). REACT concludes that customer care costs are the customer service-related costs that ComEd incurs in all of its dealings with its customers. (REACT Initial Brief at 8). REACT states that Section 16-108(c) of the Public utilities Act requires that ComEd's delivery rates must be "cost based" such that, the costs charged to customers reflect use of the "facilities and services associated with such costs." In support, it cites 220 ILCS 5/16-108(c) and (d)). It concludes that the Act requires ComEd to demonstrate a clear link between the delivery services charges for a particular customer class and the costs associated with the facilities and services used to provide service to that particular customer class. REACT states that, beyond mandating delivery services rates that are based upon the actual facilities that are used to provide service, this statute requires consideration of customer's impacts.

REACT concludes that supply-related costs should not be included in ComEd's delivery service rates. Failure to accurately allocate customer dare costs to ComEd's supply rates results in artificially-inflated delivery services rates, and inaccurate price signals that have anti-competitive effects. REACT avers that those inaccurate price signals advantage ComEd as a provider of supply service, and place alternative retail electric suppliers at a disadvantage, because alternative suppliers are forced to compete against an artificially low ComEd bundled supply rate. (REACT Ex. 5.0 at 6; REACT Initial Brief at 9-10).

ComEd and REACT agree that customer care costs "are those costs [ComEd incurs] to provide customer service for its delivery and supply customers." (Tr. 1314).

Also, Staff witness Mr. Rukosuev similarly testified that "Customer care costs are incurred to support both the distribution and supply functions and the issue here is how these costs are to be allocated between the two." (Staff Ex. 12.0 at 24-25). He also agreed that Customer Care Costs "support both the distribution and the supply functions of ComEd." (Tr. 1183). REACT concludes that therefore, the record evidence shows that customer care costs relate to both the delivery and supply functions. (REACT Reply Brief at 19-20).

According to REACT, the Switching Study approach has been historically questioned by the Commission is theoretically unpersuasive. REACT further opines that this study relies on speculative customer switching scenarios. REACT cites the *Rate Design Investigation* Proceeding, where the Commission found that REACT "raise[d] many valid points and when the two methodologies are compared, questions arise." (docket 08-0532, Final Order of April 21, 2010, at 68). The Commission further stated:

> REACT, however, points to functions that clearly support supply, yet no costs are allocated to supply for these functions in ComEd's [analysis] . . .. REACT informs us that it was unable to get this information from ComEd. Similarly, REACT raises a valid argument that some portions of the calls received by the Customer Call Center should be allocated to supply.

After concluding that "REACT's methodology is consistent with an embedded cost methodology", the Commission "directed [ComEd] to perform an embedded cost study for [Customer Care] costs and present it for consideration and discussion in [ComEd's] next rate proceeding." (*Id.;* REACT Initial Brief at 49-50).

REACT contends that the Switching Study is inconsistent with the Act and the Commission's guidance in the *Rate Design Investigation* Proceeding. According to REACT, the Switching Study purports to allocate current costs based on ComEd's "guess" about what costs will be avoided in the future based on "unknown" customer switching scenarios, rather than whether the costs are caused by supply or delivery functions today. (REACT Ex. 2.0 at 15-16, 17). (REACT Initial Brief at 51).

REACT argues that whether ComEd's costs change or stay the same in the event of additional switching has nothing to do with whether the costs were *caused* by the delivery function, that is, whether those costs fit within the definition of "delivery services" in Section 16-102 of the Act. It also states that although it arguably may reflect cost-causation at some point in the future, the avoided cost approach does not reflect whether ComEd incurred certain costs in the present, due to supply or delivery. (REACT Ex. 5.0 at 13, 15, 16). REACT points out that ComEd's Allocation Study allocates over 13 times more costs to the supply function than ComEd's Switching Study. (*See,* ComEd Exs. 19.1, 19.2).

According to REACT, the Switching Study is highly speculative. It avers that ComEd has admitted the speculative nature of its Switching Study both on cross examination and in testimony. In support, REACT cites Tr. 1334-1337; Tr. 1190-1191. It concludes that both ComEd and Staff ignore that, in order to construct the Switching Study avoided cost numbers, ComEd "had to come up with" a total cost reflecting current circumstances, heavily rely upon the estimated costs at 10% and 100%

switching for comparison. (REACT Initial Brief at 52). REACT also cites ComEd witness Mr. Donovan, who stated:

> ComEd agrees that these impacts are only **potential** as opposed to actual. They are not based on current costs, and the actual future O&M implementation costs are likely to be different from the figures that ComEd utilized in the Switching Study.

(ComEd Ex. 48.0 at 5; emphasis in original). And, REACT continues, Staff witness Mr. Rukosuev also conceded on cross-examination that the cost levels at 10% and 100% switching were "speculative future scenario[s]." (*See,* Tr. 1190). (REACT Initial Brief at 53-54).

Analysis and Conclusions

We conclude, based upon the evidence presented, that ComEd analyzed the correct pool of costs in the "Switching Study". We therefore reject REACT's proposed adjustments to the Allocation Study. While we acknowledge that ComEd's figures in the Switching Study regarding 10% or 100% of its customers switching suppliers are hypothetical, there is no evidence here indicating that ComEd's customer care costs would diminish to any significant degree, if 10% or a greater amount of its supply customers switched to retail electric suppliers. We note that some of these functions, billing and metering, to name a few, will remain constant, regardless of the number of customers that are served by alternative suppliers. Additionally, ComEd is the default provider. It must stand "ready willing and able," so to speak, to serve customers that have switched providers.

We acknowledge that, in the *Rate Design Investigation* Order, a traditional embedded cost of service study was required. However, such a study does not recognize that many of the customer care costs, such as metering, customer service calls related to power outages, etc. will be incurred by ComEd, irrespective of whether a customer takes electricity from an alternative supplier.

We also disagree with REACT's averment that the Switching Study is "guesswork." In fact, the 1% scenario therein is based on fact. The 10% and 100% scenarios therein are projections based upon the 1% scenario. No party has presented evidence indicating that these projections are scientifically invalid.

However, we additionally note that the alternative electric supplier market is just beginning to blossom. It is possible that, in the future, ComEd's customer care costs could differ from what they are now, in terms of the amounts involved and the types of services involved, as, items like IT interfacing with alternative suppliers becomes more sophisticated. Also, pursuant to ComEd's PORCB program, consolidated billing is now an option (consolidated between the alternative supplier and ComEd). Therefore, this issue may need to be explored some time in the future.

(i) Allocation Study vs. Switching Study

This issue is discussed in the issue above.

(ii) Direct O&M Costs vs. Total Costs in the Switching Study

ComEd's Position

ComEd contends that, if the Commission agrees with both ComEd and Staff and finds that the Switching Study presents a more accurate picture of cost causation than the Allocation Study, the question regarding whether to analyze direct O&M costs, or "total costs," is immaterial because the answer has no real impact on the results of the Switching Study. ComEd identified the costs to be reviewed for purposes of the customer service studies as the 2009 direct O&M costs submitted in ComEd's June 30, 2010 (initial) rate case filing. (*See,* ComEd Ex. 19.0 Rev. at 4-5). According to ComEd, this is consistent with both the ComEd *Rate Design Investigation* Order and the treatment of ComEd's administrative supply costs in Rider PE – Purchased Electricity. (ComEd Exs. 24.0 at 4-5; 50.0 at 11). ComEd concludes that thus, its analysis of direct O&M costs is appropriate and should be accepted by the Commission. (ComEd Initial Brief at 126).

In its Reply Brief, ComEd avers that there has been some confusion in the testimony and briefing about the difference between the costs that ComEd reviewed for purposes of the customer service studies and the "total costs" as described by REACT. It states that all parties agree that ComEd's detailed analysis of direct O&M costs is only different from REACT's analysis of customer services costs by $141.9 million. In support, it cites Staff Ex. 28.0 at 8-9; ComEd Ex. 48.0 at 3-4; Tr. 1331-33. (ComEd Reply Brief at 128-29).

REACT's Position

Both REACT and Staff agree that, in order to be consistent with the ComEd *Rate Design Investigation* Order, ComEd should consider "total costs," including direct operations and maintenance ("O&M"), indirect O&M, and capital costs. In support, REACT cites REACT Exs. 2.0 at 20-25; 5.0 at 6-9; Staff Ex. 28.0 at 5-8.

REACT posits that ComEd has conceded that indirect O&M costs and capital costs had been removed from the "pie" of customer care costs that ComEd is analyzing here. (*See,* ComEd Ex. 50.0 at 11). In fact, it continues, ComEd excluded many indirect O&M costs including: executive and employee compensation, office supplies and expenses that were not billed to a department, fees and expenses of professional consultants and others for general services, employee pensions, insurance, property maintenance, regulatory commission expense, general labor and expenses, and property rent. In support, it cites Tr. 1324-1326; 2282; REACT Ex. 2.0 at 21, citing to admissions in ComEd Responses to REACT data requests.). And, according to REACT, ComEd admitted that it did not consider capital costs, meaning that it excluded depreciation expenses, tax expenses, and the costs that are associated with the rate of return on the relevant assets. (Tr. 1326-1327, 2282-2283). (REACT Initial Brief at 56-57).

REACT's witness Mr. Merola presented an analysis of customer care costs that showed that the total size of the "pie" to be allocated is approximately $434 million. (REACT Exs. 2.4C and 2.5C; Ex. 5.0, at 8-9). In sharp contrast, REACT maintains, the

result of ComEd's admitted omissions of indirect O&M and capital costs is that ComEd has artificially reduced the "pie" of customer care costs by approximately $259 million (or approximately 60% of the actual total), for a proposed total of just approximately $176 million. (REACT Ex. 2.0 at 9-10). That reduction, REACT argues, was completely unjustified.

REACT argues that the plain language of the *Rate Design Investigation* Order required consideration of "these costs," referring to the total costs allocated by Mr. Merola in that docket. In support, it cites the *Rate Design Investigation* Order, docket 08-0532, Final Order of April 21, 2010, at 68). REACT also states that ComEd's witness in charge of ComEd's customer care cost analysis could not explain why ComEd's studies excluded such a large portion of these costs, other than to say that he received that instruction from a superior at ComEd. (*See,* Tr. 1323; Tr. 1314-1315). According to REACT, this falls well-short of a persuasive explanation for excluding costs that the Commission previously required to be included in this analysis. (REACT Initial Brief at 56).

Staff's Position

Staff recommends that the Commission reject ComEd's approach to base the allocation of customer care costs on only direct O&M costs. Instead, according to Staff, this Commission should require ComEd to revise its analysis, (for both the Switching Study and the Allocation Study) to include the costs associated with the full revenue requirement amount, and include that allocation in ComEd's compliance rates for this docket. (Staff Ex. 28.0, pp. 9-10). Staff states that ComEd's analysis of the customer care issue is deficient in one key respect: it employs an arbitrary definition that unreasonably limits the amount of customer care costs analyzed. Specifically, Staff continues, ComEd included direct O&M costs, but it excluded any indirect costs in its definition of customer care costs. Thus, Staff agrees with REACT witness Merola's argument that the Company defines customer care costs too narrowly. (Staff Ex. 28.0, p. 5)

Staff opines that REACT witness Mr. Merola correctly argued that ComEd's definition of customer care costs should account for the full-revenue requirement that is associated with customer care, instead of just a subset. (REACT Ex. 2.0 at p. 20). Rather than restrict the analysis only to direct O&M costs, ComEd should be required to include all costs (direct and indirect) in the revenue requirement in its analysis of customer care-related costs. (Staff Ex. 28.0 at p. 5; Staff Initial Brief at 112).

Staff states that there are significant dollar differences between these two definitions. ComEd's focus on direct O&M costs produces a total of $125.8 million in customer care costs to be analyzed, while REACT's more inclusive definition raises that amount to approximately $267.7 million, according to both ComEd witness Donovan and REACT witness Merola. (Tr. 1333). Staff states that ComEd's focus on direct O&M costs only reduces the amount of customer care costs by $144.1 million from REACT's definition. (REACT Ex. 2.0 at 20).

Staff points out that there is an additional reason to accept the broader definition advocated by REACT. Analyzing the full revenue requirement associated with

customer care costs, instead of just a subset of those costs (direct O&M costs), is consistent with ComEd's general ECOSS methodology. As a general rule, ComEd's general ECOSS allocates not just direct costs, but indirect costs as well. In fact, Staff states, ComEd's witness on the subject, Mr. Donovan, frankly admitted that the decision regarding the customer care costs to be considered was made, apparently without explanation, by ComEd's Regulatory Department and without Mr. Donovan's input. (Tr. 1322-1323). Staff concludes that ComEd has not offered any persuasive reasons for limiting its analysis to only direct O&M costs, while REACT presents good reasons for including all associated customer care costs in the analysis. Staff concludes that the weight of evidence clearly supports REACT's position on this issue. (Staff Initial Brief at 113-14).

Analysis and Conclusions

At the outset, we disagree with ComEd's assertion that analyzing the total costs, instead of merely viewing the direct O&M costs, is not meaningful because, according to ComEd, analyzing the actual costs has no real impact upon the results of the Switching Study. The impact that including the total costs here would have, at a minimum, would be to reflect reality, instead of some artificial group of costs that ComEd arbitrarily chose. Additionally, ComEd's decision in this regard ignores the mandate set forth by this Commission in the *Rate Design Investigation* Order.

We also note that Staff and REACT correctly point out that the numerical difference between direct O&M costs and total costs indicates that the difference could exceed one million dollars, which is not insubstantial. ComEd's revised figures, based upon Mr. Merola's analysis, shall be the subject of a post-record data request.

(iii) Adjustment of Allocation Study Allocators

This issue is now moot as, in the previous two sections above, this Commission has made it clear that it is not adopting the Allocation Study.

l. Other Docket No. 08-0532 Compliance Issues

m. Other Issues

1. Imposition of AMI (Advanced Metering Infrastructure) Costs on the Railroad Class

Metra's Position

Metra argues that, in disregard for this Commission's Final Order in docket 09-0263, at pp. 38-39, 43, (the docket that approved the AMI pilot program) and a waste of resources, ComEd installed six AMI meters on Railroad Class facilities and is now seeking $1,212 for AMI pilot project costs from the Railroad Class. Metra states that there is not and will not be any evidence that the Railroad Class requested the meters or can benefit from the "smart meters" in any way. Metra further states that ComEd's Manager of Regulatory Strategies and Solution, Mr. Garcia, offered the excuse that "the Commission never directed ComEd through its Order in Docket No. 09-0263 not to install the enhanced meters that are not presently serving railroad facilities," despite the

fact that the final Commission AMI-approving Order (in docket 09-0263) specifically found that the railroads do not need these meters. (ComEd Ex. 74.0 at 4). Metra argues that ComEd should be forbidden from allocating costs to the Railroad Class for AMI project costs that the Commission already has determined should not be assessed to the Railroad Class. (*See, e.g.,* Metra Memo at 5-6).

The CTA's Position

The CTA also contends that the Final Order in this docket must exclude AMI meter charges from the Railroad Class rates. It states that ComEd includes in the Railroad Class rates the costs that are associated with the AMI pilot project despite the fact that the final Order authorizing ComEd's AMI pilot program specifically excluded the Railroad Class. CTA/Metra Joint witness Bachman testified that, even if the railroads participated in the AMI pilot, which they do not, such a pilot would serve little or no useful purpose because both the CTA and Metra have already spent millions of dollars installing their own SCADA system so they know on an instantaneous basis how power is flowing through the traction power systems. (CTA/Metra Joint Ex. 1.0 at 23-25). The CTA also, states that in docket 09-0263, the Commission specifically found that the Railroad Class should not have the AMI pilot program costs imposed on this class, stating that: "Imposing the cost of this pilot program upon the CTA and Metra, when they are not the cost-causers, is unfair." (Final Order, Docket No. 09-0263 at 43). (CTA Memo at 6).

ComEd's Position

ComEd witness Garcia disagreed with Mr. Bachman and testified that there are currently six (6) enhanced meters serving railroad facilities that were deployed as part of the AMI Pilot approved by the Commission. ComEd contends that this deployment justifies the allocation (charges). Mr. Garcia also testified that Mr. Bachman's statement that the "Commission has already decided … that the AMI Pilot Is [*sic*] of no benefit to the Railroad Delivery Class" is a matter of "interpretation" . Mr. Garcia further testified that if Mr. Bachman's conclusion is solely based on the Commission's statement that "the railroads already have systems in place that equate to, or, are indeed superior to, the ones that will be included in the pilot program here" (docket 09-0263, Final Order at 43), then there is some basis for his interpretation. However, according to ComEd, despite that statement, the Commission never directed ComEd through its Order in Docket 09-0263 not to install the enhanced meters that are presently serving railroad facilities. (ComEd Ex. 74 at 4).

Citing to the Commission's Order in Docket 09-0263, Mr. Garcia testified that the Commission, in its discussion of the difficult question of who benefits from the AMI Pilot, also recognized that "many large commercial and industrial customers already have the technology and information that this program will provide," but it nevertheless adopted the IIEC proposal in that case, noting that these customers would not be "let… 'off the hook'" and would be required to "pay an amount that is commensurate with what they receive from this program." Mr. Garcia surmised that while it is clear the Commission let the Railroad Delivery Class "off the hook" (to use the Commission's words) with respect to temporary rider recovery, there is an open question as to whether the

Commission intended to let this class "off the hook" permanently with respect to the meters installed for the class under the AMI Pilot. (*Id.* at 98-105).

Analysis and Conclusions

The CTA and Metra are correct that the Final Order in the order approving the AMI pilot program, docket 09-0263, was quite clear that the Railroad Class does not need AMI meters, and, therefore, should not be part of that program. That Order was also very clear that no charge should be imposed upon the CTA or Metra for this program. Therefore, the $1,212 at issue shall not be imposed upon the Railroad Class.

We further note that, as Metra points out, installing these meters is an utter waste of resources. Installing these meters after a Commission Order issued which specifically stated that the Railroad Class does not need these meters insults the integrity of the AMI program that was approved in Docket No. 09-0263, as, that program was meant to educate persons in the general public as to their consumption. We caution that adherence to rulings in Commission orders shall be expected in the future.

D. Rate Moderation

See Section VIII C. 4. a. of this Order, entitled "Movement Toward ECOSS."

VII. Rate Design

A. Overview

<u>ComEd's Position</u>

ComEd initially explains that rate design is not about determining ComEd's revenue requirement, but rather allocating the revenue requirement among customer classes and rate elements. ComEd presented the testimony of Ross C. Hemphill, who described the policy reasons supporting ComEd's proposed rate design. He testified that ComEd's revenue requirement should be fairly allocated based on long-standing cost-causation principles. ComEd asserts that its rate design proposal is a reasonable approach to apportion costs using the Commission's preferred embedded cost approach, minimizing interclass rate subsidies.

ComEd submitted three separate rate designs over the course of this proceeding: 1) its proposed rate design; 2) a Preferred Exemplar rate design; and 3) an alternative exemplar rate design. The designs differ mainly in their recovery of the costs of the primary distribution system. ComEd's proposed rate design consolidates the current four residential delivery classes into two classes. The consolidation eliminates the distinction between residential customers that use space heat and those that do not use space heat. ComEd asserts that this proposal is reasonable, as the space heat distinction has no relationship to distribution rates. Rather, the space heat distinction is a vestige from a time when ComEd was a vertically integrated utility.

For non-residential customers, the primary difference in ComEd's three rate design proposals relates to the recovery of costs of the primary distribution system. ComEd's proposed non-residential rate design employs ComEd's current rate classes. Meanwhile, ComEd's Preferred Exemplar rate design establishes a new primary distribution class, consistent with the directive in the RDI Order. ComEd presents its Preferred Exemplar rate design in the event the Commission directs ComEd to create a

Primary Voltage Delivery Class. ComEd also submitted an alternative exemplar rate design in response to certain Intervenor concerns. The alternative exemplar rate design does not establish a new primary rate class. Rather, ComEd's existing demand-based nonresidential classes are subdivided to incorporate certain charges for service points to which electricity is delivered above a certain threshold.

ComEd's proposed a rate design also includes a straight fixed variable ("SFV") rate proposal for residential customers and small general service or watt-hour customer classes. ComEd argues that its SFV proposal, discussed in detail below, better aligns the cost of service with pricing, thus sending proper price signals to customers. ComEd proposes to phase-in its SFV rate proposal over three years, on a revenue neutral basis.

B. Potentially Uncontested Issues

1. High Voltage Rate Design Simplification

ComEd states that it has proposed to simplify rate design for the High Voltage Delivery Class as follows: (1) for both the customer charge and the standard metering service charge, the six possible charges would be reduced to a single customer charge and a single standard metering service charge; (2) with respect to the distribution facilities charges ("DFCs"), the five possible standard voltage DFCs would be reduced to a single DFC for all load provided at voltages entering customer premises below 69 kV; and (3) for all load provided at voltages entering the customer premises at or above 69 kV, there would continue to be two DFCs, one applicable if the customer's highest thirty minute demand in the past twelve monthly billing periods exceeded 10 MW and the other applicable if the customer's highest thirty minute demand in the past twelve monthly billing periods did not exceed 10 MW. ComEd adds that no party objected to its proposal. This proposal is reasonable and it is approved.

2. Rate MSPS

ComEd is proposing changes to certain charges under Rate MSPS – Metering Service Provider Service ("Rate MSPS"), applicable where a retail customer elects to be provided metering service from a metering service provider ("MSP"). ComEd does not object to Staff's recommendations to limit the increases for Meter Reading Charges, and charges to read additional meters or for special exchanges, to 50%. Further, ComEd also did not object to Staff's recommendation that additional language be included in Rate MSPS to eliminate any ambiguity related to the equipment removal charges. This proposal is reasonable and it is approved.

3. General Terms and Conditions

a. New Customers with load that includes motors equal or greater than five horsepower

ComEd proposed to revise the General Terms and Conditions ("GTC") to clarify that when a customer has load that includes motors equal to or greater than five horsepower, a 3-phase voltage is provided as standard. Staff witness Rockrohr recommended inclusion of a "grandfather provision" that states ComEd will not require existing single-phase customers with single-phase five horsepower motors to convert

their electrical entrance equipment to receive 3-phase. Although ComEd believes appropriate clarifying language is already included in the revisions to GTC proposed by ComEd in its June 30, 2010 filing, ComEd made additional clarifying tariff revisions. Neither Mr. Rockrohr nor any other party objected to the amendments reflected in the revised GTC tariff. This proposal is reasonable and it is approved.

4. Miscellaneous Charges and Fees

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

Staff witness Harden recommended approval of ComEd's proposed change to the Single Bill Option Credit. With respect to t the remaining fees, ComEd did not object to Ms. Harden's recommendation that the proposed increases in those fees be reduced by 50% and that corresponding adjustments be made to ComEd's revenue requirement.

ComEd states that based upon its analysis in connection with this proceeding and discussions with Staff and RESA, ComEd updated its proposed Interval Data Fee to $3.45 per meter. ComEd believes that this is appropriate based upon the costs of providing interval data for each meter on a customer's account and which coincides with the per meter fee proposed by Staff. ComEd explains that the updated Interval Data Fee is different than the $3.32 per meter fee proposed by Staff because it reflects the fact that Staff has withdrawn its proposed adjustment for ComEd's Annual Incentive Plan. This proposal is reasonable and it is approved.

5. Meter Lease Charges

ComEd proposed revisions to Rider ML – Meter-Related Facilities Lease ("Rider ML"), which update meter lease charges and simplify the manner in which meter leases are administered. No party objects to ComEd's proposal. This proposal is reasonable and it is approved.

6. Residential Real Time Pricing Program Costs

ComEd proposed (a) a change in the recovery of costs associated with its residential real time pricing program ("RRTP") in Rider RCA – Retail Customer Assessments ("Rider RCA") that would reduce the charge from $0.14 per month to $0.05 per month and (b) to eliminate the $2.25 monthly participation fee for the first 110,000 customers taking service under rate RRTP. ComEd updated the calculation of this charge to include the cost of meter exchanges related to the real time pricing program that was inadvertently omitted from the original calculation set forth in ComEd Ex. 23.2. While the addition of meter exchange cost did not cause a change (increase) in the proposed charge for the recovery of the costs associated with the RRTP program ($0.05), ComEd noted the update so that it is clear in future proceedings what costs are being recovered from residential customers to fund the program.

Staff witness Harden recommended approval of ComEd's proposed reduction to this charge from $0.14 per month to $0.05 per month provided that the Commission

approves Staff witness Dr. Schlaf's recommendation regarding the termination of the monthly $2.25 participation fee. Staff witnesses Harden and Schlaf raise no other issues with respect to ComEd's proposals as updated. These proposals are reasonable and they are approved.

7. Standard Meter Allowances

The Standard Meter Allowances used in the simplified manner in which meter leases are administered were changed to adjust for the identification of additional customers eligible for the exemplar Primary Voltage Delivery Class and to correct an error as to the number of customers in the Extra Large Load Delivery Class. No party objected to ComEd's proposal. This proposal is reasonable; it is approved.

C. Potentially Contested Issues

1. SFV

a. ComEd's Proposal

<u>ComEd Position</u>

In this proceeding, ComEd has proposed movement towards a straight fixed-variable ("SFV") rate design. ComEd adds that the SFV rate design applies only to residential customers and nonresidential customers in the Watt-Hour Delivery Class and establishes fixed and variable charges that track the fixed and variable costs of serving those customers. In an SFV design, distribution costs are first classified as fixed or variable. ComEd explains that fixed costs, which do not vary from billing period to billing period based on monthly energy use, are collected through charges (such as the customer charge and the standard metering service charge) that also do not vary with energy use. Those delivery costs that do vary with a customer's energy use are recovered though charges that also change with the customer's energy use (such as the proposed Illinois Electricity Distribution Tax Charge). ComEd argues that failing to properly make the distinction between fixed and variable costs results in the current rate structure that recovers an inordinate proportion of fixed costs through rates that are not fixed, but that vary with volume. Thus, ComEd concludes that this sends a distorted price signal to customers and penalizes utilities for implementing conservation programs.

ComEd explains that its proposal moves the delivery service rate design for the residential delivery classes and the Watt-Hour Delivery Class toward SFV in a manner similar to that approved for other delivery utilities. Dr. Hemphill testifies that the Commission should approve ComEd's proposal to gradually move to an 80% SFV because that proposed rate design more closely reflects the correct division between fixed and variable costs. Dr. Hemphill also refutes concerns raised by Staff witness Boggs. ComEd notes that Mr. Boggs' positions (1) were either arbitrary or inconsistent with ratemaking principles; and (2) are contrary to recent Commission decisions to either decouple or move toward an SFV in rate cases filed by North Shore/Peoples Gas, the Ameren Illinois Companies ("Ameren"), and Nicor Gas Company ("Nicor Gas"). Dr. Hemphill testifies regarding the Commission's Orders in recent cases involving the Ameren and Nicor Gas, where the Commission adopted SFV rate designs recovering 80% of fixed costs in fixed customer charges. Dr. Hemphill refutes various concerns

about the proposed SFV rate design raised by City witness Bodmer, NRDC witnesses McDermott and Cavanagh, and AG-CUB witness Rubin. ComEd maintains that a SFV rate design is appropriate for ComEd because it more closely aligns fixed and variable prices to effectuate cost recovery with the correct division between fixed and variable costs.

ComEd states that if the Commission approves Staff's proposed downward adjustment of between 20 and 40 basis points to ComEd's return on equity while approving an SFV rate design, then ComEd would have to reconsider its support for SFV. Thus, if the Commission concludes, after considering all the evidence that such an ROE reduction would be warranted, ComEd requests that the Commission should instead decline to adopt SFV rates at this time.

ComEd maintains that arguments by Staff and various Intervenors in opposition to ComEd's SFV proposal, including that SFV does not promote energy efficiency, that it inappropriately shifts costs to residential customers, and places an excessive burden on low use customers must be rejected as without merit. First, with respect to energy efficiency, ComEd maintains that distribution rates cannot be arbitrarily designed to achieve conservation objectives. When designing distribution rates, ComEd states that it must keep three things in mind with regard to rate design: (1) it is important to send correct price signals to customers and the recovery of fixed costs through the application of volumetric charges sends inaccurate price signals to customers; (2) gradualism is employed in its proposal as, over a three-year period, the use of volumetric charges is being reduced for the recovery of 40%, then 30%, and finally 20% of its overall delivery service costs; (3) as a percentage of a typical customer's total bill for bundled electric service, the portion that ComEd proposes to be recovered through fixed charges is significantly less than the amount recovered through the volumetric charges. ComEd states that there will continue to be significant overall cost recovery through the proper application of volumetric charges for electric supply service.

ComEd adds that the Commission has spoken with respect to the impact of SFV on energy efficiency. Citing Docket No. 08-0363, Order (Mar. 25, 2009), at 92. ComEd observes that it is true that electricity and natural gas consumption are conversely seasonal but no party has explained why this difference should result in different delivery pricing policies. To the contrary, ComEd explains that the fact that electricity demand peaks in the summer, when it is used for cooling, while natural gas demand peaks in the winter, when it is used for heating, illustrates how similar the industries are with respect to cost structures. ComEd Ex. 71.0 at 3. Further, with respect to Staff's argument that the SFV proposal fails to account for costs associated with the provision of electricity (Staff Init. Br. at 124-125), ComEd states that it does not produce electricity and the costs under consideration in this proceeding are associated with the delivery of electricity only. Supply-related costs are appropriately recovered through supply charges which are already volumetric in nature. ComEd Ex. 46.0 at 13.

Second, ComEd argues that the arguments that SFV unjustly shifts costs to residential customers and places an undue burden on low use customers must be rejected. ComEd states that the majority of ComEd's delivery service costs are based not upon the amount of electricity used (kWh) but rather upon the maximum rate at which electricity is used (kW). ComEd explains that this has been acknowledged by the

Commission in the 2007 Rate Case Order. 2007 Rate Case, Order (9/10/08) at 217. Dr. Hemphill testifies that ComEd must consider the maximum rate at which the electricity is used, not just the quantity of electricity used. ComEd adds that it is not appropriate for it to assign cost responsibility or recover its costs for its delivery service facilities based simply on electricity usage. ComEd maintains that there is no evidence demonstrating that delivery costs for customers using smaller amounts of electricity are necessarily lower than the delivery costs for customers using larger amounts of electricity. ComEd Ex. 71.0 at 6. Further, ComEd's states that its SFV proposal makes an appropriate distinction between single family residential customers and multi-family customers, which is appropriate because, in general, the maximum rate at which multi-family customers use electricity is less than the maximum rate at which single family customers use electricity. ComEd explains in refuting Mr. Rubin's analysis. ComEd Ex. 71.0 at 7; ComEd Ex. 16.0 3rd Rev. at 26:471-Table D8 and 26:485-Table D9. ComEd also explains that a low use customer does not equate a low income customer. ComEd notes that reducing fixed customer charges while increasing usage charges in an effort to affect social policy goals is not a reasonable objective of rate design for an entire class of residential customers. ComEd 46.0 at 19. ComEd notes that the Commission recognized this in the 2007 Rate Case. 2007 Rate Case Order at 212.

Finally, ComEd states that the AG and City assertion that ComEd's SFV proposal is actually an attempt to recover short term marginal costs must be rejected. ComEd explains that it is proposing to set the delivery service rates for all its customers to recover its embedded costs. In fact, ComEd is attempting to use its non-volumetric charges to recover 80% of its embedded total costs while the volumetric rates recover the remaining fixed costs and the embedded variable costs. ComEd maintains that there is a significant difference that all economists should recognize between average embedded variable costs and marginal costs, let alone short-run marginal costs

AG

ComEd proposes an unprecedented change in the residential customer charge that would increase residential single-family and multi-family class cost recovery through the flat, customer charge from 37% to a whopping 80% by May, 2014. ComEd In. Br. at 138; ComEd Ex. 14.0 at 11. Staff witness Christopher Boggs pointed out that the residential class is particularly punished under the ComEd SFV rate design, with the Residential and "Watt-Hour" classes experiencing significantly larger customer charge increases than other classes. Staff Ex. 13.0 at 26.

As justification for its radical proposal, ComEd argues in its Brief that "(f)ailing to properly make the distinction between fixed and variable costs results in misallocation of costs." ComEd In. Br. at 137. ComEd complains that the current rate structure recovers an inordinate proportion of fixed costs through rates that are not fixed, but that vary with volume, thereby sending "a distorted price signal to customer (sic)" that "penalizes utilities for implementing conservation programs." *Id.*

As noted in the AG Initial Brief, ComEd's SFV proposal rests on the assumption that residential customer costs do not vary with usage. ComEd Ex. 14.0 at 10. While ComEd downplays it in its Brief, ComEd witness Ross Hemphill argued that cost recovery through the distribution facilities charge ("DFC" or "usage charge") is

inappropriate because the costs of the particular lines, substations and other equipment do not change with the quantity of energy delivered over them. *Id.* But one of ComEd's own witnesses, testifying on the used and usefulness of certain rate base additions since the last rate case, contradicted this Company theory when he confirmed during cross-examination that customer usage triggers investment and all of the additional costs that go along with that new investment. ComEd witness Michael McMahan testified, for example, that the significant rate base investments that will be added to the Company's rate base in this case, such as the Northwest Reliability Project and others, were triggered as a result of the Company's conclusion that the existing facilities serving this area could no long meet the overall usage and peak demand of the customers served by these facilities. Tr. 498-505. Likewise, he confirmed that ComEd engineers look at the usage of the customers serviced by distribution investments, including, among others, transformers and substations – all used in the delivery of electric service – to determine whether these facilities needed to be expanded or replaced based on forecasted peak load. *Id.* at 505-516. He noted that these distribution facilities are examined each year to ensure that they are capable of serving customer load in the hottest of months. *Id.* at 508. Even when plant additions are made to create redundancy in the distribution system, Mr. McMahan confirmed that the Company examines customer usage to ensure that the facilities will meet usage demand in the affected areas. Tr. 510-516.

Both AG/CUB witness Scott Rubin and Staff witness Christopher Boggs likewise disputed Dr. Hemphill's unsupported theory that usage does not drive ComEd's costs, and that residential rates should be established so that only costs that vary in the short-run with energy consumption (what he terms "throughput-variable costs"; see ComEd response to data request 4.03, attached to Mr. Rubin's testimony as AG/CUB Ex. 6.06) should be recovered through an energy-related rate. Mr. Rubin pointed out that there is no support among reputable public utility economists or among public utility commissions for setting utility rates based on short-run marginal costs. This notion was floated by a few economists during the 1940s and 1950s and quickly was discredited by those who understood the public utility industry. The essential flaw in pricing electricity distribution service based on short-run marginal cost is that the industry exhibits economies of scale (as one would expect from a natural monopoly). This means that the marginal cost declines as more of the product is supplied. AG/CUB Ex. 6.0 at 16-17; AG In. Br. at 114.

While Dr. Hemphill cites Professor Bonbright for support of his proposed rate design, in fact, Bonbright's seminal work, *Principles of Public Utility Rates*, explains that pricing based on short-run cost is inconsistent with the long-run time horizon and function of a public utility and the proper setting of utility rates. Professor Bonbright explained that such a high fixed charge would be unfair to those who did not consume the product or who consumed relatively little of it. That unfairness is not just a social welfare concern, but a fundamental economic concern: requiring a non-user (or low user) of a service to subsidize the service for those who use it does not increase overall economic welfare; rather, it transfers the "consumer surplus" (that is, the benefits of a service in excess of the costs paid for the service) from one group of customers (the low users) to another group (the large users). AG/CUB Ex. 6.0 at 17-18; AG In. Br. at 114-115.

For his part, Staff witness Boggs noted that ComEd's proposed SFV customer charge would require customers who have the lowest level of electricity usage to pay the same customer charge as customers who have the highest level of usage. Mr. Boggs noted that "a more reasonable assumption would be that the customer with the highest level of usage would have a larger demand impact on the grid system than the customer with the lowest level of usage." Staff Ex. 13.0 at 25.

Staff witness Boggs likewise concurred with Mr. Rubin's conclusion that ComEd's proposed rate design is contrary to cost causation principles (the cost causer should pay) embraced by the Commission as a bedrock when analyzing rate design. He stated:

> Consider, for example, a residential customer that has the Company's lowest level of electricity usage versus a residential customer that has the Company's highest level of electricity usage. Under the SFV rate design, both residential customers would pay the same amount for fixed costs that are included in their monthly customer charges. The SFV assumes that the distribution costs they cause ComEd to incur would be comparable. However, a more reasonable assumption would be that the customer with the highest level of usage would have a larger demand impact on the grid system than the customer with the lowest level of usage.
>
> ComEd's proposed customer charge, which would ultimately recover 80% of the costs to serve the residential customer class in the Company's proposed phase-in SFV rate design, would be the same for these two customers, which means that the customer with the lowest usage and the customer with the highest usage would be paying an equal share for the recovery of these fixed costs. This result would be contrary to cost causation principles.

Staff Ex. 13.0 at 25; Staff In. Br. at 126.

ComEd's SFV proposal would also lead to great inequities among low and high use customer bills. AG/CUB witness Rubin was the only witness to carefully study the effects of the proposed SFV rate on ComEd's highest and lowest residential users. Mr. Rubin's analysis showed that ComEd's proposed rates would increase revenues from MF Heat customers by almost $5 million (a 9.6% increase) *even though ComEd's own cost study shows those customers already are paying more than the cost to serve them*. The effect would be that MF heating customers would pay nearly 20% more than the cost to serve them. *Id.* at 23.

Similarly, SF Heat customers, who currently pay rates almost exactly equal to their cost of service, would pay rates that would exceed the cost of serving SF Heat customers by more than 14%. These overpayments by the heating class relative to their cost of service were confirmed by ComEd witness Heintz, who confirmed the numbers relied upon by Mr. Rubin's for purposes of analyzing ComEd's SFV rate design were accurate, were provided by the Company, and were representative of ComEd's costs to serve (including its requested profit level) these particular customers. Tr. at 690-691.

The record evidence proved that ComEd's SFV proposal results in gross inequities in three of the four residential classes that punish low users of electricity while providing rate *decreases* for the highest usage customers. As shown in AG/CUB Ex. 6.10, under ComEd's proposal, the lowest effective annual bill for single-family No Heat customers (that paid by fewer than 5% of customers) would be about $300 per year. Under present rates, the equivalent annual bill is less than $200. *ComEd's proposal thus 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 31. 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.

AG/CUB Ex. 6.11 shows that, similar to the SF No Heat subclass, ComEd's proposal would impose very large increases on its SF Heating customers with the lowest usage (lowest annual bills). 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 34; AG In. Br. at 126. 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.*

With regard to the Multi-family No Heat residential class, Mr. Rubin also found that approximately 40% of the revenue increase would be received from the 25% of customers with the lowest current bills. *Id.* at 36-37. ComEd's proposal would result in approximately a 30% rate increase for those who use the least amount of electricity (and, therefore, are least likely to cause ComEd to incur significant demand-related costs). At the other end of the curve, the six percent of customers with the highest bills currently (and, therefore, the greatest energy usage) actually would receive rate decreases under ComEd's proposal. AG/CUB Ex. 6.12; AG/CUB Ex. 6.0 at 36-37.

These inequities fly in the face of rate design principles that strive to promote equity and fairness. The SFV proposal also sends the wrong price signals to customers when the General Assembly has declared that electric delivery utilities are charged with reducing load by investing in energy efficiency and demand response programs, because "investment in cost-effective energy efficiency and demand response measures will reduce direct and indirect costs to consumers by decreasing environmental impacts and by avoiding or delaying the need for new generation, transmission, and distribution infrastructure." *See* 220 ILCS 5/8-103. Contrary to this legislative declaration and directive, ComEd's proposed SFV rate design discourages customers' attempts to reduce usage, and suggests that demand for electricity is irrelevant to the costs of the provision of electricity.

The Commission Staff shared the principal conclusions of Mr. Rubin's review of the Company's SFV proposal: Staff In.Br. at 122-125. Staff witness Boggs highlighted numerous deficiencies in the proposal, including his view that the SFV rate design would send the wrong price signal to ComEd's residential customers. Staff Ex. 13.0 at

22. He noted that as electricity demands increase, the environmental costs of electricity generation increase. Because of this relationship, it's reasonable to associate environmental costs with usage charges, which supports an argument for higher, rather than lower usage charges. If the proposed SFV rate design is approved, the Distribution Facilities Charge, or usage charge, would decrease from its current level and lower price signals would be sent to ratepayers concerning the impact of their usage on the environment. *Id.*

In the face of this evidence, ComEd ultimately resorts in its Brief to relying on a "if they get it, we want it" argument of sorts that points out that recent Commission orders in natural gas delivery rate cases adopted SFV rate designs that recovered about 80% of the company's fixed costs. ComEd In. Br. at 138. This argument is hardly persuasive, however. As noted in Staff's Brief, there are significant environmental costs associated with electricity usage that support adoption of a rate design that retains a significant role for usage charges. Moreover, unlike the evidence produced in the referenced gas cases, ComEd's usage per customer, which declined in 2009, is expected to increase in future years. ComEd Ex. 4.0 at 7 (Tripek Revised Direct).

Moreover, adoption of ComEd's SFV proposal would run counter to electric distribution rate-setting through out the U.S. Staff witness Boggs pointed out that his review of utility rate structures throughout the country revealed that not a single state has approved SFV pricing for electricity rates. Staff Ex. 13.0 at 27. Only one state, Delaware, was even considering the rate structure. *Id.*

For all of these reasons, ComEd's flawed and inequitable SFV proposal for the residential class should be rejected. Instead, the Commission should adopt Mr. Rubin's fair, equitable rate design that both ensures (1) the recovery of ComEd's cost of service; (2) equitable rate treatment for the Company's heating and non-heating residential customers of all usage levels; and (3) the elimination of cross-subsidies between the heating and non-heating classes. In addition, the AG/CUB rate design produces rates that retain a price signal that incentivizes conservation and ensures that cost causers pay – all goals that have been embraced by the Commission in prior rate orders.

As noted in the AG Initial Brief, Mr. Rubin's testimony provides the Commission with specific instructions as to how to implement this rate design regardless of the revenue requirement number that is calculated in the order. AG/CUB Ex. 6.0 at 46-50

City of Chicago

The centerpiece of ComEd's residential rate design in this case is its recommendation that the Commission approve its proposed straight fixed variable (SFV) rate design. Dr. Hemphill referred to the SFV rate design as "The single most important step in bringing ComEd's rate design into line with its cost is to properly align the fixed and variable prices in ComEd's delivery rates with the fixed and variable costs of customers' use of ComEd's delivery system. This is accomplished by moving towards a straight fixed-variable ("SFV") rate design." ComEd Ex. 14.0 (2nd Rev.) at 8-9, LL 179-82. Remarkably, ComEd devotes just a little more than two pages to this "most important step." Maybe the utility is conceding that there is little chance the Commission will approve its proposal given the universal and contentious opposition to

the SFV rate design. Maybe the utility is "sandbagging", waiting until its Reply Brief to more fully defend its proposal.

ComEd offers only one detailed response to the myriad complaints leveled against its SFV proposal. In particular, the utility discusses the colloquy between Staff witness Christopher L. Boggs and Dr. Hemphill regarding whether recent Commission orders in natural gas utility rate cases approving large increases in the customer charges for residential customers are relevant to ComEd's SFV proposal. ComEd Init. Brief at 138. That constitutes the full extent of ComEd's detailed response. As to the many other criticisms of its SFV proposal, ComEd waves them off with the cursory comment that "Dr. Hemphill also presented extensive testimony refuting various concerns about the proposed SFV rate design raised by City of Chicago witness Bodmer, NRDC witnesses McDermott and Cavanagh, and AG-CUB witness Rubin." *Id*.

Whatever the reason for the brevity of ComEd's discussion of its SFV proposal, the record evidence is overwhelmingly against it. As noted above, there was unanimous opposition to the proposal. No party other than ComEd came out in favor of the SFV rate design. Because ComEd made only a cursory defense of its recommended rate design, the City will not go into detail about the many problems with the SFV rate design here. Instead, below is a summary of the major arguments made by the various parties in their respective Initial Briefs filed in this case.

► The SFV proposal would discourage investment in energy efficiency measures. City Init. Brief at 31-32; Staff Init Brief at 123-24; AG Init. Brief at 106; ELPC Init. Brief at 11, 14-18; NRDC Init. Brief at 4-5.

► Because the SFV proposal would discourage investment in energy efficiency measures, it is inconsistent with the General Assembly's mandates requiring that utilities promote b energy efficiency. City Init. Brief at 31-32; Staff Init. Brief at 125; ELPC Init. Brief at 14-20; NRDC Init. Brief at 4-5.

► The SFV proposal is designed to protect utility revenues. City Init. Brief at 26-27; AG Init. Brief at 105.

► The impact of the SFV proposal will fall most heavily on low-use customers. City Init. Brief at 27-29; AG Init. Brief at 105, 114-15, 116, 117-20; ELPC Init. Brief at 11-12.

► The SFV proposal is not based on cost of service. Staff Init. Brief at 126; AG Init. Brief at 105; ELPC Init. Brief at 12; NRDC Init. Brief at 4.

These are only some of the problems Staff and the parties identified with ComEd's SFV proposal. There is little record support for ComEd's proposed residential rate design. It should be rejected.

CUB

CUB argues against ComEd's proposals to increase the fixed-cost portion of its recovery and to eliminate the distinctions based upon space heating, because they violates basic rate making principles of cost causation, efficiency, social welfare, fairness and equity. CUB maintains that ComEd's proposal 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. CUB states that 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.

AG/CUB witness Mr. Rubin 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 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. CUB maintains that most importantly, 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 witness Dr. 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. CUB disagrees and states that ComEd's proposal only represents one aspect of the goals of rate design while 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. Mr. Rubin found that the cost-of-service study ComEd 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. CUB avers that 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. Furthermore, CUB explains, 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.

Mr. Rubin testifies that utilities make long-lived investments based on long-term projections of customer location, demand, and consumption. AG/CUB Ex. 11.0 at 3. He acknowledges that energy consumption 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.* Therefore, Mr. Rubin

finds that utility pricing must send customers an appropriate price signal that increases in their energy demand result in increases in costs to the system. *Id.* CUB maintains that ComEd's pricing proposal fails to do so.

Mr. Rubin's analysis showed that 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. CUB contends that 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.*

CUB explains that 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. Mr. Rubin testifies, "an equitable rate design will recover revenues in rough approximation to the cost of service." AG/CUB Ex. 6.0 at 22. CUB believes that the fairness of a proposed rate design within a rate class is most effectively evaluated through examination of a customer impact analysis, just as 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. According to CUB, the People and Mr. Rubin, 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. CUB notes that the data directly undercuts ComEd's rationale for placing most demand-related costs in the customer charge. Mr. Rubin explains that ComEd's proposal requires low-use customers to subsidize high-use customers within the same residential subclass because ComEd's rate design erroneously assumes that each customer within the residential class is responsible for the same level of demand. AG/CUB Ex. 6.0 at 31. 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.*

Mr. Rubin's analysis demonstrates that 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, Mr. Rubin explains that 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.* CUB maintains that 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.

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 reduced. CUB avers that 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. CUB argues that 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.

ELPC

The overwhelming weight of the evidence in this case contradicts ComEd's arguments for its proposed SFV rate design. ComEd's Initial Brief and ComEd witness Hemphill's testimony focus on the principle of cost causation. According to ComEd, "the evidence demonstrates that a SFV rate design is appropriate for ComEd because it more closely aligns fixed and variable prices to effectuate cost recovery with the correct division between fixed and variable costs." ComEd Brief at 138. No other party agrees with this. The problem, as explained succinctly in CUB's Initial Brief, is that ComEd focuses solely on "high-level cost causation principles," but ignores the real world impacts of its proposal. *See* CUB Brief at 71. As explained in the AG's brief:

> The evidence shows that ComEd's proposed rate design fails to meet any reasonable criteria for promoting efficiency or overall social welfare. Instead, it simply transfers social welfare from one group of residential customers to another, imposing extremely high rate increases on the lowest-use customers, while decreasing rates for ComEd's largest residential energy users.

AG Brief at 106 (discussing testimony of AG/CUB witness Rubin). Tellingly, ComEd's brief devotes only one sentence to the work done by witnesses Bodmer and Rubin to calculate and document the on-the-ground impact of ComEd's proposal. Both Bodmer's and Rubin's testimonies indicate that the proposal is inequitable and conflicts with the Company's own cost of service study. City Ex. 1.0 at 11-13; AG Brief at 117-130; *see also* Staff Ex. 13.0 at 24-25; NRDC Ex. 2.0 at 10-12. Furthermore, as explained in CUB's brief, ComEd focuses on only "one aspect of the goals of rate design" and "ignores other cost-causation realities … as well as principles of gradualism, fairness, and equity in its analysis." CUB Brief at 73.

ComEd also argues that the Commission's recent orders in gas cases support a move towards SFV rates here. ComEd Brief at 138. However, as explained in ELPC's initial brief, the different characteristics of natural gas and electricity justify different rate treatments. *See* ELPC Brief at 20-21 (citing the National Action Plan for Energy Efficiency). As explained in Staff's brief, there is "no precedent in the electricity industry for ComEd's SFV rate design proposal." Staff Brief at 126. Furthermore, the facts in the gas cases were very different than the facts here. *Id.* In the gas cases, for example, the

Commission *decreased* the utilities' authorized return on equity to compensate for their reduced risk under SFV rates. *See* Docket 07-0585 (Ameren), Order (Sept. 24, 2008) at 215; Docket 08-0363 (Nicor), Order (March 25, 2009) at 71. In this case, ComEd prefers to abandon its SFV proposal if the Commission determines that a similar ROE reduction would be warranted. ComEd Brief at 139.

ComEd's brief also fails to meaningfully address the extensive evidence that SFV rates will discourage ratepayers from conserving energy and undermine Illinois' energy efficiency and renewable energy policy goals. *See* ELPC Brief at 14-20 (citing Staff Ex. 13.0 at 18, 24; Staff Ex. 29.0C at 11-12; City Ex. 1.0 at 35; AG/CUB Ex. 6.0 at 41; NRDC Ex. 2.0 at 9-11); *see also* Staff Brief at 123-125; AG Brief at 106; City Brief at 31; NRDC Brief at 4-5. ComEd implies (without support) that customers will continue to experience adequate price signals to conserve because SFV will only apply to the distribution component (approximately 1/3) of a customer's overall bill. *See* ComEd Ex. 71 at 4-5. However, ELPC's brief uses ComEd's own numbers to demonstrate that SFV rates would have a significant impact on the economics of energy efficiency and renewable energy projects in Illinois and would make the Illinois EEPS and RPS more difficult and expensive to achieve. ELPC Brief at 14-20.

In sum, ComEd is interested in SFV rates in order to insulate Company investors from the potential loss of revenue due to variations in energy consumption – an issue best addressed by adjusting ComEd's test year. *See* CUB Brief at 71; AG Brief at 105; City Brief at 26. The Commission should not allow ComEd to do this on the backs of its lowest usage customers and at the expense of Illinois' important energy conservation policies.

Staff

ComEd presents a number of arguments to support its Straight Fixed Variable ("SFV") rate design. First, it contends that an SFV rate design is appropriate because it more aligns respective fixed and variable cost recovery with fixed and variable cost causation. (ComEd IB, p. 137) Second, ComEd contends that the current rate design penalizes utilities for implementing conservation programs. (*Id.)* Lastly, ComEd argues that the Commission has approved similar rate design methodology for other utilities. (*Id.,* p. 138*)*

ComEd's argument about aligning fixed charges with fixed costs is flawed in two respects. First, it does not consider that many of these fixed costs are driven by variable demands which more closely correspond with variable usage charges than fixed customer charges. (Staff IB, pp. 123-124) Second, ComEd's proposal does not specifically focus on the recovery of fixed costs alone. Rather, ComEd proposes to ultimately recover 80% of all costs, fixed and variable, through the customer charge. (*Id.*, pp. 126-127*)*

The second argument that ComEd presents fails to consider that the SFV would undermine conservation by encouraging ratepayers to use more electricity. Section 5/8-103 (b) of the PUA promotes conservation by requiring Illinois utilities to reduce overall

electric usage by 0.2% in 2008 escalating to 2.0% by 2015. The SFV rate design would undermine this effort by lowering usage charges and thereby reducing customers' incentive to conserve electricity. (Staff IB, p. 123)

ComEd's argument that that the Commission has approved similar rate design methodology for other utilities is problematic because there is no precedent in the electricity industry in Illinois or the nation as a whole for ComEd's SFV rate design proposal. (*Id.*, p. 126)

Staff is not alone in opposing the Company's SFV rate design proposal. NRDC, the AG, and the City of Chicago also contend that it should be rejected by the Commission. (NRDC IB, pp. 3-6; AG IB, p. 106; City of Chicago IB, p. 5) The weight of the evidence clearly fails to justify the adoption of the SFV in this case.

Commission Analysis and Conclusion:

ComEd is proposing movement towards a SFV rate design. ComEd's proposal applies only to residential customers and nonresidential customers in the Watt-Hour Delivery Class and establishes fixed and variable charges that track the fixed and variable costs of serving those customers. ComEd proposes that gradually, over a three-year period, the use of volumetric charges be reduced for the recovery of 40%, then 30%, and finally 20% of its overall delivery service costs.

The Commission is not convinced that an SFV rate design reduces the incentive to conserve electricity. First, the Commission notes that the rate design in this proceeding relates to delivery services associated with electric power and energy. The actual commodity costs associated with the electric power and energy, which is the majority of the total electric bill in addition to the delivery costs and vary directly with usage. The customers under ComEd's proposal would have an incentive to conserve because they can avoid commodity costs associated through conservation. In addition, these costs at issue here are in fact fixed costs, cannot be conserved and result in an under-recovery of fixed costs for the utility. Just as with the natural gas utilities, we conclude there is no disincentive a consumer may have by a move toward recovering fixed costs through fixed charges, as opposed to recovery on a volumetric basis. We further conclude that a SFV design that more accurately reflects a consumer's actual costs does not impede conservation. Commission decisions to either decouple or move toward an SFV in rate cases filed by North Shore/Peoples Gas, the Ameren Illinois Companies ("Ameren"), and Nicor Gas Company ("Nicor Gas"). All of which recognize the importance of recovering fixed costs predominantly through fixed charges. The Commission concludes that it is when customers respond to rates that do not accurately reflect cost causation, that inefficiency results and society suffers. Because electric and natural gas distribution utilities must have the capacity in place to serve peak loads whenever they occur, it is logical to apply pricing policies for both types of industries because they have similar underlying cost structures.

The Commission finds that a SFV proposal does not shift risk to residential customers. Further, the record does not demonstrate that low-income customers are necessarily low-usage customers, or vice versa. Further, there are other means in place that more precisely target the policy issue that the AG and City seeks to address here. Finally, we do not find that a SFV proposal is attempting to recover short term

marginal costs. Instead, the SFV proposal is intended to recover additional fixed delivery costs through higher fixed delivery charges.

The Commission has recognized the importance of recovering fixed costs predominantly through fixed charges The Commission finds that the one of the most important step in bringing ComEd's rate design in line with its costs is to properly align the fixed and variable portions of ComEd's delivery rates with the fixed and variable costs ComEd incurs to provide delivery service. We also believe that it is important to design rates that reflect cost causation. It is undisputed that ComEd recovers 37% of its fixed charges. In an effort to gradually move towards more realistic cost causation and to avoid rate shock, the Commission concludes that the use of volumetric charges be reduced so that they recover 50% of fixed delivery service costs. This conclusion applies only to residential customers and nonresidential customers in the Watt-Hour Delivery Class. The Commission will not determine whether changes need to be addressed in future year's rates; this is an issue to be addressed in future rate cases.

b. Decoupling (NRDC Proposal)

NRDC

In its initial brief, NRDC showed the State of Illinois should remove the link between ComEd's financial health and the amount of electricity consumed by its customers. "Decoupling" ComEd's recovery of its revenue requirement from its customers' electric consumption will remove the current disincentive that utilities have from investing in energy efficiency and becoming involved in activities that could lead to greater energy efficiency. NRDC also showed that its proposal was in this respect, far superior to ComEd's proposed Rider SFV, which would raise fixed charges so high that customers would be discouraged from investing in energy efficiency.

NRDC notes that ComEd does not provide any argument against NRDC's decoupling proposal. On the contrary, the Company merely stated that it believes that its proposed Rider SFV "is a superior solution" but that if the Commission approved NRDC's decoupling proposal, it could do so with the tariff ComEd had introduced into evidence during the proceeding. (ComEd Brief at 139). NRDC indicated that there should be a cap on any refunds or surcharges and over- or under-collection should be refunded on a kWh basis, ComEd's proposed tariff is an acceptable codification of its proposal. (NRDC Initial Brief at 7-8).

VIII. THE COMMISSION SHOULD NOT DEFER A DECISION ON DECOUPLING

The Commission Staff argued that the Commission should not consider decoupling in this proceeding because it has just started an experiment in decoupling with Peoples Gas Company and North Shore Gas Company. The Staff argues that the Commission should not consider another decoupling proposal until after the four year period of that experiment is completed and the Commission conducts a "complete assessment/evaluation" of that program. (Staff Brief at 128). NRDC already addressed this issue in its initial brief (NRDC Initial Brief at 16-17). Briefly, due to the numerous differences between gas and electric utilities, little will be gained by waiting until the completion of the assessment and evaluation of the Peoples' experiment contemplated

by the Staff; the Commission will merely be giving up the opportunity to gain experience with decoupling in the electric industry.

Along the same lines, ELPC argues that the experience to date under the People's Gas decoupling pilot "raises questions that we should answer before allowing ComEd to decouple." (ELPC Brief at 27). In reality, the experience to date under the People's pilot shows very clearly, two things. First, the large refunds to customers made under the People's decoupling pilot show very clearly that if sales are higher that projections due to weather factors, decoupling will protect consumers from paying more than the utility's authorized revenue requirement, while current ratemaking policy would allow the utility to simply keep those earnings. Second, it shows that decoupling is one factor among many that affect utility energy efficiency spending. People's Gas new three year energy efficiency plan was filed in response to a state law that set minimum savings goals for the first years at levels lower than were already being achieved by People's. This factor, along with uncertainty about whether the decoupling pilot would be made permanent, could very well have resulted in a decision to reduce energy efficiency program budgets.

A. Decoupling Is Not Improper Single Issue Ratemaking.

CUB, ELPC and the Attorney General all argue that the NRDC decoupling proposal violates the prohibition against single issue ratemaking and/or is an improper rider in violation of the Illinois Appellate Court decision in *Commonwealth Edison Co. v ICC*. None of their arguments are valid. As NRDC explains, its decoupling proposal does not violate the prohibition against single issue ratemaking because it does not change any portion of a utility's revenue requirement in isolation. Instead, it merely measures actual utility collection of fixed costs against the fixed cost revenue requirement *authorized by the* Commission, adjusted for the number of customers, eliminating the incentive for a utility to increase its sales between rate cases in the affected rate classes. This difference is key, because, as articulated by the Appellate Court in *Commonwealth Edison Co*., "The rule against single issue ratemaking makes it improper to consider in isolation *changes in a particular portion of a utility's revenue requirement*." *Id*. 937 N.E.2d at 707; 344 Ill. Dec. 684, (emphasis added). Under NRDC's proposal, all components of ComEd's revenue requirement are being considered in this docket and then the Commission would establish a revenue per customer figure against which refunds or charges would be made. ComEd is at risk for any of the components of its revenue requirement changing – expenses and construction costs, cost of capital, changes in number of customers under decoupling and changes in sales to customers not under decoupling – every one of these components of ComEd's revenue requirement are outside of the decoupling proposal. Thus, regardless of how any of these items change, refunds or charges would remain the same. ComEd thus has incentive to act efficiently in every respect. The only incentive it would no longer have is to encourage customers in the affected rate classes to use more electricity.

Nor is the decoupling proposal a violation of the *Commonwealth Edison Co*., decision in respect to the Court's analysis of allowable riders. The Appellate Court determined in that case that there should be a two part test for riders: "(1) the cost is imposed upon the utility by an external circumstance over which the utility has no

control and (2) the cost does not affect the utility's revenue requirement." *Id.* 937 N.E.2d at 710; 344 Ill. Dec. 687. Here, NRDC is not proposing a rider to recover an isolated cost. Rather, it is proposing a rider that addresses over or under collection of Commission-authorized revenues per customer based on changes in sales compared to those projected in the rate case. As noted above, changes in ComEd's costs will not impact the decoupling calculation, thus they are not just out of ComEd's control – they are completely irrelevant. Nor does the proposal affect ComEd's revenue requirement. On the contrary, it takes away an incentive for ComEd to maintain sales volumes so as to over-collect its revenue requirement to the detriment of society by increasing its customer's electric usage.

B. Decoupling Does Not Shift Risk to Ratepayers.

The Attorney General, CUB and AARP argue that the decoupling proposal shifts risk from ComEd to ratepayers. (AG Brief at 139; CUB Brief at 78; AARP Brief at 11). For example, according to the Attorney General,

> All business risks arising from changes in sales volumes are shifted from the utility to its customers under decoupling through the automatic rate adjustment mechanism that ensures the utility will fully recover its revenue requirement.
>
> (AG Brief at139).

On the contrary ComEd is still subject to every risk of operations but one – the average use per customer. Even this one exception is just as likely to benefit ratepayers as it is to benefit ComEd. For example, if ComEd territory experiences hot weather that result in customers using more electricity than in the test year, then they would receive a refund. Thus, it is completely inaccurate to claim that the proposal shifts risk to ratepayers. At most, it takes one risk – the risk of use per customer – and moderates it by allowing neither ComEd nor customers to receive benefit or harm from changes. Whether those changes are a reduction in use per customer caused by ComEd taking an active role in promoting energy efficiency or increases caused by hot weather, there is no risk being shifted. Nor is ComEd ensured of fully recovering its costs of providing reliable service: cost drivers other than sales in the affected rate classes will continue to change between rate cases. ComEd will be exposed to the same expense, revenue, construction cost and capital cost risks as every other utility.

Taking a slightly different approach, AARP argues that the decoupling proposal "would allow electric rates to be raised higher for all residential customers, on a piecemeal per customer basis." (AARP Brief at 10). The Attorney General looks at the flip side of this coin and argues that ComEd does not need the revenues it would receive from decoupling:

> NRDC has failed to provide any analysis to support the premise that ComEd has any financial need for the revenue that would be impacted by decoupling. . . Mr. Cavanagh's testimony provides no evidence that ComEd has failed to recover its fixed costs under traditional, test-year regulation since initiating its statutory energy efficiency programs or that his concern for ComEd shareholders is even justified.

(AG Brief at 139-140).

The AARP and Attorney General's statements represent a fundamental misunderstanding of the proposal because it is designed to be neutral, with refunds being as likely as surcharges. In fact, if the decoupling proposal had been in effect for the past two decades, customers would have received refunds rather than paid surcharges. More specifically, the average use per customer essentially doubled during that period, which would have resulted in huge refunds under the decoupling proposal. (NRDC Ex. 2.0, p. 20). In fact, the only decrease that the Attorney General could point to was for the period since 2005, which of course, coincides with the recent recession.

With the eventual economic recovery, there is no reason to believe that sales per customer will shrink absent aggressive energy efficiency measures. During the hearings in this proceeding, counsel for the People of the State of Illinois attempted to impeach Mr. Cavanagh with statements from a recent report from the Washington State Utilities and Transportation Commission issued on November 4th, 2010. One of those statements read into the record to impeach Mr. Cavanagh was as follows:

> While customer use of natural gas has been declining in recent years, this does not appear to be the case for electric utilities. Our experience and understanding informs us that electric – electricity use per customer has been either steady or even increasing. . .
>
> We attribute this trend generally to the addition of so-called plug load associated with increased consumer use of appliances and electronic devices. Such increased usage could become more pronounced in the future, should consumers shift away from automobiles powered by petroleum and toward electric vehicles.
>
> Tr. 1469-70.

Rather than impeach the testimony of Mr. Cavanagh, this statement supports his position that customers may very well benefit from decoupling by receiving refunds for increases in energy consumption caused by the items mentioned by the Washington State Utilities and Transportation Commission.

Moreover, to the extent that surcharges are caused by ComEd successfully implementing energy efficiency measures for its customers, then customers' bills will fall, even if there are positive rider charges. As explained by Mr. Cavanagh, the savings from reduced consumption would far outweigh any increased charges, thus resulting in lower electric bills.

> Bills will go down. There will be a modest increase in rates, assuming a sustained reduction in per-customer electricity use. I think the most important point to make is that bills will be going down.
>
> Tr. 1447.

C. Decoupling Does Not Allow ComEd to Retain All Revenues From New Customers.

One misunderstanding that is held by some of the parties in this proceeding is that NRDC's decoupling proposal allows ComEd to retain all revenues from new customers. Thus, it would benefit from any growth that is likely as the country recovers from its recent downturn in the economy. The Attorney General's Brief provides an example of this misconception:

> To the extent economic recovery results in adding new residential customers, the NRDC decoupling approach would simultaneously protect ComEd against declining usage "per-customer" while allowing ComEd to retain for its shareholders all new revenues associated with serving new customers.
>
> (AG at 140).

Mr. Cavanagh addressed the misunderstanding of the treatment of new customers during his cross examination.

> Q . isn't it correct that under your proposed form of revenue decoupling, those revenues gained from the new customers would be retained by the Company?
>
> A I think this is a misunderstanding and that's turned up in several of the rebuttals. Our proposal is simply that not all of the revenues would be retained. There would be a revenue requirement per customer that the Company would adopt -- or that the Commission would adopt; and, yes, the Company would keep those revenues, but not all of the revenues from the new customers, only the revenue-per-customer limit adopted by the Commission.
>
> Tr. 1426-27.

The best way to understand the impact of ComEd experiencing a growth in customers due to a better economy is to examine the calculation underlying the refund/surcharge. Explaining that calculation, Mr. Cavanagh stated:

> What you do is you count the customers every year. You count the electricity sales. So you know whether total fixed cost recovery was above or below the authorized level and you true-up. New customers are treated exactly like existing customers for this purpose.
>
> Tr. 1428-29.

In summary, if ComEd sees an increase in customer base subsequent to the issuance of the Commission's order in this proceeding, it will not retain every penny it earns from those customers. Instead, those customers and their electric use would become part of the calculation to determine refunds or surcharges.

D. Decoupling Will Not Affect Regulatory Lag.

AARP argues that adoption of decoupling would decrease the beneficial impact of regulatory lag: "However, NRDC's *per customer* decoupling proposal would actually reduce regulatory lag, and thus weaken the incentive for cost efficiency." (AARP Brief at 11). Again, this argument represents a misunderstanding of the proposal. NRDC's decoupling proposal only affects ComEd's revenues: strong financial performance (profits) will continue to be driven by ComEd's revenues and its ability to control its costs. If ComEd forecasts sales declines, indeed the only hope for superior financial performance in the affected rate classes is cost control, as the Company under NRDC's proposal no longer has the option of profiting from over-recovery of its costs when sales are above rate case expectations.. The only item decoupling would address is electric use per customer. ComEd is at risk for changes in every other component of its revenues and expenses and thus has an incentive to be as efficient as possible – efficiency that would flow through to ratepayers in the form of delay in new rate case filings.

E. Decoupling Does Not Necessitate a Reduction in ComEd's Allowed Rate of Return.

The Attorney General argues that the decoupling proposal is deficient because it does not contemplate a reduction in ComEd's allowed rate of return. (AG Brief at 145). The underlying assumption of this argument is that the proposal will reduce ComEd's risk of earning its allowed return. Thus, the Attorney General argues: "The Commission should absolutely reject the notion that guaranteeing a utility's last asserted revenue requirement is as an appropriate focus of regulation." (AG Brief at 137). Along the same lines, the Attorney General argues: "Revenue decoupling is a regulatory mechanism that ensures that the utility collects its Commission-authorized revenue requirement." (AG Brief at 139).

These statements are simply not true. The only impact of the decoupling proposal will be to moderate one element of ComEd's revenue requirement – it's per customer electric use. Every expense it incurs, every change in the markets affecting cost of capital, every change in construction costs and very simply EVERY other item impacting expenses and revenues, will affect ComEd's ability to earn its allowed return. Nothing is guaranteed and nothing ensures that ComEd earns its allowed return.

NRDC recognizes that at some time in the future when there is more experience with decoupling, ComEd's allowed return may be positively impacted by decoupling because it will moderate the impact of changes in sales per customer. In fact, in its next rate case, a standard analysis of allowed return on equity will capture its impact to the extent investors have reacted positively to decoupling in ComEd territory and/or for comparable companies used in a return on equity analysis. But given the lack of data at this time, NRDC cannot recommend a specific adjustment to ComEd's allowed return.

F. Decoupling Will Have a Positive Impact on Energy Efficiency in the ComEd Service Territory.

ELPC argues that decoupling cannot result in more efficiency in ComEd's service territory because the company is already doing everything it can do under current law to

maximize the potential for cost-effective energy savings. (ELPC Brief at 24-26). However, there is ample evidence before this Commission to conclude that there is much more ComEd could do to promote energy efficiency than is required of it under the current statutory framework in 220 ILCS 8-103.

As NRDC Witness Ralph Cavanagh testified, there exists an enormous gap between what is being achieved under these programs and what is cost-effectively possible. By 2016, ComEd could save more than 13,000 GWh of electricity at a cost of about four cents per kWh, while current programs are designed to achieve a fraction of this potential. (NRDC Ex. 2.0, p. 4). To be sure, under the current statute ComEd cannot simply increase the budgets of its current programs to capture all cost-effective potential to the benefit of its customers, but there are other ways to achieve some or all of this potential for savings. For example, ELPC and NRDC have supported allowing the Illinois Power Agency to procure energy savings instead of just supply side resources as part of its annual procurement event. Not surprisingly, ComEd has opposed this measure as it would add, potentially very significantly, to the revenue erosion it already faces. When one combines that potential savings with the savings that could result from advocacy at the state and federal level for better building codes and appliance standards or higher savings targets, assistance in implementing building codes or low-income assistance program, and alternative financing mechanisms such as on-bill financing, it becomes evident that a properly motivated utility in ComEd's position could take actions that would substantially increase the proportion of that cost effective savings potential being captured to the benefit of its customers.

ELPC further argues that by "adjusting its test year" to incorporated projected sales decline resulting from energy efficiency programs would eliminate the need for decoupling. This argument entirely misses the point of decoupling. It should go without saying that in a rate case the sales projections should incorporate existing knowledge about declining sales from all causes, including energy efficiency programs, and the rates should be set to recover the revenue requirement accordingly. Knowingly using unrealistic sales projections to set rates and then using a decoupling mechanism to recover or refund the gap between the revenue requirement and the recovered revenue is a grave misuse of a decoupling true up. However, no matter how accurate those projections are, the utility will benefit from higher sales than projected between rate cases and customers will benefit from lower sales than projected between rate cases. It matters very little how frequently rate cases occur, what test year is used, or how accurate the sales projections are, without decoupling the utility will have an incentive to resist doing anything that might cause sales to be lower than projected. Decoupling makes a difference between rate cases, not during rate cases when the test year adjustment is relevant.

For the reasons provided NRDC's proposes that the Commission should reject ComEd's proposed Rider SFV and instead approve Rider DA: Decoupling Adjustment (ComEd Ex. 46.2) with the modification of adding a 3% cap on refunds or charges, with any unrecovered balances carried forward and refunds or charges based on a per kWh basis.

AARP

AARP is also opposed to the Natural Resources Defense Council's ("NRDC's") alternative rate design, which is an unreasonable version of "decoupling" presented by NRDC witnesses McDermott and Cavanaugh. NRDC Ex. 1.0 and 2.0. Professor McDermott acknowledges that there is a risk of variations in electric sales and usage that must be borne by the shareholders, the ratepayers, or both and that such risk cannot simply be made to disappear; however, he would not necessarily acknowledge that NRDC's decoupling proposal would shift that business risk to consumers. Tr. 1394-1396. AARP strongly disagrees, because although this proposed decoupling mechanism would not change the overall revenue requirement, it would allow electric rates to be raised higher for all residential customers, on a piecemeal per customer basis, as explained by the testimony of AG/CUB witnesses.

AG/CUB witness Brosch opposes NRDC's decoupling proposal, which he states 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.NRDC's plan ignores the fact that utility expenses, rate base, and cost of capital are dynamic and that decoupling does indeed shift business risks associated with changes in sales volumes from the utility to its 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. Id.

AG/CUB witness 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. 14.0, pp. 14-27. He points out that decoupling should be rejected because: (1) it is inconsistent with sound regulatory policies that have been developed over many decades; and (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. AARP further notes that although NRDC's proposed per customer decoupling would attempt to decouple sales from the establishment of fair rates; it would fail to actually link rates to any existing or future energy efficiency goals.

While NRDC and ComEd argue that decoupling "removes a disincentive" related to the utility's desire to promote energy efficiency, the specific proposal under consideration does nothing to *create any additional incentive* towards conservation or energy efficiency. Under NRDC's decoupling proposal, even those customers that aggressively conserve on electric usage would experience higher rates that traditional ratemaking would allow, robbing those customers of the full benefit of their

conservation. Prof. McDermott admits that while such customers might experience a lower overall electric bill, it is possible that the energy savings experienced by those customers would be lessened by this proposal. Tr. 1405. The NRDC proposal would allow residential rates to be increased on a piecemeal basis across the board to all residential customers, including low-income customers; however, the so-called "removal of disincentive" to the utility would do nothing to provide assistance to low-income customers in financing energy efficiency investments. Tr. 1406.

There is another incentive that would be changed by the adoption of NRDC's decoupling proposal. By increasing the level of revenue that is likely to be collected by ComEd, decoupling would reduce regulatory lag on a single-issue basis. Prof. McDermott recognizes that a "properly designed regulatory program" can use regulatory lag to promote the cost effective operations of a utility. Tr. 1400. However, NRDC's *per customer* decoupling proposal would actually reduce regulatory lag, and thus weaken the incentive for cost efficiency. Prof. McDermott further admits that the NRDC proposal contains no component with an enforceable commitment to promote energy efficiency. Tr. 1403.

AG

The NRDC, in response to ComEd's SFV proposal, presented a decoupling proposal, consistent with its national agenda of promoting revenue decoupling in states throughout the country. In its Brief, NRDC argues that its decoupling proposal is similar to ComEd's SFV proposed rate design because "(i)f sales lag below the assumptions underlying the rates approved by the Commission in its last rate case, then the company will not recover its approved revenue requirement for the fixed costs of distribution service." NRDC In. Br. at 3.

This observation betrays a principal flaw in the per customer revenue decoupling proposal promoted by the NRDC – its failure to recognize that revenues and cost recovery are not merely a function of per customer consumption. Decoupling, as noted in the AG Initial Brief, violates the rule against single-issue ratemaking because it fails to properly account for (1) the revenues the company gains when new customers are added; (2) changes in usage and sales to customer classes not decoupled; (3) changes in operating expenses, such as labor force reductions and operating efficiencies gained through new technology; (4) changes in the rate base; and (4) changes in the cost of capital – all elements that affect a utility's revenue requirement.. *See* AG In. Br. at 142-144.

NRDC recognizes the potential for per customer revenue decoupling to provide a windfall to the Company in its argument that a 3% cap on revenues collected through the rider is needed to protect customers from paying excessive rates. NRDC In. Br. at 7-8. ComEd, however, is unwilling to include such a safeguard. ComEd Ex. 46.2.

NRDC argues that its decoupling proposal will remove ComEd's incentive to maintain its electric sales level, and would encourage ComEd to devise innovative ways to meet or exceed its statutory targets. NRDC In. Br. at 6. But this central tenet of the NRDC proposal is thwarted by ComEd's assertion in the record that it would not commit

to increasing its energy efficiency effort beyond that required by Section 8-103 of the Act, even with a decoupling rider in place. Tr. at 464. Conspicuously absent from the NRDC Brief is any recognition of this fact.

NRDC argues, in response to AG/CUB witness Rubin's rebuttal testimony, that their decoupling proposal is not intended to incent customers to embrace energy efficiency, but rather to incent the utility. NRDC In. Br. at 18. But this declaration fails to address the disincentives that may be created when customers realize their delivery service rates are being adjusted upward when residential per customer revenues decline.

NRDC witness Ralph Cavanagh dismisses concern over the possibility of inordinate price increases under decoupling. Yet, his recommendation that a 3% cap be included in a decoupling mechanism speaks volumes about the threat of additional surcharges to customers. In addition, cross-examination revealed that significant rate increases have followed in jurisdictions that adopted decoupling. Tr. at 1454-1463. While Mr. Cavanagh characterizes some of these increases as de minimis, he does so in the context of a utility's total revenues. No analysis is provided as to whether these increases are, in fact, significant to the residential and small business customers that would be paying the surcharges.

NRDC further argues that its decoupling proposal does not violate the rule against single-issue ratemaking. NRDC In. Br. at 23-24. But the NRDC Brief acknowledges that single-issue ratemaking will occur, noting that the per customer form of decoupling being promoted would protect a utility during economic downturns because the revenues gained from new customers would offset any declines in usage. NRDC In. Br. at 18. This point highlights the piecemeal nature of decoupling. It adjusts customer rates based on isolated elements of a utility's revenue streams – per customer usage – while ignoring the variable nature of a utility's expenses, *overall* revenue streams (such as revenues derived from adding new customers) and cost of capital.

NRDC further opines that the recent decision in under *Commonwealth Edison Co. v. Illinois Commerce Comm'n,* ("*ComEd*"), 937 N.E.2d 685 (2d Dist. 2010) does not render its decoupling proposal illegal. NRDC argues it is inapposite because decoupling recovers lost *revenues,* not expenses. NRDC In. Br. at 23-25. But this point only highlights why decoupling is illegal, not permissible. Riders, as the Court noted, are to be used to recover *costs* or *expenses* – not lost revenues. The Court in *ComEd* specifically held that because riders always permit direct recovery of a single cost, rather than incorporating that cost into the aggregate calculation of the revenue requirement, they always pose, at the very least, a "danger of single-issue ratemaking." *City of Chicago II*, 281 Ill. App. 3d at 628; *see also ComEd*, 937 N.E.2d at 708 ("Because a rider is a method of single-issue ratemaking, by nature, it is not allowed absent a showing of exceptional circumstances."). The Court concluded that exceptional circumstances necessary to justify a rider arise only when the proposed rider is designed to "recover a particular cost if (1) the *cost* is imposed upon the utility by an external circumstance over which the utility has no control and (2) the *cost* does not affect the utility's revenue requirement." *Id.* at 687 (emphasis added). The Court further held:

> In other words, a rider is appropriate only if the utility cannot influence the cost (*Citizens Utility Board,* 166 Ill.2d at 138 [‘a rider mechanism is effective and appropriate for cost recovery when a utility is faced with unexpected, volatile, or fluctuating expenses’) and the expense is a pass-through item that does not change *other expenses or increase income* (*Citizens Utility Board,* 166 Ill.2d at 138 (*a valid rider has no ‘direct impact on the utility’s rate of return*’).

Id. at 687.

In its review of Illinois law, the Court reconciled and distinguished past cases affirming Commission approval of riders that involved the recovery of expenses related to the purchase of natural gas, federally-mandated environmental remediation costs and a municipality’s franchise fee. The Court concluded:

> In each instance, the expense was an externality imposed on the utility, and the expense was passed directly on to the consumer without affecting the utility’s return on investment.

Id. at 688.

As noted in the AG Initial Brief, the NRDC/ComEd decoupling proposal fails to meet the test for permissible riders spelled out by the Court. First, recovery of per customer revenues is not recovery of a pass-through “expense.” Second, the sole purpose of a decoupling rider is to increase income and directly impact the utility’s rate of return. Under ComEd and the cases cited in the Second District opinion that came before ComEd, the decoupling tariff would not pass legal muster.

For all of these reasons, and the reasons supplied in the AG Initial Brief at pages 138-148, the Commission should reject approving a decoupling rider as an alternative to ComEd’s SFV proposal.

CUB

CUB opposes NRDC’s decoupling proposal, which AG/CUB witness Mr. 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. CUB maintains that 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. CUB states that 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 decoupling was approved; and (3) there are better ways to promote energy efficiency investments. *Id.* at 15.

STAFF

NRDC recommends in its Initial Brief that the Commission approve a modified version of its initial decoupling plan with one that would include adoption of Rider DA presented by ComEd as a substitute for the Company's SFV rate design proposal. NRDC would also add a "3% cap on refunds or charges, with any unrecovered balances carried forward and refunds or charges based on a per kWh basis." (NRDC IB, p. 26) NRDC assures that the decoupling proposal "is consistent with the Appellate Court decision and is permitted under Illinois law. There is also no reason to delay the implementation of a decoupling plan." (*Id.*, p. 16) NRDC further believes it is reasonable to act now because "[t]he parties have had an opportunity to review and challenge the plan proposed by NRDC, which is based on decoupling mechanisms used throughout the country." (*Id.,* p. 16)

NRDC's arguments present problems. For one, NRDC's claim that the proposal is consistent with the Appellate court decision is questionable. Staff understands that the Illinois Appellate Court, Second District has found a ComEd rider, Rider AMI, contrary to the PUA and there is reason to believe that ruling calls into question the role of riders in the ratemaking process. It is Staff's understanding that this decision by the Illinois Appellate Court has been appealed to the Illinois Supreme Court and in the meantime, the legality of riders remains in question. (Staff Ex. 29C, p. 19)

In addition, Staff believes it is possible to implement a reasonable rate design in this case that sends appropriate price signals to ratepayers and does not require the adoption of a cumbersome decoupling apparatus. That would be accomplished by approval of Staff's proposed rate design.

Staff also finds that the complexity and amount of time involved in properly reviewing and designing the tariff details to ensure proper implementation of such a proposal renders it impracticable to adopt NRDC's proposal in this rate case at this late stage. (Staff Ex. 29C, p. 19)

Finally, the AG also weighs in against NRDC's decoupling proposal, stating:

> Mr. Cavanaugh's proposal, which mirrors the decoupling agenda NRDC promotes throughout the United States, is based on neither accepted rate design principles nor ComEd's cost of service. Worse yet, it includes no analysis of rate impacts on ComEd customers. Finally, the decoupling rider is unlikely to pass Illinois Appellate Court scrutiny, in light of the Second District Appellate Court's recent ruling in *Commonwealth Edison Co. v. Illinois Commerce Comm'n,* ("*ComEd*"), 937 N.E.2d 685, 708-711

> (2d Dist. 2010) (reversing Commission's decision to authorize a rider and discussing five prior Illinois court decisions addressing riders.) For these and other reasons…, this ill-conceived proposal should be rejected. (AG IB, p. 137)

For these and those arguments previously stated in Staff's Initial Brief, the Commission should reject NRDC's decoupling plan.

ELPC

NRDC argues that "the current regulatory model discourages utilities from both investing in energy efficiency and becoming involved in activities that could lead to more efficiency, such as advocacy for appropriate building standards and effective public education." NRDC Initial Brief at 1. Along these lines, NRDC argues:

> The Commission should not assume that ComEd's obligation under Section 5/8-103(b) of the Public Utilities Act to meet prescribed energy efficiency goals eliminates the need to take additional measures to encourage energy efficiency. While that law mandates that ComEd undertake energy efficiency measures, traditional rate of return regulation puts the company at odds with the public policy goals of meeting and exceeding minimum targets. Removing ComEd's incentive to maintain its electric sales level would encourage ComEd to devise innovative ways to meet or exceed its statutory targets.

NRDC Initial Brief at 8. While in some states NRDC's argument may make sense, NRDC ignores the circumstances and law in Illinois. Foremost, ComEd operates under a rate cap that will control its spending in the next three year plan, regardless of decoupling. In its totality, the energy efficiency law in Illinois sets targets, penalizes ComEd by taking away the programs if it fails to meet goals, while also limiting the company's spending on energy efficiency. Given these hard parameters, Illinois customers would get very little benefit from decoupling.

In terms of consumer benefits, the record reflects that ComEd has exceeded its savings targets during the first two years of its Energy Efficiency Plan (the only years we have results for to date). Moreover, the Company has stated its strong commitment to meeting its targets in the next Plan regardless of rate structure. ComEd witness Jensen testified that the Company will make every effort to provide all available efficiency under the budget cap. Tr. at 2309. In essence, ELPC does not believe that the consumers will get the benefits touted by NRDC.

Additionally, ELPC disagrees with NRDC's legal analysis regarding decoupling. NRDC argues that nothing in the recent Illinois Appellate Court decision *Commonwealth Edison v. ICC* challenges the legitimacy of NRDC's decoupling proposal. NRDC continues, the test for determining whether a rider constitutes impermissible single-issue ratemaking is whether "(1) the cost is imposed upon the utility by an external circumstance over which the utility has no control and (2) the cost does not affect the

utility's revenue requirement." NRDC Initial Brief at 23 (citing *Commonwealth Edison Co. v. ICC*, 937 N.E. 2d 685, 710 (Ill. App. 2d 2010)). ELPC agrees that this is one of the tests that the Appellate Court articulates. However, we disagree with how NRDC applies the test.

In *Commonwealth Edison* the Court addressed the issue of ComEd's cost recovery of smart grid investments through Rider SMP. The Court states, "Rider SMP is a classic example of single-issue ratemaking because AMI is the type of cost that should be addressed through normal ratemaking procedures…we conclude that Rider SMP amounts to single-issue ratemaking." *Id.* at 683. Like with the smart grid investments, ComEd can recover any lost revenue from energy efficiency through traditional ratemaking. While the energy efficiency programs will affect ComEd's revenues, the effect is no different than many other factors – such as customers replacing old appliances with more energy efficient ones. ComEd could have easily adjusted its test year to account for the revenue changes from the efficiency programs by using a future test year that adjusted revenue consistent with ComEd's statutory goals. The Company chose not to do that.

The lost revenue from energy efficiency does not constitute a cost imposed upon the utility by external circumstances over which the company has no control. The courts have allowed riders in circumstances such as CILCO's coal tar remediation clean up, where the costs could vary from a few thousand dollars to several million, and the court determined the costs were "unexpected, volatile and fluctuating." *Commonwealth Edison*, 937 N.E. 2d at 709, (citing *Central Illinois Light Company v. Illinois Commerce Commission*, 255 Ill. App. 3d 876, 885 (Ill. App. 3d 1993)). Loss of revenue from energy efficiency programs is not unexpected, volatile, or fluctuating (any fluctuation is likely to be small). Thus, decoupling does not qualify as the type of situation where the Illinois courts have looked past the single issue ratemaking hurdle to grant the type of true-up NRDC seeks with decoupling.

ComEd Response

ComEd argues that a revenue decoupling rate design should be considered as an alternative means to SFV of eliminating or significantly weakening the link between the revenue of a utility and the utilization of its system by customers. ComEd addresses the merits and the shortcomings of the NRDC proposal, and also provides additional information for the Commission's consideration with respect to the issue of decoupling. ComEd maintains that SFV is a superior solution but, it did offer a sample tariff reflecting NRDC witness Mr. Cavanagh's proposal to ensure that the NRDC proposal, if approved, is implemented in a way that is consistent with ComEd's other tariffs.

Commission Analysis and Conclusion:

The Commission finds that the decoupling proposal is less favorable to the customers and has the potential of leading to higher rates. This proposal is also overly complicated and has not been adopted for an electric utility in this state. The

Commission has concluded at this time that it will not adopt the NRDC's proposal of Decoupling. With the adoption of the modified SFV charge, this is not necessary.

1. Class Definitions

a. Residential Rate Design – Consolidation of Residential Classes

ComEd's Position

ComEd proposes to reduce the number of residential delivery classes from four to two. Specifically, ComEd proposes to combine the two single-family delivery classes (Single Family with Space Heat and Single Family without Space Heat) into one class: the Residential Single-Family Delivery Class. It also proposes to combine the two multi-family delivery classes into one class: the Residential Multi-Family Delivery Class. In doing so, ComEd proposes to have one DFC for all single-family customers and one DFC for all multi-family customers. The effect of this change is to eliminate separate delivery service rates for those customers with electric space heat and those who do not use electricity for space heat.

ComEd witness Mr. Alongi testified that designing electric delivery service rates based on the end use of electricity by customer, such as for space heat, is "inappropriate," requiring ComEd to "police" the use of electricity within customers' homes for billing purposes. ComEd states further that the Commission has already taken steps to eliminate the distinction between residential customers with electric space heat and those without electric space heat. It states that the Commission approved Rider PE, ("Purchased Electricity") which has specific grandfather provisions that were approved in docket 05-0159. Pursuant to Rider PE, separate supply charges for electric space heat are applicable only to residential customers and their successors who were eligible on January 1, 2007, to take service under ComEd's then-effective residential electric space heat rate (ILL. C. C. No. 10, Rider PE Original Sheet No. 322). Those charges do not apply to residential customers whose homes were either was built on or after January 2, 2007, or had electric space heating facilities installed for the first time on or after January 2, 2007. (ComEd Initial Brief at 140-41).

Finally, ComEd contends that the phase-in of its proposed SFV results in a significant reduction in the revenue that it will obtain through the application of the volumetric per kWh DFC charges. It also eliminates "meaningful" distinctions between distribution rates for customers with and without electric space heat, thereby obviating any rationale for maintaining separate delivery classes for customers with electric space heat. (ComEd Ex. 16.0 2nd Rev. at 17). ComEd further argues that the proposal made by AG AG/CUB witness Mr. Rubin to have a single one NCP for the residential sector while maintaining four residential customer class designations should be rejected. In support, ComEd cites 220 ILCS 5/16-108(c), which requires utilities to design rates in a manner that is cost-based. ComEd also cites 83 Ill. Adm. Code 285.5110(b), which requires Cost of Service Studies to include a list of all demand and/or energy loss factors by customer class used in the study. (ComEd Initial Brief at 105).

The AG/CUB Position

AG/CUB witness Mr. Rubin opposed ComEd's proposal to eliminate rate distinctions based on space heating. In Mr. Rubin's opinion, ComEd's cost of service study demonstrates that existing rates for the residential heating classes exceed its proposed cost of serving those classes. The AG/CUB contend that ComEd should retain the four existing residential subclasses due to the significant differences in the usage characteristics and cost of service for each type of customer. Specifically, they argue that the cost to serve multi-family with heat customers is approximately $45.6 million, however, under ComEd's present rates, those customers already are providing ComEd with $49.9 million. They aver that ComEd's proposed rate consolidation would increase this even further to $54.7 million, even though those customers are already paying more than the cost to serve them.

The effect, the AG/CUB state, would be that these customers would pay nearly 20% more than the cost to serve them. (AG/CUB Ex. 6.0 at 23). On the other hand, single-family customers with heat, 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 single-family with heat customers by more than 14%. The AG/CUB conclude that 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, which runs contrary to cost-causation principles. (*Id.* at 24; *See also* AG Initial Brief at 103-130).

The AG/CUB contend that no residential subclass should receive an increase that is more than 1.5 times the average increase for the residential class. Because ComEd has proposed an overall residential increase of 20.8%, they assert that there should not be any significant group of residential customers that would receive more than a 31% increase in delivery service rates pursuant to ComEd's proposed revenue requirement. (CUB Memo at 16: AG Memo at 17-18).

The City of Chicago's Position

The City of Chicago argues that ComEd's proposal should be rejected. It states that currently, ComEd's residential rates consist of three components – the customer charge, the meter charge, and the distribution charge. The customer charge and the meter charge are fixed charges; that is, they do not vary with usage. In contrast, the distribution charge is a per-kilowatt-hour charge, meaning that the distribution charge increases, as a customer uses more electricity. (*See,* AG/CUB Ex. 6.0 at 4).

The City cites the testimony of Mr. Rubin, who testified on behalf of the AG/CUB. According to the City, Mr. Rubin established that ComEd's proposal to reduce its residential sub-classes to two will increase the costs that would be allocated to multi-family customers. Attached to Mr. Rubin's direct testimony as AG-CUB Ex. 6.01 is a cost study performed by ComEd showing what the results of its ECOSS would be, if ComEd continued to include four sub-classes within the residential class. (AG/CUB Ex. 6.0 at 7-8).

Mr. Rubin testified that one would expect that modifying the cost study to include four sub-classes rather than two should not affect the overall costs attributed to the residential class. However, he stated, that is not the case. Mr. Rubin opined that moving from four sub-classes to two has the effect of increasing the costs that are allocated to multi-family (apartment or duplex dwellers) customers by $8.4 million. At the same time, it avers, single-family residential customers would see a $4.2 million reduction in costs, and so would non-residential customers. (*Id.* at 9, City Initial Brief at 5-7).

According to Mr. Rubin, this anomaly is due to the way that ComEd has allocated secondary costs within the residential sub-classes. Mr. Rubin stated that Com does not allocate these costs to the residential class as a whole, but instead, applies the NCP method to each sub-class within the residential class. (AG/CUB Ex. 6.0 at 8). The City asserts that ComEd's ECOSS showed that the multi-family residential sub-class as a whole has a NCP demand of 1,929,290 KW. (ComEd Ex. 22.1, Sch. 2b, line 19). Mr. Rubin testified that the NCP demand for the 87% of multi-family residential customers who do not use electricity for space heating is 1,649,910. (AG/CUB Ex. 6.0 at 8; AG/CUB Ex. 6.01, Sch. 2b, Line 19). Mr. Rubin then stated that one would assume that the NCP demand for the multi-family with heat sub-class would be 279,380 KW (1,929,290 – 1,649.910.) However, because ComEd calculates the NCP for each sub-class separately, and because the multi-family with heat sub-class peaks during the winter, its NCP is 839,327. This increases the NCP demand for the residential class as a whole "to 2,489,237 KW, an increase of almost 30%."

Mr. Rubin opined that the amount of costs that are assigned to the residential class should not be affected by whether there are two or four sub-classes. Also, the costs assigned to non-residential customers should clearly not be affected by the manner, in which, costs are allocated among the residential sub-classes. (AG/CUB Ex. 6.0 at 9). Due to this anomaly, and the fact that Mr. Rubin established that present rates for heating customers provide revenues in excess of ComEd's proposed costs for those sub-classes, the City of Chicago argues that the Commission must reject ComEd's proposal to reduce its residential sub-classes from four to two. It also recommends that the Commission require that in future rate cases, ComEd should be required allocate costs to the residential class as a whole and then reallocate those costs among the four residential sub-classes. (City Initial Brief at 7).

Staff's Position

Staff witness Mr. Boggs recommended that the Commission approve ComEd's proposal to reduce the number of residential delivery classes from four to two, as long as the Commission does not order ComEd to eliminate the separate supply charges for each of the classes in this rate proceeding and also does not eliminate them without an in-depth analysis and review of the impact on customer bills by ComEd, Staff and interested parties. (Staff Memo at 14-15; Staff Ex. 13.0 at 30-34).

Staff witness Mr. Clausen recommends that the Commission initiate a separate proceeding to investigate ComEd supply charges. Staff recommends that the Commission initiate a Section 9-250 proceeding to address issues related to supply rate design. ComEd witness Mr. Hemphill stated that ComEd supports the proposal for the

Commission to initiate a proceeding to address residential supply charges and further recommends that any such investigative proceeding should be initiated with a firm deadline for its completion in order to avoid unnecessary outlays in effort, time, and money (ComEd Ex. 46.0 at 28). Staff agrees that the Commission's Initiating Order should include a specific deadline for entering a Commission Order. (Staff Memo at 19).

ICEA's Position

ICEA supports Staff's efforts to develop a more robust market on this issue. (ICEA Memo at 5).

Analysis and Conclusions

We decline to permit consolidation of the residential classes in the manner proposed by ComEd. As the AG/CUB witness Mr. Rubin points out, there is evidence indicating that the manner, in which, ComEd allocates certain costs could raise the cost of electricity for multi-family residential customers in a manner that is not proportionate to usage. ComEd witness Mr. Alongi's conclusion that ComEd is currently required to "police" the use of electricity under the current rate structure is factually unsupported and we need not consider it. Additionally, merely stating that something is "inappropriate," without stating why something is "inappropriate," is not a legal argument and it is not a policy argument. Both types of arguments require a statement as to the harm that will ensure if an "inappropriate" method is adopted. We further note that why ComEd would be required to "police" the use of electricity is not stated and it is far from obvious.

We further adopt Staff witness Mr. Clausen's suggestion to initiate a Section 9-250 proceeding to address issues related to supply rate design regarding residential customers. This proceeding should also address the proper allocation of NCP demand amongst the four residential customer classes. Staff shall present an initiating order regarding this proceeding within four weeks after the time when a final Order issues in this docket. With regard to the deadline for completion of a final Order in that docket, that deadline should be 18 months, which is an extraordinarily short period of time for litigation that is contentious. Any shorter amount of time only ensures that there will be inadequate discovery, inadequate development of the issues at the evidentiary hearing, and inadequate time for informal resolution (settlement) of issues, if this case is highly-contentious. It also ensures, if this case is highly-contentious, that rehearing is likely.

However, if this proceeding is not highly-contentious, every effort should be made by the parties, Staff, and the ALJ assigned to this docket to complete it much sooner than 18 months and otherwise as quickly as is possible without sacrificing due process issues like those that were just previously stated.

Moreover, it appears, after an examination of Section 9-250 of the Public Utilities Act, that the utility investigated has the burden of proof. Generally, the party with the burden of proof is the party that is more able to hasten the litigation process.

To help ensure that this docket is not unnecessarily quagmire, Staff's initiating order shall state that ComEd shall file a pleading, in a manner and time frame that is set forth by the ALJ assigned to this docket, which sets forth its legal and factual position(s),

and all parties shall file pleadings in a manner set forth by the ALJ thereafter. While legal and factual positions can vary as a case progresses, cases tend to move faster when the issues are set forth early on. We also note that there really can be no resolution of an issue (*e.g.,* settlement) until it is clearly defined. At a minimum, pleadings are a starting point for definition of issues, and for quick resolution of those issues, after the parties have been informed as to what they are in the pleadings.

Because a Section 9-250 proceeding will be opened, we need to entertain the propriety of Mr. Rubin's proposal to require ComEd to allocate costs to the residential class as a whole and then reallocate those costs among the four residential sub-classes.

b. New Primary Voltage Delivery Class vs. Primary Subclass Charges

ComEd's Position

ComEd proposes to redefine the commercial delivery service classes by creating a new PVD class, which would consist of all of the Small Load, Medium Load, Large Load, Very Large Load and Extra Large Load delivery class customers in one class. According to ComEd, its proposed nonresidential delivery classes account for voltage differences amongst these classes because they include a delivery class for customer premises, at which, electricity is delivered at or above 69 kV. (ComEd Initial Brief at 142-43). Also, all non-residential customers in demand-based delivery classes that are greater than 400 kW are considered primary voltage customers. ComEd's proposed rate design also provides for a rate reduction for customers that provide their own transformation through a credit under Rider ACT – Allowance for Customer Owned Transformers. (ComEd Ex. 73.1). ComEd avers that the rate design in ComEd Ex. 73.1 reflects Commission directives in the Rate Design Investigation Order (docket 08-0532) and previous Commission Orders.

ComEd further avers that it has submitted an Exemplar Rate Design to provide for the institution of a Primary Voltage Delivery Class. (ComEd Ex. 21.1). However, ComEd is not proposing to use this Exemplar Rate design. The Exemplar Rate Design was subsequently revised and submitted as ComEd Ex. 73.2. Should the Commission direct ComEd to institute a Primary Voltage Delivery Class, ComEd contends that its preferred Exemplar Rate Design that is set forth in ComEd Ex. 73.2 should be adopted. (ComEd Initial Brief at 142-43).

ComEd also prepared an Alternative Exemplar Rate Design, in which, the existing demand-based nonresidential classes are subdivided to incorporate DFCs and transformer charges for service points to which electricity is delivered at or above 4 kV but below 69kV. (*See,* ComEd Ex. 49.0 Rev. at 6). The Alternative Exemplar Rate Design does not create a new delivery class. (ComEd Ex. 73.0 2nd Rev. at 24). However, ComEd argues that this rate design, also, should not be supported because customers who receive primary voltage without transformation are similar in terms of the facilities that are required to provide service to them. (ComEd Initial Brief at 142-43).

Staff's Position

Staff states that the alternative exemplar rate design that ComEd presented for the primary class for customers receiving service from 4 kV up to, but not including, 69 kV service should be approved in this case. In Staff's opinion, this alternative approach significantly improves upon the exemplar primary class presented in ComEd's Initial Filing because it incorporates cost differences based on customer size, while the previous approach did not. The exemplar charges for primary service presented in ComEd's Supplemental Direct filing consist of a single customer charge; standard metering charge and a demand, or a distribution facilities charge (a "DFC" charge) for primary voltage. These customers who, in many instances, also receive service at a secondary level would all pay the same secondary distribution facilities charge under this proposal. (Staff Ex. 10.0 at 32). Staff states that there are just under one thousand ComEd customers who would qualify for this rate according to ComEd witness Mr. Alongi. (Staff Initial Brief at 131).

Staff further explains that this exemplar rate design applies the same charges to all customers in ComEd's proposed primary class. These customers, Staff avers, vary considerably in size, ranging from Small Load (up to 100 kW) up to Extra Large Load (over 10,000 kW). (Staff Ex. 10.0 at 32). This "one-size-fits all" approach for primary customers, Staff continues, is inconsistent with ComEd's proposed rate design for secondary and high voltage customers which feature size-based rates. Staff states that secondary service consists of six different rate classes which are differentiated by customer usage levels and demands, (*See,* ILL.C.C. No. 10, Original Sheet Nos. 136-137) while high voltage class customers face different demand charges above and below 10,000 kWs. Thus, it appears to Staff as though ComEd considers rate differences based on size to be appropriate for the exemplar secondary and high voltage classes, but not for the exemplar primary class. (Staff Ex. 10.0 at 32-33).

Staff further states that previously, the cost information for these customers was a factor in justifying significant size-based variations in customer and metering charges among nonresidential customers. Now that they have been separated, Staff states, it is not clear why size differences are not considered to be meaningful in setting primary service customer and metering charges. (Staff Ex. 10.0 at. 33-34; Staff Initial Brief at 131-32).

Staff avers that a similar issue arises for the DFCs presented in ComEd's Exemplar Primary class rates. While ComEd's Exemplar Primary class customers face a single Primary and Secondary DFC, similar-sized customers in secondary classes face a range of secondary DFCs depending on their maximum demands. Staff argues that ComEd has not explained this differing approach for Exemplar Primary class customers. (Staff Ex. 10.0 at 34-35).

ComEd witness Mr. Alongi defended ComEd's primary class rate design, arguing that primary customers "are in fact similar in terms of the facilities used to serve them and the associated cost of those facilities." He identified the common facilities for

primary customers and contrasted those facilities with the equipment necessary to serve a typical secondary customer. (*See,* ComEd Ex. 49.0. 31). Staff contends that this argument uses a limited analysis of a small range of physical customer costs to draw sweeping conclusions about all customer costs for primary customers. Staff opines that a broader discussion considering all customer costs is needed to justify differing treatment for primary and secondary customers. (Staff Ex. 26.0 at 23-24; Staff Initial Brief at 132).

Staff acknowledges that Mr. Alongi did present an Alternative Exemplar rate design approach for the primary class that is responsive to Staff's concern. This Alternative rate design divides primary nonresidential customers into the same size categories as secondary customers. It also breaks down demand-based DFC charges into two components, one pertaining to costs for the primary system and another, which consists of secondary costs. Under this rate structure, Staff continues, primary customers would pay only the applicable DFC charge for the primary system while secondary customers would pay both the primary and secondary DFC charges. (Staff Ex. 26.0 at 24). In Staff's opinion, this Alternative Exemplar rate design is reasonable because it aligns primary customers with secondary customers and limits rate differences to the fact that one group receives power from the secondary distribution system while the other does not. Staff recommends adopting that rate structure should be adopted by the Commission in this proceeding. (Staff Ex. 26.0 at. 25; Staff Initial Brief at 132-33).

The IIEC's Position

The IIEC points out a person must define the customer classes before determining the level of cost caused by each class. Differing rate class definitions account for some of the variation in the Cost of Service Studies presented in this case. It posits that ComEd's Proposed Cost of Service Study, presented in ComEd Ex. 75.1, uses existing delivery service class definitions. ComEd's Preferred Exemplar Cost of Service Study, presented in ComEd Ex. 75.2, redefines the delivery service classes by creating a new PVD class, consisting of customers from the Small Load, Medium Load, Large Load, Very Large Load and Extra Large Load delivery classes. This, the IIEC avers, redefines all of these classes.

However, ComEd's Alternative Exemplar Cost of Service Study, presented in ComEd Ex. 75.3, uses existing delivery service class definitions, but differentiates primary and secondary load subclasses within the existing classes. (*See*, ComEd Exs. 51.0 at 4-5; 75.0 at 1). The IIEC's Cost of Service Study, presented by IIEC witness Mr. Stowe in IIEC Exs. 3.0C and 6.0, uses existing rate class definitions, but, it divides the Medium Load through Extra Large Load delivery classes into primary and secondary service subclasses, in order to examine the cost of serving these subclasses. (The Small Load subclass having too small of a difference to actually have a financial impact).

The IIEC opposes use of ComEd's proposed Cost of Service Study, ComEd Ex. 75.1 and the predecessors' versions of this Study, because it does not provide for voltage-differentiation amongst the subclasses set forth above. (IIEC Ex. 5.0-C at 23).

It also opposes use of ComEd's Preferred Exemplar Cost of Service Study, ComEd Ex. 75.2, and the predecessors' versions, because this Study uses a new "PVD" service class that aggregates customers with what the IIEC views as dissimilar costs.

Instead, the IIEC proposes that the current delivery service rate classes should be retained and that the distinctive delivery service costs that are associated with voltage differences should be reflected by creating two subclasses within the medium Load, Large Load, Very Large Load and Extra Large Load delivery service rate classes. These two subclasses are a primary voltage subclass and a secondary voltage subclass. (IIEC Ex. 2.0 at 16-17).

The IIEC opposes use of ComEd's Alternative Exemplar Cost of Service Study, and the earlier versions of this Study, as; the IIEC views this study as one that is inferior to its Cost of Service Study. The IIEC acknowledges that ComEd's Alternative Exemplar rate structure is similar to its recommended rate structure. However, it contends that its rate structure is preferable, because, according to the IIEC, it best meets this Commission Rate Design Order's (in Docket 08-0532) voltage-differentiated class directive. (IIEC Initial Brief at 31-2). The IIEC argues that in Docket No. 08-0532, the Commission recognized the value in distinguishing the costs imposed by primary customers, which are customers who receive service at 4,000 volts ("4 kV") and above, from those imposed by secondary customers, who receive service at below 4 kV. It quotes that Order as follows:

> Our concern (in Docket 07-0566) was that although the vast majority of ComEd's customers take service at lower voltages that utilize its extensive distribution system, a small number of customers take service at higher voltages that bypass significant portions of the distribution infrastructure. Their cost of service is therefore lower on a per kilowatt basis. The rates charged to these primary system customers should reflect this lower cost of service. . . . Consistent with the foregoing, we direct ComEd to develop and provide in its next rate proceeding: . . .
>
> consideration of redefining rate classes on the basis of voltage or equipment usage to better reflect the cost of service. . . . . The Commission, having considered the entire record herein and being fully advised in the premises, is of the opinion and finds that: . . .
>
> the following decisions are final and should be reflected in the cost of services for consideration in any subsequent action in the Company's next rate case:
>
> a) customers receiving power at 4kV or higher are primary system customers who should be identified. <u>Rates charged to these customers should be adjusted to reflect that they do not use the secondary distribution system</u>;
>
> b) customers receiving power at levels below 4kV <u>should be considered secondary system customers and charged accordingly.</u>

(Emphasis added; *See,* 08-0532, Final Order of April 21, 2010, at 35, 40, and 84).

The IIEC contends that a rate design that does not differentiate between primary and secondary customers' costs does not comply with the Commission's directives in that Order. ComEd's proposed rate design does not make such a differentiation. It states that this failing must disqualify ComEd's proposed rate design, which can be found at ComEd Exs. 15.1, 51.1 and 75.1, from adoption in this case.

The IIEC also avers that ComEd's new primary class improperly groups customers of different sizes and usage characteristics, which is counter to traditional rate design. It maintains that, as was pointed out by Staff, this proposed "one-size-fits-all" approach is inconsistent with ComEd's approach for customers served at secondary voltage and customers served at high voltage. (IIEC Ex. 2.0-C at 14-15; Staff Ex. 10.0, at 32-33). The IIEC further argues that therefore, this Commission must determine whether to adopt a new rate class composed of primary customers from each of ComEd's traditional, size-differentiated delivery classes (leaving only secondary customers in the existing classes) or, to create sub-classes within the existing classes to distinguish primary and secondary customers, with distinct DFCs for primary and secondary customers. (IIEC Initial Brief at 63-66).

The IIEC states that pursuant to its cost of service study, any change in ComEd's approved revenue requirement would be reflected in the DFCs. It avers that its proposal is a simpler and better approach to implementation of the Commission's directive to present voltage-differentiated rates, as it is less disruptive to customers. It avers that no new classes are needed, customers remain in their existing classes, and only the DFCs paid by customers would change. It points out that these customers' DFCs would change pursuant to the instant case in any event. All of the customers in a particular rate class would pay the same customer charge, meter charge and IEDT charge (if applicable). Only the DFC for these customers would differ, depending on whether they were in the primary subclass or the secondary subclass. (IIEC Exs. 2.0-C at 16-18; 5.0-C at 23-24).

REACT's Position

REACT is neutral as to which of the three primary/secondary approaches best reflects cost causation and achieves the Commission's directives from the Special Investigation Proceeding. (React Initial Brief at 23-24).

The Commercial Group's Position

The Commercial Group opines that, if the Commission decides to establish a primary customer class in this proceeding, it should use the cost of service study in ComEd Exhibit 73.2 as a guide for class revenue allocation. This cost of service study, the Commercial Group states, corrects the allocation of secondary distribution line costs that was erroneously presented in ComEd Exhibit 22.1. However, if the Commission decides not to implement a Primary Voltage Class in this case, the Commercial Group maintains that it should use the cost of service study in ComEd Ex. 73.1 as a guide for class revenue allocation. (CG Exs. 1.0 at 23; 3.0 at 2). (Commercial Group Initial Brief at 6).

The Commercial Group states that ComEd witness Mr. Alongi justified the similar cost treatment of primary voltage customers within a single primary class, instead of

diverse cost treatment in numerous primary subclasses (found in the alternative exemplar rates and in IIEC's proposal) because:

> a customer that takes service at a primary voltage from ComEd without any transformation is provided identical facilities (e.g., primary wire tap, fusing, and primary voltage metering) regardless of the load requirement and those facilities are different from the type of facilities provided to a typical secondary voltage customer (e.g., transformation to a secondary voltage, fusing, secondary voltage metering) in a demand-based class.

(*See,* ComEd Ex. 73.0 at 25). Mr. Alongi also averred that setting different primary and secondary subclass charges could actually result in secondary subclass customers subsidizing primary subclass customers. (*Id*. at 28). The Commercial Group concludes that trying to correct a perceived intra-class inequity may simply create an inequity going in the other direction. It finds Mr. Alongi's cost explanation to be reasonable and supports ComEd's position.

Analysis and Conclusions

ComEd has not made a sufficient showing that the rate classes that it proposes to consolidate, which are, the Small Load, Medium Load, Large Load, Very Large Load and Extra Large Load delivery classes, have the same characteristics, justifying making one rate class for all of these very different customers. While ComEd witness Mr. Alongi testified that all of the primary voltage customers are provided with the same facilities, regardless of voltage, he testified that the *on property* facilities are identical. (ComEd Ex. 73.0 at 25-6). He did not state that the cost of providing services to these classes is the same. In fact, based upon the evidence presented, it appears that ComEd's proposed rate design (ComEd Ex. 73.1) and its Exemplar Rate Design (ComEd Ex. 73.2) attempt to group customers with usage patterns that differ, widely, and that have very different usage patterns. We therefore decline to consolidate the Small Load, Medium Load, Large Load, Very Large Load and Extra Large Load delivery classes into one class.

It also appears that Mr. Alongi's testimony justifying the consolidation of these classes mentioned only a small range of physical customer costs and not all of the costs involved in providing service to these customers. Additionally, as the IIEC points out, ComEd's preferred rate design (ComEd Ex. 73.1) does not differentiate between primary and secondary customer costs. Also, ComEd's Exemplar Rate design (ComEd Ex. 73.2) appears to impose DFC charges on the secondary classes that are not explained.

Having so concluded, we note that ComEd's Alternative Exemplar Rate Design, that which is reflected in its Exs. 75.3, and substantiated with its embedded cost of service study in ComEd, 73.3, is the only embedded cost of service study that comports with the final Order in docket 08-0532, as it is the only study that divides primary non-residential customers into the same size categories as those for secondary customers and breaks down demand-based DFC charges based on primary/secondary

considerations. Therefore, this is the only cost of service study that we will consider. We acknowledge, however, that ComEd's Alternative Exemplar ECOSS does not conform in other ways with the Investigation of Rate Design Order. (*See,* the Section herein entitled "Compliance with Docket No. 08-0532.").

We further adopt the IIEC's further-refined ECOSS as the applicable cost of service study to use here, as it further differentiates the DFC based upon primary/secondary considerations. We note that no party has asserted that the IIEC's ECOSS is not accurate or is otherwise deficient.

2. Non-Residential

a. Movement Toward ECOSS Rates

(i) Extra Large Load, High Voltage Customer Classes

The Railroad Class

ComEd seeks to move the rates for the Railroad Delivery Class 10% closer to what ComEd states is its actual cost of service. Staff and the Commercial Group seek to impose a greater move toward actual cost of service. The CTA and Metra do not oppose imposition of an additional 10% for this docket, but they do object to imposition of a greater percentage.

ComEd's Position

ComEd proposes to move the Railroad Delivery Class by 10% closer to what ComEd states is the cost of service for the Railroad Class. ComEd notes that in the past, this Commission has given special attention to the Railroad Class. It has also expressed that this particular class should not face rate shock due to public interest considerations. (ComEd Exs. 49.0 Rev at 9; 71.0 at 8-9). ComEd has proposed a ten-step process to move the Railroad Class closer to cost of service in order to mitigate the effects of rate shock. (ComEd Ex. 73.0 2nd Rev. at 8-9). ComEd asserts that its proposal provides for movement toward cost-based rates in accordance with previous Commission direction. (ComEd Initial Brief at 145-46).

Staff's Position

In ComEd's most recent rate case, the Commission directed ComEd, for the benefit of public interest, to avoid rate shock to the Railroad Class by gradually moving revenues toward full cost recovery for this class. However, in Staff's opinion, contrary to the Commission's directive from the previous rate case, ComEd's proposed 2nd step proposal is a movement of only 10% toward a cost-based DFC. Staff states that this is not consistent with the Commission's previous directive to move toward cost-based rates in a four-step process. Staff points out that, if the Commission accepts ComEd's proposed 10% DFC increase in this case, it would take more than the four steps toward full revenue recovery that the Commission ordered in previous ComEd rate cases. As a result of ComEd's proposed 10% increase, the revenue allocation for the Railroad Class would yield a below-average rate increase, compared to the nonresidential delivery class average. This results in revenues that fall below their cost of service. It also

requires other nonresidential classes to make up the difference. (Staff Ex. 29.0C at 4-5).

Staff proposes that the Commission increase the Railroad Class' cost of service from ComEd's proposal by 25% of the difference between ComEd's exemplar revenues that were presented in ComEd Ex. 43.3 (updated in ComEd Ex. 73.3) and the fully-embedded costs for the Railroad Class. This approach, Staff states, will achieve full cost recovery from the Railroad Class in fewer steps than ComEd's proposed ten-step approach while moderating revenue increases to avert rate shock for these customers. (Staff Ex. 13.0 at 12; Staff Initial Brief at 36-37).

The CTA's Position

The CTA is a member of the Railroad Delivery Class. It states that Staff has rejected ComEd's 10-step process (movement toward actual cost of service for the Railroad Class 10% each time there is a rate case). Instead, according to the CTA, Staff seeks to impose a higher rate increase on the Railroad Class. It argues that Staff's position should be rejected and ComEd's 10% movement should be accepted only for this docket. (CTA Initial Brief at 17).

The CTA states that ComEd's embedded cost of service study improperly allocates costs for facilities below 12 kV to the Railroad Class. This means that the total amount allocated to the Railroad Class is too high. If the Railroad Class' rates were set at what ComEd alleges is its full cost of service, the CTA posits that ComEd would over-recover its cost to serve the Railroad Class. (CTA Memo at 7).

Additionally, according to the CTA, the Commission's past Orders concluded that there is a public interest concern that must be taken into account when setting rates for the Railroad Class. In the past, this Commission has recognized that mass transit systems provide an overall benefit to the community and state of Illinois because the use of mass transit reduces the level of total energy consumption and it provides environmental benefits as well. These benefits, the CTA continues, have been recognized by this Commission in ComEd's earlier rate cases, dockets 05-0597 and 07-0566. (CTA Ex. 2.0 at 2; CTA Initial Brief at 17).

The CTA maintains that even in cases that were not general rate cases, this Commission has found that any requirement for the Railroad Class to pay for the pilot program ran "counter to this Commission's policy of encouraging the use of public transportation for environmental reasons" and that the Rider costs proposed to be charged to the Railroad Class were against public policy because "imposing costs on public transportation providers can limit these providers' ability to provide this transportation." (Final Order, docket 09-0263 at 43). It concludes that therefore, the Railroad Class rate should not be at full cost of service. (CTA Initial Brief at 19-20).

Metra's Position

Metra also is a member of the Railroad Class. Metra points out that this Commission has recognized, in three separate dockets, Dockets 05-0597, 07-0566 and 09-0263, that there are public interest considerations that must be taken into account

when setting the rates for the Railroad Class in order to avoid the adverse effects of increased rates. Those public interests are ones that are associated with affordable public transportation and the benefits that mass transit provides to the overall reduction in energy consumption and adverse environmental impacts. Metra also states that there is unrebutted testimony in this case concerning the congestion mitigation and environmental benefits of the public transportation services provided by Metra and the CTA, citing Metra Ex. 2.0 at 2-5 and CTA Ex. 2.0 at 2-6. (Metra Initial Brief at 2-4).

Metra also avers that ComEd's proposal is very gradual, thus avoiding rate shock. Also, according to Metra, ComEd's Cost of Service Study produces inflated rates for the Railroad Class, thus, using the more gradual increase advocated by ComEd makes it less likely that the rate set will exceed the proper, "currently unknown" cost-based rate in which 4 kV facilities' costs are not allocated to the Railroad Class. (Metra Initial Brief at 13-14).

The Position of the Commercial Group

The Commercial Group contends that a number of representatives of the largest load classes "insist" that they deserve rate subsidies because of potential rate increases that may occur from moving to cost. (*See,* Tr. 1247-1248). The Commercial Group states that Staff's proposal to move rates closer to cost is a reasonable step, in light of the Commission's 2007 rate case final order. It avers that in that order, part of the reason for moving only 25% toward cost in that 2007 order was that the Commission was not sure that ComEd's Cost of Service Study in that case fully-reflected actual cost. The Commercial Group avers that the Commission stated at page 213 of the final order: "What is unclear, and will remain unclear until an ECOSS (Cost of Service Study) is evaluated in compliance with our findings above, is how significant the rate inequities are under this ECOSS." The Commission also accepted ComEd's Cost of Service Study with certain specified modification," that there be a four-step instead of two-step move toward ECOSS rates. The Commercial Group opines that ComEd has now improved its ECOSS in this current rate proceeding, incorporating many proposals of the subsidized customer classes. It concludes that therefore, there is even less need to move slowly toward cost.

Also, according to the Commercial Group, ComEd's proposed increases for the Railroad and High-Voltage classes are only 4.6% and 7.4% respectively. It argues that rate shock cannot be the basis for a lower step up to cost because ComEd's witness Dr. Hemphill agreed that even increasing the rates for those classes by the system average of 14.8% would not constitute rate shock. (*See,* Tr. 334). It concludes that to the extent that the Commission determines that "subsidies" should continue, the burden should be spread to all other classes of customers, and not to certain non-residential classes alone. (Commercial Group Initial Brief at 9-10).

The IIEC's Position

IIEC witness Mr. Stephens disagrees with ComEd's contention that the Railroad Class should be moved only 10% of the remainder of the way to cost-based rates. Instead, Mr. Stephens recommends that the Railroad Class should be moved 33% of

the remainder of the way to cost of service. (IIEC Ex. 2.0 at 6). However, it defers to the Commission's judgment regarding the Railroad Class. (IIEC Initial Brief at 70).

It is also the IIEC's position that, if the Commission determines that the Railroad Class requires additional rate impact consideration, the rate increase for the Railroad Class could be limited by using a lower multiple of the system average increase such as 100% or 125%. (IIEC Ex. 5.0 at 11-12).

Analysis and Conclusions

We decline to extend the Railroad Class' increase in its cost of service beyond 10%. As the CTA and Metra have noted, there are public interest concerns regarding providing affordable public transportation, and the benefits that mass transit provides to the overall reduction in energy consumption and adverse environmental impacts. At this time, we decline to raise the rate that the CTA and Metra will incur beyond 10%. We note that any increase in the rate supplied to these two customers could be passed on to consumers. Also, an increase in the costs incurred by the CTA and Metra, beyond the modest one proposed by ComEd, could limit these providers' ability to provide public transportation to millions of people.

It is not clear what the context is for the Commercial Group's contention that ComEd's proposed increases for the Railroad and High-Voltage classes are only 4.6% and 7.4% respectively. Without the necessary factual foundation for these figures, we shall not consider it.

Extra-Large Load and High Voltage Customers

ComEd proposes to move the rates for these two classes 33% toward the actual cost of service.

ComEd's Position

ComEd states that its proposed rates for these two classes of customers reflect the next step in a Commission-directed progression towards charges that reflect the cost of providing service. It avers that, as the Commission noted during ComEd's 2007 rate case, the DFCs for non-residential customers in the Extra-Large Load, High-Voltage and Railroad delivery classes are set at levels that result in significant under-recovery of the costs necessary to serve them. Therefore, ComEd must over-recover from other nonresidential customer classes to meet its revenue requirements. In that proceeding, the Commission ordered ComEd to move these customer classes 25% toward the actual cost of service.

ComEd contends that it now seeks to undertake the second step of that process with a 33% movement from the current DFCs of the Extra-Large Load and High-Voltage delivery classes towards cost-based DFCs. This would follow the 25% movement that was previously ordered by the Commission as the first step. This 33% movement reflects the fact that there are now only three steps left. ComEd argues that its proposal is consistent with the Commission's long-standing goal of assigning costs to the cost-causers. However, ComEd states, its proposal also reflects the Commission's concerns regarding rate shock by applying the principle of gradualism. (*See,* ComEd Exs. 46.0 at

27; 16.0 3rd Rev. at 12, citing docket 07-0566, Order of Sept. 10, 2008 at 213). The four-step process toward cost-causation for the Extra-Large Load and High-Voltage delivery classes, according to ComEd, reflects both of those principles, as this proposal provide for movement toward cost-based rates. (ComEd Initial Brief at 144-45).

ComEd disagrees with IIEC witness Mr. Stephens' proposal to limit the increase in rates to any delivery class or subclass to 150% of the system average increase. ComEd contends that based upon the "data" in ComEd Ex. 49.1, under Mr. Stephens' proposal, the Watt-Hour, Small Load, Extra Large Load, and General Lighting delivery classes would all be limited to an increase of 27.6%. However, ComEd avers. that would mean that ComEd could not follow the Commission's directive with respect to moving the Extra Large Load Delivery Class 33% of the remainder of the way to cost-based rates.

ComEd further states that all the residential and lighting delivery classes, as well as the Watt-Hour Delivery Class, have proposed rates set at 100% of an equal percentage of embedded cost ("EPEC") for each individual class. If limits were placed on the increase to the Watt-Hour and General Lighting delivery classes, other classes that are currently proposed to be at 100% of embedded cost would probably have to bear more than their fair share of the costs to provide them with electric service. ComEd avers that it has cost-based rates for a number of delivery classes. It concludes that therefore, it would be a step backward to require the implementation of rates that diverge from that fundamental concept in rate design. Finally, ComEd states that Mr. Stephens calls for the 150% limit to be applied to subclasses, which adds yet another level of complexity to what could become a very complicated rate design. ComEd recommends that the Commission reject Mr. Stephens proposal and instead implement a rate design that provides for 100% of embedded cost recovery for as many delivery classes as possible.

The IIEC's Position

The IIEC contends that the Order in ComEd's last rate case established a four-step process to move the Extra-Large Load, High-Voltage and Railroad Class rates toward the actual cost of service, primarily due to the Commission's doubts about the validity of ComEd's cost of service study in that case. According to the IIEC, the Commission recognized the likelihood that ComEd's proposed cost of service for these classes was overstated, It was therefore unwilling to move more rapidly toward the wrong end point. In support, the IIEC cites docket 07-0566, Final Order of September 10, 2008, at 213.

The IIEC states further that ComEd filed rates in this case that seek to comply with the Commission's four-step directive in that case. The IIEC cites the testimony of ComEd witness Mr. Alongi, who stated the following:

> The mitigation mechanism ComEd employs in its proposed and exemplar rate designs in this proceeding is exactly the same as the mitigation mechanism that it used to develop the rates ComEd filed on September 12, 2008, in compliance with the Commission's Order in Docket No. 07-

> 0566. Those rates and the associated work papers that developed those rates were reviewed and accepted by the Commission's Staff.

(ComEd Ex. 73.0 2nd Rev. at 6; IIEC Initial Brief at 68-69).

The IIEC further asserts that Staff proposes to deviate from the Commission's process by moving rates additional increments toward cost of service. This proposal, it states, is above the 33% that is mathematically the first of three remaining steps in the Commission's four-step process. As IIEC understands Staff witness Mr. Boggs' proposal, he would begin with ComEd's proposed rates for the Extra-Large Load and High-Voltage classes, which already reflect a 33% movement toward what ComEd contends is its cost for these two classes, and then move them an additional 33% toward the costs alleged. (Tr. 1217-18; Staff Ex. 29.0C at 5; Staff Sched. 29.01-C at 1).

The IIEC witness Mr. Stephens testified that the existing four-step process should be continued, moving the rates of the Extra-Large Load and High-Voltage classes, 33% of the way from current revenues to cost of service, as was measured by IIEC's rebuttal ECOSS Study. (IIEC Exs. 2.0-C at 4-8; 5.0-C at 3-19). The IIEC points out that this approach does not necessarily advantage the Extra-Large Load and High-Voltage classes. It states that, depending upon the Commission's determinations on customer class structure, P/S split issues, and allocations of various cost of service items such as primary lines and substations and the IEDT, one or more of the subclasses may be entitled to a larger rate decrease under movement to cost of service. (IIEC Ex. 2.0-C, at 18). Despite this potential, the IIEC does not disagree with the Commission's four-step process. (IIEC Initial Brief at 68-70).

The IIEC additionally posits that undue rate impacts must be avoided for all rate classes. It contends that the Commission should, consistent with its recent decision in *Central Illinois Light Company,* docket 09-0306, (the Ameren Rate case docket), approving a rate moderation plan that would ensure that no customer class or subclass experiences an increase in delivery service charges greater than 150% of the system average rate increase for ComEd (including the impact of the IEDT) in this case. Thus, pursuant to the IIEC's proposal, if ComEd receives a 20% increase in its delivery service rates in this case, no class or subclass would see an increase greater than 30%. (IIEC Exs. 2.0 at 6-8; 5.0 at 15-19).

REACT's Position

REACT posits that its witnesses Mr. Fults and Mr. Terhune testified that the Commission should reject any increase in rates based on ComEd's embedded cost of service study for the Extra Large Load customer class, unless and until ComEd provides sufficient information and/or a study that verifiably evaluates the assets used to serve the Extra Large Load class. This study is a necessary prerequisite, REACT states, because ComEd's rates must be cost-based, meaning they must correlate to "the facilities and services associated with such costs." (220 ILCS 5/16-108(c)). In the last four proceedings in which ComEd's embedded cost of service studies have been examined, including three rate cases and a special investigation into its rate design,

ComEd has faced strong and consistent criticism showing that its embedded cost of service study does not accurately establish cost-based rates for its largest customers. REACT argues that it makes no sense to move further toward cost of service studies that this Commission has consistently criticized. (REACT Exs. 1.0C at 12-20, 22, 3.0C at 8, 4.0 at 11-22; 6.0 at 30-33; REACT Memo at 12; REACT Initial Brief at 66).

REACT asserts that, based on its analysis, ComEd charges the over 10MW customer classes for distribution system assets that these customers either do not use, or, use in a manner that is far less than what was assumed in ComEd's ECOSS. (REACT Initial Brief at 68). Additionally, according to REACT witness Mr. Terhune, and also the IIEC's witness Mr. Stowe, the Extra Large Load customer class used a very low level of secondary assets. (*See,* REACT Initial Brief at 69).

Staff's Position

Staff posits that in docket 07-0566, the Commission approved a four-step increase in the DFC to cost. With three steps remaining, the second step proposed by ComEd in this case would increase the DFC by 33% toward a cost-based level for the Extra Large Load and High Voltage classes. (Staff Ex. 13.0 at 7-8). This focus on the DFC charge creates a problem for the High Voltage class, Staff states, because it moves this class farther away from, rather than closer to, the cost of service. The revenue increase for the High Voltage class is 7.4%, which is half of the average for nonresidential classes. It does produce a higher 31.8% increase for the Extra Large Load class, but, Staff opines, this class had the largest revenue recovery percentage deficit to overcome. (Staff Initial Brief at 122-24).

In addition, Staff continues, ComEd's proposal for these classes is not consistent with the approach taken for other rate classes. For the Extra Large Load, High Voltage and Railroad classes, the proposed rate design determines the revenue allocation, whereas the revenue allocations for other rate classes are based on the cost of service. Staff opines that this undermines the concepts of fairness and equity, which require that a consistent, cost-based approach be taken for all classes.

Staff witness Mr. Boggs proposes an alternative approach where each of these classes receives increases that move their revenues closer to the associated cost of service. The objective of his revenue allocation proposal is to move overall revenues for these classes, not just the DFCs, in a three-step process towards costs.

Because the High Voltage and Extra Large Load classes currently under-recover costs relative to other classes, Staff finds that they must receive greater-than-average increases to move closer to cost. Staff's specific proposal is to increase the class revenue allocations for the Extra Large Load and High Voltage classes an additional 33% toward full cost recovery from the exemplar revenue allocations presented in ComEd Ex. 49.3. (Staff Ex. 13.0 at 12). Stated otherwise, total revenues for each of these classes would be increased an additional 33% above the difference between ComEd's proposed revenues and fully embedded costs. This approach would place the Extra Large Load and High Voltage classes on the path to full recovery of their costs at the conclusion of ComEd's next two rate cases. (Staff Ex. 29.0C at. 3-4).

Staff acknowledges that its proposal still would not fully recover costs from these three classes. The Extra Large Load class would proffer 79% of the costs to serve the class. This would be a higher percentage revenue increase than the 67.2% cost of service that ComEd proposes. The High Voltage class would proffer 88% of the costs to serve this class. This would be a higher percentage revenue increase than the 84.2% cost of service that ComEd is proposing. (*Id. at* .6-8 Staff Initial Brief at 133-35).

Kroger's Position

Kroger supports Com Ed's proposal to move toward cost-based rates. The proposed phase-in to costs for the Extra Large Load, Very Large Load, and Railroad delivery classes is consistent with the Commission's directive in the last general rate case. With respect to the exemplar revenue allocation, Kroger recommends that the movement toward differentiation in rates by voltage level also should be made gradually. (Kroger Initial Brief at 2-3).

The Commercial Group's Position

See the discussion herein regarding the Commercial Group's Position in the Railroad portion of this Section.

Analysis and Conclusions

We decline to implement a rate design that moves these two classes more than what ComEd has proposed to do. While we appreciate that Staff's proposal moves these classes closer to actual cost, Staff's proposal is not consistent with the principle of gradualism, which avoids rate shock. We also acknowledge that ComEd's rate design focuses on the DFC charge for these classes, which is "putting the cart before the horse," as the rates design here determined the revenue allocation, instead of having the cost of service determine the revenue allocation. However, we note that it appears that this was the case in ComEd's last rate case, where the model was created to have 25% increases toward cost of service for these two classes. We decline to alter that model at this time. We therefore decline to adopt Staff's proposal. We also decline to impose the caps that the IIEC proffers for rate increases. If limits are placed on some rate classes, other rate classes would be "making up the difference." We therefore approve ComEd's rate design.

In so ruling, we acknowledge, as REACT points out, that this movement toward ECOSS-based rates is, in fact, based upon faulty ECOSS studies. However the study approved herein is greatly-improved over what has been previously submitted in other dockets. And, rulings made herein have improved its accuracy. While the ECOSS approved here still needs further refinement, which shall take place in a future rate case, it is accurate enough to move, gradually, toward cost-based rates for these two classes.

The Revenue Shortfall

The Commercial Group's Position

The Commercial Group contends that the over 10MW load classes (the Extra Large Load and High Voltage classes) have received subsidies exceeding $23 million per year since the conclusion of Docket No. 01-0423. (CG Cross-Ex. 1 at 2). It states

that this annual subsidy, which does not include any subsidy to the Railroad Class, increased to over $29 million per year. According to the Commercial Group, only the customers in the Small to Very Large Load non-residential classes have been burdened with 100% of this subsidy burden. It concludes that because this burden has continued for many years, if anything, these classes should receive below-cost rates. (Commercial Group Initial Brief at 10-11).

REACT's Position

REACT witness Mr. Fults testified that, even with ComEd's "claimed" moderation of rate implementation, there is an extremely high-dollar impact on the over-10 MW customers (REACT Ex. 4.0 at 2- 6:10; *see also* REACT Ex. 1.0C, at 22-25 (discussing rate impact before ComEd adjustments in rebuttal testimony). REACT argues that this is contrary to the Public Utilities Act's requirement that the Commission "shall take into account customer impacts when establishing" delivery services charges. In support, REACT cites 220 ILCS 16-108(d). (REACT Memo at 10-11).

Staff's Position

Staff states that in ComEd's most recent proposal (ComEd Ex. 73.3, NR tab), the nonresidential rate classes that over-recover revenues are the Small Load, Medium Load, Large Load and Very Large Load delivery classes. This exhibit establishes that each of these classes has an over-recovery of revenues by 2.2%. All other non-residential classes (other than the Railroad, High Voltage and Extra Large Load) recover 100% of the cost to serve their respective classes.

Staff has no objection to the Small Load, Medium Load, Large Load and Very Large Load classes providing subsidies to the classes that suffer from a revenue shortfall from not moving 100% to cost of service. However, Staff recommends that the Commission consider the approach used in Staff Ex. 29.01C, (pp. 2-3 of 5) as the basis for this recommendation. In this approach, the same four classes (the Small Load, Medium Load, Large Load and Very Large Load classes) provide the subsidy for the classes that under-recover revenues, but the amount of subsidy that each class provides is lowered to 1.5%. This recommendation minimally affects only four classes, but it allows all other delivery classes to fully recover their respective costs to serve the customers in each class. Staff states that the subsidies that these four classes provide should decrease in ComEd's next rate case before eventually disappearing at the conclusion of the fourth and final step toward full revenue recovery for all rate classes. (Staff Initial Brief at 137-38).

Analysis and Conclusions

As we understand Staff's proposal, greater, but proportionate, recovery of the shortfall would come from four classes (the Small Load, Medium Load, Large Load and Very Large Load classes) where the rates proposed by ComEd already exceed the cost of providing service by 2.2%. This proposal minimally affects only four classes and it also allows ComEd to fully-recover costs. This proposal also applies the principle of gradualism that Kroger, the Commercial Group and others advocate. Staff's proposal will therefore be adopted.

b. Allocating Secondary Costs Among Customer Classes

Staff states that ComEd's choice of a non-coincident Peak (NCP) allocator rather than a Coincident Peak (CP) allocator for secondary costs in its Supplemental ECOSS is deficient and it should be replaced by the alternative approach for these costs presented in ComEd's Initial Filing.

Staff contends that this problem with the Supplemental ECOSS allocator was raised by both Commercial Group witness Mr. Baudino and IIEC witness Mr. Stowe. Mr. Baudino noted that the NCP allocator for these secondary costs in the Initial Filing appropriately "did not allocate the costs of secondary distribution lines to customers over 400 kW since these customers do not use the secondary distribution system." (*See,* Commercial Group Ex. 1.0 at 10). However, in the Supplemental ECOSS, ComEd revised the allocator to reflect a different definition of secondary customers which reflects the mandate in this Commission's 08-0532 (*Rate Design Investigation*) Order. Mr. Baudino opined that this reallocation is contrary to ComEd's findings that "100% of customers with demands of greater than 400 kW are estimated to bypass the secondary distribution system." (Commercial Group Ex. 1.0 at 14-15). He proposed to replace the supplemental allocator on the respective NCP demands of all secondary customers with the Initial Filing approach that allocates a larger share of costs to smaller customers. (*Id.* at 20). ComEd witness Mr. Alongi has acknowledged this argument by revising ComEd's exemplar ECOSS to incorporate Mr. Baudino's preferred allocator for these costs. (*See,* ComEd Ex. 49.0 at 23).

Staff finds this argument to adopt the original allocator contained in ComEd's Initial Filing for secondary distribution lines to be reasonable. Staff states that the Commission's rejection of ComEd's proposed definitions of primary and secondary service in docket 08-0532 does not undermine ComEd's previous conclusions concerning the allocation of these secondary costs. In that docket, Staff found this allocation to be reasonable. (Staff Ex. 26.0 at 14; Staff Initial Brief at 138-39).

Analysis and Conclusions

It appears that no party objects to use of the original allocator contained in ComEd's Initial Filing for secondary distribution lines. This proposal is reasonable and it is hereby approved.

c. Railroad Customers – ComEd's Use of Railroad Class' Facilities

ComEd's Position

In ComEd's last rate case, the Commission directed ComEd, the CTA and Metra to conduct a study to determine to what extent ComEd uses or needs Railroad Class facilities to serve other customers. (*See,* 2007 Rate Case Order at 220). ComEd and the Railroads agreed upon a study methodology that focused on a sample of 24 of the 71 railroad traction power facilities. The study showed that, on occasion, electricity flows through railroad-owned equipment to other non-railroad ComEd customers.

However, it did not establish that these flows were necessary to serve customers under normal conditions, or that restoration from power outages requires use of railroad facilities. (ComEd Exs. 14.0 Rev. at 24-25; 16.4). Based on that study, ComEd has proposed to reflect a cost allocation adjustment in its embedded cost of service study that reallocates approximately $452,000 from the railroad classes to other classes. (ComEd Initial Brief at 128-29).

ComEd states that it does not normally make a cost allocation adjustment when a customer unilaterally operates its facilities in a manner that makes it harder or easier for ComEd to serve other customers. However, four unique circumstances exist here. The Commission has directed that CTA and Metra receive special rate consideration, citing its 2007 Rate Case Order at 223. Also, ComEd avers, power is actually flowing through the railroads' equipment to serve other customers, rather than just incidentally helping other customers or improving local conditions. Further, it continues, the systems serving the railroads were installed in cooperation with ComEd over several decades, and the installation of the equipment cannot be deemed to be unilateral. Finally, the railroad equipment is constructed to utility standards; it is operated in a manner that is comparable to how a utility would operate it, which allows ComEd to make use of the equipment during contingency conditions. (ComEd Ex. 14.0 Rev. at 25-26).

ComEd contends that it determined the cost allocation in a manner that is analogous to how it allocates cost for equipment that is used in a shared manner for service to its retail customers and others. It argues that, due to the lack of precise data about the equipment's installation date and the original owner of this equipment, it adopted what it states is "a very favorable" assumption for the Railroads that the total costs equaled the costs that ComEd would incur to install 12kV busses and breakers on a completely un-depreciated basis. ComEd avers that "data" is not available to reflect the numerous contingencies that could result in its use of railroad facilities to serve other customers. Also, use alone would not reflect the dependability and insurance created from the railroads' facilities. ComEd therefore estimated a usage ratio (the ratio of ComEd's use to serve other customers over railroad use) of 1/3 to determine the shared costs. (ComEd Ex. 14.0 Rev. at 26-27). ComEd's proposed adjustment reallocates (to other customer classes) one-third of the annual carrying cost of the un-depreciated investment that would be required for it to install 12kV busses and breakers at locations equivalent to the railroad-owned facilities at the 71 railroad traction power substations. (ComEd Initial Brief at 128-130).

ComEd disagrees with Metra's argument that the credit should be either 50% or 100% of the cost of replacement facilities. According to ComEd, Metra has produced no quantifiable evidence to support this contention. ComEd states that it estimated a usage ratio to determine the shared costs, which arguably favors the Railroads. Also, ComEd's methodology was endorsed by Staff and the CTA. (ComEd Reply Brief at 130-31). ComEd does not oppose Staff's recommendation that the Commission order ComEd, the CTA and Metra to reconfigure the traction power substations. However, it

states that all of the affected parties agree that this should be a long-term goal, not something that is subject to a mandatory deadline. (*Id.*).

The Position of Metra

Metra points out that ComEd provides traction power to all of the Railroad Class' substations via at least two separate circuits. The circuits are tied together with a circuit breaker that is owned by the relevant Railroad Class member. The circuit breakers are typically operated in closed fashion, which allows electricity to flow from one circuit to the other. This effectively allows ComEd to use one of the circuits as a means of serving non-Railroad Class customers on the other circuit. (CTA/Metra Ex. 1.0 at 6, 10-11; Metra Initial Brief at 16).

Metra acknowledges that ComEd evaluated the cost to construct facilities that would be used to avoid the need to use Railroad Class facilities to serve other customers. ComEd has also proposed that the cost to serve the Railroad Class should be reduced by approximately $452,000. That amount, Metra continues, was computed by estimating the installed cost of the railroad electric facilities through which power may flow, which is about $10.721 million; allocating 33% of that installed cost, $3.57 million, as ComEd's share to reflect ComEd's use to serve other customers as being secondary to the railroads' primary use for traction power; and multiplying by 12.65% to convert the resulting ComEd share amount to an annual revenue requirement. In support, Metra cites ComEd Ex. 16.0 2d Rev. at 13.

Metra asserts that it should receive credit of at least 50% and more reasonably 100% of the cost of replacement facilities, rather than 33%, which means that the credit would be either $678,104 or $1,356,207. Metra avers that ComEd has been enjoying the free use of the Railroad Class' facilities for more than 40 years. (Metra Initial Brief at 16).

With regard to Staff's proposals to end ComEd's reliance on, and use of, Railroad Class facilities, Metra states that this option is not acceptable to the Railroad Class because ownership of the substations and transformers is critical to the reliability of the Railroad Class' service. In the past, Metra has purchased substations from ComEd to ensure the reliability of electricity supply to its stations. (CTA/Metra Ex. 2.0 at 13- 15).

Staff witness Mr. Rockrohr also suggested that another solution might be to ask the railroads to operate their 12,000 volt buses with one of the breakers open. Metra objects to this approach because the necessary reconfiguration changes for nonstandard service could cost millions of dollars. (CTA Ex. 4.0 at 5- 8). Metra argues that there is no operational reason to change the current configuration. At the evidentiary hearing, Staff witness Mr. Rockrohr testified that he did not particularly advocate implementation of any of his ideas. Instead, he testified that he thought that there should be a plan in place to eventually eliminate ComEd's reliance on the Railroad Class' facilities. (Tr. 835). Mr. Rockrohr acknowledged that the current configuration has been in place for several decades. (*Id.* at 829). He also was not aware of a single

operational problem that has occurred as a result of ComEd's reliance upon the Railroad Class' equipment. (*Id.* at 830).

Metra avers that it is not disputed that Staff's suggestions would be quite costly for both ComEd and the Railroad Class. For that reason, both ComEd and the two Railroad Class members have opposed Mr. Rockrohr's suggestion for a fixed schedule regarding Staff's suggestions. Instead, ComEd and the Railroad Class have agreed that the more reasoned approach is to change the operations of the traction power substations when new ones are added or existing ones are renovated and the costs justify the change. (CTA/Metra Ex. 2.0 at 16; ComEd Ex. 67.0 at 73-81). Metra argues that, if the Commission is inclined to issue an Order in that regard, the Order should not adopt a fixed schedule, but should instead allow the parties to change the operations of the traction power substations when new substations are constructed or existing ones are substantially renovated, and when the costs justify the change. (Metra Initial Brief at 18-21). With regard to Staff's position that ComEd should be required to present a plan to eliminate its use of Railroad Class facilities over time, Metra contends that ComEd's plan should initially focus on those railroad traction power substations, upon which, ComEd is most dependent to supply other customers. (Metra Reply Brief at 9-11).

The Position of the CTA

The CTA maintains that Staff's proposals regarding the Railroad Class load flow study should be rejected. It points out that Staff witness Mr. Rockrohr does not oppose a credit for the use of railroad, but, he recommends that ComEd and the CTA and Metra reconfigure their systems to eliminate the power flow through the traction power substations. While no party opposes this suggestion as a long-term goal, both ComEd and the Railroad Class members reject any proposal to impose a time deadline for such modifications, and that these modifications should be mandatory.

The CTA states that, pursuant to Mr. Rockrohr's recommendation, the configuration at the traction power substations would change from a closed loop to an open loop configuration. Under an open loop configuration, the bus at the substation would no longer allow flows from one circuit to another circuit. Such a change requires that:

> ComEd have sufficient capacity on at least one circuit to serve 100 percent of the traction power load on a long-term continuous basis. The "stand-by" circuit must also be rated to serve 100 percent of the traction power load on at least a short-term basis while the normal line is being repaired. To ensure passengers are not stranded or needlessly frightened, switching from a failed line to a backup line needs to happen quickly, on the order of a minute or less. Under the present scheme where two ComEd lines are connected through a closed bus tie, there is no outage at all when a ComEd line fails; the offending line simply causes the incoming line breaker to trip and the load is instantly transferred to the second line. With 59 of 61 CTA traction power substations presently operating in a closed loop configuration, it would take considerable time and money to engineer and install interlocks that would be required for

> safe operation of the equipment under the proposed open line breaker scheme. Many of ComEd's circuits would need to be modified as well. As new traction power substations are added, or if existing traction power substations undergo major renovation, this recommendation will be considered and has already been designed into three proposed substations.

(*See,* CTA Ex. 4.0 at 5-6; CTA Initial Brief at 20-22).

It asserts that the timing of specific upgrades to ComEd and the individual Railroad Class members' facilities should be based on the cost, versus the benefit, of making such a change. Because the closed-loop system is operating today, as it has for at least the last 50 years without major problems, the CTA argues that a costly, mandatory rebuild should not be ordered.

The CTA additionally contends that any changes proposed by Staff witness Mr. Rockrohr would need to be paid for by the CTA under ComEd's Rider NS. For some traction power substations, CTA witness Mr. Harper testified that "ComEd has quoted costs into the millions of dollars per circuit." (CTA Ex. 4.0 at 7-8). The CTA argues that the more appropriate resolution is to compensate the Railroad Class members for the use of the facilities, as was proposed by ComEd. In this way, ComEd's customers would continue receiving the benefits that the CTA traction-power substation's closed bus configuration provides. As present equipment is retired and replaced or as new substations are added, an automatic transfer scheme similar to Mr. Rockrohr's proposal will be considered and, if appropriate, on a substation by substation basis, implemented. (CTA Initial Brief at 20-22).

Staff's Position[10]

Staff recommends requiring ComEd to present a plan to eliminate its current practice of supplying its other customers through use of equipment at railroad traction power substations that are owned, operated, and maintained by the CTA and Metra. In support, Staff states that the railroad traction power substations included in the power flow study discussion identified as ComEd Ex. 16.4 can be generally grouped into two categories. Railroad traction power substations in the first category are those that ComEd uses to supply other customers, but ComEd is not dependent upon these facilities to do so. In other words, ComEd could supply its other customers with other distribution facilities that it owns, if it needed to do so. Railroad traction power substations in this category can receive a reliability benefit because they are able to receive electricity from either one of the two separate ComEd circuits to which they are connected. Each of ComEd's circuits that supply the railroad traction power substation in this category has adequate capacity to supply both the railroad traction power substation and also those of ComEd's other customers that are connected directly to it. Staff opines that the railroad traction power substations in this category probably

[10] Originally, Staff proposed a reduction of the $452,069 to $316,437. (*See,* Staff Initial Brief at 139-40). However, in Staff's Reply Brief, this contention was not mentioned. (*See,* Staff Reply Brief at 79). We therefore conclude that this issue is resolved. However, we again admonish all parties to state, affirmatively, when an issue has been resolved, as opposed to merely omitting to mention an issue.

receive the type of service that was intended when the closed-loop supply (ComEd's circuits tied together through the railroad traction power substation 12,000 volt bus) was initiated.

Staff further states that Railroad traction power substations in the second category are those that ComEd depends upon in order to supply its other customers. ComEd's power flow study indicated that, for some of its circuits that supply railroad traction power substations, ComEd has not maintained adequate capacity to supply both the railroad traction power substation and the load of its other customers. For railroad traction power substations in this category, ComEd depends upon its ability to supply its customer through use of railroad traction power substation 12,000 volt buses. For railroad traction power substations in this category, ComEd fully depends upon CTA and Metra facilities to supply its other customers. These are facilities that ComEd does not own, maintain, or control. ComEd's power flow study indicated that ComEd was dependent upon CTA and Metra equipment at 4 of the 24 railroad traction power substations in its study. Because ComEd studied power flows at only approximately one-third of the 71 railroad traction power substations that it supplies, ComEd has assumed that it depends upon twelve of the railroad traction power substations to supply its other customers. In support, Staff cites ComEd Ex. 16.4. (Staff Initial Brief at 168-175).

Staff avers that ComEd's dependence upon customer-owned equipment that it does not maintain or control to supply its other customers is a poor utility practice. In addition, Staff pointed out that, at those railroad traction power substations where ComEd depends upon CTA and Metra equipment to supply its other customers, the railroad customers do not receive the intended reliability benefit from ComEd's closed-loop supply. Though the railroad traction power substation is still connected to two distribution circuits, ComEd is able to support the load of the railroad traction power substation on only one of the two distribution circuits. (Staff Ex. 6.0 at 26-31; Staff Initial Brief at 168-175).

Staff witness Mr. Rockrohr provided two examples of alternatives to ComEd's existing circuit configuration. One alternative is that ComEd could convert its supply to an open-loop configuration, meaning that one of the breakers on the customer-owned bus would be opened, so that current would not normally flow through CTA and Metra equipment to supply ComEd's other customers. Another alternative is that ComEd retains the existing closed-loop arrangement, but assumes ownership and maintenance of the bus and breakers at railroad traction power substations that it uses to supply other customers. (Staff Ex. 6.0 at 30-31).

In response to ComEd witness Mr. Born's opinions about operating in an open-loop configuration, Mr. Rockrohr stated that an open-loop configuration would require ComEd to maintain adequate capacity on each of its distribution circuits that supply the railroad traction power substations, as, ComEd would be unable to normally supply its other customers through use of railroad equipment. The railroads would also receive

the intended reliability benefit of their dual-circuit supply from ComEd. (Staff Ex. 21 at 20-22).

Staff avers that Mr. Rockrohr did not intend to represent that the two solutions he presented in direct testimony were the only two solutions available to ComEd and the railroads. For example, Staff continues, ComEd could install automatic throw-over switchgear outside of the railroad traction power substations so that all switching between ComEd's circuits would take place on ComEd's distribution equipment, rather than through the railroads' bus and breakers. He also stated that it is difficult to estimate how long it should take ComEd to eliminate its use of railroad customer equipment to supply other customers, regardless of the solution ultimately chosen, but a reasonable plan would cover a 7-10 year period. (*Id.*).

Staff states that it is concerned by ComEd's and the railroads' recommendation that ComEd continue to use customer-owned and customer-maintained facilities in an open-ended fashion. While Staff understands that the Railroad Class members desire a reduction in ComEd's charge as compensation for ComEd's historical use of its facilities, Staff does not agree that, looking forward, continued compensation to the railroads by other customer classes is a good long-term solution. Members of other customer classes might understandably disagree with a permanent allocation of railroad service costs to them, especially if there are reasonable economical alternatives to eliminate ComEd's use of railroad facilities, and therefore the need for such an allocation. (Staff Ex. 21.0 at. 21-22). Also, ComEd's dependence upon railroad facilities to avoid overloads on its own distribution system is not a good utility practice, regardless of the compensation other customer classes provide to the Railroad Class. (Staff Ex. 6.0, p. 29) Staff further state that the contemplated re-allocation of costs from the railroad class to other customer classes in this proceeding appears to be based upon the value of the railroads' equipment, which is not necessarily the value of equipment that ComEd would need to install if it were unable to use railroad equipment. (CTA/Metra Ex. 2.0 at 13).

Staff also points out that, after conducting its power flow studies, ComEd concluded that, for approximately 12 of the railroad traction power substations, it would be unable to supply its other customers, if the railroad equipment became unavailable during heavy loading periods. (*See,* ComEd Ex. 16.4 at 2). In the future, as the level and location of customer loads on ComEd's distribution circuits change over time, ComEd could become dependent upon additional/different railroad traction power substations to supply its customers. (Staff Ex. 6.0 at 27-28). Staff considers this to be a serious reliability risk. If the customer-owned equipment were to fail and become unavailable for ComEd to use, ComEd's other customers might be without service for an extended period of time. Staff opines that ComEd should modify its distribution facilities so that it can supply its other customers, even if railroad equipment became unavailable. (Staff Ex. 21.0 at 22).

Staff acknowledges that the CTA has expressed concern over the potential costs that ComEd would assign to it under Rider NS to cover modifications to existing

distribution circuits. It is not clear to Staff why there would be any ComEd charges under Rider NS from ComEd, as the CTA and Metra already have connections to two different ComEd circuits, and Staff's recommendations require ComEd to make no change to that configuration. ComEd estimated it would need to spend $2.1 million to modify its circuits to eliminate the overloads that would exist on its circuits, if it no longer supplied customers through railroad traction power substation. (*See,* Tr. 1707-1708). Staff is not aware of any claim by ComEd in this proceeding that it would charge the CTA "tens of millions of dollars" under Rider NS. Staff also does not believe that any such charge could be appropriately made. (Staff Reply Brief at 89-92).

Staff further seeks to clarify that ComEd's computation of the $452,000 amount was not based upon its cost to construct facilities to avoid the need to use Railroad Class facilities, as Metra represents, but rather its estimate of "...the installed cost of the railroad electric facilities through which power may flow, which is about $10.721 million..." (*See,* ComEd Ex. 16.0, 2nd Rev at 13). Staff avers that this clarification is important because ComEd's $10.721 million estimate is more than five times higher than ComEd's $2.1 million estimate to eliminate its dependence upon those railroad electric facilities. (Tr. 1707-1708; Staff Reply Brief at 89-92).

Staff concludes that, while it is sensitive to the CTA's and Metra's concerns regarding the potential costs involved in eliminating ComEd's use of their railroad traction power substations to supply other customers, Staff is also sensitive to the ongoing subsidies that other customer classes may be required to provide to the CTA and Metra, as a result of ComEd's ongoing use of railroad facilities. Views about whether costs justify modifications to ComEd's existing closed-loop service to the railroad traction power substations may depends upon whether a party is receiving or providing the subsidy. Staff is therefore opposed to the proposed subsidy being used as a long-term answer to ComEd's use of railroad facilities to supply its other customers. (Staff Reply Brief at 89-92).

Analysis and Conclusions

Metra and the CTA (the total Railroad Class) have a unique relationship with ComEd whereby ComEd uses facilities on the CTA's and Metra's premises to provide electricity to other customers. This relationship should be approached with caution because disentanglement of this relationship could prove to be costly. Metra and the CTA also assert that, while this relationship is not desirable, except for the situation discussed below, at this time, there is no evidence of operational harm resulting from this unique relationship.

It is not disputed that ComEd is dependent upon some of these facilities (approximately 12 facilities) in that, it needs these facilities in order to provide electricity to other, non-railroad customers. This condition has the obvious potential to harm the general public, if it has not already done so in the past. In this situation, ComEd is dependent upon entities, over which, it has no control. It is also worth mentioning that both the CTA and Metra, the entities that ComEd is dependent upon, are higher-end users of electricity.

Therefore, within 60 days from the date that a final order issues in this docket, a workshops shall commence, in which, the safe operation of these facilities (the facilities, upon which ComEd is dependent in order to provide electricity to other customers) is fully investigated and solutions are explored. These workshops should also include long-term goals regarding the railroad facilities, upon which, ComEd is not dependent on railroads in order to provide service to other customers. We note that while informal resolution through workshops is desirable, if no resolution of these issues occurs through workshops, a docket may be opened to resolve what issues are outstanding.

With regard to the remaining facilities, as Staff witness Mr. Rockrohr pointed out, this situation is undesirable for ComEd and for the CTA and Metra. At this time we require all three parties to work together to provide updates as to ComEd's use of the facilities and any other pertinent information, on a quarterly basis. We also encourage these parties to arrive at a meaningful solution to this situation on a case-by-case (substation by substation) basis.

However, at this time, we decline to require these parties to select any particular avenue, or, to impose a deadline upon them. Decisions in this regard involve complicated legal questions (*e.g.,* what party will be responsible for maintenance and repair of these facilities, what role these facilities might play in an emergency, to name a few) that are beyond the scope of the evidence presented here. These issues also require a thorough and well thought-out plan, which could differ on a case-by-case basis, based upon such factors as the location of the facility on the CTA or Metra premises, the age of the particular facility, and ComEd's level of need to use a particular facility locally.

Regarding the amount of the credit that the Railroad Class customers should receive for use of these facilities, we note at the outset that any determination herein shall not serve as precedent for future rate cases. While it may be appropriate in future rate cases to allocate some credit for use of these facilities, the amount of the credit may vary, as these substations are reconfigured and redesigned. In addition, as Staff correctly points out, a credit is not a permanent solution.

ComEd's estimated value, as we understand it, is a percentage of the cost of replacement facilities. At issue is not this (albeit very preliminary) estimated cost of replacement facilities. Rather, it is the percentage of this cost that is at issue. ComEd proffers a credit of 33% of this cost, although this figure is multiplied by 12.65%. (*See,* ComEd Ex. 16.0 Rev. at 13). Metra asserts that a greater percentage is warranted, as, ComEd has had unfettered use of these facilities for at least 40 years without any compensation. Metra contends that 50% of this figure or 100% is warranted.

We agree with Metra that some additional amount of compensation is warranted, due to the fact that ComEd has been using these facilities for decades, without any compensation. However, as Staff has pointed out, the CTA, Metra, ComEd and the general public are best served by finding a solution, or solutions, to this dilemma. These interests are not well-served by a great amount of compensation to Metra and the CTA, as, such an amount only provides the CTA and Metra with the motivation to continue being compensated, instead of solving the problem. Therefore, we conclude

that the correct credit should be the 50% figure, or, $678,104. We reiterate that this compensation is but a temporary situation.

Finally, the CTA's evidence stating that ComEd will charge millions of dollars pursuant to Rider NS, if Staff's recommendations were adopted was not considered. This bit of evidence flies in the face of the rules of evidence. This Rider (Rider NS) states what it states, irrespective of what a person testifies about it. Therefore, this testimony is not the best evidence. Also, there is no indication that the CTA witness involved, Mr. Harper, actually was the recipient of these Rider NS cost estimate conversations. In any event, this evidence is rank hearsay, as it is an out of court statement used to prove the truth of the matter asserted. It may very well be double or triple hearsay, as there is no evidentiary foundation for this statement.

d. Dusk to Dawn Street Lighting

The City of Chicago's Position

The City of Chicago avers that, in the Rate Design Investigation Order, the Commission concluded that in its next rate case, ComEd should include $183,000 in its embedded cost of service study as the amount that ComEd incurs for secondary facilities used to serve City residential and arterial street lights. In support, it cites the *Rate Design Investigation* Order at 53. Despite what the City terms as a clear mandate, ComEd only reluctantly complied with the directive, stating that it disagreed with the Commission's conclusion. In support, the City cites ComEd Ex. 16.0, 2nd Rev. at 32. Also, allegedly, when complying with the *Rate Design Investigation* Order, ComEd attempted to modify the conclusion reached in that Order. The City further avers that each of ComEd's proposed modifications increase the secondary costs that are allocated to the City of Chicago's street lights. (City Initial Brief at 13).

The City points out that the secondary costs that ComEd incurs to serve street lighting customers was one of the issues that was litigated for 18 months in the *Rate Design Investigation* case. In its Order in that case, after hearing all of the arguments, the Commission found that City witness Mr. Bodmer's proposed method for determining secondary costs for street lighting customers was the fairest method for doing so. In that case, ComEd made numerous complaints about Mr. Bodmer's proposed method in that case. In support, it cites the *Rate Design Investigation* Order at 47-48, 53. The City avers that, in that case, the Commission considered ComEd's arguments, found that they lacked merit, and adopted the City's position. Starting from that point, the City concludes that ComEd should face an uphill battle to convince the Commission that it should reverse a decision it so recently made. (City Initial Brief at 19).

City witness Mr. Bodmer advocated modifications to his calculation of secondary costs for City residential and arterial lights that the Commission adopted in its *Rate Design Investigation* Order. The City contends that Mr. Bodmer's changes were designed to determine ComEd's costs with greater precision. Some of Mr. Bodmer's changes actually increased costs to the City, while others reduced the City's costs.

It avers that ComEd witness Mr. Alongi voiced displeasure with what he called the "Chicago Method" for calculating secondary costs for City residential and arterial street

lights. Mr. Alongi described what he opined were several flaws with the "Chicago Method." Essentially, the City states, he asked the Commission to revisit its decision adopting Mr. Bodmer's analysis in the Rate Design Investigation proceeding. (*See,* ComEd Ex. 16.0 2nd Rev. at 32-34). He recommended that the "Chicago Method" should be modified to reflect the costs that he contended are incurred by ComEd in connecting City residential and arterial lights to ComEd's system. (City Initial Brief at 13-14).

The City contends that its witness Mr. Bodmer agreed with ComEd's criticism that he failed to include an operations and maintenance (O&M) component in his analysis; he therefore modified his analysis to reflect O&M costs. He also changed his method to include a provision for general and intangible plant. While Mr. Bodmer conceded that ComEd made certain valid criticisms of his method, he opined that ComEd's other assertions were incorrect.

One of Mr. Alongi's errors, according to the City, was his assertion that ComEd employees make the connection between the wire for City residential and arterial street lights and ComEd's system. Mr. Alongi averred that Mr. Bodmer's method failed to reflect the costs that ComEd incurs in making such connections. In order to ascertain the validity of this assertion, Mr. Bodmer met with City Engineers to discuss the process, by which, City residential and arterial street lights are connected to ComEd's system. (*See,* City Ex. 1.0 at 46). In his investigation, which entailed conversations with City Engineers, Mr. Bodmer learned that for as long as any City employee could remember, City employees and contractors have been making the connection between the City wire and ComEd's facilities. He was informed that, because ComEd cannot make the City-ComEd connection on a timely basis, the City of Chicago has taken that task upon itself. Thus, the City concludes, contrary to Mr. Alongi's assertion, ComEd does not incur any costs in connecting City of Chicago street-lighting wire to the ComEd system. In fact, it is the City of Chicago that incurs those costs. Because the City makes these connections, Mr. Bodmer recommended that the City should be allocated $0 for this service, which ComEd does not actually provide. (City Initial Brief at 15).

The City contends that a second error in ComEd's calculation of secondary costs concerning the cost of the wire that is used to connect City facilities to the ComEd system. In the Rate Design Investigation case, Mr. Bodmer assumed that the cost of wire was $1.82 per foot. (City Ex. 1.0 at 54). For this case, using the same approach with updated data, Mr. Bodmer assumed that the cost of wire was $1.78 per foot. He derived his "number" from a combination of primary and secondary wire in the City because of the odd circumstance that the cost of secondary wire in the City is higher than the cost of primary wire. (City Initial Brief at 15).

However, the City states, ComEd assumed a cost of wire of $3.05 per foot, which is an amount that is significantly higher than Mr. Bodmer's assumption. Mr. Bodmer testified that the reason that ComEd's number was so much higher was due to one entry in ComEd's USOA Account 365. In particular, the "Other" entry for secondary wire in the City Account 365 was $6.69 per foot. Mr. Bodmer opined that ComEd's number was skewed because of the $6.69 figure, a clear "outlier" in USOA Account 365. He included a table in his testimony that showed the cost of wire with and without the very expensive wire from the "Other" entry in Account 365. (City Ex. 1.0 at 55). The City

contends that Mr. Alongi's contention that the City should be allocated $250,000 for connections made between City street light facilities and the ComEd system is inconsistent with reality, as it is the City and the contractors who make those connections. It concludes that therefore, allocating these costs to the City for work that there is no evidence that ComEd actually does is patently unfair. (City Initial Brief at 15, 17).

Finally, Mr. Bodmer adjusted his approach to the wire between ComEd's transformer and the City's connection box, where the connection is between ComEd's wire and the wire for the City's residential and arterial street lights. In this process, he used ComEd's estimate that the piece of wire that is needed averages 113 feet in length. However, he pointed out that a piece of wire does not only serve City facilities. Residences and businesses are also served from that wire. He recommended that the length of wire should be divided by three to account for the other taps on the wire. (City Initial Brief at 15). The City asserts that ComEd never responded to Mr. Bodmer's analysis of the cost of wire, which is contained in Mr. Bodmer's direct testimony. (City Initial Brief at 17).

According to the City, ComEd witness Mr. Alongi "chided" Mr. Bodmer for not including alley lights in his analysis. Mr. Alongi stated that Mr. Bodmer "assumed" that ComEd uses no secondary wire to serve City alley lights. He then testified that ComEd sampled 16 alley lights in the City and found that the average length of secondary wire from the transformer to the light is 109 feet. Adjusting Mr. Bodmer's method to include alley lights, according to Mr. Alongi, increased the secondary costs assigned to City's Dusk-to-Dawn lighting to $900,302, or $762,686 more than ComEd's cost study allocated to the City's alley-lighting and its non-alley lights. (ComEd Ex. 49.7 Rev.).

However, Mr. Bodmer opined that Mr. Alongi's estimate of the secondary costs that ComEd incurs to serve City alley lights is inaccurate. He noted that ComEd Ex. 49.7 Rev., which sets forth ComEd's changes to Mr. Bodmer's method, allocated one-third of secondary costs to City alley lights. According to Mr. Bodmer, this allocation is patently ridiculous. In Mr. Bodmer's testimony in the *Rate Design Investigation* case, he testified that alley lights should be distinguished from residential and arterial lights because they have a completely different configuration. This Commission agreed with him in its *Rate Design Investigation* Order, because it approved Mr. Bodmer's method for calculating ComEd's secondary costs to serve City street lights. Mr. Bodmer also testified that:

> Mr. Alongi's rebuttal testimony with respect to alley lights issue simply confirms that the alley lights must be distinguished from the non-alley lights in the cost-of-service analysis. The small amount of power used by a 250 or a 150 watt bulb cannot be allocated the same amount of power line costs as other consumers along the wire span who use a whole lot more energy than a single light bulb. The very small amount of power used by a single alley light is significantly less than the power used by integrated systems of residential or arterial lights.
>
> (*See,* City Initial Brief at 18).

The City also contends that, upon cross-examination, Mr. Alongi implicitly conceded that it was not realistic to allocate one-third of secondary wire costs to City alley bulbs. Mr. Alongi was asked to review ComEd Ex. 49.8, which included a sample of four alleys in the City of Chicago. (Tr. 2042-46). He testified that there are roughly 20 residences or businesses that are provided with distribution service from the wires that transverse the alleys in ComEd's sample. He admitted that the demand for five alley lights in one of the sample alleys would be 250 watts (the size of the bulb) times 5 (the number of the bulbs) or 1.25 kW. Mr. Alongi then testified that the average demand for a residence is 3 kW. Multiplying the approximately 20 houses on each block times 3 kW yields a demand of approximately 60kW for the residences served by the same wire serving the five alley lights. (*Id.* at 2052). The City argues that comparing the 60 kW demand for the business and residences to the 1.25 kW demand for the five alley lights shows that the demand for residents and businesses is 48 times greater than that for alley lights. The City concludes that a fairer allocation of secondary costs to alley lights would be 2%, not the 33% that ComEd advocated. It concludes that ComEd's decision to allocate one-third the cost of the wire is not correct. (City Initial Brief at 19).

The City further contends that, on cross-examination, it was demonstrated that it is not realistic to allocate one-third of secondary wire costs to City alley bulbs. Mr. Alongi was asked to review his ComEd Ex. 49.8, which included a sample of four alleys in the City. Jan. 19, 2011. Mr. Alongi was then shown an image take from Google Earth of his four sample alleys. He agreed that there are roughly 20 residences or businesses that are provided with distribution service from the wires that transverse the alleys in ComEd's sample. He also admitted that the demand for five alley lights in one of the sample alleys would be 250 watts (the size of the bulb) times 5 (the number of the bulbs) or, 1.25 kW. Mr. Alongi then testified that the average demand for a residence is 3 kW. Multiplying the approximately 20 houses on each block times 3 kW yields a demand of approximately 60kW for the residences served by the same wire serving the five alley lights. (*See,* Tr. 2042-44). The City avers that thus, this proves that comparing the 60 kW demand for the business and residences to the 1.25 kW demand for the five alley lights shows that the demand for residents and business is 48 times greater than that for alley lights. (Tr. 2046, 2052). The City concludes that thus, a fairer allocation of secondary costs to alley lights would be 2%, not the 33% that ComEd advocated.

It further states that, in order to properly reflect the secondary costs that ComEd incurs to serve City residential and arterial street lights, the Commission should adopt the table from page 57 of Mr. Bodmer's Direct Testimony. (City Ex. 1.0). That table sets forth the method that he used to determine those costs. The City also avers that, if the Commission decides to allocate a portion of secondary costs to alley lights, it should use the same approach it adopted as to residential and arterial lights in its *Rate Design Investigation* Order. (City Reply Brief at 13-14).

ComEd's Position

ComEd states that, in the ComEd *Rate Design Investigation* Order, the Commission directed it to exclude from its embedded cost of service study the secondary system costs that were attributed in that docket to the Dusk to Dawn Lighting

Class, as was calculated by the City of Chicago. ComEd calls this process the "Chicago Method." Any excluded costs would be reallocated to other customer classes. (*See,* ComEd *Rate Design Investigation* Order at 51-54). ComEd argues that it has complied with the Order in its proposed cost allocation, but, it nevertheless asks this Commission to reconsider its decision due to what it terms are several flaws in the "Chicago Method." Thus, in essence, ComEd asks this Commission to revisit a previous decision, without any new facts or laws.

ComEd's opposition to use of the "Chicago Method," it asserts, is due to the fact that the "Chicago Method" results in an unfair and illogical reallocation of secondary facilities and service connection costs from the Dusk to Dawn Lighting Class to other delivery classes. (ComEd Initial Brief at 119). According to ComEd, the defects in the "Chicago Method" include failure to include the costs that ComEd incurs to provide service to the Dusk to Dawn Lighting Delivery Class, including ongoing maintenance and operating costs, and various other costs, including wire. Also, the secondary costs are recognized in ComEd's ECOSS using specific accounts of the Uniform System of Accounts. ComEd argues that this information does not reveal the customers or classes of customers who take service directly or indirectly from specific assets at any particular time CP and NCP-based allocators are generally used to allocate these costs. ComEd concludes that therefore, the allocation of certain secondary costs for one subset of customers results in an inappropriate adjustment to ComEd's CP and NCP allocators within the existing ECOSS. In support, it cites the testimony of its witness Mr. Alongi, ComEd Ex. 73.0 2nd Rev. at 38-39.

However, ComEd argues that, if the Commission nonetheless decides to retain its previously-approved "Chicago Method," it offers two recommendations to improve it. The "Chicago Method, it states," should not assume a zero cost for service connections. Also, the "Chicago Method" should apply to alley lights, which are included in the customer class and connect to the same secondary distribution system as the arterial lights. (ComEd Initial Brief at 119-120).

Analysis and Conclusions

We note at the outset that, despite 18 months of litigation regarding this issue in the *Rate Design Investigation* docket, ComEd continues to argues that the conclusions reached on this issue in that docket were incorrect. While we acknowledge that, in the appropriate circumstance, such as, a change in the applicable law, a matter should be revisited, that is not the situation here. This is true because there is no new significant evidence here, or a change of law, indicating that what ComEd terms as "the Chicago Method" which was adopted by the Commission in the *Rate Design Investigation* docket is incorrect. We note that there is no evidence indicating that the "Chicago Method" unfairly or illogically reallocates costs.

ComEd asserts that City witness Mr. Bodmer failed to reflect the ComEd labor that is involved in connecting its wire for arterial street lights to ComEd's system. Yet, there really is no evidence that ComEd employees ever make these connections. Mr. Alongi's estimates as to what the labor costs would be does not establish that there are, in fact, such labor costs. And, Mr. Bodmer's conclusion that these connections are

performed by City employees, based upon his investigation, is uncontroverted. We therefore conclude that ComEd's assertion in this regard lacks evidentiary support.

ComEd also argues that Mr. Bodmer's calculations as to the cost of the wire that is used to connect City of Chicago facilities to ComEd's system is inaccurate. Because the evidence indicates that Chicago employees make these pertinent connections, there really is no evidence here that the wire that City of Chicago employees install is actually supplied by ComEd. Absent affirmative evidence that ComEd provides this wire to the City, we decline to conclude that ComEd pays for this wire, as, it is illogical to assume that a party that does not install wire pays for it. We therefore disallow any cost of wire regarding this issue.

Finally, ComEd maintains that the City underestimated its costs for alley lighting. However, as the City points out, its cross-examination of the pertinent ComEd witness on this subject, Mr. Alongi, discredited this argument. In that cross-examination, it was established, with certainty, that alley lights do not use very much electricity. It was also established, with certainty, that the amount that ComEd has claimed for alley lights is far greater than what is actually used to light Chicago alleys. So that the record is clear, Mr. Alongi's testimony in this regard is incredible, due to the cross-examination on the part of the City of Chicago.

A post record ALJ data request shall issue requiring the parties to make the necessary computations, starting from the original costs that each party has proposed, and then, adjusting these costs based upon the findings herein regarding this issue. All parties are cautioned, in the future, to state what dollar amount is at issue and what the adjustment proposed is. So that the record is clear, the "Chicago Method" is again adopted here, with any pertinent adjustment made in the Briefs on Exception.

We further caution that use of the "Chicago Method" by other municipalities must take into account alley lighting. Many municipalities in Illinois do not have alleys, and therefore, do not have alley lighting. Other municipalities using this method must state whether they have alleys and appropriately account for the difference used by the City of Chicago and the respective municipality(s).

3. Collection of Illinois Electricity Distribution Tax

ComEd's Position

ComEd seeks to recover the Illinois Electricity Distribution Tax in the same manner that this tax is imposed on ComEd itself - on the basis of total kilowatt-hours delivered. ComEd Ex. 16.0 3rd Rev. at 18. The proposed change would have no impact upon residential, watt-hour, and lighting customers because costs associated with the Illinois Electricity Distribution Tax are already recovered through per kWh DFCs for these customers. Id. at 19. However, no per kWh charge exists for delivery service for demand-based nonresidential delivery classes. Instead, the tax is currently recovered through *per kW* DFCs for these classes. Accordingly, low load factor customers are currently subsidizing the high load factor customers with respect to recovery of this tax from these customers. ComEd's proposed recovery of the Illinois Electricity Distribution Tax associated with these customers would eliminate this intra-class subsidy. ComEd Ex. 49.0 Rev. at 17.

ComEd notes that the Commission already has approved a similar treatment for recovery of the Illinois Electricity Distribution Tax in the recent Ameren rate cases. Central Ill. Light Co., et al., Docket Nos. 09-0306 (cons.), Order dated Apr. 29, 2010("Ameren Order") at 243. Further, Staff agrees that ComEd's proposal is reasonable.

ComEd has proposed that the Illinois Electricity Distribution Tax be recovered through a separate line item on customer bills. The proposed change would have no impact upon residential, watt-hour, and lighting customers because costs associated with the Illinois Electricity Distribution Tax are already recovered through per kWh DFCs for these customers. ComEd Ex. 16.0 3rd Rev. at 19. ComEd contends that no party has produced credible evidence in this proceeding that would warrant a change in ComEd's proposed methodology for the recovery of the Illinois Electricity Distribution Tax.

CTA

ComEd inappropriately proposes to charge the CTA what ComEd calls the Illinois Electricity Distribution Tax (IEDT) on a per kilowatt hour basis as a separate line item on the CTA's bill. This attempt to collect the IEDT charge, which is actually the Public Utilities Revenue Act tax that was established when the electric utility industry was deregulated in 1997 from the CTA, 35 ILCS 620/2-1 *et seq*., is improper for two reasons. First, the CTA's enabling statute exempts the transit authority from paying this type of tax. Second, if the tax were to be imposed, it should not be assessed solely on a kilowatt hour basis.

The CTA, as a municipal corporation formed pursuant to the Metropolitan Transit Authority Act, 70 ILCS 3605, is except from paying the tax. Section 33 of the Transit Act states:

> The Authority shall be exempt from all state, county, municipal and other units of local government taxes. . . All property of the Authority is declared to be public property devoted to an essential public and governmental function and purpose and shall be exempt from all taxes and special assessments of the State, any subdivision thereof, or any unit of local government.

Because as a matter of law the CTA is exempt from paying this tax, ComEd's proposal to collect the tax from the CTA must be rejected.

Even if the tax were appropriately assessed against the CTA, ComEd's proposal to collect it on a per kilowatt hour basis would not be a correct allocation. The Illinois Industrial Energy Consumers witness Robert Stephens proposes that the tax be collected in two parts. The first part would allocate a portion of the total amount of the tax using a "plant in service" allocator. This approach would more accurately reflect the fact that the Public Utilities Revenue Act tax uses, as a floor for the amount to be collected, what the utility paid in 1997 under the old invested capital tax structure, i.e. $99.5 million. The second part would collect amounts in excess of the $99.5 million

based on energy use. IIEC Ex. 2.0, Stephens Direct at 25/557-26/599. As Mr. Stephens testifies, this approach better reflects the cost-causation of the tax charge. "This allocation method is consistent with cost causation, since a utility's tax liability in any given year is not driven exclusively by its energy deliveries. In fact, for ComEd, the correlation between its energy deliveries and the annual tax burden is relatively weak." IIEC Ex. 5.0, Stephens Rebuttal at 31/679-682.

IIEC's Position

According to IIEC, since the elimination of the personal property tax in 1970, Illinois utilities have been subject to a tax on invested capital, pursuant to the Public Utilities Revenue Act (35 ILCS 620/1 et. seq.). Prior to 1998, for electric utilities, the tax was assessed at a rate of 0.8%. In 1997, in conjunction with the Electric Service Customer Choice and Rate Relief Law of 1997, (the "Restructuring Law" - Public Act 90-561), the Illinois legislature determined that it would change the computation of the tax to keep it competitively neutral, while maintaining essentially the same level of tax revenues (adjusted for inflation) from each of the Illinois electric utilities, individually and in the aggregate, through a series of charges designed to be applied to each utility's delivered energy. (35 ILCS 620/1(a)). ComEd has allocated this tax in delivery service rates since 1999 on the basis of kWh delivered. IIEC proposes to modify the allocation in this case, to allocate a portion of the tax on the basis of allocated utility plant in service and a portion on the basis of kWh delivered, for the reasons described further below.

a. Reasonableness of Current Allocation

According to IIEC, the level of the IEDT was fixed at the level of tax imposed on electric utilities, on the basis of their invested capital (plant investment), prior to 1998. It has escalated each year by 5%, or the percentage increase in the Consumer Price Index ("CPI"), whichever is less. Thus, the total amount of tax imposed on Illinois electric utilities is capped at the level of tax on invested capital experienced by each utility in 1997, subject only to inflationary adjustments. The tax is not and never has been, exclusively a function of kWh delivered.

IIEC opines that, while the growth in the level of the tax beyond the 1997 level is somewhat related to growth in kWh deliveries, that relationship exists only to a point. As noted above, the tax is essentially capped at the pre-1998 level of the invested capital tax adjusted for inflation. Therefore, says IIEC, per kWh sales/deliveries can play only a small role in the determination of the amount of tax paid by each utility.

IIEC asserts that, if the cap is reached in any particular year, increases in the number of kWh delivered by a utility do not automatically translate to additional IEDT responsibility. Collected tax revenues in excess of the cap in a given year are refunded to the utilities in proportion to their tax payments. Since the cap has been exceeded in every year since the IEDT was initiated, increases in kWh sales have not increased the utility's real tax burden beyond the cap in any year since 1997. Thus, ComEd's current tax responsibility is not strictly a function of increases or decreases in kWh sales, according to IIEC.

IIEC posits that there are additional reasons, grounded in un-rebutted empirical evidence, why the claim that the IEDT is a direct function of kWh deliveries is incorrect. As IIEC witness Stephens demonstrated, when the IEDT cap is exceeded (as it regularly is) a utility's tax burden is dependent more on its proportional share of tax payments, in relation to other utilities, than it is on the change in its own kWh deliveries. If the utility maintains the same proportional share of deliveries over time, it makes no difference whether it delivers more or fewer kWh in a year; its tax burden remains the same, adjusted only for the lesser of a non-energy related 5% or the percentage change in the CPI. In fact, it is possible for the utility's tax burden to go down when its deliveries of kWh go up and *vice versa*.

Furthermore, according to IIEC, there is not even a high statistical correlation between ComEd's tax burden and its kWh deliveries. IIEC witness Stephens presented a linear regression analysis of the relationship between IEDT paid by ComEd and total billed energy by ComEd for the years 2001 through and including 2009. This un-rebutted analysis demonstrated that kWh deliveries had only a weak explanative value for changes in the IEDT, which has a base amount that is exclusively a function of ComEd's pre-1998 invested capital, in IIEC's view. Thus, contrary to the position of Staff and ComEd, IIEC declares that ComEd's kWh sales do not cause (or even adequately explain) the levels of ComEd's IEDT burden.

In response to Staff's claim that changes in plant investment do not lead to changes in tax liability, IIEC points out that the bulk of ComEd's tax is not due to changing investment but to a static plant investment tax amount retained by the revised statute. Therefore, according to IIEC, the Commission is left with a choice; (1) allocate the tax on the basis of the kWh factor that modifies less than the last 10% of the tax; or (2) recognize that the tax paid by ComEd is a function of multiple factors, but is primarily a function of pre-1998 invested capital tax level, which in turn was a function of plant in-service. IIEC claims its allocation more closely reflects the reality that the Commission's policy on cost causation is meant to capture and that no party contends that the IEDT is entirely and exclusively a function of kWh delivered.

IIEC asserts that ComEd's 1997 IEDT payment represents 91.5% of ComEd's 2009 test year IEDT, and that payment was exclusively a function of the 1997 invested capital tax paid by ComEd. ComEd's 2009 IEDT of $108.8 million is only about 8.5% above the 1997 invested capital tax that was determined exclusively by the tax on ComEd's invested capital – wholly apart from its kWh deliveries. These figures are not disputed by other parties. Under the circumstances, IIEC proclaims that it is unreasonable to continue to allocate IEDT on the empirically rebutted presumption that it is exclusively a function of kWh delivered.

b. IIEC Recommended Allocation

Based on the above analysis, IIEC concludes that there is no credible basis for claiming that 100% of ComEd's IEDT responsibility is related to kWh sales, when over 90% of the tax responsibility is fixed at the level of ComEd's 1997 invested capital tax, with only the remaining 8.5% affected to some small degree by kWh sales. Accordingly, IIEC recommends an allocation approach that gives recognition to these facts and to the Commission's policy of allocations on the basis of cost causation. IIEC proposes to

recognize the empirical causes of IEDT through distinct causal categories and different allocation factors in ComEd's cost of service study.

The first category of IEDT cost under IIEC's proposal is the portion of IEDT attributable to ComEd's 1997 levels of IEDT ($99.5 million). This cost category would be allocated on the basis of plant in service, recognizing that this portion of the IEDT approximates ComEd's 1997 investment-based IEDT. The second category of IEDT cost would consist of the remaining portion of IEDT ($9 million in the current case) which, according to IIEC, is partly a function of ComEd's kWh delivered, at least in some years. That portion of IEDT would be allocated based on kWh sales, using the allocation factors developed by ComEd in its cost of service study.

IIEC asserts that, although changes in plant levels do not affect the IEDT on a going-forward basis, over 90% of ComEd's current tax responsibilities are fixed, and they are a function of ComEd's 1997 plant investment. It makes no sense whatsoever under cost causation principles to allocate that portion of the tax on the basis of kWh deliveries in 2009, IIEC declares. IIEC indicates that there is a direct and undeniable causal connection to historical plant in service that should be recognized. That causality is recognized in IIEC's proposed allocation approach.

Staff

IIEC also opposes ComEd's proposed method of collecting the IEDT tax. IIEC asserts that the IEDT tax is imposed directly on ComEd, not its customers and, therefore, should be considered part of the Company's overall cost of service. IIEC argues that such costs should be recovered through existing delivery service charges without a compelling reason to do otherwise which ComEd has failed to provide. Thus, IIEC opposes the imposition of a new per-kWh charge for larger customers. (IIEC IB, pp. 71-72)

IIEC then responds to ComEd's claim that a per-kWh charge is justified because "the IEDT is imposed on ComEd on the basis of kWh delivered." IIEC contends that it has, in fact, demonstrated that not to be the case based on the previously-discussed analysis and therefore, continued base rate recovery is justified. (IIEC IB, p. 72)

The issue boils down to the previous discussion of whether these costs are related to plant or usage. Staff has already refuted IIEC's arguments that they pertain to plant and instead show that they are determined by usage. Since the IEDT is related to usage, cost causation principles would argue for recovery through a per-kWh charge from all customers. Thus, IIEC's argument on this issue should be rejected.

CTA makes a novel argument that "as a matter of law the CTA is exempt from paying the [IEDT] tax" and therefore "ComEd's proposal to collect the tax from the CTA must be rejected." (CTA IB, pp. 13-14) The Commission should reject this argument. CTA argues that under the Metropolitan Transit Authority Act, 70 ILCS 3605, the CTA is exempt from paying to ComEd a charge for the IEDT. (*Id.*) CTA fails to recognize that while it may be exempt from certain taxes, the IEDT as pointed out by IIEC in its Initial Brief is not a tax imposed on customers but rather is directly imposed on ComEd. (IIEC IB, p. 71) Therefore, Section 70 ILCS 3605 does not apply to the IEDT tax imposed on ComEd. In addition, as IIEC further points out, the IEDT is similar to sales taxes,

income taxes, property taxes and other taxes imposed on ComEd. (*Id*., pp. 71-72) Not surprisingly, CTA has not claimed that 70 ILCS 3605 somehow exempts it from paying for those taxes through charges imposed on them by ComEd. For these reasons, the Commission should reject CTA's argument.

Commission Analysis and Conclusion

In the Ameren rate cases, the Commission reviewed the legislative history of the Public Utilities Revenue Act ("PURA") and determined that the General Assembly intended "to replace the invested capital/plant in service tax with a kWh tax in response to the changing nature of the Illinois electric utility industry." Ameren Order at 243. The legislature was anticipating that vertically integrated utilities like ComEd and Ameren might shed their generation assets (a significant part of plant in service), an event that has, in fact, occurred.

We agree with Staff that since the IEDT is related to usage, cost causation principles would argue for recovery through a per-kWh charge from all customers. The proposed change would have no impact upon residential, watt-hour and lighting customers because costs associated with the Illinois Electricity Distribution Tax are already recovered through per kWh DFCs for these customers. This is not a tax imposed on customers but rather is directly imposed on ComEd, Therefore, Section 70 ILCS 3605 does not apply to the IEDT tax imposed on ComEd and we find that the CTA is responsible for this tax.

In light of our prior treatment of the Illinois Electricity Distribution Tax in the Ameren Order, the Commission adopts ComEd's proposal to modify its rate design to provide a separate volumetric charge for the recovery of the Illinois Electricity Distribution Tax and uncollectible costs associated with the application of the tax for all of the reasons stated herein.

4. Distribution Loss Factors

ComEd's Position

ComEd states that an inevitable consequence of electricity flowing through a system is distribution system losses. Thus, Distribution Loss Factors ("DLFs") are calculated for each delivery class to account for the losses of electricity that occur in delivering electricity across its distribution system. DLFs are used to determine the amount of electricity that must be procured for a retail customer in accordance with the formula provided in Rate RDS – Retail Delivery Service ("Rate RDS"). (ComEd Initial Brief at 148).

ComEd contends that it has conducted its distribution system loss study using accepted engineering principles and the most accurate information that is practically available in order to determine the extent of these losses, so that they can be used when determining customer needs and the amount that must actually be distributed. It states that the distribution losses were determined by subtracting the energy that is delivered to retail and wholesale customers, plus transmission losses from the ComEd Zone Load, which is the summation of the net output of all generators within the ComEd Zone, plus net transmission interchange. (ComEd Ex. 67.1 Rev. at 2).

ComEd avers that, during the course of this proceeding, it has adjusted its distribution system loss study and DLFs in several ways to improve the allocation of energy losses to the customer classes. It modified the assignment of secondary and service losses to certain classes to reflect the material energy losses in the service conductors. It also excluded the Dusk to Dawn Lighting Delivery Class when reconciling its value for peak losses. Additionally, the study was amended where certain retired transformers had been included in the total calculation and some new installations had been omitted. Further, ComEd updated the allocation of losses in 138-69kV transformers to the High Voltage Electric Service Station ("HVESS") class. ComEd's allocation of these losses was also amended to recognize that customers metered at 138kV and higher have no material distribution losses. (ComEd Ex. 67.0 at 2-3; ComEd 148-49).

With regard to transmission losses, which are those losses assessed for power system components that are classified as transmission in accordance with Federal Energy Regulatory Commission ("FERC") regulation, ComEd used a 1998 report, according to which, annual energy losses are 1.6% of the transmission load. The magnitude of transmission losses was determined by multiplying 1.6% by the total energy delivered, plus distribution losses. ComEd plans to complete an update of this study by the end of 2011. (ComEd Ex. 34.0 6-7; ComEd Initial Brief at 150).

ComEd states that it recognizes that updated information regarding transmission losses and other indicators of distribution losses will result in a more accurate class load study. ComEd does not object to filing a tariff revision to reflect updated distribution loss factors as recommended by Staff, but it argues that also, the Commission should authorize the submission of much more. Specifically, ComEd avers that the Commission should authorize it to update its class load study, which would then be reflected in an updated ECOSS and possibly changes to rate design. It further states that the Commission should authorize it to file revisions of other charges, (such as Purchased Electricity Charges) for informational purposes, that are affected by changes in distribution and/or transmission loss factors. Finally, ComEd contends that the Commission should authorize it to apply the revised charges that are affected by such updates in DLFs in the next monthly billing period after such revised tariffs and information sheets become effective. (ComEd Ex. 68.0 at 7; ComEd Initial Brief at 150-51). ComEd disagrees with Staff's position that these additional changes are not necessary. (ComEd Reply Brief at 150).

ComEd urges to reject REACT's proposal to require ComEd to update DLFs annually, stating that this would requires sizeable effort. It concludes that such effort would unnecessarily complicate and burden the rate-setting process for what would probably be small changes in the values of the DLFs. (ComEd Ex. 73.0 at 40; ComEd Initial Brief at 151).

Staff's Position

Staff agrees with ComEd in that, in Staff's view, ComEd's revised distribution loss studies in ComEd Exs. 34.1 and 34.2 are preferable to the distribution loss study that ComEd initially filed. Also, Staff does not object to the further revisions provided in ComEd Ex. 67.1 and ComEd Ex. 67.2. Staff is concerned, however, by ComEd's use of an outdated transmission loss study for its distribution loss study calculations. (Staff Ex. 21.0 at 19). Staff recommends that ComEd complete a transmission loss study and then update its distribution loss factors with the information from the transmission loss study and then re-file its tariffs that use, or refer to, those updated distribution loss factors, rather than holding any revisions to its affected tariffs until its next rate case filing. (Staff Ex. 21.0 at 19).

Regarding ComEd's request to file an updated ECOSS as well as many other items, Staff states that the additional authorizations that ComEd seeks exceed the changes that Staff contemplated when presenting its recommendation. (*See,* Staff Ex. 6.0 at 26). Staff argues that the interested parties deserve an opportunity to review and provide arguments about the extensive evidence that ComEd seeks to file. While Staff continues to opine that ComEd should update its distribution loss factors for use with Rate RDS promptly following completion of updated transmission loss and distribution loss studies, rather than waiting until its next rate case filing, Staff contends that the additional authorizations that ComEd requests should be included in ComEd's next rate proceeding. (Staff Initial Brief at 144-45).

In response to the Commercial Group's objections to ComEd's Distribution Loss Study, Staff states that, as is indicated by the title of Appendix C to ComEd's distribution loss study, "2009 Loss Factors-Percent of Class Load through Elements," the values listed in each cell of the table represents the percentage of each class load that uses each element of ComEd's distribution system. For the SEC/SERVICE element, which represents ComEd's secondary distribution facilities as well as its services to individual customers, Staff understands ComEd's "SEC" elements to consist of low-voltage secondary conductors that can supply multiple customers, such as those that exist along many urban streets, and ComEd's "SERVICE" elements to consist of the conductors on private property that supply individual customers. (Tr. 818-19).

Regarding the Commercial Group's argument that the correct SEC/SERVICES values for Medium and Large Load classes is "guesswork," Staff states that it agrees with the Commercial Group that what the exact values should be are not known; however, Staff avers that the values indicated therein are the result of "an approximation based upon engineering judgment of the people conducting the study." (Tr. 849). Staff witness Mr. Rockrohr explained his rationale for recommending the values of 50% and 40%, and stated "I would consider alternative non-zero percentages to represent losses in the services to members of the 100-400 kW and 400-1000kW classes if a reasonable argument were to be presented for those alternative values." (Staff Ex. 6.0 at. 25; Staff Reply Brief at 86).

Staff also disagrees with the Commercial Group's argument that the Very Large Load and Extra Large Load classes have higher levels of current flowing through their service drops than the Medium Load and the Large Load classes. Staff witness Mr. Rockrohr previously pointed out that often; customers in the Very Large and Extra Large Load classes take service at a non-transformed voltage level, such as 12 kV, so that the line that supplies them would not be included as a SEC/SERVICE element at all. (Tr. 817-19) Staff concludes that therefore, it is logical that the Very Large and Extra Large Load classes have a SEC/SERVICE value in Appendix C that is significantly lower than the Medium and Large Load classes. (Staff Reply Brief at 86).

In response to the Commercial Group's argument regarding the assumption that that no losses occur through the SEC (secondary) part of the SEC/SERVICE element of ComEd's distribution model for the Medium and Large Customer classes, Staff points out that Mr. Rockrohr already made this point when making his recommendation. He explained that he believed the values of 50% and 40% would "strike a reasonable balance between the reality that these customers do not typically utilize ComEd's secondary systems, and the reality that the current that does flow on the services to these customers is typically large, so some losses are present." This is true, Staff states, because "Line losses are calculated by the formula: Loss = the square of the current through the line times resistance." (Staff Ex. 6.0 at. 25; Staff Reply Brief at 87).

Lastly, the Commercial Group referred to a cost study that indicated ComEd's costs assigned to the Medium and Large Load classes for service lines is only 0.7% and 0.25%, respectively of ComEd's total service line costs. (*See,* Commercial Group Initial Brief at 14). Staff opines that the cost of services for any single class of customer does not provide any indication of the percentage of the load for each class that passes through those services. In other words, Staff avers, the statistic that the Commercial Group presents is not an indicator of losses.

Staff also does not believe that the Commercial Group has provided a reasonable argument for its proffered alternative values. Staff does not support the Commercial Group's recommendation that the values of SEC/SERVICE for the Medium and Large Load customer classes should be reduced to 20% and 10% respectively. In Staff's opinion, those values would under-represent class use of the SEC/SERVICE elements of ComEd's distribution system. (Staff Reply Brief at 87-88).

Staff supports the Commercial Group's suggestion that ComEd should be require to further study how the various customer classes use each element of ComEd's distribution system. Staff adds that in the future, ComEd should also segregate the SEC (secondary) and SERVICE elements to eliminate future disagreement and confusion. Staff, however, believes the distribution loss study ComEd presented in ComEd Ex. 67.1 Revised and ComEd Ex. 67.2 should be accepted at this time. (Staff Reply Brief at 87-88).

The Commercial Group's Position

The Commercial Group states that during this proceeding, ComEd made a significant change to its SEC/SERVICES distribution loss factor that was not supported by substantial evidence. It concludes that ComEd's proposal should therefore be

rejected. The SEC/SERVICES factor refers to the losses through secondary distribution lines (SEC) and service lines (SERVICES) for the various customer classes. In its initial filing, ComEd continued its historic practice of assigning zero losses for the Medium Load, Large Load, and Very Large Load classes for secondary and service lines. According to the Commercial Group, this reflects the facts that: 1) secondary distribution lines are not used to serve customers above 100 kW in load (and therefore there are no losses from the SEC factor), and 2) the service lines (the SERVICES factor) for these classes are relatively short or non-existent (where larger customers are served directly from electric service stations). (Commercial Group Initial Brief at 13).

The Commercial Group avers that resistance through a line is a factor of the length of the line and the cross-sectional size of the line, citing Staff witness Mr. Rockrohr. (Tr. 814-815). It posits that Mr. Rockrohr testified that "services (to customers above 100 kW) are typically short and of larger conductor size"; hence, "there is little resistance in the service conductor" for such customers. Although the resistance is small, Mr. Rockrohr concluded that the resistance "is not zero" and he added that more current may flow through these wires than for smaller load customers. (Staff Ex. 6.0 at 24). During the hearings, Mr. Rockrohr stated that he had not performed a study to come up with the 50% for the Medium Load class and 40% for the Large Load class, and that lower estimates could be reasonable. (Commercial Group Initial Brief at 13-14; Tr. 815, 820).

The Commercial Group further states that ComEd witness Mr. Born adopted Mr. Rockrohr's recommendation, saying only that "there are no secondary conductor losses" for Medium and Large Load classes but that "there are material energy losses in the service conductors used by customers in the 100-400 kW and 400-1000 kW classes." In support, the Commercial Group cites ComEd Ex. 34.0 at 7-8. Mr. Born also changed the SEC/SERVICES line losses for the Very Large and Extra Large Load classes from 0% to 5%, in response to Mr. Rockrohr's testimony that some service line losses occur. But, it avers, Mr. Rockrohr, when asked whether he agreed to this change for the Very Large and Extra Large Load classes, said only that he "[didn't] disagree with it" because "it's reasonable that there would be some losses" and that without a study of these losses, the analysis is similar to that for the Medium and Large Load classes. (Tr. 816, 817). It argues that therefore, the changes from 0% to 50% and 40% are based solely on evidence that the losses are "greater than zero." (Commercial Group Initial Brief at 14).

The Commercial Group concludes that thus, the large changes to the SEC/SERVICE factor that were made in this docket were based upon conjecture. It states that there are no SEC losses from the SEC/SERVICES factor. Also, service lines to Medium and Large Load customers have a very low resistance, because they are short and of significant size. It argues that the only explanation for changing the SEC/SERVICES figure from 0% to 50% (Medium) and 40% (Large) is that the current flowing through such service lines may be larger than the current flowing through service lines serving customers under 100 kW. However, it continues, the Very Large and Extra Large Load customers may have even higher levels of current flowing through their service drops, which, it avers, does not justify assigning only a 5% SEC/SERVICES value to these two customer classes. Finally, it states that ComEd

witness Mr. Heintz' cost study "backs this up" by showing that the cost assigned to the Medium and Large Load classes for service lines is only 0.7% and 0.25% respectively of ComEd's total service line cost. (*See,* ComEd Ex. 15.1, Sch. 2A, p. 5, line 83).

The Commercial Group reasons that therefore, the correct SEC/SERVICES values for the Medium and Large Load classes are probably closer to the original 0% than 50% or 40% but what the exact values that are at issue should be is "guesswork." The Commercial Group offers that it would agree to a SEC/SERVICES factor of 20% for the Medium Load class and 10% for the Large Load Class. Thus, the SEC/SERVICES factor would be: Medium (20%), Large (10%), Very Large (5%) and Extra Large (5%). (Commercial Group Initial Brief at 14).

REACT's Position

Although REACT supports ComEd's final proposed Distribution Loss Factors ("DLFs") for purposes of setting the rates in this proceeding, in REACT's opinion, the Commission also should require ComEd to update its Distribution Loss Study annually. It states that in essence, DLFs operate as a tax on purchased electricity, requiring each end-user to purchase an additional quantity of electricity in proportion to the DLF, in order to account for electricity that is lost within the system. For very high-volume purchasers of electricity, what appear to be small changes in the DLFs, such as ComEd's initial proposed 4% increase, can have a substantial impact upon such a customer's bill; it is therefore critical, according to REACT, for high-volume users, such as the customer members of REACT, that the DLFs are not artificially high. (REACT Initial Brief at 70-71).

REACT states that the Commission should be concerned by the huge swing in ComEd's DLFs. This swing, it avers, demonstrates the need for additional oversight of the calculation of distribution losses. To remedy this situation, REACT requests that the Commission order ComEd to update its Distribution Loss Study to the Commission every year. Although REACT expects the DLFs to fluctuate from year to year, the massive increases from the 2005 ComEd Rate Case to the DLFs that were initially proposed in the present case (15.78% for Extra Large Load, and 72.59% for over-10 MW High Voltage) represent an enormous change that probably would not have even been proposed, if there were proper annual oversight of the inputs to this charge. REACT Initial Brief at 71).

The IIEC's Position

The IIEC supports ComEd's modifications of its distribution loss study and the DLF for customers in the high-voltage class with demands over 10,000 kW resulting there from. It also supports ComEd's resulting DLF for high-voltage zero-distribution loss customers of 0.6% to 0.7%. (*See*, IIEC Initial Brief at 73-74).

ICEA's Position

ICEA, as well, supports ComEd's proposed modifications of its distribution loss study. (ICEA Initial Brief at 47-48).

Analysis and Conclusions

We decline to adopt REACT's argument. It appears that the "massive spike" in the DLF for these large users of electricity from its 2005 rate case and 2007 rate case was due to the fact that the evidence presented by ComEd now is much more accurate than when it was when originally proposed in earlier cases. Therefore, updating ComEd's Distribution Loss Study on an annual basis is an onus that does not appear to be justified. The better approach is the one that this Commission has taken, which is, to urge parties to present accurate and complete evidence in support of their positions. We do so here.

We also disagree with the Commercial Group's contention that the evidence proffered here regarding this issue is mere conjecture. As Staff has pointed out, the correct values for the Medium and the Large Load customers is an approximation, which was based upon the engineering judgment of the persons who conducted the study. An approximation is not the "guesswork" that the Commercial Group suggests. Also, typically, the Extra Large Load and Very Large Load customers take service at a non-transformed voltage level; therefore, the lines that supply them, usually, would not be included as a SEC/SERVICE element. The Commercial Group has not established that the values attributed to these two classes is incorrect. Further, the cost of service for a particular class is not indicative of distribution losses. Therefore, the cost of service study prepared by Mr. Heintz does not aid the Commercial Group. However, to eliminate future confusions, ComEd shall segregate the SEC and SERVICE elements in any future rate case in its initial filing.

We also decline to adopt the values that the Commercial Group proffers, as it presents no evidence to support these values. In fact, the Commercial Group acknowledges in its argument that the values it proffers are ones that it would accept; it does not state that these values reflect reality.

We additionally agree with Staff's contention that ComEd should not be allowed to, in addition to updating its transmission loss information, file an updated cost of service study, and provide many other items. All of this evidence should be subject to the due process mechanisms that occur in litigation, such as pleadings, discovery and cross-examination.

However, requiring ComEd to update its Distribution Loss Study with information from an updated Transmission Loss Study is uncontested and it does not appear to be a recommendation that needs the mechanisms involved in litigation. We therefore adopt Staff's recommendation in this regard. ComEd shall re-file its tariffs with this updated information by the end of 2011. Additionally, so it is clear, the Distribution Loss Studies in ComEd Exs. 67.1 Rev. and 67.2 are approved.

a. High-Voltage Customers--The Issues Presented by the United States Department of Energy and the IIEC (Uncontested)

ComEd and the U.S. Department of Energy (the "DOE") state that DOE and IIEC witnesses have proposed, and ComEd witnesses have agreed to, certain changes in

the calculation of loss distribution factors and in the resultant loss factors themselves. It is therefore the DOE's understanding that ComEd, the IIEC, and the Department itself are in agreement in regard to the subject of distribution loss factors. No party has directly or indirectly challenged or otherwise contradicted these testimonies. (ComEd Memo at 3; DOE Memo at 1-2; IIEC Memo at 13).

ComEd presented Mr. Born, the ComEd official who actually performed the Distribution Loss Study. In response to DOE testimony, he lowered ComEd's recommended 1.86 distribution loss factor by more than 50%. He further revised the loss study by, among other things, adding a customer category titled "HV DLF= 0" to represent customers metered at 138kV and higher that have no material distribution losses. (ComEd Ex. 34). ComEd witness Mr. Alongi agreed with these changes and presented calculations necessary to implement them. (ComEd Ex. 49). In response, the DOE witnesses stated that Mr. Born's changes addressed their concerns and are acceptable. (DOE Exs. 3.0, 4.0). In further rebuttal testimony, IIEC witness Mr. Stevens pointed out a refinement that could be made to the loss study methodology. (IIEC Exs. 5.0–5.5). Mr. Born accepted this refinement. (ComEd Exs. 67, 67.1, 67.2). ComEd provided DLFs (Distribution Loss Factors) that correspond to the revised loss studies provided In Mr. Born's testimony. (*See,* ComEd Exs. 34.1 and 34.2). Updated DLFs are provided in ComEd Ex. 49.9 which also incorporates provisions to address DOE witness Mr. Etheridge's concerns regarding the DLFs applicable to customers with service points, at which, electricity is metered at or above 138 kV.

ComEd's systems are designed to apply DLFs on an account-level basis, not a meter-level basis. Consequently, ComEd proposed to address the DOE's concerns by determining and applying the weighted average DLF for all points of delivery for the 18 accounts that have at least one point of delivery metered at 138kV or higher. ComEd finds Mr. Etheridge's recommendation to clarify the definition of the Dc component of the DLF computation as shown in Rate RDS to be reasonable. ComEd Ex. 49.10 provides a further revision to Sheet No. 75 in Rate RDS to accommodate Mr. Etheridge's recommendation. (DOE Memo at 1-2).

Analysis and Conclusions

The revisions proposed by the DOE and the IIEC, and agreed-to by ComEd, as is set forth above, are hereby adopted.

5. General Terms and Conditions

a. Residential Service Station (Ownership of Non-Standard Residential Connections)

ComEd's Position

ComEd states that it proposed to add one word, "pole", to an existing section of General Terms and Conditions describing the responsibilities for installation of a Residential Service Station (ILL. C. C. No. 10, 1st Revised Sheet No. 165) to further clarify its existing practice that the residential customer "must furnish, install, own and maintain the remainder of the overhead primary service connection including the first support on private property" that already exists in ComEd's General Terms and Conditions (*See,* ILL. C. C. No. 10, Original Sheet No. 160; ComEd Initial Brief at 151).

ComEd argues that the revision it proposes is merely further clarifying long-standing terms and service policy for such residential customers that have existed since at least 1955. It further argues that, pursuant to Staff's proposal to require ComEd to assume ownership of certain non-standard customer-owned facilities that are used to bring power from the ComEd system into privately-owned residential property, it is unclear as to how or when ComEd will assume ownership of property that is customer-owned. Also, even if ComEd could assume such ownership, Staff's proposal does not grant ComEd the easements that are necessary in order for ComEd personnel to access a customer's property to perform necessary maintenance. It also, according to ComEd, does not address the clearance issues for trees and other vegetation. (ComEd Ex. 41.0 at 5).

ComEd also avers that offering customers the ability to have ComEd assume ownership on a prospective basis would create confusion and a permanently dual system of those customers who own their own overhead primary facilities and those customers who have let ComEd assume ownership. In support, it cites ComEd Ex. 41.0 at 5. Additionally, ComEd states that it already offers residential customers who are willing to pay the associated costs with the option to replace customer-owned overhead primary facilities and the ComEd-owned overhead Residential Service Station transformers with ComEd-owned underground direct-buried primary facilities and a pad-mounted Residential Service Station transformer. (ComEd Initial Brief at 152).

ComEd agrees that safety issues are unquestionably important. It emphasizes that it is committed to operating at an industry-leading level of safety. It argues that it has had decades of experience, on which, to base a sound conclusion about the safety of its practices regarding customer-owned facilities. (*Id.*).

ComEd presents an alternative proposal to address Mr. Rockrohr's safety and reliability concerns. It proposed to work jointly with Staff to study the issues that Mr. Rockrohr has raised, to encompass both the safety and performance of these facilities as compared to similar ComEd-owned facilities and examine the costs, benefits, and potential legal and practical obstacles to ComEd attempting to acquire ownership of these facilities. ComEd agrees to bear the cost of the study and record it in a regulatory asset, with the goal of returning a report to the Commission by the end of 2011. (ComEd Initial Brief at 152-53).

In its Reply Brief, ComEd states that Staff has not provided any evidence substantiating that "relatively few" residential customers would be affected by Staff's proposed change. And, according to ComEd, there is no evidence substantiating the existence of a safety risk. In the event that the Commission does not reject Staff's proposal regarding ownership of certain non-standard customer-owned facilities, ComEd asserts that the Commission should accept its alternative proposal to study the issues raised by Staff relating to these facilities. (ComEd Reply Brief at 151-52).

Staff's Position

Staff objected to ComEd's proposed requirements for providing overhead service to residential customers. In fact, Staff states, ComEd's proposed tariff requires that residential customers install and maintain primary conductors, the poles that support those primary conductors, and even the pole that supports ComEd's distribution transformer, though ComEd would install, own, and maintain the transformer. Staff thus recommends that ComEd own and maintain the overhead primary service connection facilities for residential customers in a similar manner as it currently does for non-residential customers. Staff opines that ComEd's provision of these primary voltage facilities would be safer and less confusing for customers. Staff states that its recommendation affects only the relatively few residential customers in ComEd's service territory with primary voltage facilities located on their private property. (Staff Exs. 6.0 at 15-20; 21.0, at 12-18; Staff Initial Brief at 145-46).

In response to ComEd's assertion that for existing facilities, there is no way that ComEd can simply assume ownership of customer-owned property, Staff pointed out that, if a customer were to prevent ComEd from maintaining the poles and service conductors on private property, the result would be less reliable service to that customer, and/or disconnection of service, if ComEd discovered an unsafe condition. Staff opines that residential customers would probably not object to ComEd owning and maintaining primary voltage facilities on private property, but if they were to do so, other ComEd customers would not be affected. (Staff Ex. 21.0 at 15)

Staff further states that in surrebuttal, ComEd proposed to conduct a study to compare the safety and performance of customer-owned primary service connection facilities on residential private property with similar ComEd-owned facilities, citing ComEd Ex. 60.0, at. 18-19. Staff states that such a study is not necessary because it is apparent to Staff that it is not reasonable to expect residential customers to own, operate, and maintain what is in essence an extension of ComEd's 12,000 volt electric distribution system. (*See*, Staff Ex. 6.0 at. 17; Tr. 847; Staff Initial Brief at 146-47). Staff also agues that ComEd has not explained why it will not simply agree to modify its tariff in a manner that provides overhead primary service connections to residential customers in the same manner as it provides them to non-residential customers, as Staff continues to recommend. (Staff Ex. 21.0 at 17-18; Staff Reply Brief at 82).

Analysis and Conclusions

What Staff recommends entails complicated legal issues, such as, ensuring that ComEd personnel has access to the facilities (easements) for maintenance and repair, and who would be responsible for vegetation clearance. Such matters must be carefully thought out. They also are beyond the scope of the evidence presented in this docket. We therefore decline to adopt Staff's recommendations regarding this issue.

However, Staff has identified potential safety concerns with ComEd's present system. At this time, we adopt ComEd's proposal to work jointly with Staff to study the issues that Mr. Rockrohr has raised, to encompass both the safety and performance of

these facilities, as compared to similar ComEd-owned facilities and examine the costs, benefits, and potential legal and practical obstacles to ComEd attempting to acquire ownership of these facilities, with a report to this Commission, prepared by ComEd, that shall issue by the end of 2011.

b. Limitation of Liability Language

ComEd's Position

ComEd proposed to modify its General Terms and Conditions in a manner that would add specific Limitation of Liability language to the Nature of Service portion of its General Terms and Conditions. According to ComEd, the reason for this modification is to incorporate limitation of liability language that is uniform with the other Illinois utilities (ComEd Exs. 16.0 3rd Rev. at 41-42; 49.0 Rev. at 41). According to ComEd, this change ensures consistency amongst the entities with which ComEd interacts. (ComEd Ex. 16.0 3rd Rev., at 42). ComEd also contends that its proposed limitations apply only to parties that have some connection between the claimed liability and ComEd's provision of electricity to the party. (ComEd Initial Brief at 153-54).

According to ComEd, the arguments proffered by the CTA and Metra are really nothing more than an ill-considered assertion by the railroads that what is good for everyone else is not appropriate for them. It concludes that the members of the Railroad Class are not entitled to be treated differently than any other customer with respect to such liability. (ComEd Reply Brief at 152-53).

Metra's Position

Metra states that ComEd's proposed revisions to its General Terms and Conditions provide that ComEd could only be held liable for gross negligence. ComEd has also proposed language that would require customers, such as Metra, to indemnify ComEd for damages resulting from occurrences on customers' property due to ComEd's own negligence. Metra concludes that therefore, if a third-party were to be injured on Metra's property due to ComEd's negligence, pursuant to ComEd's proposed language, Metra would be required to indemnify ComEd for third-party claims against ComEd due to ComEd's own negligence. (*See,* ComEd Ex. 16.0 2d Rev. at 42-43; ComEd Ex. 16.21 at Sheet No. 155; Metra Initial Brief at 21-22).

Metra argues that the granting of civil privileges and immunities in favor of a party to alter its otherwise applicable common-law duties obviously operates to the disadvantage of other parties. It avers that the Illinois courts and the Illinois legislature have been very reluctant to grant civil privileges and immunities, or to allow the traditional standard of care to be altered, except in limited and carefully circumscribed circumstances. In support it cites *People v. Illinois Highway Comm.*, 3 Ill. 218, 224-27, 120 N.E.2d 35, 39-41 (1954), determining that sovereign immunity does not apply to Tollway as it is a local unit of government); Illinois Constitution of 1970, Art. XIII, Sec. 4 (abolishing sovereign immunity, except as established by statute); 705 ILCS 505/8 (limited Court of Claims jurisdiction for specified claims against the State); the Local Government and Governmental Employees Tort Immunity Act, 745 ILCS 10/8-101; Construction Contract Indemnification for Negligence Act, 740 ILCS 35/1 *et seq.*

(providing that contract provisions purporting to indemnify one for its own negligence in construction are void as against public policy). Metra points out that, to the extent that limited privileges and immunities have been recognized or established, they have been restricted to governmental entities. (Metra Initial Brief at 22).

Metra further argues that the attempt by ComEd to reduce the standard of care and require indemnification for its own negligence is particularly egregious as applied to Metra, the CTA and other units of local government who enjoy the limited protection of the Local Government and Governmental Employees Tort Immunity Act, 745 ILCS 10. As explained in the testimony of Metra's Director of Risk Management, Mr. Capra, the Tort Immunity Act grants Metra, among others, immunities and creates heightened liability standards for parties seeking to sue Metra in tort. Metra points out that the General Assembly's purpose in enacting the Tort Immunity Act was "to prevent the diversion of public funds to payment of damage claims", citing *DeSmet Ex Rel. v. County of Rock Island,* 219 Ill. 2d 497, 505, 848 N.E.2d 1030, 1037 (2006), and *Bubb v. Springfield School Dist. 186*, 167 Ill. 2d 372, 378, 657 N.E.2d 887, 891 (1995). (Metra Initial Brief at 23-24).

Metra further states that the record here is devoid of any evidence to support, on public policy grounds, lowering the standard of care applicable to ComEd's delivery of electricity, or to justify shifting the consequences of ComEd's negligence to its customers. By its nature, Metra continues, electricity is a very dangerous commodity, particularly when it is delivered at 12,000 volts, as it is to the Railroad Class. Additionally, Metra points out that there is no evidence in this record indicating that ComEd has sustained serious losses or has been plagued by numerous lawsuits. (Metra Initial Brief at 24).

Metra's Director of Risk Management, Mr. Capra, testified that he is concerned that the limitation of liability could be applied to override Metra's contracts with ComEd, in situations where Metra allows ComEd employees to enter Metra's property in order to serve other customers. (Metra Ex. 1.0 at 5-10). In its Initial Brief, ComEd asserted that "the limitations apply only to parties that have some connection between the claimed liability and ComEd's provision of electricity to the party." (See, ComEd's Initial Post-Trial Brief at 154). However, Metra avers that the proposed tariff language is bereft of any words or phrases suggesting that the standard for application of ComEd's limitation of liability language actually turns on whether there is proof of "some connection between the claimed liability and ComEd's provision of electricity to the party." The proposed tariff language provides in relevant part:

LIMITATIONS OF LIABILITY

****

> Without limiting the generality of the provisions in the preceding paragraph, the Company is not liable for any damages, direct or otherwise, which an applicant for electric service, retail customer, RES, or MSP may sustain by reason of any failure or interruption of electric

> service, reversal of electric service, increase or decrease in electric voltage, change in the electrical characteristics of electric service, or mechanical failure, whether caused by accident, repairs, or other causes except when caused by gross negligence on the Company's part.
>
> **********
>
> Moreover, the Company is not liable for damages that may be incurred by the use or presence of the Company's facilities or property on an applicant's or retail customer's premises; the Company is not responsible for or liable for damage to an applicant, retail customer's, RES's, or MSP's equipment or property caused by conditions not due to the gross negligence of the Company.
>
> **********
>
> The Company is neither responsible nor liable for electric power and energy from and after the point at which it passes from Company facilities to equipment owned or controlled by a retail customer, RES, or MSP. The retail customer, RES, or MSP, as applicable, must protect and keep the Company harmless from all claims for any injury or damage occurring after such point, except in the event that such injury or damage is shown to have resulted solely from the gross negligence of the Company.

Metra concludes that there is no language in the proposed tariff to support ComEd's statement that its proposed limitation of liability applies only to situations where there is "some connection between the claimed liability and ComEd's provision of electricity to the party." Metra concludes that, either ComEd does not fully understand the implications of its own language, or it is obfuscating the issue. (Metra Reply Brief at 14-15). Metra states that the other concern expressed by Mr. Capra, is that the proposed tariff language exposes Metra to substantial liability arising out of claims by third-parties that have been injured on Metra's property. (Metra Ex. 1.0 at 9-12). It also contends that the proposed standard is so indefinite that it is incapable of serving as a meaningful application standard. (*See,* Metra Ex. 1.03; Metra Reply Brief at 13-14).

In support, Metra provides two examples. The first example is when a ComEd service repairman enters Metra property to repair an electrical cable providing service to Metra. In the process, the cable slips or is released from the ComEd serviceman's control and it strikes a third-party. The third-party then sues ComEd for negligence. Under the terms of the proposed tariff language, Metra would be required to indemnify ComEd against the third party's claim for damages.

In the second example, a ComEd serviceman is driving his service truck onto Metra property to perform electrical repairs on Metra's service lines. A Metra employee helps guide the ComEd service truck as it is backing into position. A third-party is struck by the truck and falls to the pavement, resulting in a severe brain injury. Suit is filed on behalf of the injured third-party against Metra for negligence. Under ordinary circumstances, Metra would probably have a contribution claim against ComEd for its negligence. Metra points out that due to the proposed tariff language, it cannot bring

that claim because then, Metra would be responsible for damages due to ComEd's negligence. (Metra Reply Brief at 15-16).

The CTA's Position

The CTA, also, contends that the Commission should reject ComEd's attempt to shift liability to the CTA for all but ComEd's gross negligence. It states that the new language would make ComEd liable for personal injury or death or other damages only when it is grossly negligent. This language would shift liability to all customers for any damages, injuries, and death arising out of ComEd facilities. Such a shift would severely affect the CTA because ComEd has multiple facilities located on, over, and under CTA property pursuant to a written contract between the CTA and ComEd. (CTA Initial Brief at 26).

The CTA points out that currently, ComEd's general terms and conditions deal only with liability resulting from interruption of service. They state:

> The Company is not responsible for damages for any failure to provide electric service, or for interruption to one or more phases, or reversal of such service, if such failure, interruption, or reversal is without willful default or negligence on the Company's part. Nor is the Company responsible for interruptions, by under frequency relays or otherwise, required to preserve the integrity of the electric delivery system in the Company's service territory or the regional interconnected electric systems.

ComEd proposes to eliminate this section and substitute the language cited by Metra which is quoted above.

The CTA avers that in responses to CTA "data requests," ComEd stated that the language is intended to supersede provisions in the CTA/ComEd contract. (*See,* CTA Ex. 3.0, at 6). The current CTA/ComEd contract provides, in pertinent part:

- Article 15. This article provides that ComEd, with the consent of the CTA, "shall have the right to locate its Facilities on, in or over CTA Facilities provided that such right is and shall continue to be exercised so as not to interfere with the use of such CTA Facilities by CTA." CTA Ex. 1.02 at 15, Section 15.02. The CTA states that, as a result of this provision, ComEd has installed facilities on, in, and over CTA Facilities and rights-of-way.

- Section 20.01. This section provides that ComEd is not liable to the CTA "for any loss or damage resulting from non-delivery of all or any portion of the electricity to be supplied to the CTA unless such non-delivery occurs through the negligence or willful default of Edison."

- Section 20.02. Edison shall, during the term hereof, indemnify CTA against any and all claims for damages in favor of any third person

> or persons, corporation or corporations, founded upon or arising from (a) the construction, installation, relocation, removal, insulation, operation or maintenance of any Edison Supply Facilities or any Edison Facilities in Edison Joint Substations or in CTA Facilities, or (b) Edison's improper or negligent construction, installation, relation, removal, insulation, operation or maintenance of Conversion Facilities in Edison Joint Substations or CTA Facilities in CTA's Special Substations; and Edison shall pay and reimburse CTA for all damages, costs, expenses and attorneys' fees that CTA may be put to or incur in defending, or by reason of, any suit brought against it for such damages.
>
> - Section 21.01 provides that each party to the contract assumes "full responsibility for insuring the property, structures, facilities and equipment owned by such party, or deemed by the provisions of this agreement to be owned by such party, to the extent considered appropriate by such party."

(See, CTA Ex. 3.0 at 3-4; CTA Initial Brief at 29).

The CTA avers that ComEd currently asks the CTA to place ComEd facilities on, over, and under CTA rights-of-way. It states that these requests by ComEd to place its facilities on CTA property are continuing in nature. For example, since this docket was filed, ComEd has made at least three requests to put its facilities on CTA property. (*See,* CTA Ex. 4.0 at 10).

The CTA avers that ComEd did not discuss the tariff change with the CTA prior to filing the new tariff. However, from the inception of the 1958 contract between the CTA and ComEd, ComEd and the CTA have mutually agreed to modifications of the contract through the issuance of "advices." The advices are agreements signed by both parties formally making changes to the contract. (*See,* CTA Ex. 4.02, 4.03 CONFIDENTIAL).

It further states that in docket 05-0597, (a previous ComEd Rate Case) ComEd decided that it could unilaterally change contract provisions. While allowing some tariff modifications, the Commission recognized that the parties to this contract should negotiate modifications to it. It stated: "[T]he Commission would have expected ComEd to negotiate a new contract for the delivery of power and energy with the CTA and present it to the Commission for approval." In support, the CTA cites docket 05-0597, Final Order at 188. (CTA Initial Brief at 30).

The CTA further cites the testimony of its witness Ms Kovalan, who stated:

> [T]he proposed tariff is detrimental to CTA passengers in the event of any damage, injury, or death caused by malfunctioning ComEd equipment or negligence of ComEd employees while on CTA property because the tariff absolves ComEd of any responsibility for such damages, injuries, or death. This is bad public policy.

> I understand that in past ComEd rate cases that the Commission has found that there is a public interest in providing mass transit services in the Chicago area. By approving this language, the Commission would be shifting costs to the very public agencies it has vowed to assist.
>
> (CTA Ex. 3.0 at 7; CTA Initial Brief at 30-31).

Analysis and Conclusions

At the outset, we disagree with ComEd's interpretation of its proffered language. In fact, this language holds the CTA, Metra, and possibly others liable for ComEd's own actions, unless those actions are "grossly negligent," a term that is not defined in ComEd's tariff. The term "gross negligence" is vague, as it is unclear whether the conduct in question is willful and wanton or some sort of elevated form of negligence. We would be remiss to allow parties to use a vague term, especially here, when generally, willful and wanton conduct can result in the imposition of punitive damages, while, a less willful form of negligence would not result in the imposition of punitive damages.

We also note that stating that the terms that ComEd seeks to impose upon Metra and the CTA are in the interest of uniformity with the other Illinois utilities overlooks the fact that Metra and the CTA are unique. Chicago is the third-largest city in the United States and Metra and the CTA provide public transportation within Chicago and the metropolitan area. There simply is no comparable situation elsewhere in Illinois.

However, it appears that, irrespective of the uniqueness of the CTA and Metra within Illinois, ComEd's proposal is contrary to sound public policy. Both Metra and the CTA have contracts with ComEd. ComEd seeks to impose its proposed terms over and above those contracts. Normally, contract modification requires consideration, which apparently did not occur here. (*See, e.g., Doyle v. Holy Cross Hospital*, 186 Ill. 2d 104, 112, 708 N.E.2d 1140 ((1999); *Ross v. May Co.,* 377 Ill. App. 3d 387, 392-93, 880 N.E.22d 210 (1st Dist. 2007)).

Further, ComEd's proffered language appears to ignore Section 5-201 of the Public Utilities Act, which applies to some, but not all, of the situations in which a utility could find itself liable for its tortious conduct. It provides that:

> In case any public utility shall do, cause to be done or permit to be done any act, matter or thing prohibited, forbidden or declared to be unlawful, or shall omit to do any act, matter or thing required to be done either by any provision of this Act or any rule, regulation, order or decision of the Commission, issued under authority of this Act, *the public utility shall be liable to the persons or corporations affected thereby for all loss, damages or injury caused thereby or resulting there from, and if the court shall find that the act or omission was willful, the court may in addition to the actual damages, award damages for the sake of example and by the way of punishment.* An action to recover for such loss, damage or injury may be brought in the circuit court by any person or corporation.

(220 ILCS 5/5-201; emphasis added). This law was enacted in 1913. Clearly, it holds public utilities liable for their tortious conduct, reparable by compensatory damages, and, in the proper cases, punitive damages when those actions violate the Public Utilities Act, a Commission Order, or the myriad Commission rules, including its safety rules. This provision appears to encompass some, but not all, of the situations involved with ComEd's proffered language. Therefore, irrespective of any tariff language that ComEd seeks to proffer, pursuant to Section 5-201, it would still be legally responsible for its actions in many instances, when its employees cause harm to others. We decline to adopt a tariff provisions that appears to contravene this provision in the Act.

Finally, as Metra has noted, it is simply bad public policy to encourage indemnification from another party for a party's own actions. This is why the many laws and cases that Metra cites are relevant here. This type of indemnification would discourage ComEd's personnel from acting with care for the welfare of other persons and entities. ComEd's proposed tariff modifications regarding this issue are therefore rejected, in their entirety.

6. Rider UF

This issue is no longer contested. In response to Mr. Alongi's rebuttal testimony, Staff witness Ms. Pearce revised her calculation of uncollectibles and incorporated the use of net write-offs instead of bad debt expense. (Staff Ex. 18.0 at 37-38). ComEd Ex. 68.2 provided a computation of the distribution-related uncollectible percentage using net write-offs instead of bad debt expense, resulting in an overall distribution related uncollectible percentage of 1.37%, which is consistent with the value provided by Ms. Pearce. (ComEd Ex. 68.0 at 8). Such use of net write-offs in the determination of uncollectible cost factors would begin in the calendar year following the final Order in this rate case. (ComEd Initial Brief at 154-55).

Analysis and Conclusions

Use of net write-offs instead of bad debt expense is reasonable and it is hereby approved.

7. Notification Regarding Elimination of Self-Generation Customer Group

This issue, also, is not contested. ComEd proposed to eliminate the Self-Generating Customer Group because it is applicable to only nine customers. ComEd agreed with Staff witness Ms. Harden's recommendation to require ComEd to notify the nine customers affected by the ComEd's proposal to eliminate the Self-Generating Customer Group. If the Commission approves the elimination of the Self-Generating Customer Group, ComEd will send a direct notice to the affected customers that explains the options the customers have available to them upon the elimination of the Self-Generating Customer Group. This notice will explain the billing structure of each of the available options. (ComEd Initial Brief at 155).

Analysis and Conclusions

We agree that the Self-Generating Customer Group should be eliminated, due to the fact that it has only nine customers. This measure is therefore approved. ComEd shall send these customers notice advising them of their options. That notice shall also explain the billing structure of the available options.

8. Docket No. 08-0532 Compliance Issues

*See, S*ection VII C 1 (b)(i) herein, entitled "Appropriate Methodology/Compliance with Docket No. 08-532"

G. Other Issues

a. Street Lighting

REVENUES

H. Uncontested Issues - Other Revenues – Rate Relief Payment

ComEd accepted the proposal by Staff witness Ms. Hathhorn and AG/CUB witness Mr. Effron to adjust other revenues to eliminate an inadvertent and incorrect $8 million reduction for a rate relief payment. (ComEd Ex. 30.0 at 19). This adjustment is reasonable; it is therefore approved.

I. Miscellaneous Revenues

AG/CUB withdrew their proposed adjustment to miscellaneous revenues as unnecessary. (AG-CUB Ex. 7.1, Sch. C-2).

J. Weather Normalization

K. Late Payment Charge Revenues

ComEd's Position

ComEd assesses late payment charges upon unpaid and delinquent customer account balances. ComEd argues that the revenues it receives from these late payment charges that are solely related to the delivery services, as opposed to the supply charges for the electricity delivered, should be included in ComEd's "Other Revenues," which correspondingly reduce ComEd's Illinois jurisdictional revenue requirement. ComEd opines that it is appropriate to reduce its revenue requirement by $11.1 million in delivery services-related late payment charge revenues. (ComEd Ex. 6.0 Rev. at 43; ComEd Initial Brief at 158).

ComEd states that, in order to determine the amount of late payment charge revenues that are properly allocated to delivery services, it determined the ratio of 2009 delivery services revenues to ComEd's total 2009 revenues and applied that ratio to the total late payment charge revenues. (*See,* ComEd Ex. 6.0 Rev. at 43). ComEd argues that it is undisputed that the additional charges that AG/CUB witness Mr. Brosch seeks to include are not related to delivery services, instead, they are indisputably related to supply services. (ComEd Exs. 30.0 at 20-21 56.0 3rd Rev. at 23).

According to ComEd, the AG/CUB argument sets aside the Commission's statutory ratemaking principles in an appeal to general "fairness" that is not the appropriate standard in Illinois. It avers that the delivery service rate is not a "catch all" rate; just because a revenue component is not functionalized as transmission does not mean it should be functionalized as delivery. (ComEd Reply Brief at 155-56).

The AG's Position

The AG states that when consumers miss the due date on their bills and pay late, ComEd's tariffs provide that they must pay a late charge in the amounts of 1.0% of the late bill for local governmental agencies and qualifying schools, and 1.5% for all other customers. ComEd identified $25,110,000 in late payment revenues, but subtracted $15,995,000 of this amount from Illinois jurisdictional revenues and attributed them to "Other" jurisdiction. The AG argues that the Commission should include a total of $23,101,000 in late payment charges in ComEd's revenues when calculating ComEd's revenue requirement, recognizing that ComEd identified only $2 million that was allocated to the FERC jurisdiction.

According to the AG, ComEd was not able to identify how the remaining $13.9 million is credited to consumers or otherwise accounted for. This results in a $13,986,000 increase in revenues. (ComEd Ex. 56.0 3rd Rev. at 23-24. AG/CUB Ex. 7.1, Sch. C-14).

ComEd witness Mr. Fruehe argued that it was unfair to bundled customers to include these revenues in ComEd's revenue requirement because bundled customers are disadvantaged relative to retail electric suppliers. The AG argues that this argument overlooks the fact that both bundled and retail electric suppliers' customers may be charged late fees on the supply portion of their bills. The tariff states that:

> For a situation in which the Company does not receive payment in full for charges assessed on a bill on or before the due date shown on such bill, the amount not received by the Company on or before such due date is subject to a late payment charge.

(*See* Commonwealth Edison Co., Ill.C.C. No. 10, 1st Rev. Sheet No. 207). The late payment charge is a percentage of the outstanding balance on the bill, irrespective of whether it is supply, delivery or anything else. The AG asserts that customers who pay ComEd delivery rates are entitled to the benefit from including late payment revenues in calculating ComEd's revenue requirement. (AG Initial Brief at 150). As a delivery company, the AG continues, ComEd bills for functions other than delivery, and assesses late charges on any unpaid balance on a bill, irrespective of the function underlying the charge. The AG concludes that in the absence of a specific credit of late payment revenues to some other regulated business function, the Commission should include all of the non-FERC late payment charges in ComEd's revenue requirement. (AG Initial Brief at 150-51).

The AG states that Staff witness Ms. Hathhorn based her agreement with ComEd regarding this issue on the appearance that some supply revenues would be included in delivery services revenues, and the statement that ComEd's transmission

formula rate includes $2 million of jurisdictional late payment charges. (Tr. 1957). However, according to the AG, Ms. Hathhorn did not do any additional analysis to discover where the remaining $13.9 million was allocated, did not review ComEd's late payment tariff to see whether the tariff distinguishes between supply and distribution charges. (Tr. 1957, 1959). The AG argues that Staff's recommendation on this issue (*see* below) should be rejected because Staff's testimony "fails to completely account for the non-FERC Late Payment revenues," leaving $13.9 million unattributed, to the detriment of ratepayers. (AG Initial Brief at 151).

The AG asserts that ComEd is wrong in arguing that it should only apply an allocated portion of these charges to its revenue requirement because only a portion of each bill is for delivery services. It opines that removing $13.9 million from "other revenues" without accounting for how consumers are otherwise credited for these payments effectively transfers these revenues to ComEd's shareholder. The AG finally asserts that ComEd's revenue requirement includes a calculation of expenses, as well as revenues. The AG concludes that an underestimate of revenues provided by consumers results in an overstatement of rates, and is unjust and unreasonable. In support, the AG cites *Business and Professional People in the Public Interest v. Illinois Commerce Comm.,* 146 Ill.2d 175, 238 (1991). (AG Reply Brief at 70-71).

CUB's Position

CUB avers that late payment charges are levied on customers who have unpaid and delinquent customer account balances. CUB further states that ComEd has excluded $13.986 million of its 2009 test year recorded late fees as non-jurisdictional; however, not all of these late fees have been recognized by the FERC, the only other jurisdiction, to which, they could be claimed. CUB argues that ComEd has failed to explain how charges that it collected from delivery service customers for not paying their delivery service bills, could not be considered to be jurisdictional. CUB concludes that to reflect the late payment charge reclassification to include all non-FERC-related late payment charges, an adjustment to revenues of $13,986,000 is necessary. AG/CUB Ex. 7.1 Schedule C-14. (CUB Initial Brief at 80).

Staff's Position

Staff recommends that the Commission reject the AG/CUB adjustment. Staff's position is that because it appears that the adjustment would result in supply revenues being included in the delivery services revenue requirement, the Commission should reject the AG/CUB adjustment. (Staff Ex. 17.0 at p. 10; Staff Initial Brief at 152).

Analysis and Conclusions

Staff's and ComEd's argument on this issue appears to be that, because ComEd is only in the business of delivery services, (the cost of the actual electricity being procured from other entities and billed at approximately actual cost) any profits (late payment charges) that ComEd makes from the electricity delivered, cannot reduce ComEd's revenue requirement, even though all parties seem to agree that ComEd actually received these late payments charges, and, that it receives a profit upon both delivery services and the actual electricity it procured, in the form of these late payment

charges. No party has stated any legal basis for ignoring this reality. In fact, it appears that the argument proffered for excluding the $13.986 million ignores common sense.

ComEd has classified the $13.986 million as non-jurisdiction. However, as CUB points out, the only "other jurisdiction" that ComEd is subject to is the FERC. Yet clearly, except for $2 million, which, was accounted for by Mr. Effron, these are not FERC-related charges. Additionally, ComEd is in the business of delivering electricity, In that capacity, to many customers, it provides the electricity to deliver. Therefore, whether the late charges are upon delivery charges or upon the electricity delivered, they are imposed to the delivery service that ComEd provides to the individual customer involved.

To illustrate the fallacy of ComEd's argument, we point out that a consumer's total bill has many charges, including such items as those for energy efficiency and state and local taxes. The interest charge is imposed on all of these charges. Yet, it cannot be said that ComEd's energy efficiency program, or state and local taxes are non-jurisdictional. We conclude that ComEd has failed to establish, on an evidentiary basis, that a portion of these charges ins not jurisdictional

We further reject ComEd's argument that, pursuant to AG/CUB witness Mr. Brosch's approach, retail electric suppliers' customers would receive an unfair "advantage," due to the fact that they are subject to a lesser charge to ComEd (but one that will undoubtedly also be charged by retail electric suppliers). There has been no showing here that the system, which creates the potential for great profit (late payment charges) for bundled service customers who are late, versus a lesser profit for ComEd (use of a retail electric suppliers for the supply of electricity, and, therefore, a lesser amount, upon which, ComEd can charge a late payment fee percentage) creates any "advantage" for retail electric suppliers' customers. The only "advantage" is that ComEd receives greater profit from bundled customers. We fail to see how receipt of a greater profit from one group of customers could elevate into discriminatory charges, or, any legally-recognized "advantage." Also, this charge is only imposed upon customers when they do not pay their bills on time. We therefore adopt AG/CUB witness Mr. Brosch's adjustment on this issue.

L. New Business Revenue Credit

AG/CUB witness Mr. Effron proposes an adjustment to ComEd's projected new business revenues, thereby reducing ComEd's revenue requirement, by an additional $3.800 million. Both Staff and ComEd contest the propriety of this proposed adjustment.

ComEd's Position

ComEd contends that its revenue requirement should be reduced by $3.513 million, which, it states, represents its new business revenue credit. (ComEd Exs. 30.0 at 24-25; 30.1 at Sched. 2.9 Rev.). As it has done in its last two rate cases (dockets 05-0579 and 07-0566), ComEd has included a new business revenue credit to account for the estimated revenue from growth in customers during the *pro forma* period. ComEd offsets the cost increase from its *pro forma* additions with the revenues that it may receive from new customers in the *pro forma* period. To accurately estimate the

amount of the credit, one must ascertain which customers are new, and thus, must also take into account customer migration between customer classes. (ComEd Ex 56.0 3rd Rev. at 21-22; ComEd Initial Brief at 159-60).

According to ComEd, AG/CUB witness Mr. Effron's approach is flawed because under his approach, a migrating customer – who does not provide ComEd with any new revenue – is treated like a new customer who does provide ComEd with new revenue. Also, if the length of ComEd's *pro forma* plant additions period is reduced, the new business revenue credit should be correspondingly reduced. According to ComEd, Staff agrees with this principle, but has improperly calculated the corresponding adjustment. In support it cites Staff Ex. 16.0 at 25-26; ComEd Ex 56.0 3rd Rev. at 22-23). In addition to a mathematical error, Staff used the capital associated with customer operations instead of the New Business plant additions to determine its adjustment. (ComEd Ex 56.0 3rd Rev. at 23). ComEd states that, if Staff's recommendations regarding the *pro forma* period are adopted, the proper new business revenue credit adjustment is a reduction of 33% or $1,142,000. (ComEd Ex. 56.5 Rev.; ComEd Initial Brief at 160.

ComEd argues that the example that the AG provides in support of its *de minimus* argument is incorrect. In attempting to show that migration away from the Large Commercial and Industrial customer classes ("LCI") is immaterial, the AG adjusts the Small Commercial and Industrial customer class ("SCI") revenue credit down by $49,000. (*See,* AG Initial Brief at 152-53). The problem with the AG's example, it continues, is that it assumes that anticipated revenues from the LCI class will remain the same, which is not true, due to the expected reduction in LCI customers. (*See,* ComEd Ex. 30.2 WPC- 2.9; ComEd Ex. 56.4; ComEd Reply Brief at 157).

The AG's Position

The AG states that its witness Mr. Effron did not include the effect of a decline in the number of Large Commercial and Industrial (LCI) customers in his credit because any decline in the number of customers, by definition, is not related to plant additions to serve new customers. Removing the effect of the decline in LCI customers predicted by ComEd, Mr. Effron calculated the new business revenue credit as $8,776,000, if plant additions through June 30, 2011 are allowed. If, consistent with Mr. Effron's recommendation elsewhere, plant additions through March 31, 2011 are allowed, the new business revenue credit through March 31, 2011 is $7,313,000. (AG Initial Brief at 86).

ComEd witness Mr. Fruehe suggested that by failing to account for possible migration from the LCI class to the Small Commercial and Industrial class, Mr. Effron could, in effect be double-counting those migrating customers. (*See,* ComEd Ex. 56.0 3rd Rev. at 22; Tr. 2449). However, according to the AG, the effect of correcting for such double counting, if any, is *de minimus*. For example, using the average number of kilowatt hours for small C&I and the kilowatt hour charge, each small C&I customer adds only $1,589.28 each annually (kilowatt hour charge of $0.01750 x average number

of kilowatt hours of 90,816). The AG concludes that therefore, if the entire 31 LCI customer reduction on ComEd Exhibit 30.2, Workpaper WPC-2.9 were due to customer migration to the Small C&I customer class, the adjustment to the Small C&I revenues necessary to eliminate his alleged double count would be approximately only $49,000. (AG Initial Brief at 87).

According to the AG, ComEd unreasonably incorporates a decrease in demand and number of customers when the very purpose of the adjustment is to recognize the increased demand and revenues associated with new plant. It concludes that the Commission should adopt the new business revenue credit of $8,776,000, if plant additions through June 30, 2011 are allowed, or $7,313,000, if plant additions through March 31, 2011 are allowed, as calculated by AG/CUB witness Effron. (AG Initial Brief at 87).

CUB's Position

CUB witness Mr. Effron proposes an adjustment to ComEd's projected new business revenues to reflect ComEd's updated sales forecasts, which show higher growth in sales than what ComEd reflects in its *pro forma* adjustment for post-test year growth in sales. (AG/CUB Ex. 2.0 at 16-17). This adjustment increases ComEd's *pro forma* test year rates by $3,800,000. (AG/CUB Ex. 7.1, Schedule C-1; CUB Initial Brief at 81).

CUB states that no party has disputed that ComEd should make an adjustment for its anticipated growth in customers during the *pro forma* period which offset the cost of *pro forma* plant additions with the revenues it may receive from new customers during that same period. This calculation matches revenues from new customer growth with *pro forma* plant additions made to serve new customers. However, ComEd also seeks to recognize a decline in customers. According to Mr. Effron, this is not appropriate, as the purpose of the credit is to offset plant additions for new customers. No plant additions are made because of customer decline. (AG/Cub Ex. 8.0 at 160; CUB Reply Brief at 37).

Staff's Position

Staff agrees with ComEd. Staff recommends that any adjustment to ComEd's proposed level of *pro forma* plant additions in the category of New Business approved in the final order should also be reflected in an adjustment to the New Business Revenues. (Staff Ex. 16.0, pp. 25-26). ComEd pointed out certain corrections in surrebuttal testimony (ComEd Ex. 56.5) which Staff accepted and has reflected on Appendix A, p. 20 to its Initial Brief, along with Staff's final position regarding New Business Projects placed in service. However, Staff states that any changes to the new business projects as proposed by ComEd also should be reflected in the projected new business revenues. (Staff Initial Brief at 152-53).

Analysis and Conclusions

We agree with Staff and ComEd on this issue. No party has presented evidence indicating that a percentage of Large Commercial and Industrial customers in ComEd's

service territory is not decreasing in size and therefore becoming Small Commercial and Industrial customers. While Mr. Effron is correct in stating that any decline in the number of customers, by definition, is not related to plant additions to serve new customers, ComEd's adjustment just reflects the reality that the current trying economic times have produced.

We also note that the AG does not appear to have accounted for the decline in the Large Commercial and Industrial class customers when proffering that the migration from Large Commercial and Industrial to Small Commercial and Industrial will have a *de minimus* effect. Both the AG and ComEd agree that Mr. Effron's calculations are incorrect in the amount of $49,000. We decline to concur with the AG's contention that $49,000 is *de minimus*. Also, it is indicia that his calculations here, generally, are incorrect. ComEd's adjustment is therefore approved, as adjusted for the time period set forth herein in the discussion regarding *pro forma* capital additions and the depreciation thereof.

IX. OTHER

A. Retail Electric Supplier Services Issues

1. Requiring ComEd to Provide Alternative Electric Suppliers with Historical Interval Data within One Business Day

ComEd has agreed to process the requests for historical interval data within one business day, if a request is made by 5 p.m. on a given day, unless there is a communication barrier or some other unforeseen circumstance. It is also willing to add this matter to its RES handbook regarding the deadline for submitting requests in order to receive the requested information on the next business day. ICEA states that this satisfies its concern on this issue. ICEA also avers that no further action is warranted at this time. (See, e.g., ICEA Initial Brief at 3). This process is reasonable; it is hereby approved.

2. Retail Electric Suppliers' Use of Multiple DUNS+4 Numbers

ComEd has agreed to, subject to technical limitations and cost recovery, allow retail electric suppliers to have multiple DUNS + 4 numbers. This allows a retail electric supplier to separate its load into different sub-accounts at PJM. It also allows retail electric suppliers to better understand and manage the cost to serve different customer classes. ComEd further agreed to use its best efforts to put this recommendation into effect as soon as possible in 2011, which is acceptable to ICEA. (ICEA Initial Brief at 3). This matter, therefore, is no longer at issue. This process is reasonable; it is hereby approved.

3. ICEA's Contention that ComEd's Initial 814 Change Response Should Include an Effective Date

ICEA states that an accurate effective date should be required for the EDI 814 change request regarding Rider SBO–Single Bill Option ("SBO"), whether the change relates to initial enrollment on Rider SBO, or a change to billing under SBO. Previously, ComEd responded to an 814 enrollment for SBO with an EDI acceptance and effective date, but ComEd personnel did not review the requested change until a time that was just before the first SBO bill was issued. That initial acceptance was often faulty, as

subsequent review would reveal issues with SBO eligibility. However, now, ComEd's Rider SBO eligibility reviews will take place at the time of the initial enrollment, instead of being delayed until just before the first SBO bill is issued. ICEA maintains that this earlier eligibility review process described by ComEd satisfies ICEA's concerns regarding confusion regarding effective date for an initial SBO eligibility/enrollment.

ICEA states that the second issue arises when a RES requests a change to a customer's service under Rider SBO other than with an enrollment, for example, if a customer requests a billing change. Previously, the EDI transaction provided by ComEd noted an effective date that was not consistent with the meter reading or billing cycle date, thus requiring manual activity by the RES to identify the appropriate date. ICEA states ComEd has confirmed that it will update the RES Handbook to reflect the new rules that accommodate the new EDI standards. (ICEA Initial Brief at 3-4).

Analysis and Conclusions

We note that this issue appears to be resolved. However, to the extent that new EDI standards do not solve issues regarding mid-contract changes, we encourage the parties to work together and with the Commission's Office of Retail Market Development in order to ensure changes that may benefit the competitive retail electric market.

4. Proposed Changes to the PowerPath Website

ICEA's Position

ICEA recommended that ComEd reinstate the display of certain information on its PowerPath website, and that it develop a test site for future PowerPath changes, with releases during non-business hours and not over a holiday weekend. (ICEA Ex. 1.0 at 10-12). Based on ComEd's representations, ICEA believes that ComEd's bill estimator tool resolves concerns regarding access to information on the PowerPath website. As to future changes to the site, ICEA recommends the initiation of a test site, which is the best mechanism to evaluate the effect that potential changes to the Power Path site may cause. ICEA also recommends establishment of a technical working group. ComEd's commitment to a minimum of twenty (20) days advance notice regarding future changes to the Power Path site, with notification and discussion on each of the RES operational calls, as well as the technical working group, may be acceptable. ICEA states that more significant changes to the Power Path site may require even longer advanced notice. (ICEA Ex. 2.0, at. 10-12:ICEA Initial Brief at 3).

ComEd's Position

ComEd took no position on this issue.

Analysis and Conclusions

We encourage ComEd to establish a technical working group to better assess the impact that changes may have on ComEd's customers and electric suppliers.

5. Competitive Retail Market Development Issues

a. A Simple and Straightforward Price to Compare

ICEA states that ComEd is willing to determine and provide fixed-price supply charges under Rate BES for customers with demands under 100kW in large measure. This resolves ICEA's concerns, provided that the customer choice page is easy to find on ComEd's web site, and the Price to Compare is prominently displayed on that page. ICEA states that this recommendation is not meant to foreclose or in any way supplant the Office of Retail Market Development's "Plugged In Illinois" efforts, or its desire to establish a Commission-based Price to Compare website. (ICEA Ex. 2.0 at 12-13). This process is reasonable; it is hereby approved.

b. Creation of an "Eligible Customer List" of Residential Customers

ICEA states that it recognizes that there may be legal questions involved in producing such a list and recommends that the issue be discussed further with the Commission Office of General Counsel and the Attorney General's Office and other interested stakeholders. (ICEA Memo at 5). Therefore, this matter is no longer at issue.

B. UUIR

ComEd's Position

As part of its Alternative Regulation proposal, (*See,* docket 10-0527) ComEd proposed the Urban Underground Facility Reinvestment ("UUFR") program (also referred to as Urban Underground Infrastructure Reinvestment program ("UUIR")) as an 18-month pilot program during which, ComEd would expend nearly $50 million to explore a new way of improving the reliability of certain types of underground mainline feeder cables. The UUIR program does not generally accelerate the replacement of lead insulated mainline cable or the refurbishment of manholes; instead, during its 18-month lifespan, UUIR program work would only occur on a small subset of those mainline cables and associated manholes. (*See,* ComEd Ex. 65.0 at 2).

According to ComEd, Staff witness Mr. Stutsman's recommendation to proceed with the UUIR program in this docket should be rejected because, although the UUFR project would provide additional reliability benefits, it is not required in order for ComEd to meet its service reliability obligations. Also, Mr. Stutsman's recommendation is really a request that the Commission issue an un-funded mandate, compliance with which would necessitate significant cutbacks in other areas. (ComEd Initial Brief at 161-62).

Staff's Position

Staff contends that this Commission should require ComEd to proceed with the UUIR project, irrespective of what occurs in ComEd's Alternative Regulation docket. Staff states that ComEd is being irresponsible in denying customers the benefits of the

UUIR project by conditioning its implementation on the Commission's complete adoption of its Alternative Regulation proposal. Staff opines that ComEd is using what Staff views as a necessary project to leverage the adoption of the Alternative Regulation proposal and the current rate case.

Staff states, essentially, that ComEd's current underground maintenance program is not in good shape. The current underground maintenance program is a "reactive approach," Staff avers, that spends and invests as little as possible. According to Staff, based on ComEd's current approach, refurbishment of all manholes could take up to 100 years to complete, and replacement of cable will only occur as failure indicators appear. Staff is of the opinion that it is bare bones, reactive approach that, since 2006, is losing ground with a growing backlog in "joint issues" and "manholes requiring repair" where manholes and related cables are refurbished opportunistically, as failures occur, or new business or capacity expansion projects require. Staff concludes that the current program does not proactively address "root causes" of customer interruptions and/or system outages, which is not consistent with the objectives in Section 8-401 of the Public Utilities Act. (*See,* Staff Exs. 9.0 at 4, 6; 24.0 at 14-16; Staff Initial Brief at 155-56).

Staff reviewed the UUIR project and determined that it was necessary to meet the requirements in Section 8-401 of the Public Utilities Act that utilities must provide adequate, efficient, reliable, environmentally safe and least-cost and that it provides appropriate consideration to costs of service interruptions while protecting the public health, safety and welfare under Section 1-102 of the Public Utilities Act. Staff additionally states that this project will have a long-term positive impact on utility earnings.

Staff found convincing ComEd's description of the "leading cause" of underground mainline feeder cable system failures that the UUIR project has been designed to proactively address, along with the many benefits provided in reliability, safety, environmental and operational efficiencies derived from implementation of the UUIR project. (*See,* Public Staff Group Cross Ex. 1 at. 21, 23, 27, 29, 31-32, 36, 42, 44, & 52-56). By addressing "leading causes" of underground system failures, the UUIR project will be addressing factors that would tend to cause grouping or pockets of excessive unreliability and, thus, the project helps ComEd fine-tune reliability work, as it targets a root cause of "unreliability pockets."

The UUIR project, Staff opines, addresses "leading causes" of underground system failures in a proactive Reliability Centered Maintenance approach. ComEd has collected the "data" that has identified underground mainline feeder cable system failures, which occur in and around manholes, as a leading cause of customer interruptions. By proactively testing and inspecting PILC (Paper-Insulated, Lead-Covered) cables, joints, and manholes and then initiating repairs or replacement when defects or faults are evident, before failure is evident, Staff opines that customer interruptions are avoided. Also, repairs would be more cost-effective, without the extra expense involved in fixing infrastructure failures in order to restore service. (Staff Initial Brief at 156-58).

Analysis and Conclusions

Staff avers that the UUIR program is a necessity, due to ComEd's failure to proactively address underground maintenance. ComEd avers that, if it were to proceed with this $50 million program, it would have to make significant cutbacks in other area. This is due to ComEd's decision to use a historic test year. The expenditures on this program would not occur during that test year period.

We decline to require ComEd to move forward with this program on an un-funded basis. Staff cites system improvements as a source of possible savings; however, Staff does not indicate that ComEd will save the cost of the program ($50 million). Additionally, while it may be possible for ComEd to include the cost of this program in a future rate case, requiring ComEd to complete this program, when it is currently not funded, does not provide this Commission with assurance that it will be completed in a thorough or even competent manner.

We additionally note that this is a test program of limited duration and it is on a small subset of mainline cables and associated manholes. It does not appear to address the totality of the concerns that Staff has expressed.

However, Staff has articulated a legitimate and serious concern. That is, according to Staff, ComEd's current maintenance program is but a "bare-bones" approach. We additionally note that ComEd has identified underground mainline feeder cable system failures as a leading cause of customer interruptions. We conclude that workshops shall be conducted for the purpose of developing proactive methods of identifying problems with underground mainline feeder cables, with ComEd to report to this Commission within nine months from the date of issuance of a final Order in this docket. This report shall include: a) the results of the workshops; and b.) what ComEd is doing to proactively identify underground system problems before they cause service interruptions.

C. Updated Distribution Loss Study

This issue is discussed in Section VIII C 6 herein.

D. Meters and Meter Reading

1. Timely Meter Reading

ComEd's Position

Staff witness Mr. Rockrohr and ICEA witness Mr. Fein have expressed concerns about meter reading and estimated bills and, in Mr. Fein's case, unbilled meters. According to ComEd, its personnel attempts to read meters in accordance with the Commission's rules governing meter reads and bill estimation. (*See,* ComEd Exs. 61.0 Rev., 12-13; Ex. 36.0 2nd Rev. at 26). However, it states, to address those circumstances where ComEd is prevented from reading meters for reasons outside of its control, ComEd is looking to an Information Technology solution to assist customer service agents and others faced with such a circumstance. In support, it cites the testimony of its witness, Mr. Marquez. According to ComEd, there have not been significant delays in delivering meter data to retail electric suppliers. ComEd avers that

it is also "working on" process improvements and assigning additional resources to mitigate the volume of delayed bills. (ComEd Ex. 61.0 Rev. at 13). ComEd concludes that it has addressed all of the issues regarding meter reading, estimated bills and unbilled meters. (ComEd Initial Brief at 162-63).

ICEA's Position

ICEA states that, over the past six months preceding the filing of direct testimony in this docket, its members have been subject to a significant number of instances where current usage data for meters was not provided by ComEd, or was substantially delayed. (ICEA Ex. 1.0 at. 8-9). This causes problems for customers, as it places them under greater financial strain when the meter is finally read and billed. It also causes problems for retail electric suppliers, as they do not receive timely payment for service provided. Also, according to the ICEA, retail electric suppliers will be confronted with an increased amount of calls from customers, and potential complaints stemming from the delay and the necessarily higher "make-up" bill from ComEd. ICEA further states that, if a customer has changed retail electric supplier during the time period, in which, the meter has not been read, those problems for retail electric suppliers are compounded and they will probably face an increase in uncollectible accounts that would not have occur, if ComEd's billing were timely and accurate.

ICEA further avers that ComEd has indicated informally that it established processes and developed a plan to resolve the problem, but a comprehensive, detailed written plan for resolving this issue has not been provided in this proceeding. In addition to resolving the underlying backlog, ICEA posits that ComEd should: (1) send out communications to affected customers indicating that ComEd has experienced difficulties that have prohibited ComEd's personnel from providing the necessary data to alternative electric suppliers; and (2) provide a weekly report to alternative electric suppliers regarding its progress in resolving the issue, as well as expectations for the coming weeks, which specifically identifies those situations, in which, meter readings are delayed based on restricted access to the meter. (ICEA Ex. 2.0 at 8-10; ICEA Initial Brief at 5-6).

Staff's Position

Staff has observed a high number of meter seals missing from ComEd's meters at customers' premises. Staff recommends that ComEd consistently keeps seals on its meters to counteract tampering and theft. It also promotes safety. (Staff Ex. 21.0 at. 24). ComEd responded to Staff's concern about unsealed meters by stating that only employees wearing proper personal protective equipment (PPE) can safely seal the meters. (ComEd Ex. 61.0 at. 12). However, Staff would expect that ComEd's employees who re-seal its meters would wear appropriate PPE. Because ComEd provided no indication as to how it will change its existing practice, (which Staff believes to be ineffective) Staff recommends that this Commission require ComEd to promptly seal or re-seal unsealed meters that are discovered in the field. Staff makes this recommendation because ComEd's personnel cannot know whether customers or other individuals are disturbing or tampering with un-sealed meters. (Staff Ex. 6.0 at 33 Staff Initial Brief at 166-67).

Additionally, Staff states that it is concerned about high numbers of estimated meter readings that are associated with ComEd customer accounts. Staff notes that estimated bills are the cause of many customer complaints and requests for meter accuracy tests. Staff states that its concern that ComEd personnel either underestimates, or is not concerned by, the scale of this problem. Staff recommends that the Commission require ComEd to develop internal audits that include accountability for occurrences of meters going unread without a valid and documented reason. (Staff Reply Brief at 88-89).

Analysis and Conclusions

Except when exigent circumstances are present, utilities are required to read meters "at least every second billing period." (83 Ill. Adm. Code 280.80). Both Staff and ICEA have presented evidence indicating that ComEd is experiencing a high level of unread meters, which suggests that ComEd's personnel is not abiding by this regulation. Staff additionally addresses a safety concern, which is a high number of unsealed meters. What Staff and ICEA have voiced here appears to be a personnel problem on the part of ComEd that causes unnecessary bill dispute issues with customers and alternative retail electric suppliers. These disputes also result in an unnecessary divergence of ComEd's manpower and resources, as its personnel must address them when they arise. We conclude that therefore, ComEd shall develop and implement an improved personnel policy that addresses timely meter reading and unsealed meters. This policy shall include periodic internal audits of its meter-reading personnel. ComEd shall, additionally, develop a policy that documents, in writing, to the customer and to ComEd, the instances, in which, access to a meter was not obtained and the circumstances regarding lack of access to the meter. ComEd shall report to this Commission regarding its implementation of this policy within six months from the date upon which a final Order issues in this docket.

However, at this time, we decline to adopt ICEA's proposal. An improved personnel policy should address both Staff's concerns and that of ICEA.

E. New Section 9-250 Investigation of ComEd's Electric Rate Design

This issue is discussed in Section VIII C 3 a herein.

F. Other

XI. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having considered the entire record herein and being fully advised in the premises, is of the opinion and finds that:

(1) Commonwealth Edison Company is an Illinois corporation engaged in the transmission, distribution, and sale of electricity to the public in Illinois and is a public utility as defined in Section 3-105 of the Public Utilities Act;

(2) the Commission has jurisdiction over the parties and the subject matter herein;

(3) the recitals of fact and conclusions of law reached in the prefatory portion of this Order are supported by the evidence of record and are hereby adopted as findings of fact and conclusions of law; the Appendix attached hereto provides supporting calculations;

(4) the test year for the determination of the rates herein found to be just and reasonable should be the 12 months ending December 31, 2009; such test year is appropriate for purposes of this proceeding;

(5) for the test year ending December 31, 2009 and for purposes of this proceeding, as adjusted, the Company‘s rate base is $6,629,441,000;

(6) a just and reasonable return which ComEd should be allowed to earn on its net original cost rate base is 8.51%; this rate of return incorporates a return on common equity of 10.50% and on long-term debt of 6.52%;

(7) the rate of return set forth in Finding (6) results in base rate operating revenues of $2,213,408,000 and net annual operating income of $564,164,000 based on the test year approved herein;

(8) the Commission, based on ComEd’s original cost of plant in service as of December 31, 2009, before adjustments, of $14,758,892,000, and reflecting the Commission’s determination adjusting that figure, approves $14,423,422,000 as the original cost of plant as of said date;

(9) ComEd‘s rates which are presently in effect are insufficient to generate the operating income necessary to permit ComEd the opportunity to earn a fair and reasonable return on net original cost rate base; these rates should be permanently canceled and annulled;

(10) the specific rates proposed by ComEd in its initial filing do not reflect various determinations made in this Order regarding revenue requirement, cost of service allocations, and rate design; ComEd‘s proposed rates should be permanently canceled and annulled consistent with the findings herein;

(11) ComEd should be authorized to place into effect tariff sheets designed to produce annual base rate revenues of $2,213,408,000 which represent an increase of $166,088,000 or 8.11%; such revenues will provide ComEd with an opportunity to earn the rate of return set forth in Finding (7) above; based on the record in this proceeding, this return is just and reasonable;

(12) the determinations regarding cost of service, rate design, and terms and conditions of service contained in the prefatory portion of this Order are reasonable for purposes of this proceeding; the tariffs filed by ComEd should incorporate the rates, rate design, and terms and conditions set forth and referred to herein;

(13) new tariff sheets authorized to be filed by this Order should reflect an effective date not less than thirty (30) days after the date of filing, with the tariff sheets to be reviewed by the Rates Department of the Commission, and corrected, if necessary, within that time period.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that the tariff sheets presently in effect rendered by Commonwealth Edison Company are hereby permanently canceled and annulled, effective at such time as the new tariff sheets approved herein become effective by virtue of this Order.

IT IS FURTHER ORDERED that the proposed tariffs seeking a general rate increase, filed by Commonwealth Edison Company on June 30, 2010, are permanently canceled and annulled.

IT IS FURTHER ORDERED that Commonwealth Edison Company is authorized to file new tariff sheets with supporting workpapers in accordance with Findings (11), (12), and (13) of this Order, applicable to service furnished on and after the effective date of said tariff sheets.

IT IS FURTHER ORDERED that Commonwealth Edison Company's embedded cost of service study is accepted as a basis for setting rates in this proceeding.

IT IS FURTHER ORDERED that any motions, petitions, objections, and other matters in this proceeding which remain outstanding are hereby denied.

IT IS FURTHER ORDERED that, subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the Administrative Review Law.

DATED:	April 1, 2011
BRIEFS ON EXCEPTIONS DUE:	April 8, 2011
REPLY BRIEFS ON EXCEPTIONS DUE:	April 15, 2011

Glennon P. Dolan
Claudia Sainsot
Sonya J. Teague
Administrative Law Judges
Illinois Commerce Commission