STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

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

REPLY BRIEF ON EXCEPTIONS OF COMMONWEALTH EDISON COMPANY

PUBLIC VERSION

ORAL ARGUMENT REQUESTED

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REPLY BRIEF ON EXCEPTIONS OF
COMMONWEALTH EDISON COMPANY

Commonwealth Edison Company ("ComEd") respectfully submits this Reply Brief on Exceptions in accordance with Section 200.830 of the Rules of Practice of the Illinois Commerce Commission (the "Commission" or "ICC"), 83 Ill. Admin. Code § 200.830, and the schedule established by the Administrative Law Judges ("ALJs"). Any additional modifications to the Proposed Order that are required in response to Staff's and other parties' Briefs on Exceptions are noted within the body of this brief.

I. INTRODUCTION

The Proposed Order recognizes that ComEd's reasonable and prudent costs of providing electric delivery services have risen significantly since ComEd rates were last set. The rates it would set recognizes, for example, that ComEd's rate base has significantly grown due to nearly $2 billion in new investment, that ComEd has incurred substantial additional expense in providing appropriately for the health and welfare of its workers and retirees, and that ComEd's future ability to invest in and maintain its system depends on setting an accurate rate of return reflecting the requirements of the capital markets in which ComEd competes with other companies for funds. While no one likes cost increases, they have been necessitated by ComEd's obligations to serve its customers well and to provide Northern Illinois with a reliable electric infrastructure.

The Proposed Order also recognizes that establishing a just and reasonable rate means protecting consumers and utilities alike or, as the Supreme Court put it, 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) ("*BPI II*"). Thus, "[a]llowing 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,[1] but also by fundamental principles under the Act and the Illinois and federal constitutions." PO at 10 (additional citations omitted). The principle of full cost recovery is enshrined in the law not only out of a requirement to be fair to shareholders. Parties as diverse as Staff, CUB, and ComEd all acknowledge and agree that when a utility's reasonable and prudent costs are not recovered, customers suffer in the end. ComEd Init. Br. at 2-6; McNally Dir., Staff Ex. 5.0, 2:31-42; Thomas, Tr. 1762-63. The business of encouraging the Commission to reject recovery of prudent and reasonable utility costs is not in the public interest.

The Proposed Order recognizes many of ComEd's needs for increased revenues, yet falls somewhat short of even a middle ground. As ComEd noted in its Brief on Exceptions ("BoE"), the Proposed Order, while recognizing and allowing recovery of approximately $160 million of ComEd's increased costs, left ComEd with a dangerous continuing revenue deficiency of about $170 million dollars annually. ComEd BoE at 1. That will hurt customers over time and hasten the need for additional rate relief. Despite that, however, Staff and many parties' Briefs on Exceptions encourage the Commission to cut ComEd's revenues even further below its costs. In

[1] "Charges for delivery services … shall allow the electric utility to recover the costs of providing delivery services through its charges to its delivery service customers …." 220 ILCS 5/16-108(c).

this Reply Brief on Exceptions ("RBoE"), ComEd will explain why those efforts are unlawful and unsupported, and why, on those issues, the Proposed Order should be accepted.

Many of the reasons those exceptions should be rejected are peculiar to the individual argument and will be discussed solely in the body of this Brief. However, there are several new and troubling themes that will be highlighted here.

Results-oriented arguments that turn their backs on the advocate's own testimony. The apparent desire to cut ComEd's revenues no matter the evidence has led several parties to take positions *inconsistent with the testimony of their own witnesses*. For example:

- AG-CUB witness Effron from the beginning recommended that the Commission recognize ComEd's *pro forma* plant additions in the first quarter of 2011. Effron Dir., AG/CUB Ex. 2.0, 4:89-90. Yet, now AG and CUB oppose the position his sworn testimony supported and propose to reject all forecast 2011 additions. AG BoE (Corr.) at 5-6[2]; CUB BoE at 1-2.
- Throughout this case and even into post-hearing briefing, Staff has opposed reducing ComEd's distribution revenue requirement for non-distribution late payment charges. Hathhorn Reb., Staff Ex. 17.0, 10:196-201; *see also* Staff Init. Br. at 152. Yet, Staff's BoE includes no exception to a $14 million deduction for just those non-jurisdictional charges.
- AG and CUB repeatedly emphasize our depressed economic conditions. Yet, not only do they ignore the economic benefits of infrastructure investment, they argue for normalized pension costs based on pre-recession figures, and contrary to the

[2] All cites herein are to the AG BoE filed on April 11, 2011 unless otherwise noted as AG BoE (Corr.) to reflect a citation to the Corrected BoE filed on April 14, 2011 as an attachment to the AG's Motion for Leave to File Corrected Brief on Exceptions.

most current actuarial report, even though their pension expense witness testifies that we have not returned to pre-recession conditions. Smith, Tr. 540:20-541:3.

In none of these cases is an explanation given. The prior sworn testimony is not even referenced. The positions taken in the BoEs are simply the positions that cut ComEd's rates the most.

Efforts to induce the Commission to unlawfully attempt to restrict ComEd's right to file rates. REACT tries yet again to advocate for its already thrice-rejected effort to "dismiss" ComEd's tariffs based on claims that ComEd violated the *Rate Design Investigation* Order by not providing certain information with its initial filing.[3] REACT BoE at 21-22. As ComEd pointed out, this is an unprecedented remedy and legally unauthorized that REACT sought only after ComEd already had provided the information about which it was complaining. Now, however, REACT is attempting to perpetuate its argument into the ComEd's *next* rate case. The Commission, in general, has the authority to order ComEd to perform studies, gather information, work with its Staff, and report to the Commission. But, the Commission may not bar ComEd from filing a future rate case until that work is complete. Article IX of the Public Utilities Act ("PUA") allows utilities to file new tariffs, proposing new rates, at any time. The Supreme Court has made clear that the law "does not restrict when or how often a utility may file for a rate increase," and, further, that "the Commission cannot impose a rate moratorium upon a utility during [any] period without the agreement of the utility." *Bus. & Prof'l People for the Pub. Interest v. Illinois Commerce Comm'n*, 136 Ill. 2d 192, 225, 230 (1989) ("*BPI I*"). As ComEd's BoE pointed out, the Commission cannot suspend ComEd's ability to file future tariffs by requiring that any such filing occur only after additional work and studies are complete.

[3] *Illinois Commerce Commission v. Commonwealth Edison Co.*, ICC Docket No. 08-0532 (Order, April 21, 2010) (hereinafter, the "RDI Order").

ComEd BoE at 6-7, 75-76. While ComEd will respect and conform to lawful Commission directions, REACT's express invitation to bar rate case filings until that work is complete is asking the Commission to commit grave legal error.

I. OVERALL REVENUE REQUIREMENT AND REVENUE DEFICIENCY

Staff's BoE (at 103) indicates that its "Appendix A" attached thereto is intended to reflect corrections to the figures in the Proposed Order's Appendix A on five topics: (1) four revenue requirement-related items, one of which is cash working capital; plus (2) the original cost determination. Staff's BoE (at 103) makes clear that its Appendix A is not intended to reflect Staff's Exceptions but simply to correct the Proposed Order's Appendix A's figures on these five topics given the recommendations contained in the Proposed Order.

ComEd has the following comments on Staff's Appendix A. First, ComEd is unable to verify Staff's Appendix A's cash working capital figure, because Staff has not supplied all of the information underlying the calculation. Second, Staff's Appendix A does not correct for the omission in the Proposed Order's Appendix A of the Proposed Order's recommended late payment charge revenues adjustment. Finally, of course, neither Staff's Appendix A nor the Proposed Order's Appendix A reflects ComEd's Exceptions.

II. RATE BASE

A. Overview

The Proposed Order (at 11) adopts $13,925,117,000 as the appropriate amount for the determination of ComEd's original cost of plant – commonly referred to as an "original cost finding" – as of December 31, 2009. Staff is correct that that amount is the result of starting with ComEd's $13,932,447,000 (Houtsma Dir., ComEd Ex. 6.0 Rev., 22:449-453), and then subtracting the amount of $7,330,000 associated with the uncontested portion of Staff's

capitalized incentive compensation adjustment. PO at 11; Staff BoE at 2; Ebrey Reb., Staff Ex. 16.0, Sched. 16.15, line 5.

Staff proposes that the $13,925,117,000 be reduced further, to $13,908,457,000, "if the conclusions in the PO are approved by the Commission". Staff BoE at 2. What Staff means by that, more specifically, is that the $13,925,117,000 figure should be reduced by the following four items, if and only if the Proposed Order's recommendations on these four items are approved in the Commission's final Order: (1) $15,693,000 for Staff's proposed adjustment to decrease General and Intangible ("G&I") Plant on the grounds of functionalization, (2) $896,000 for the contested portion of Staff's proposed capitalized incentive compensation adjustment relating to the Exelon 2009 Key Manager Restricted Stock Award Program, (3) $62,000 for Staff's proposed adjustment to the capitalized portion of perquisites and awards, and (4) $9,000 for Staff's proposed adjustment to the capitalized portion of professional sports activity-related costs, a total of $16,600,000. *Id*. ComEd opposes all four of those other adjustments. ComEd BoE at 32-37, 46, 56-57, 59-60.

However, to the extent, that the Commission's final Order were to approve any or all of those four other adjustments, then ComEd, in the interests of narrowing the issues, does not oppose reducing the $13,349,227,000 original cost finding figure consistent with the approved amount(s) of the adjustment(s), provided that the amount is reduced by no more than the $16,660,000 that Staff's proposes, meaning that the original cost finding figure can be reduced to no less than Staff's proposed figure of $13,908,457,000. The evidentiary record does not support any figure below $13,908,457,000.[4]

[4] ComEd notes that, consistent with its technical Exception No. 66 (*see* ComEd BoE at 107), the original cost finding figure that is correctly determined here for purposes of this portion of the Proposed Order text also should be repeated in Findings and Ordering Paragraph (8).

B. ***Pro Forma*** **Capital Additions**

Staff, the AG, and CUB raise exceptions intended to increase the Proposed Order's reduction of ComEd's proposed *pro forma* adjustment for plant additions. As explained below, Staff's incorrectly argues that the Proposed Order's allowance of specific New Business blanket projects is not supported by the record while AG/CUB's request for an additional adjustment for December 2010 *pro forma* plant additions is contrary to and not supported by the record.

1. Response to Staff

a. The Record Contains Extensive Evidence Supporting the Proposed Order's Allowance of ITNs 5968, 5972, and 24143

Staff claims that the Proposed Order "errs in accepting three blanket projects to be acceptable pro forma plant additions (PO, p. 22) because there is no evidence in the record to support these blanket projects (ITNs 5968, 5972, and 24143) as known and measurable." Staff BOE at 3 (emphasis added). To the contrary, there is extensive evidence in the record supporting the Proposed Order's proper conclusion that the plant additions to be made under these blanket investment tracking numbers ("ITNs") "are reasonably likely to be in place before June 30, 2011" and are "known and measurable." PO at 22. Staff's allegation that there is no evidence in the record to support the Proposed Order's conclusions is a gross mischaracterization of the record. Further, it demonstrates Staff's failure to confront the robust and unrefuted evidence as to how prudent utility management meets its very important obligation to serve new customers by grouping and managing small repetitive work under blanket projects. To demonstrate, ComEd recites the very detailed evidence that follows. While the following showing is limited to the three ITNs addressed in Staff's Brief on Exceptions, it is representative of the record support that exists for all of the *pro forma* plant additions that Staff would disallow.

Investment tracking numbers ("ITNs") 5968: Inside Chicago Baseline, 5972: Outside Chicago Baseline, and 24143: CE Distrib Transformers-New Business were specifically identified in ComEd's direct testimony. *See* ComEd Ex. 8.2, p. 6; ComEd Ex. 6.2, WPB-2.1a, p. 10. ComEd witness Mr. Donnelly testified that "new commercial and residential business" was one of the areas of investment reflected in ComEd's proposed *pro forma* adjustment for plant additions. Donnelly Dir., ComEd Ex. 8.0, 51:1077-81. Mr. Donnelly explained that documentation and databases regarding the categories of investment, including New Business, "are and will be available in ComEd's data rooms" and "will allow an interested party to trace virtually every dollar of [ComEd's] pro forma plant additions from the highest category of costs down to the lowest level of documentation – work orders, purchase orders, timesheets, etc." *Id*. at 50:1056-51:1065, 51:1069-73.[5] Mr. Donnelly also explained that:

> independent engineering experts with decades of utility industry construction and engineering experience have conducted a thorough analysis of the pro forma plant additions. That analysis included interviews of ComEd employees who are responsible for the planning, management and implementation of the pro forma plant additions; review of the procedures and practices for making such investments and the documentation associated with pro forma projects in various stages of implementation, including those that are completed, in-flight and planned for in-service later in the pro forma period.

Donnelly Dir., ComEd Ex. 8.0, 53:1112-19.

ComEd witness Mr. Donnelly's response to Staff's original proposal to disallow 100% of ComEd's *pro forma* plant additions to be placed in service after September 30, 2010 included testimony that "blanket programs represent the baseline routine investment activities that ComEd must – with certainty – complete in order for ComEd to continue to provide basic service."

[5] Indeed, ComEd provided presentation boards "designed to assist interested parties in understanding the documentation available with respect to *pro forma* plant additions" as well as searchable electronic access to the extensive supporting documentation. Donnelly Sur., ComEd Ex. 58.0 Rev., 11:229-12:263; ComEd Ex. 58.3. This information was available in the Springfield and Chicago data rooms since August of 2010. *Id*.

Donnelly Reb., ComEd Ex. 32.0 Rev., 2:34-35. Mr. Donnelly explained that "[b]lanket programs are a superior means of managing groups of similar, high volume, recurring tasks such as installation of new services, replacement of underground facilities, installation of new meters and local distribution transformers, and replacement of overhead facilities." *Id*. at 25:513-26:516. He further explained that:

> investments [managed under blanket programs] lend themselves not only to being managed together, but also to being analyzed in the aggregate. For each blanket, ComEd has data concerning the nature of the work as well as both historical data and forward-looking data about the required level of activity. The best evidence of future blanket activity is the level of current activity and investment, trend data, and analyses of the underlying need(s) driving the work. Because blankets are, by their very nature, repetitive activities, this type of data is predictable …. Reasonable certainty concerning both the timing and cost of blanket plant additions can be achieved based on such data.

Id. at 26:527-27:539.

Mr. Donnelly also described the processes and procedures by which ComEd tracks and executes New Business work from the time a customer makes a new service request to engineering design and through construction. *Id*. at 45:946-46:952. He also explained that a detailed discussion of the nature of this work and the relevant management procedures was included in a Report prepared by industry experts at Power Delivery Research & Consulting Corp. ("PDR&C") entitled "Install New Services" submitted in response to Staff data requests. *Id*. The Install New Services Report was admitted into evidence as ComEd Ex. 59.2.

Mr. Donnelly specifically addressed the three blanket ITNs at issues here. Donnelly Reb., ComEd Ex. 32.0 Rev., 46:954-47:978. He explained that if a project is estimated to exceed $100,000 it is managed as a unique project, but that "the vast majority of the new connections [ComEd] provide[s] for customers cost less than $100,000" and are managed as routine new business work under these ITNs. *Id*. Mr. Donnelly testified to the nature of the work to be

performed and described the types of documents that support the work under ITNs 5958 and 5972:

> During the complete pro forma period, more than $118.1 million will be invested through thousands of relatively small and separate tasks and managed under one of two blanket projects which we categorize as either Inside the City of Chicago Baseline (ITN 5968) or Outside Chicago Baseline (ITN 5972). $56.3 million of investment under these two ITNs will be placed into service over the last two months of 2010 and the first two quarters of 2011. ComEd Ex. 32.2 includes examples of work packages for projects completed under the baseline blankets. As one can see, these projects typically begin with a customer request, require ComEd (or the customer) to obtain appropriate permits and approvals and ultimately engineer, schedule, and complete the work. While these projects do not individually involve large dollars, they still require engineering analysis, planning, work crew coordination and, in most cases, coordination with a customer's construction schedule.

Id. at 46:960-71. He provided similar testimony for ITN 24143:

> We have one other blanket ITN for ComEd Distribution Transformers, ITN 24143. We expect to place into service during the current pro forma period approximately $8.4 million through this ITN. ComEd places thousands of distribution transformers into service each year. In order to obtain favorable pricing, ComEd typically acquires transformers in bulk through its supply function and then assigns transformers to the various functional areas so that it may appropriately track utilization.

Id. at 47:973-78.

Finally, Mr. Donnelly established why the plant additions to be made under these three ITNs are known, measurable, and reasonably certain to occur:

> The Commission can be reasonably certain that this plant will be placed in service for at least three reasons:
>
> First, ComEd has many years of experience performing this type of customer driven work. We consider much, if not most, of this work "baseline" because it occurs regularly and at fairly predictable levels. This allows us to develop meaningful and informed projections of the labor and materials that will be needed to carry out the work in our numerous regions. We expect to place into service $106.7 million of plant relating to this core work category during the remainder of 2010 and the first two quarters of 2011.
>
> Second, the volume of work that is currently in the queue for service by the end of the second quarter 2011 is significant. We have more than 3,500

> pending requests for new services to be completed in the three quarters ending second quarter of 2011, and ComEd currently has more than 13,000 work orders open under the New Business category.
>
> Finally, ComEd recognizes that economic conditions may influence New Business work activity. There is a strong correlation between economic metrics and New Business baseline activity. ComEd has developed models that translate future economic predictions (Moody's Economy and McGraw Hill Construction data) coupled with historical service completions into New Business baseline forecasted activity. Based upon these models, a forecast of the number of baseline services anticipated in 2010 and 2011 was determined. These projections have been utilized as an input in determining the spend required to perform this work scope.

Donnelly Reb., ComEd Ex. 32.0 Rev., 47:981-48:1002.

ComEd also responded to Staff's attack on *pro forma* plant additions in general and blanket ITNs in particular with the testimony of PDR&C industry expert Mr. Donohue describing his thorough review, analysis, and conclusions regarding ComEd's pro forma plant additions. *See generally* Donohue Reb., ComEd Ex. 35.0 Rev. Mr. Donohue confirmed that the blanket projects he reviewed included the three blanket ITNs at issue here and that his analysis included reviewing planning documents and interviewing personnel; he also concluded that the remaining work to be performed under the three blanket projects "is typical of work ComEd routinely performs and presents no unusual risk to its ability to forecast and implement consistent with its forecast." *Id*. at 9:178-82, 13:266-67, 28:588-97, 41:824-5; ComEd Exs. 35.4, 35.5, 35.6 and 35.7. Mr. Donohue also testified to the prudence and reasonableness of managing work under blanket programs in general, and explained that ComEd's practices in this regard compare favorably to industry practices. *Id*., ComEd Ex. 35.0 at 11:229-24, 40:805-18, 43:872-86; ComEd Ex. 35.8.

Staff's rebuttal testimony moved its proposed cutoff for *pro forma* plant additions from September 30, 2010 to December 31, 2010, but did not respond or address the specific information and testimony discussed above regarding ITNs 5968: Inside Chicago Baseline, 5972:

Outside Chicago Baseline, and 24143: CE Distrib Transformers-New Business. *See generally* Ebrey Reb., Staff Ex. 16.0. In surrebuttal, Mr. Donnelly reviewed the large ITNs that remained subject to Staff's proposed *pro forma* plant adjustment disallowance, including the ITNs at issue here. Donnelly Sur., ComEd Ex. 58.0 Rev., 24:524-25:540. Given Staff's general objection to these ITNs, Mr. Donnelly's response consisted of a general review of the work to be performed and information that supported ComEd's determination of the work to be performed under these ITNs during the *pro forma* period. *Id*. at 31:689-33:728, 36:792-98.

Mr. Donohue provided surrebuttal testimony explaining that Staff incorrectly asserted that he did not review specific projects, and he provided general testimony regarding Staff's inappropriate view that investment to be made under blanket projects are not known and measurable. Donohue Sur., ComEd Ex. 59.0 3:50-6:108. Mr. Donohue also attached reports covering his prior reviews of the blanket ITNs Staff would disallow, and explained why this work is known, measurable, and reasonably certain to occur (including reports on new services and distribution transformers). *Id*. at 8:144-58; ComEd Exs. 59.2, 59.6. Regarding Staff's attack on ComEd's *pro forma* adjustment for plant additions to be installed pursuant to blanket projects, Mr. Donohue also testified and concluded that:

> ComEd has committed the labor, tools, fleet, facilities, management systems, as well as entered into material supply contracts and ordered or received much of the materials that will be used to perform the work during the first half of 2011. For these investments ComEd knows that it will be investing in poles, wires, insulators, relays, transformers, and other similarly standard types of property.

Donohue Sur., ComEd Ex. 59.0, 10:191-95. Staff chose not to cross examine Mr. Donohue on this testimony. Indeed, Staff chose not to cross examine any ComEd witness on the details supporting these three ITNs. Staff's failure to acknowledge this and the other information

discussed above does not negate the fact that it is contained in the record and supports the Proposed Order's conclusions.

b. <u>Staff Wrongly Implies that Documentation Regarding ITNs 5968 (New Business, Inside Chicago Baseline), 5972 (New Business, Outside Chicago Baseline), and 24143 (Distribution Transformers) Was Specifically Requested In Data Request TEE 14.03</u>

Staff also contends in its Brief on Exceptions that in response to Staff data request TEE 14.03 ComEd only provided documentation on ITNs 5968 and 5972, not ITN 24143. Staff BOE at 3. Staff further states that "nothing was included in that documentation for work extending into 2011 for these ITNs, only work for 2010." *Id*. Staff's argument omits material information and is totally lacking in merit.

Staff fails to state the specific request made in Staff Data Request TEE 14.03, which was the following:

> Provide the total number of projects and the cost of the projects the company has included as pro forma plant additions that will be closed by June 30, 2011 but after December 31, 2010 for the following categories:
>
> a) Capacity Expansion projects that are "summer critical".
>
> b) Facility Relocation projects that were required by a Government entity.
>
> c) CWIP projects that do not include AFUDC.
>
> d) Projects for which there are signed contracts.

Staff Group Cross Ex. 1, p. 185. Staff Data Request TEE 14.03 did not request any documents at all, and neither New Business ITNs in general nor the three blanket ITNs at issue here were identified as one of the "categories" for which certain information was requested. By arguing that no documentation about these ITNs was provided in response to TEE 14.03, Staff's improperly and unfairly implies that such documentation was sought – it was not. The documents in Attachment 3 that are the subject of Staff's argument were voluntarily provided by

ComEd in response to part (d) of TEE 14.03 that requested information about "[p]rojects for which there are signed contracts." *Id*. ComEd identified the ITNs for which there were contracts, and voluntarily provided copies of the underlying contracts. No documentation was asked for or even generally referenced in TEE 14.03. Staff's assertions implying that requested relevant documentation was requested but not produced is meritless, and its argument that as a result ComEd has somehow not proven up its case is baseless. Moreover, since ComEd performs work with its own crews, the existence or non-existence of signed third-party contracts says nothing about the existence or non-existence of support for ComEd's plant additions. As discussed above, there is extensive support for these three ITNs.

Staff also states that documentation for ITNs 5968 and 5972 included in ComEd Ex. 32.2 does not correspond to the approximately $42 million projected in surrebuttal testimony by the Company for those ITNs in 2011." *Id*. This statement simply ignores the extensive evidence provided on these ITNs discussed above. The work under these blanket ITNs is small and repetitive. The basis for the investment to be made was explained, and ComEd's testimony specifically pointed out that the documentation provided in "ComEd Ex. 32.2 includes examples of work packages for projects completed under the baseline blankets." Donnelly Reb., ComEd Ex. 32.0 Rev., 46:960-71. The work performed under these baseline blankets is described in extensive detail as set forth above, and Staff's assertion that it "has seen no evidence of what makes up the $42 million" is plainly wrong. Staff BOE at 3. Similarly, Staff incorrectly asserts that "[t]he Company believes providing a sample of the types of documentation available to support its pro forma plant additions obviates its burden of proof necessary to demonstrate that these costs are known and measurable." *Id*. To the contrary, and as found by the Proposed

Order, ComEd did provide evidence meeting its burden of proof on these ITNs – Staff simply continues to ignore this evidence.

c. <u>Staff's Argument is Contrary to Law</u>

While ComEd did provide evidence and documentation supporting these ITNs, it should also be noted that Staff's position is also contrary to the law and constitutes an attempt to impose a rule that has not been adopted. Staff's attempt to argue that the *pro forma* standard can only be satisfied by certain documentary evidence has been previously rejected by the Illinois appellate court. *See Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 322 Ill. App. 3d 846, 849 (2nd Dist. 2001) (Commission held to have committed clear error in rejecting various rate base items on the unlawful ground that they were supported only by sworn testimony). Staff's attempt to raise this failed and previously rejected argument is improper and should again be rejected here.

d. <u>Staff's Admits that Support has been Provided</u>

Finally, Staff acknowledges that "ComEd offers statistics regarding the amount of new connections it has installed historically as the basis for the amounts projected for the first 6 months of 2011for ITNs 5968 and 5972," but argues that this same type of information was rejected by the Proposed Order for the remainder of 2011's pro forma plant additions. Staff BOE at 3-4. First, the statistics are only part of the evidence provided by ComEd, and Staff's acknowledgment is contrary to its earlier argument that "no evidence" was provided. While similar evidence was provided for certain other blanket ITNs, the PO does not specifically discuss or reject this evidence as inferred by Staff. If anything, Staff's argument shows why the other ITNs should be allowed as well. When the Proposed Order focused on and analyzed

ComEd's evidence, it found it adequate. Staff's claim in no way supports its view that the New Business blanket ITNs should be disallowed.

For all the foregoing reasons, Staff's exception should be denied.

2. <u>Response to AG/CUB</u>

The AG and CUB argue that ComEd's forecast of plant additions in December 2010 is unreasonable and should be reduced from $100.8 million to $50 million because the December 2010 amount of plant additions to be placed in service is above the average of plant additions for the first 11 months of 2010. AG BOE at 5-10; CUB BOE at 1-3. As an initial matter, it should be noted that the amount of December 2010 plant additions expected to be placed in service has been available at all times throughout this case. See ComEd Ex. 8.2 (listing expected in-service months for each ITN, including projects with December 2010 in-service date). If the AG/CUB wanted to challenge the amount of *pro forma* plant additions to be placed in service in December 2010, they should have presented testimony regarding those amounts (which would have allowed ComEd to respond via testimony) instead of laying in the weeds until cross examination of Staff's witness (who did not recommend such an adjustment, but rather recommended allowing ComEd's projected *pro forma* plant additions through and including December 2010). AG/CUB's witness on *pro forma* plant additions made no proposal to limit December 2010 plant additions. *See generally* Effron Dir., AG/CUB Ex. 2. Thus, AG/CUB's position is inconsistent with and beyond the testimony of their own witness.

The AG contends that "[t]he Proposed Order acknowledged that AG/CUB pointed out the disproportionately large amount of pro forma plant additions that ComEd proposed for December 2010 ($100.8 million), nearly twice the level of average actual monthly plant additions of $50 million for the first eleven months of 2010." AB BOE at 5. The Proposed

Order contains a summary of the AG's argument made in briefs, but contains no acknowledgment that there is any validity whatsoever to that argument as suggested by the AG's Brief on Exceptions. The AG's similar attempt to misread the Proposed Order's recommendations regarding *pro forma* plant additions for January through June of 2011 as applicable to the AG's "December 2010" *pro forma* amount argument are contrary to the language and intent of the Proposed Order and are unavailing.

The AG/CUB's testimonial arguments fare no better. As pointed out in ComEd's Reply Brief (at 27-28), the AG/CUB's reliance on the cross examination of Staff witness Ms. Ebrey misstates the record because Ms. Ebrey clarified that she would question whether or not December was reasonable, but had not performed any specific review:

> Based on a question that [AG counsel] had to me where she indicated that the budget for December was two times the monthly budget for the rest of 2010. I would -- I would question whether or not it was reasonable. I, once again, haven't gotten into that review.

Ebrey, Tr. 752:5-10. Indeed, the cross examination language cited by AG/CUB to claim that Staff found these amounts unreasonable leaves out the balance of the sentence which refutes that claim: "Subject to my review of the – this statement that the budget is twice – the December budget is twice the monthly budget for the rest of 2010, it probably is not reasonable; <u>but like I've said, I have not had the time to get into the details of those updated numbers</u>." Tr. at 731-32 (emphasis added). Nor has Staff advocated a reduction of ComEd's December 2010 *pro forma* amount. Moreover, the argument advanced by AG/CUB is rank speculation and misleading. There is no evidence that ComEd has performed twice the average work in December 2010, only that a larger than average amount of investment was scheduled to be placed in service in December 2010. This makes particular sense given that utility projects related to governmental or commercial work with end of year deadlines also have to be completed in December.

ComEd's evidence identifies the specific projects and programs going into service in December 2010. See ComEd Ex. 55.2, Workpaper WPB-2.1a, Support (January 3, 2011 REVISED). The record fully supports ComEd's *pro forma* plant additions for December 2010, and provides no support whatsoever for AG/CUB's argument.

C. Accumulated Provisions for Depreciation and Accumulated Deferred Income Taxes (ADIT)

Staff, AG, CUB, and IIEC exceptions all take exception to conclusions of the Proposed Order on Accumulated Depreciation and ADIT. No roll forward of the depreciation reserve or ADIT is appropriate *on the facts of this case*. ComEd BoE at 23-28.

ComEd further pointed out in its BOE that whatever impact the appellate decision in the appeal of ComEd's 2007 rate order[6] had on the "roll forward" of the depreciation reserve, it has none on the roll forward of ADIT. The two accounting entries are separate and distinct, and the fact that both are generally deducted from plant in service to arrive at net rate base does not compel the conclusion that both should be treated equivalently for purposes of the *pro forma* rule. The ADIT issue was not addressed by the Appellate Court in that decision. Indeed, the rationale of the *ComEd 2010* decision makes clear that ADIT is different from the depreciation reserve for this purpose: "Section 9-211 of the Act provides that a utility's rate base may include 'only the *value* of such investment which is both prudently incurred and used and useful in providing service to public utility customers.' … Here, the dispute on the accumulated depreciation issue is not whether the planned plant additions will be used and useful, but how to measure the value of all the plant in service. Accumulated depreciation reduces plant investment at original cost by the decline in investment value recorded in the reserve for accumulated

[6] *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 405 Ill. App. 3d 389 (2nd Dist. 2010) (hereinafter "*ComEd 2010*").

depreciation…. 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." 405 Ill.App.3d at 404-05 (emphasis in original). Quite simply ADIT does not "reduce plant investment value." Although the two issues are separate and distinct, the Briefs on Exceptions filed by Staff, the AG, IIEC and CUB erroneously treat them as though they are identical. The Commission should ensure that they are, as they should be, treated individually.

The issue raised by the Staff, AG, CUB and IIEC Briefs on Exception all relate to the roll forward required on account of the 2011 *pro forma* additions allowed by the Proposed Order. Staff argues that no roll forward into 2011 is appropriate because the few *pro formas* allowed does not constitute a "comprehensive restatement" of ComEd's overall rate base. Staff BoE at 6. The AG, CUB and IIEC argue that the Proposed Order is deficient in not more specifically stating how accumulated depreciation and ADIT is to be "rolled forward" with respect to the 2011 *pro forma* plant additions permitted by that Order. CUB proposes that a "proportion" test be adopted, *i.e.*, that accumulated depreciation and ADIT on test year embedded plant be rolled forward in the same proportion that the allowed *pro forma* adjustments bear to total *pro forma* adjustments. CUB BoE at 3-4.

IIEC and belatedly the AG, by contrast, argue that accumulated depreciation and ADIT should be rolled forward in its entirety through 2011, even though only a small amount of *pro forma* projects are being allowed in 2011. IIEC BoE, Appendix A, Exc. 1; AG BoE (Corr.) at 13-18. ComEd has already stated its arguments why accumulated depreciation and ADIT on embedded plant do not need to be rolled forward in this case (ComEd BOE at 23-28) and

incorporates but will not repeat those arguments here. Furthermore, with respect to those periods in which ComEd is allowed some but less than all of its *pro forma* additions, the "proportion" test advanced by CUB is not appropriate and should be rejected. The IIEC test is so extreme as to violate any sense of "matching" gross plant and depreciation, which was an important basis of its argument and the Court's decision in *ComEd 2010*: "IIEC argues that the Commission violated sections 287.20 and 287.40 of title 83 of the Administrative Code, as well as corresponding test-year principles, by mismatching 2008 gross plant investment and 2006 test year accumulated depreciation." 405 Ill. App. 3d at 406. "Consistent with the matching requirement, accumulated depreciation is subject to test-year principles because depreciation expense is subject to test-year principles." *Id.* at 407. "ComEd's interpretation also is plainly inconsistent with basic matching principles." *Id.* How a handful (no more than 18%) of *pro forma* plant additions in 2011 "matches up" with rolling forward 100% accumulated depreciation on all of ComEd's test-year plant is unexplained by IIEC and its recent convert, the AG. The fact is, of course, the "match" does not exist.

First, nothing in the Appellate Court's September 2010 decision addressed this issue. None of the *pro forma* additions at issue there were in periods in which fewer than all were allowed. Thus, the outcome of this issue is not controlled by that decision, and neither the CUB proposal nor the IIEC proposal is needed to, in CUB's words, "ensure conformity with" that decision. CUB BoE at 3.

Second, the AG argues that its proposal is required in order to assure that rate base will include only "those portions of plant that are actually used and useful." AG BoE (Corr.) at 14. That argument is misconceived. No question has been raised, nor could it, that some of the plant at issue is not or may not be used and useful. Moreover, the roll forward of accumulated

depreciation and ADIT is wholly unrelated to, and separate from, the "used and useful" issue. Plant is neither more nor less "used and useful" because of some accounting convention regarding these two entries. As the Appellate Court said in *ComEd 2010,* "the dispute on the accumulated depreciation issue is not whether the planned plant additions will be used and useful, but how to measure the value of all the plant in service." 405 Ill.App.3d at 405.

The AG further argues that by allowing limited plant additions in 2011 with no roll forward of accumulated depreciation or ADIT on embedded plant, the Proposed Order "is putting the Company in a *better* position than it would be in than if all of ComEd's *pro forma* plant additions had been accepted and netted against offsetting adjustments." AG BoE (Corr.) at 15 (emphasis in original). Notably, the AG cites no record evidence to support this proposition and therefore it would be legal error to base any decision on this assertion. The $50 million per month plant in service additions referenced in the previous paragraph of AG's BoE is based on only ten months in 2010, and completely ignores ComEd's own projections for the last two months of that year and all of 2011, as well as the increase in depreciation expense related to those additions. *See* AG Cross Ex. 25 and Tr. 2397-98. ComEd believes that all of the evidence would show that the assertion is false, that when all relevant factors are considered - - including other plant additions, depreciation expense and removal costs - - ComEd would have a higher revenue requirement with the allowance of *all* the *pro forma* projects and the complete roll forward of the depreciation reserve and ADIT than it would under the Proposed Order's treatment of this issue.

Moreover, this issue should not be decided on the basis of what treatment makes ComEd "better off" or "worse off." The question should be one of a principled and legally supportable analysis and neither CUB's approach nor the IIEC (and now AG) approach is principled or

legally supportable. In fact the IIEC approach would lead to the absurd result that allowance of any amount of *pro forma* adjustments in a particular period – even $1 million or less – would trigger a roll forward tsunami of all accumulated depreciation and ADIT on $7 billion of embedded plant. Neither logic nor fairness would support such a result.

Staff's position in the "roll forward" issue in the context of the limited 2011 plant additions allowed for 2011 is the only appropriate one. That is especially true based on the record of this case. Because rate base is not being comprehensively restated by the recognition of only part of ComEd's projects, it is not realistic to conclude that rate base is likely to be overstated in the absence of a roll forward through the *pro forma* period given the fact that additional investment unquestionably being made during that period is being excluded. No one contends that these additional, excluded projects will not be completed; on the contrary, they are being excluded only because of an unduly strict reading of the "known and measurable" and "determinable" requirements in the *pro forma* rule. Thus, if anything, the gross plant in service will be understated. Moreover, if the "known and measurable" and "determinable" standards are to be applied consistently, it is not proper simply to estimate the amount of the roll forward through some type of "proportionality" approach as CUB recommends. If ComEd's historically-proven track record of completing *pro forma* projects cannot satisfy the *pro forma* rule, surely the CUB approach, which was never the subject of any evidence in this case, must be rejected. For reasons stated above, the IIEC approach is even less defensible. Similarly, the AG's arguments on this issue lack any substance, and are based on non-record "evidence" and should be rejected.

D. CWIP – Construction Work in Progress

The Proposed Order (at 33-35) correctly approves ComEd's inclusion in rate base of $12,591,000 for small projects Construction Work in Progress ("CWIP") that does not accrue Allowance for Funds Used During Construction ("AFUDC"), and the Proposed Order correctly rejects AG/CUB's proposal to remove from rate base all of the non-AFUDC CWIP.

The AG and CUB Exceptions on this subject (AG BoE at 1, 14-23; CUB BoE at 4-8) are wrong both factually and legally. They should be rejected.

History and Law. The Commission has approved the inclusion of CWIP in rate base for over 90 years, and the Act confirms its legal authority to do so. The Commission has approved the inclusion of CWIP in rate base since at least the 1920's. *Citizens for a Better Env't v. Illinois Commerce Comm'n*, 103 Ill. App. 3d 133, 140 (4th Dist. 1981). Moreover, in 1985, the General Assembly added Section 9-214 to the Act, 220 ILCS 5/9-214, confirming the authority of the Commission to include CWIP in rate base. Section 9-214(e) states: in part: "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."

The Commission has approved the inclusion of non-AFUDC CWIP in rate base in every ComEd delivery services rate case.

Year Case Filed	Amount of non-AFUDC CWIP Included in Rate Base in Commission's Final Order	Citations
1999	$79,963,000	*Commonwealth Edison Co.*, Docket No. 99-0117 (Order Aug. 26, 2999), at Appendix A, Schedule 3, line 7
2001	$20,813,000	*Commonwealth Edison Co.*, Docket No. 01-0423 (Interim Order April 1, 2002), at Appendix A, Schedule 3, line 8; and (Order March 28, 2003), at Appendix A, Schedule 3, line 8

Year Case Filed	Amount of non-AFUDC CWIP Included in Rate Base in Commission's Final Order	Citations
2005	$41,047,000	*Commonwealth Edison Co.*, Docket No. 05-0597 (Order June 26, 2006), at Appendix A, p. 5, line 7
2007	$33,682,000	*Commonwealth Edison Co.*, Docket No. 99-0117 (Order Sept. 10, 2008), at Appendix A, p. 4, line 7

In only one of those cases, the 2005 case, did any witnesses ever question the propriety of inclusion of non-AFUDC CWIP in rate base as such, and they each later withdrew that position and supported the inclusion of a normalized level of CWIP in rate base. In the 2005 case, two witnesses, a Staff witness and a witness for the combination of CUB, the Cook County State's Attorney's Office, and the City of Chicago ("CCC"), each initially questioned the inclusion of non-AFUDC CWIP, on the theory that it was a double-count with ComEd's *pro forma* capital additions, but, after ComEd confirmed that its figure for non-AFUDC CWIP in rate base was intended to represent a normal level of non-AFUDC CWIP and not the particular projects in non-AFUDC CWIP at the historical measurement period, the Staff, CCC, and ComEd witnesses each testified in support of inclusion of the normalized level of non-AFUDC CWIP approved in the final Order. *Commonwealth Edison Co.*, Docket No. 05-0597, p. 5 (Order June 26, 2006).

<u>The Instant Case</u>. In the instant case, ComEd seeks to include $12,591,000 of non-AFUDC CWIP in rate base, a reasonable level based on the test year level and looking forward. *E.g.*, Houtsma Dir., ComEd Ex. 6.0 Rev., 26:524 – 27:533; McMahan Dir., ComEd Ex. 9.0, 52:1020 – 53:1050. That $12,519,000 figure is less than 1/2 the level approved in its 2007 rate case and less than 1/3rd the level approved in its 2005 rate case.

ComEd's direct case included not only Schedule B-7, showing the $12,591,000 figure, but also the eight-page work paper WPB-7, showing the 235 small projects that made up the non-AFUDC CWIP balance of $12,590,910 as of December 31, 2009, that ComEd used as a

representative level for non-AFUDC CWIP. ComEd Ex. 6.1, Sched. B-7; ComEd Ex. 6.2, work paper WPB-7; McMahan Dir., ComEd Ex. 9.0, 53:1040-1045.

The AG/CUB Arguments. Despite the above facts, including the testimony CUB's 2005 rate case witness, the AG and CUB in the instant case propose to disallow all non-AFUDC CWIP in rate base. They make what amounts to six arguments for their novel proposal:

1. Section 9-211 of the Act supports disallowance of all CWIP in rate base as not "used and useful";
2. Section 9-214 does not mandate inclusion of CWIP in rate base;
3. ComEd's evidence supporting its non-AFUDC CWIP is insufficient;
4. the Proposed Order reversed the burden of proof on this issue;
5. ComEd's non-AFUDC CWIP is or may be vendor-financed; and
6. the Proposed Order's requirement that ComEd submit a lead/lag analysis of its costs in relation to CWIP not accruing AFUDC in its next rate case is insufficient.

See AG BoE at 1, 14-23; CUB BoE at 4-8. None of the six AG/CUB arguments justifies the disallowance of ComEd's non-AFUDC CWIP in rate base.

Section 9-211 and the Used and Useful Standard. To begin with, the AG/CUB argument that Section 9-211 supports disallowance of all CWIP in rate base as not "used and useful" is frivolous, for three different reasons. First, even supposing that non-AFUDC CWIP must be used and useful to be included in rate base, ComEd's non-AFUDC CWIP is used and useful even under the most stringent notion of what it means to be used and useful. ComEd accrues AFUDC on projects with a total expected expenditure of greater than $25,000 and an expected construction period of within 30 days. McMahan Dir., ComEd Ex. 9.0, 52:1025-1028. Thus, "projects not accruing AFUDC will, by definition, be in service within a short period of time. However, as those investments are placed in service, they are constantly being replaced by new 'short-term' non-AFUDC projects." *Id.* at 52:1035-1037. Accordingly, the non-AFUDC CWIP

balance is representative of the balance as of the end of the period as to which the Commission's approves ComEd's *pro forma* additions, and thus the non-AFUDC CWIP balance involves projects that are generally expected to go into service within 30 days of that date and that will be used and useful during the vast majority of the period for which rates are being set. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:707-711.

Second, AG/CUB's Section 9-211 / used and useful argument is wrong, in any event, because it misapplies the used and useful standard as to CWIP. In other words, CWIP is used and useful. The courts and the Commission have found that CWIP is used and useful and that the used and useful standard is not inconsistent with approval of CWIP in rate base. In *Citizens for a Better Env't v. Ill. Commerce Comm'n*, 103 Ill. App. 3d 133, 138-141 (4th Dist. 1981), the Appellate Court noted the Commission's finding that CWIP may be used and useful, the court found that the CWIP in question was for plant that was being prepared to be used to generate nd distribute electricity and therefore was used and useful, and concluded that the General Assembly had acquiesced in the Commission's decisions that CWIP may be included in rate base consistent with the Act's used and useful standard.[7] Mr. Brosch and AG/CUB have not mentioned that the Commission rejected Mr. Brosch's testimony that CWIP be disallowed on various grounds, with the Commission finding, among other things, that notwithstanding the "used and useful" doctrine, CWIP may be allowed in rate base, in *The Peoples Gas Light and Coke Company*, Docket No. 90-0007, 1990 Ill. PUC Lexis 593, *17-23 (Order Nov. 9, 1990). In *North Shore Gas Company*, Docket No. 91-0010, 1991 Ill. PUC Lexis 636, *19 (Order Nov. 8,

[7] This case was decided under former versions of the Act, but its conclusions on this subject are confirmed by the later addition of Section 9-214 to the Act, noted above and discussed further below. The Proposed Order (at 34) declines to apply the case here because it predates Section 9-214, but the addition of Section 9-214 only confirms the case is correct.

1991), the Commission rejected a proposed disallowance of non-AFUDC CWIP, stating in part: "The Commission has consistently ruled that CWIP is used and useful and, thus, the inclusion of CWIP provides a proper 'matching' with the capital structure supporting rate base."

Finally, AG/CUB's reliance on Section 9-211 is erroneous. Even if AG/CUB were not wrong about CWIP not meeting the used and useful standard, Section 9-214(e) confirms that CWIP may be included in rate base. Section 9-214 is the more recent section and the more specific of the two statutes concerning CWIP. AG/CUB's reading of Section 9-211 as to CWIP improperly would nullify Section 9-214(e). AG/CUB's argument (AG BoE at 14) that the Act should be construed as a whole, while an acceptable generalization, cannot rationalize using an older, general provision to override and nullify a later and more specific provision in the same statute. PO at 34; *Knolls Condominium Ass'n v. Harms*, 202 Ill. 2d 450, 459 (2002) ("Statutes relating to the same subject must be compared and construed with reference to each other so that effect may be given to all of the provisions of each if possible. Even when an apparent conflict between statutes exists, they must be construed in harmony with one another if reasonably possible. It is also a fundamental rule of statutory construction that where there exists a general statutory provision and a specific statutory provision, either in the same or in another act, both relating to the same subject, the specific provision controls and should be applied.") (citations omitted); *Jahn v. Troy Fire Protection Dist.*, 163 Ill. 2d 275, 282 (1994) ("The fundamental rule of statutory construction is to give effect to the intent of the legislature. When choosing between two statutes in direct conflict, the more recent enactment generally will prevail as the later expression of legislative intent.") (embedded citations omitted). This point is moot, however, because AG/CUB are wrong in the first place in arguing that Section 9-211's used and useful standard is not met as to CWIP, as discussed above.

Section 9-214. AG/CUB's second argument, that Section 9-214 does not mandate inclusion of CWIP in rate base, is technically correct. However, that is not a ground for disallowance, as illustrated by the Commission's prior decisions.

ComEd's Evidence. AG/CUB's third argument, that ComEd's evidence supporting its non-AFUDC CWIP is insufficient, is wrong. ComEd's direct case submitted evidence supporting its non-AFUDC CWIP in rate base that was similar to the evidence that it submitted in its four prior delivery services rate cases. In each of those cases, the Commission approved non-AFUDC CWIP in rate base. AG/CUB do not even claim that ComEd's evidence falls short of its evidence in the prior cases. The AG's BoE (at 15) suggests that ComEd failed to show that the investments are scheduled to be placed in service within 12 months of the rate determination. That is false, as illustrated by the discussion above of the testimony of Mr. McMahan and Ms. Houtsma. Indeed, AG/CUB's witness Mr. Brosch himself testified that these projects have a construction completion period shorter than 30 days. AG BoE at 16. The Proposed Order (at 34) does state that ComEd's evidence is vague in one respect, but that is not as to ComEd's support of the non-AFUDC CWIP but rather as to ComEd's response to Mr. Brosch's vendor financing theory, discussed below. If the Commission, on this evidentiary record, were to hold that ComEd's evidence somehow were insufficient, it would be on a new ground, not found in the Commission's rules or in any prior Order, and it should be prospective only.

The Burden of Proof. AG/CUB's fourth argument, that the Proposed Order reversed the burden of proof, is incorrect factually and legally. Once a utility presents a *prima facie* case of the costs needed to provide service, the burden of going forward with the evidence shifts to other parties to show that the costs are unreasonable because of inefficiency or bad faith. *Illinois Bell Tel. Co. v. Illinois Commerce Comm'n*, 327 Ill. App. 3d 768, 776 (3rd Dist. 2002); *City of*

Chicago v. Cook County, 133 Ill. App. 3d 435, 442-443 (1st Dist. 1985). The utility does not bear the burden of proof to refute any issue that conceivably could be raised relevant to a rate's reasonableness, nor is it required to anticipate and disprove the arguments other parties might make. *City of Chicago v. Cook County*, 133 Ill. App. 3d 435, 442 (1st Dist. 1985). Here, ComEd's direct case presented ample evidence, consistent with the proof in prior cases, supporting its non-AFUDC CWIP, as discussed earlier. Page 34 of the Proposed Order does not reverse the burden of proof. Rather, based on its review of Ms. Houtsma's and Mr. Brosch's testimony, it concludes that it cannot state with reasonable certainty that ComEd's non-AFUDC CWIP is vendor financed as Mr. Brosch had claimed.

The Vendor Financing Theory. AG/CUB's fifth argument, that ComEd's non-AFUDC is vendor financed, lacks merit. In rebuttal and surrebuttal, Ms. Houtsma responded to Mr. Brosch on the subject of CWIP, including his vendor financing theory. Houtsma Reb., ComEd Ex. 29.0, 42:897 – 43:926; Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:701 – 34:723. Among other points she made are (1) that the vendor financing will at best only exist for a matter of weeks (until the invoices are paid) and cannot be considered a long-term source of financing for these investments; and (2) on a going forward basis, because non-AFUDC CWIP constantly is turning over, a new Accounts Payable balance will always be related to new non-AFUDC CWIP not included in rate base. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 33:718-721. As noted above, the Proposed Order (at 34) reviewed the testimony and concluded that it did not warrant adopting Mr. Brosch's theory.

The Proposed Order's Recommendation as to Future Cases. AG/CUB's sixth and final argument, that the Proposed Order's recommended requirement that ComEd submit a lead/lag analysis of its costs in relation to non-AFUDC CWIP in its next rate case is insufficient, does not

justify AG/CUB's proposed disallowance. As discussed above, the disallowance lacks merit. The Proposed Order's findings rejecting the AG/CUB proposal are not undercut by the Proposed Order's recommendation that additional information be provided on this subject in a future rate case, particularly when no Commission Rule or prior Order required that information.

B. <u>West Loop Project</u>

The Proposed Order rejects disallowing – and compelling ComEd to write off – an approximately $4 million high voltage cable that was damaged due to an unprecedented series of events.[8] PO at 36. The Proposed Order correctly recognizes that the law of prudence governs here and that accidents do not warrant disallowances absent very specific facts proving imprudence that are not present here. PO at 35-36. Only Staff takes exception, and Staff cites to only three pages from its own testimony and two from its own brief, despite the extensive evidence, including investigation reports, in the record. Staff's conclusion that "ComEd's management allowed the cable to fail" (BoE at 8), is simply unsupportable. Both the law and the record amply support the Proposed Order's conclusion.

The law is clear and uncontested. Management is prudent when it exercises a "standard of care which a reasonable person would be expected to exercise under the same circumstances encountered by utility management at the time decisions had to be made." *E.g.*, *Illinois Power Co. v. Illinois Commerce Comm'n*, 339 Ill. App. 3d 425, 435 (5th Dist. 2003); *Illinois Commerce Comm'n v. Commonwealth Edison Co.*, Docket No. 84-0395 (Order Oct. 7, 1987) ("*ComEd '87*"), at 17. Staff agrees. Mr. Rockrohr's testimony quotes almost identical language. Rockrohr Dir., Staff Ex. 6.0, 5:102-13; Tr. 863:21 – 864:5

[8] No one contests the necessity of the repair, the manner in which it was carried out, or its costs. Rockrohr, Tr. 857-58. Rather, Staff's theory is that the cable only failed because of imprudence and, thus, the costs of even a flawless repair should be disallowed.

Finding imprudence requires evidence meeting a very strict set of standards. Among them are three standards of particular relevance here:

- *Imprudence may not be shown in hindsight.* Past actions can appear unreasonable given what we know now, but that is never the test of prudence. On this, Staff and ComEd agree. Rockrohr, Tr. 864:6-12. "In determining whether or not a judgment was prudently made, only those facts available at the time the judgment was exercised can be considered. Hindsight review is impermissible." *ComEd '87* at 17 (emphasis added); *accord Illinois Power Co.,* 339 Ill. App. 3d at 428; *Business and Professional People for the Public Interest v. Illinois Commerce Comm'n,* 279 Ill. App. 3d 824, 828 (1st Dist. 1996) ("*BPI '96*"); Rockrohr, Tr. 865:7–15.

- *A finding of imprudence may not be made based on a bona fide professional disagreement.* Engineers can and do disagree about conclusions, just as do other professionals. They can also disagree about what is reasonable. Rockrohr, Tr. 864:16-22. To be imprudent, an action or omission must lie outside that realm of reasoned disagreement. "Imprudence cannot be sustained by substituting one's judgment for that of another. The prudence standard recognizes that reasonable persons can have honest differences of opinion without one or the other necessarily being 'imprudent'." *ComEd '87* at 17; *accord Illinois Power Co.,* 339 Ill. App. 3d at 435; *BPI '96,* 279 Ill. App. 3d at 828. Therefore, "a reasonable difference of opinion with respect to engineering judgment cannot sustain a finding of imprudence." Rockrohr, Tr. 865:3-5.

- *Human error, even egregious human error, is not evidence of imprudence.* Indeed, error, even egregious error, is unavoidable. *See* Rockrohr, Tr. 858:2-18, 859:22 –

860:6; *BPI '96*, 279 Ill. App. 3d at 833. Prudence does not require perfect performance (Rockrohr, Tr. 864:13-15), and the fact that an accident or accidents occurred does not mean that ComEd management was at fault. *E.g.,* Rockrohr, Tr. 859:3-21. Moreover, management must consider the cost of preventing error, which can be high. *BPI '96,* 279 Ill. App. 3d at 831. Thus, the law prevents a utility from being "faulted for the human error of its employees unless the evidence shows that [it] failed to adequately hire and train the proper employees." *Id.* at 829. In short, some human error, even egregious error, is unavoidable. *See* McMahan Reb., ComEd Ex. 33.0, 14:303-4; McMahan Sur., ComEd Ex. 60.0, 7:143-5; Rockrohr, Tr. 858:2-18;*BPI '96*, 279 Ill. App. 3d at 833.

In sum, "reasonable operating costs should include employee errors which management cannot reasonably prevent," and that one "cannot justify punishing Edison for any mistakes where management has directed matters responsibly." *BPI '96*, 279 Ill. App. 3d at 832.

The evidence here is clear that the original cause of the failure of the cable was an utterly unprecedented error. Absent impermissible hindsight, it could not have been anticipated by ComEd management. ComEd management had, in fact, taken all reasonable steps to prevent this type of error. The record shows:

- [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

Staff also appears to contend that, even after the cable was critically damaged, ComEd wrongly failed to detect the damage earlier, inferring that this could have minimized the ultimate effect. The evidence does not support a claim that ComEd should have detected the problem earlier. It also supports no inference that earlier detection would have minimized the damage. The evidence is clear:

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

- There is no evidence that had ComEd's management had learned of the circumstances sooner, the ultimate damage would have been mitigated. [redacted]

In short, for Staff to claim that "ComEd's management" ignored or did not investigate a condition it was aware of is an unsubstantiated distortion of the record. No evidence supports a finding of management imprudence, and extensive evidence shows that ComEd's management acted within the range of reasonableness "under the circumstances encountered … at the time decisions had to be made." *ComEd '87* at 17; McMahan Reb., ComEd Ex. 33.0, 1:18-22. The Proposed Order's decision to reject the disallowance is correct and should be adopted.

C. <u>Underground Cable Assets</u>

In ComEd's 2007 rate case, the Commission excluded from rate base approximately $18 million of underground cable assets serving customers solely because it found that ComEd had not proven that they were acquired at reasonable and prudent cost. PO at 37. In this case, ComEd proved that they were, and no party presented any contrary evidence. ComEd Init. Br. at 34-37; ComEd Reply Br. at 41-43. Staff and CUB nonetheless take exception to the Proposed Order's conclusion to include these assets in rate base. PO at 37. Their arguments rest on the claim that ComEd "itself viewed this [2007] disallowance as permanent" because the assets were written off on ComEd's books. Staff BoE at 9; CUB BoE at 8. This argument is incorrect and irrelevant.

It is irrelevant because the Commission, in fact, excluded those assets from rate base in 2007 not for any "permanent" reason, but because it found there was a lack of evidence that has now, undeniably, been cured. Nothing prevents assets disallowed once based on a failure of proof to be later included in rate base provided, as here, they remain used and useful. *See, e.g.*, *BPI II*, 146 Ill. 2d at 222 (recognizing that under the Act, "the Commission is to include in a utility's rate base only the value of a new … plant which is used and useful in providing service to public utility customers."). The Commission does not have to call it "temporary," because a failure of proof is inherently temporary. Once assets serving customers are proven to have been acquired reasonably and prudently, both Illinois law and Constitutional principles require that they be included in rate base. *See, e.g.*, 220 ILCS 5/16-108(c); *Bluefield Water Works & Improvement Co. v. Public Serv. Comm'n*, 262 U.S. 679, 690 (1923) ("Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment."); *Citizens Util. Bd. v. Ill. Commerce Comm'n*, 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."). What Staff and CUB claims ComEd assumed is irrelevant. There are no grounds to continue to disallow these assets.

Moreover, Staff's and CUB's inference about ComEd is false. ComEd did not consider these assets permanently disallowed. ComEd wrote these assets off when they became impaired after the Commission's 2007 decision. *See* ACS 360-10-35-21(3c), *formerly* FAS 144, ¶ 8. It made no difference that that "adverse regulatory action" was potentially reversible in a future case; these were assets in a specifically identifiable "long lived" asset group the costs of which

ComEd could not then recover. As such, they were required to be written off. The only inference that can be drawn is ComEd followed the accounting rules.

In sum, these are $18 million of assets that today are serving customers and ComEd acquired prudently and reasonably. Legally, they must be included in rate base, as the Proposed Order correctly recommends. No changes should be made to the Proposed Order and no change to the result it reached can be lawfully made.

D. Whether to Include PORCB (Purchase of Receivables and Consolidated Billing Service) Costs in Base Rates

The Proposed Order recommends an adjustment that reduces ComEd's rate base by $14,147,000 for jurisdictional PORCB capital costs and by another $2,722,000 for deferred O&M expenses of the PORCB project, and further provides that ComEd may recover these costs through filing a new PORCB-related rider under Section 16-118 of the Act, 220 ILCS 5/16-118. PO at 39-41 and Appendix A, p. 7, col. (b) and (d) (citing Ebrey Reb., Staff Ex. 16.0 and Sched. 16.10). ComEd's BoE requested that, if the Proposed Order's recommendation is adopted, then certain language changes and corrections to figures should be made. ComEd BoE at 28-32; ComEd Exception No. 4.[9]

Dominion and Staff have filed Exceptions. Dominion argues that only $2,474,211 should be recovered through the rider and the rest through rate base. Staff argues once again that the Commission should defer the allocation decision. ComEd responds as follows.

[9] ComEd notes that Dominion's BoE and Staff's BoE each confirm a portion of ComEd's Exception No. 4, *i.e.*, that Dominion is not raising a prudence issue but only an allocation issue. Dominion BoE at 11; Staff BoE at 10.

1. **Dominion's Exception**

Dominion's Position. Dominion's BoE argues for a narrower reading of Section 16-118, and that, under that reading, only $2,474,211 should be removed from rate base for rider recovery under Section 16-118 (taking no position on whether ComEd should file a new rider versus a revised rider). These are the costs Dominion considers to be for work on the core POR service. The other costs should remain in rate base.

As ComEd's testimony and prior briefing indicate, ComEd agrees with Dominion that the Commission should determine in the instant case which costs do and do not qualify for rider recovery under Section 16-118, and ComEd's BoE at 28-31 and Exception No. 4 support proposed language changes that would clarify the Proposed Order's findings on this subject.

With respect to the merits of Dominion's position, ComEd refers to its post-hearing briefs, which detailed the evidence in the record regarding the costs that make up the total PORCB-related costs and the jurisdictional PORCB-related costs included in rate base, and the alternatives before the Commission, including that of keeping in rate base the costs associated with the Retail Office / Customer Data Warehouse work while removing the other costs in rate base for rider recovery. *See*, in particular, ComEd's Reply Br. at 43-49.

Whatever the Commission's determination on Dominion's Exception, ComEd requests that the final Order be clear that it is making a final determination of which costs are to be subject to rider recovery and which are to be included in rate base, and that, as to rider recovery, the findings be such that they do not deny ComEd the opportunity to recover fully its costs. ComEd is entitled to recover fully these costs. ComEd BoE at 28-31.

Finally, Dominion's $2,474,211 figure needs to be corrected; only the $2,192,151 jurisdictional portion of that $2,474,211 was included in ComEd's proposed rate base. ComEd Reply Br. at 44-45, 48 n.7.[10]

Dominion's Proposed Language. As stated above, Dominion's proposed language including the $2,474,211 figure (rounded to $2.5 million), needs to be corrected if Dominion's position were to be adopted.

Dominion's proposed language in most other respects would not be problematic, if Dominion's position were to be adopted, but certain changes should be made.

- Dominion's proposed language appears to continue to take the position that certain of ComEd's PORCB costs are for CB service under Section 16-118(d) of the Act. That is incorrect, because ComEd is offering only a POR service combined with CB, under Section 16-118(c) of the Act. ComEd BoE at 29 n. 14.

- In addition, the language does not make certain of the changes, such as the changes relating to a new rider versus a revised rider, found in ComEd's Exception No. 4.

1. Staff's Exception

Staff's Position. Staff's BoE on this subject is somewhat confusing, and advocates language changes in the Proposed Order that, in part, are inaccurate and inappropriate.

Staff's BoE initially focuses on the Proposed Order's characterization of Staff's original position supporting deferral of the allocation decision to the PORCB reconciliation proceeding in 2014, but then takes a new position that the Commission should make an allocation decision in the instant Docket only as to the Retail Office / Customer Data Warehouse costs and defer decision as to the remaining costs. *See* Staff BoE at 10-13.

[10] On March 28, 2011, ComEd filed a motion for leave to file certain errata regarding certain of the PORCB-related cost figures. That errata does not affect the above $2,474,211 and $2,192,151 figures, but it does affect some other PORCB-related figures and should be considered by the Commission in the context of any ruling on Exceptions on this subject.

Any deferral of the allocation decision in whole or in part is unwarranted. ComEd and Dominion have shown that the Commission should decide this issue in the instant Docket, and that deferral of the decision is contrary to the interests of customers, RESs, and the utility. ComEd has also shown that Staff's position can result in ComEd ultimately being denied recovery of some of its costs even though they should have been recovered in rate base. *E.g.*, ComEd Reply Br. at 45-47; ComEd BoE at 28-32. Staff's BoE still has not come to grips with those points.

Staff's BoE also makes a separate claim, which is that on March 17, 2011, ComEd filed its initial Consolidated Billing Adjustment under Rider RCA, and that, based on work papers, ComEd included a jurisdictional total of $14,518,540 of costs, compared with the $16,622,000 of jurisdictional costs identified in ComEd's surrebuttal, which Staff claims is a discrepancy. Staff BoE at 12-13. Staff seeks to take administrative notice of this filing and claims if the Commission approves any of the PORCB-related costs for inclusion in rate base, then ComEd may need to file a revised Consolidated Billing Adjustment under Rider RCA, allegedly to avoid double-recovery of costs.

If the Commission entertains Staff's request for administrative notice on this subject, Staff remains mistaken. The jurisdictional amount of Consolidated Billing costs of $14,518,540 as filed with ComEd's workpapers as part of the March 17, 2011, Consolidated Billing Adjustment did not include the costs associated with the Purchase of Receivables, which, as per Rider PORCB, are to be initially collected separately from the Retail Electric Suppliers via the 50 cent reduction to each receivable purchased (Rider PORCB, Original Sheet Nos. 398 and 399). The jurisdictional amount of $16,622,000 included in ComEd Ex. 55.6 reflects the total amount of costs associated with both Consolidated Billing and Purchase of Receivables. ComEd

agrees, however, that if the Commission includes some of the PORCB costs in ComEd's rate base, then ComEd likely would have to file a revised Consolidated Billing Adjustment under Rider RCA reflecting the lower amount of costs to be collected through the rider.

Staff's Proposed Language. Certain of the language in Staff's proposed Exception is inaccurate and inappropriate.

- Staff requests that the Commission add the following sentence to the "Analysis and Conclusions" section of the Proposed Order: "When it comes to the issue of the so-called PORCB costs, it appears that both ComEd and Dominion's positions are unreasonable." Staff BoE at 15. That language is inappropriate. ComEd and Dominion have engaged on the issue at hand, addressed the facts and the law, and recommended that the Commission make an allocation decision now because that is in the best interests of customers, RESs, and the utility. In contrast, Staff has chosen not to review and present evidence on the facts, and instead advocated a deferral of the allocation decision that would be detrimental for everyone and that could result in ComEd being denied recovery of costs that it is entitled to recover.

- Staff's BoE at 15 requests that a sentence of the Proposed Order be deleted. ComEd takes no position on that portion of Staff's Exception.

- Staff's BoE at 16 proposes to strike the remaining paragraphs of the Proposed Order's "Analysis and Conclusions" section. Instead, they should be revised as shown in ComEd's Exception No. 4.

- Staff's BoE at the bottom of page 16 through the second to last paragraph on page 17 proposes inaccurate and tendentious language that should not be adopted. The language simply is not a reasonable and fair discussion, as is shown by the history of the evidence and briefing in this Docket.

- Staff's BoE from the last paragraph of page 17 through page 18 proposes language on the subject of the Retail Office and Customer Data Warehouse costs. The language should not be adopted. Staff's assertion that ComEd and Dominion have agreed on these costs is inaccurate. ComEd's alternative position (*see* ComEd Reply Br. at 47-49) agrees with Dominion as to these costs. In addition, Staff's inclusion of language deferring a decision on the other PORCB-related costs is unwarranted and detrimental to customers, RESs and the utility. The remainder of the language is unnecessary in light of the language proposed by ComEd.

E. Cash Working Capital

The Proposed Order (at 49 and Appendix A, p. 6, line 10) approves ComEd's lead/lag study and resulting cash working capital ("CWC") requirement subject to certain Staff-proposed adjustments, approves a CWC figure of $79,807,000, and correctly rejects AG/CUB's proposal to disallow all cash working capital ("CWC"). AG/CUB have filed Exceptions, and an improper new affidavit. The AG and CUB BoEs and Exceptions on this subject are highly misleading and internally contradictory as to the evidence, the arguments, and the Proposed Order, and they are without merit. Staff has filed two Exceptions. Staff's first Exception is technical. Staff's second Exception raises a point but does not propose a change to the Proposed Order.

1. AG/CUB's Exceptions

The primary complaint of the AG and CUB is that ComEd used certain assumptions, especially the "midpoint" assumption for certain groups of receivables, in calculating the revenue collections lag portion of its lead/lag study. However, the AG and CUB never even mention, much less try to refute, ComEd's evidence showing that its assumptions were conservative, and that a version of the lead/lag study without the challenged assumptions yields an even higher revenue collections lag, which would mean a higher CWC amount in rate base. The AG and CUB arguments on pension / other post-employment benefits ("OPEB") expenses, severance expenses, and the Illinois Electricity Excise Tax ("IEET") suffer from the same problems. They ignore that ComEd's methodology was conservative and understated its CWC requirement.

The AG and CUB BoEs Rely Largely on Empty Rhetoric. The AG and CUB BoEs contain a number of generalizations that are unsupported and specious. For example:

- The AG's BoE (at 25) begins by claiming that ComEd failed to meet its burden of proof, citing 22 pages of the AG's Initial Brief, without identifying any specific

alleged deficiency.[11] That is meaningless. The 8 pages of its BoE do not and cannot show any such failure, nor did its Initial Brief. ComEd Reply Br. at 52-65. The lead/lag study that calculates and supports ComEd's CWC in rate base was prepared by and amply supported by the direct, rebuttal, and surrebuttal testimony of independent expert 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).

- The AG's BoE (at 25) next states: "The Proposed Order rejects the AG/CUB recommendation to assign a zero Cash Working Capital (CWC) allowance to the ComEd test year rate base, as was allowed ComEd in its prior rate case." That is highly misleading. As the AG knows, but does not mention, ComEd did not perform a lead/lag study, nor request CWC, in its 2007 rate case. Subbakrishna Reb., ComEd Ex. 31.0, 25:508-510. Nor did Staff or any intervenor present a lead/lag study. *See Commonwealth Edison Co.*, Docket No. 07-0566 (Order Sept. 10, 2008). Moreover, the AG, here having cited a non-existent ruling in ComEd's 2007 rate case, later spends much of the remainder of its briefing on this issue arguing that ICC rulings in other cases that support ComEd do not matter. *E.g.*, AG BoE at 26-28.

- The AG's BoE (at 25-26) then claims that it "appears" that the Proposed Order's rejection of the AG/CUB proposal rests on a single, one-sentence conclusion. The AG here fails to mention the two additional paragraphs of the Proposed Order (at 49) rejecting the AG/CUB arguments.

- Similarly, CUB's BoE (at 9) complains that the Proposed Order (at 49) did not explain its finding that AG/CUB's arguments are inconsistent. The Proposed Order actually found, among other things, that: "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." The evidentiary record and briefing contains ample proof and illustration that the AG/CUB arguments are not well-founded and are inconsistent. If the Commission believes that the foregoing finding should be accompanied by examples or citations, they may be found in the "ComEd's Position" portion of the CWC section of the Proposed Order and in the discussion below.

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[11] The applicable law regarding the burden of proof is discussed in the Construction Work in Progress section of this RBoE. The AG's BoE (at 30-31) cites *People ex rel. Hartigan v. Illinois Commerce Commission*, 117 Ill. 2d 120 (1987), but that case involved a presumption of reasonableness and is a red herring here. Moreover, *Hartigan* only eliminated the presumption of reasonableness as to nuclear plant costs in light of then-new Section 9-213 of the Act, 220 ILCS 5/9-213, in any event. *See Hartigan*, 117 Ill. 2d at 133; *The Peoples Gas Light and Coke Co.*, No. 91-0586, 1992 Ill. PUC Lexis 376, *152-154 (Order Oct. 6, 1992); *North Shore Gas Co.*, No. 91-0010, 1991 Ill. PUC Lexis 636, *125-127 (Order Nov. 8, 1991).

The Revenue Collections Lag. The AG and CUB complain primarily about the assumptions used in ComEd's lead/lag study in calculating the collections revenue lag, especially the "midpoints" assumption used for certain groups of receivables, although the AG also throws in a passing reference to their past complaint about the inclusion of receives aged 91 to 365 days old in the calculation. *See* AG BoE at 25-26; CUB BoE at 9-10. Their complaints are disingenuous and wrong.

The study, as to the initial one or two billing periods in which customers have "grace periods" to pay their bills, conservatively assumes away the time value of money as to those periods by giving them a zero weight. Mr. Brosch and the AG professed to find the initial zero weighting assumptions arbitrary and perplexing, even though ComEd repeatedly explained that it made the zero weighting assumptions to make its study even more conservative. *See* AG Init. Br. at 31-32. The study then uses assumed midpoints to weight the older receivables aging intervals. The AG and CUB criticisms of the midpoint assumptions used for the older receivables aging intervals boil down to their 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. at 25-35. The AG and CUB attacks on the revenue collections lag component of the lead/lag study lacks merit, for many reasons.

First, the AG's and CUB's BoEs once again ignore that if ComEd's revenue collections lag were to be re-calculated without the zero weighting assumptions for the initial aging period(s) and without the midpoints assumption for receivables older than the initial aging

period(s), then ComEd's revenue collections lag would increase by a very large amount, to 49.55 days. Subbakrishna Sur., ComEd Ex. 57.0, 8-164 – 9:181; ComEd Ex. 57.2.[12]

Second, the Commission has repeatedly approved a collections lag methodology using midpoints similar to those in ComEd's study in the 2009. Subbakrishna Reb., ComEd Ex. 31.0, 2:30-34, 3:52-58, 8:169-9:179 and fn. 1; Subbakrishna Sur., ComEd Ex. 57.0, 6:131-137 and fn. 10, 7:145-8:154; Subbakrishna, Tr. 1148:14 – 1150:11. *See Central Ill. Light Co., et al.*, ICC Docket Nos. 09-0306 Cons. (Order on Rehearing Nov. 4, 2010), *North Shore Gas Co., et al.*, ICC Docket No. 09-0166 Cons. (Order, Jan. 21. 2010), and *Northern Illinois Gas Co.*, ICC Docket No. 08-0363 (Order, March 25, 2009). Remarkably, the AG's BoE (at 26-27), like the AG/CUB witness, continues to rely inappropriately on the *original* Order in the 2009 Ameren cases on this point. ComEd Init. Br. at 45.

The AG attempts to brush away past Commission decisions. Its BoE (at 28-29) claims that those cases did not involve comparable methodologies, but ComEd showed otherwise, the AG's claim is unsupported, and the AG/CUB witness, Mr. Brosch, admitted that he did not even analyze the collections lag portion or cash working capital results of any of those cases. Brosch Tr. 1526:19 – 1527:10. The AG also seeks to avoid those past Commission decisions by arguing that they are not *res judicata*. The AG does so even though the AG itself cites a non-existent ruling in ComEd's 2007 rate case (as noted earlier) as well as the original Order in the 2009 Ameren cases (and the AG/CUB witness also cited various other cases, mostly from other jurisdictions). The AG is right that past Commission decisions are not *res judicata*. That does not change the ratemaking point, however, that ComEd should not be subject to an adjustment,

[12] The calculation includes receivables over 365 days old (Subbakrishna Sur., ComEd Ex. 57.0, 9:175-176), but the data show that, even if it had not, the revenue collections lag would not decrease below the 36.32 days figure used as of surrebuttal in ComEd's study (discussed further below). *See* ComEd Ex. 57.2.

much less complete denial of all CWC, because it used a methodology similar to methodologies the Commission approved in its Orders in the three most recent major rate cases, which involved a total of six utilities.

Third, the AG and CUB BoEs fail to address the fact that they never presented any calculation that "corrects" for the supposedly flawed midpoints methodology. AG/CUB previously claimed that if the collections revenue lag were revised "using more reasonable assumptions", then ComEd would have a negative CWC (AG Init. Br. at 24, citing Brosch Dir., AG/CUB Ex. 1.0, 24:537-539), but Mr. Brosch's claims to that effect are based not on rejecting the midpoints assumption but rather on his premise that receivables over 90 days should be ignored. *See* Brosch Dir., AG/CUB Ex. 1.0, 33:723 – 34:741; AG Init. Br. at 35. His premise was debunked, and the AG and CUB do not appear to have pursued that criticism in their BoEs, except for a passing reference on page 29 of the AG's BoE. ComEd previously has shown that the AG and CUB criticisms of the inclusion of receivables aged 91 to 365 days old lack merit and, once again, even have part of it backwards. *See, e.g.,* ComEd Reply Br. at 60-61.

Fourth, the AG and CUB still do not recognize, much less explain, Mr. Brosch's inconsistency in accepting the study's assumption that the midpoint methodology is a proper basis for determining ComEd's service lag (AG Init. Br. at 25), which he indicates also applies to other utilities (*id.* at 31), and his accepting (not questioning) the study's use of midpoints to calculate various expense leads. Subbakrishna Reb., ComEd Ex. 31.0, 9:179-185.

Fifth, the AG's BoE (at 25-26) complains about ComEd and Staff not performing certain additional analyses. However, the AG previously acknowledged that ComEd's information systems do not contain the data that would be needed for those analyses. *E.g.,* AG Init. Br. at 26. AG/CUB have never claimed, much less shown, that ComEd was required to modify its

information systems to collect that data, whether for any business purpose or by law or under any past Commission Order. Nor did they refute ComEd's points that for a utility of ComEd's size, the other methodologies to which AG/CUB refer would not be more reliable, and they also would be burdensome and unduly expensive. *E.g.*, Subbakrishna Reb., ComEd Ex. 31.0, 11:234 – 13:271. The data that ComEd used to calculate its revenue collections lag is data from receivables reports that ComEd uses for normal business purposes. Subbakrishna Dir., ComEd Ex. 7.0, 10:196-198.

Sixth, while the AG BoE (at 25-26) complains about ComEd and Staff not performing other analyses, the AG once more ignores that ComEd, in rebuttal, recalculated its revenue collections lag using intervals within the 121-365 days range, *i.e.*, 91 to 120 days, 121 to 150 days, 151 to 180 days, 181 to 210 days, 211 to 270 days, and 271 to 365 days, using the same midpoints methodology as its original study, and that increased "granularity" only reduced the lag from 39.16 days to 36.32 days. Subbakrishna Reb., ComEd Ex. 31.0, 6:126-7:141. Staff, in rebuttal, proposed that the 36.32 days figure should be used, and ComEd, in surrebuttal, in order to narrow the issues, accepted that proposal. Subbakrishna Sur., ComEd Ex. 57.0, 2:29-33, 3:63-4:70, 8:156-59; Staff Init. Br. at 27; AG Init. Br. at 25-26.

Seventh, the AG BoE (at 29) claims that ComEd's original 39.16 days figure is "clearly unreasonable" compared to the 32.72 of Peoples Gas, the 23.24 days of North Shore Gas, and the 28.13 days of Ameren and that this is unexplained by ComEd and the Proposed Order. To begin with, ComEd's final study used 36.32 days, not 39.16 days, as noted above. Also, the numbers are not so very different. Furthermore, as noted above, Mr. Brosch, admitted that he did not even analyze the collections lag portion or cash working capital results of any of those cases, so AG/CUB is not in a position to claim that they prove anything. Finally, the different numbers

resulting as to those utilities are not inconsistent with ComEd's figure and do not mean it is overstated. Subbakrishna Sur., ComEd Ex. 57.0, 8:159-163. ComEd also debunked Mr. Brosch's reliance on results from non-Illinois cases. ComEd Reply Br. at 59-60.

Finally, the AG previously claimed that ComEd's revenue collections lag figure, if correct, implied that most customers are delinquent on their payments (*e.g.*, AG Init. Br. at 29), but that is not true, because it ignored the effects of customer size, consumption, and durations of amounts owed. Subbakrishna Reb., ComEd Ex. 31.0, 10:207 – 11:233.

Pension / OPEB, Severance, and IEET. The AG BoE (at 30) and the CUB BoE (at 10) also present cursory versions of their prior arguments relating to pension / OPEB, severance, and IEET costs. The Proposed Order (at 49) rightly rejects those arguments.

ComEd proved it actually had understated its CWC requirements relating to pension / OPEB costs. Mr. Subbakrishna showed that in detail in his rebuttal and again in his surrebuttal. Subbakrishna Reb., ComEd Ex. 31.0, 4:78-85, 21:424 – 22:448; Subbakrishna Sur., ComEd Ex. 57.0, 5:91 – 103, 17:345 – 19:379. The AG's past implications that ComEd's huge pension contributions in 2005 and 2009 somehow were not cash, but non-cash accruals (AG Init. Br. at 40-41), and that the timing of the payment contributions is unclear (*id.*), are false. *E.g.*, Subbakrishna Sur., ComEd Ex. 57.0, 5:93-103; Houtsma Dir., ComEd Ex. 6.0 Rev., 30:605-607.

The AG/CUB objection to ComEd's calculations relating to severance costs similarly is without merit, one of its fatal flaws being the false implication that the severance costs were not cash but non-cash accruals. Subbakrishna Reb., ComEd Ex. 31.0, 4:78-85, 21:424 – 22:448; Subbakrishna Sur., ComEd Ex. 57.0, 5:91 – 103, 19:380 – 20:401; Houtsma Dir., ComEd Ex. 6.0 Rev., 48:982 – 49:988.

Mr. Subbakrishna's rebuttal testimony also fully refuted the AG/CUB objection to the lead/lag study's calculation relating to the IEET. Subbakrishna Reb, ComEd Ex. 31.0, 22:450 – 23:485. Mr. Brosch did not even attempt to respond on this subject in his rebuttal.

Final Calculation. The AG's BoE (at 31-32) and CUB's BoE (at 11) are correct that the CWC figure in the final Order should be updated to reflect the applicable inputs from the final revenue requirement.

Improper New Affidavit. The AG's BoE (at 31) references Mr. Brosch's improper new affidavit. ComEd has moved to strike that affidavit.

2. Staff's Exceptions

In the interests of narrowing the issue, ComEd does not object to Staff's BoE's (at 19) technical Exception.

Staff's BoE's (at 19-20) second Exception, if it is an Exception, raises a methodological point. Staff does not propose any specific change in the Proposed Order. Because Staff does not make any particular proposal, ComEd cannot respond.

F. ComEd's 2009 Pension Trust Contribution

The Proposed Order (at 51-52) properly rejects the disallowance of ComEd's 2009 pension trust contribution proposed by Staff, CUB and the AG.

Staff argues that ComEd's cost recovery related to the pension trust contribution it made in 2009 be limited to the amount by which the jurisdictional portion of pension *expense* is reduced because of this contribution. Staff BoE at 22. The difference between this method of recovery and that proposed by ComEd, which is to include the entire contribution in rate base where the contribution can earn ComEd's overall cost of capital, is a $1.4 million reduction to ComEd's revenue requirement. Staff's recommendation cannot be reconciled with applicable

and traditional cost recovery principles and bears no relationship to the economic cost to ComEd of properly funding its pension plans. It should therefore be rejected. Staff appears to base its recommendation on the following claims: (1) the Proposed Order "would overturn years of Commission precedent" (Staff BoE at 20); (2) the contribution was somehow designed to benefit shareholders (*id.*); and (3) for expenses Staff characterizes as "discretionary," the Commission should allow recovery only to the extent that the recovery "does not unduly burden ratepayers." (*id*, at 20-21). None of these positions has any merit. Indeed, if anything would "overturn years of Commission precedent" it is Staff's newly-proposed and unworkable test for recovery of certain types of costs that are claimed to be "discretionary."

Preliminarily, it is important to address Staff's assertion that these pension contributions ought to be treated differently because they are governed by rules and specific accounting guidelines applicable to the funding of pension plans. Staff BoE at 21. That is true, but irrelevant. Those rules do not affect in any way the fact that when ComEd makes a contribution like the one at issue here, it incurs an economic cost equal to its weighted average cost of capital. Nor do those rules make the timing of recovery of this economic cost any less important than is true of other costs, as Staff obliquely suggest. *Id.*

The only Commission precedent that Staff identifies as being "overturned" by the Proposed Order's conclusion on this issue is the decision in Docket No. 05-0597 concerning ComEd's 2004 pension contribution. That case does not afford any real precedent for this case. First, Staff's argument to the contrary notwithstanding, no "cap" on the recovery of the cost of a pension contribution at the level of customer benefit was approved in Docket No. 05-0597, and the Commission never suggested such a hard cap was within its contemplation. Instead, the Commission simply noted that the pension contribution at issue there did serve to reduce

customer pension expense, but then independently selected a mechanism for cost recovery that was based on an assumed hypothetical cost of debt, had ComEd issued debt to fund the contribution. *Commonwealth Edison Co.*, Docket No. 05-0597, (Corr. Order on Rehearing, Dec. 20, 2006) at 28.

Moreover, any attempt to draw a parallel between the 2009 contribution and the contribution at issue in Docket No. 05-0597 is fundamentally flawed. The contribution there was funded by an equity infusion from ComEd's parent and the Commission was concerned this may not have been the lowest cost source of capital, thus the hypothetical debt return. In stark contrast, the funds used for the 2009 contribution were ComEd internally generated funds. Houtsma Dir., ComEd Ex. 6.0 Rev., 30:605-11; Houtsma Reb., ComEd Ex. 29.0, 17:355-18:375, 25:525-29; Trpik Dir., ComEd Ex. 4.0 Rev., 23:429-31. For the same reason, the AG's unsupported assertion that allowing the contribution would be contrary to the "Commission's well-established policy" (AG BoE at 33) is also unavailing. The circumstances relating to ComEd's 2009 contribution are unlike those of the 2005 contribution. Moreover, there can be not argument that the 2009 contribution was made with "ratepayer funds," because ComEd earned less that its allowed return at all times between the prior rate case and the 2009 pension contribution.

Staff's hyperbolic assertion that the contribution was intended to "pump up" ComEd's rate base for the benefit of shareholders (Staff BoE at 22) is not only unsupported by the record, it is flatly wrong. All parties, including Staff, agree that the contribution was prudent and proper. *See*, *e.g.*, Pearce Reb., Staff Ex. 18.0, 7:160-68. The contribution was needed to address the seriously underfunded status of the plan resulting from the 2008 stock market crash and persistently low interest rates, and the evidence shows it was made for that reason. Houtsma

Reb., ComEd Ex. 29.0, 17:346-50, 19:387-89, 21:442-44. Moreover, the suggestion that ComEd would put $152 million of scarce capital at risk on the off chance that it might receive a return of and on that amount beginning at best two years later borders on the absurd. The record reflects that the contribution was made because it was the "right thing to do," to provide a measure of protection for the retirement benefits of ComEd's work force, a position echoed and strongly supported by the testimony of Dean Apple, President of the International Brotherhood of Electrical Workers Local 15, which represents 3,800 ComEd employees and 5,638 retirees whose pension benefits and retirement security depend on the pension fund. Apple Reb., ComEd Ex. 27.0, 3:53-4:82.

Third, Staff's newly-minted test of "no undue burden to ratepayers" applicable to so-called "discretionary" expenses is not only unprecedented but unworkable and unwise. It is unworkable because, if consistently applied, it would require the Commission to identify and determine which of hundreds or thousands of test year expenses are "discretionary." In the context of a case in which a number of parties, including Staff, express concern over the level of rate case expenses such a suggestion is especially ironic and ill-timed, as this test would surely multiply the costs of litigating rate cases. Added to that would be the requirement that the Commission then identify and limit recovery of the costs of such "discretionary" expenditures only to the extent that ratepayers are not 'unduly burdened." The instant case is a good example of the hairsplitting this test would require the Commission to engage in were it to adopt the novel Staff test. The revenue requirement difference between ComEd's proposal for cost recovery and that proposed by Staff is, as stated earlier, about $1.4 million. If Staff seriously contends that ratepayers will be "unduly burdened" by an additional $1.4 million revenue requirement, it has not cited to any evidence which establishes or supports that conclusion, nor has it proposed any

test by which any evidence could be judged. No such determination is possible because the issue is inherently subjective. The lawful test is a bright line – either the expense is prudent and reasonable or it is not. If it is the former, the opportunity for full recovery must be allowed.

Finally, if the "undue burden" is deemed to be anything in excess of test-year savings to customers, capping recovery at this level will create the perverse incentive not to make this kind of contribution, but rather encourage the utility to devote its capital to other investments on which it is allowed to earn a full return. This would undermine the important goal of adequate pension funding. To limit recovery of the costs of investments in this way implies that some investments are less worthwhile or important than others, and would set the Commission on the path of attempting to prioritize, and make value judgments concerning, the uses of utility capital. Because this type of "cap" is one-sided, it will ensure that the utility cannot have an opportunity to recover its full costs of service – unless it is entitled to recover the amount of customer savings regardless of ComEd's costs. The treatment of Exelon Way severance costs is instructive. There, ComEd is allowed to recover $18.5 million per year for investments that produce $70 million in annual customer benefits. *See* discussion at IV.C.1., *infra*. If the customer benefits test were to be applied symmetrically, ComEd would be allowed to recover the full $70 million. That too would be a violation of the cost recovery principle, but no more so than the asymmetrical cap approach advocated by Staff with respect to the 2009 pension contribution. ComEd most emphatically does not support this kind of "customer benefits" approach and points out this example only as an illustration of the one-sided and unfair nature of the cap approach, and the fundamental change in and threat to ratemaking principles that it represents.

No matter how it is couched or phrased, Staff's proposal would bar ComEd from recovering the capital costs of its contribution even at the cost determined to be just and

reasonable by the Commission. This will punish ComEd for acting responsibly to protect its employees and retirees, and would render rates unreasonable because they would not reflect costs to serve customers. Staff's approach would also require the Commission to engage in endless and difficult (if not impossible) efforts to "match" a broad spectrum of costs with related benefits. Tierney Reb., ComEd Ex. 39.0, 19:405-11. Staff's proposal to "cap" recovery of these costs at the level of customer benefits should be rejected.

AG and CUB, in contrast, continue to assert that if greater contributions had been made in 2006-2008, the 2009 contribution would be unnecessary. CUB BoE at 13; AG BoE at 34. This argument is a red herring for several reasons.

Even if ComEd made contributions in 2007 and 2008 in amounts equivalent to annual pension accruals and reduced the 2009 contribution by a corresponding amount, the result would be roughly the same because all of the above amounts would have appeared on ComEd's balance sheet as of December 31, 2009. Houtsma Reb., ComEd Ex. 29.0, 25:516-521. This is not the same as an expense item in a test year. The timing of the pension contributions is irrelevant. Whether they had been made in 2007 and 2008 instead of 2009 would make no difference, as even Mr. Effron agreed. Effron Reb., AG/CUB Ex. 8.0, 9:189-92. Neither CUB nor AG ever introduced any evidence to the contrary, and they do not make any contrary argument in their respective Briefs on Exceptions.

G. <u>Customer Deposits</u>

The Proposed Order (at 55) correctly rejected AG/CUB's and Staff's proposal to use a 2009 year-end balance instead of an average 2009 balance to calculate customer deposits, but incorrectly accepted AG/CUBs proposal to add non-jurisdictional (non-delivery services)

customer deposits to the jurisdictional (delivery services) customer deposits that ComEd already had deducted from rate base. ComEd's BoE (at 41-44) explained by that was error.[13] The AG's, CUB's, and Staff's Briefs on Exceptions challenge the first ruling. AG BoE at 34-36, CUB BoE at 13-15, Staff BoE at 23-24. They err.

The customer deposits figures at issue are as follows (from ComEd Ex. 29.1, Sched. B-13, p. 1) (not including interest accrued in 2009, which is addressed elsewhere):

Positions	Jurisdictional (Delivery Services) Using Average 2009 Balance	Jurisdictional (Delivery Services) Using 2009 Year-End Balance	Total (Non-Jurisdictional Plus Jurisdictional) Using Average 2009 Balance	Total (Non-Jurisdictional Plus Jurisdictional) Using 2009 Year-End Balance
	$45,220,000	$47,375,000	$124,572,000	$130,510,000
Proposed Order			$124,572,000	
ComEd Position	$45,220,000			
ComEd Position if ICC Includes non-Jur. Customer Deposits			$124,572,000	
AG/CUB and Staff Position				$130,510,000

The use of an average, rather than a year end, balance is appropriate because it smoothes out seasonal variations, providing a more accurate reflection of customer deposit amounts. Houtsma Reb., ComEd Ex. 29.0, 37:786-95.

Both AG/CUB witness Brosch and Staff witness Tolsdorf contended that ComEd's customer deposits should be determined using a year-end, rather than an average balance, on the

[13] ComEd notes that on the subject of incentive compensation, Staff's BoE (at 28) argues that only delivery services-related costs should be recovered through delivery services rates. That principle supports ComEd's Exception here, which objects to the inclusion of non-delivery services customer deposits in rate base.

basis of a perceived trend of increased customer deposits from 2006 to 2009. Brosch Dir., AG/CUB Ex 1.0, 37:814-19, Brosch Reb., AG/CUB Ex 7.0, 31:673-84; Tolsdorf Reb., Staff Ex. 19.0, 4:77-5:99. Mr. Tolsdorf also presumed that new business would be accompanied by increased customer deposits. Tolsdorf Reb., Staff Ex. 19.0, 5:93-99.

No party has presented any evidence showing that the three year increasing trend posited by Messrs. Brosch and Tolsdorf is likely to continue in the future. The growth from January 2006 through December 2009 is predominantly in 2009 itself, *i.e.,* the growth in total customer deposit balances between January 2006 and January 2009 was only from $111,770,000 to $119,709,000 or about 2.3% per year on average. *See* ComEd Ex. 6.1, Sched. B-13; p. 2. *See also* ComEd Ex. 29.1, Sched. B-13, p. 2, upon which AG/CUB witness Brosch relies (AG/CUB Ex. 1.0, 37:814-19). If this "trend" were applied to 2009, the year-end balance would be only about $122,462,000, or more than $8 million less than the actual year-end 2009 balance and about the same as the average balance ComEd used for the total ($124,572,000). In 2009, by contrast, total customer deposits grew from $119,709,000 in January to $130,510,000 in December, or slightly over 9% for that year alone. Thus, using an average for 2009 more than fully captures the so-called "growth" in customer deposit balances that Staff and AG/CUB identify. Moreover, the year-end 2009 balance that AG/CUB prefers is not representative of the four-year period that AG and CUB analyze, being the highest balance during that period, and nearly 10% higher than any monthly balance during 2006-2008. AG/CUB and Staff cite to no evidence to suggest that the customer deposit balances will continue to grow in 2010 or 2011, much less at anywhere near the rate experienced in any of the years 2006-2009. Likewise, the record contains no evidence supporting the supposition that new business will be accompanied by increased customer deposits.

Finally, it is clear that 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. Houtsma Reb., ComEd Ex. 29.0, 37:786-95.

H. Materials and Supplies Inventories

Staff's Exceptions to the findings of the Proposed Order (at 57) relating to Material and Supplies Inventories should be rejected. As explained in ComEd's BoE, the Proposed Order improperly reduces the amount of ComEd's material and supplies inventories included in rate base, based on the recommendation of Staff, by deducting from the inventory level amounts related to accounts payable. ComEd BoE at 44-45. This disallowance is improper and duplicative because the benefit derived by ComEd from these accounts payable has already been accounted for by decreasing the Cash Working Capital balance in rate base to the extent of the payables.

If, however, ComEd's material and supplies inventories balance is reduced (and it should not be) then consistency requires, as ComEd has stated several times in the record, that the material and supplies inventories balance and the associated accounts payable be calculated in the same manner. ComEd believes that (if the order finds that the inventory balance should be reduced for accounts payable) a thirteen month average should be used to calculate the material and supplies inventories balance as well as the associated accounts payable rather than the year-end balance proposed by Staff in its BoE. The Proposed Order, while not clearly stating that the thirteenth month average should be used, appears to have calculated the material and supplies inventories balance and the accounts payable using a thirteen month average as reflected in its Appendix A. PO, App. A, at p. 6, line 6. Staff on the other hand, seeks to compound the Proposed Order's erroneous decision to reduce ComEd's material and supplies inventory balance

by claiming that the amounts in the Proposed Order's Appendix A should instead reflect a year-end material and supplies inventories balance of $71,326,000 (Staff BoE at 26), and an accounts payable balance based on the year-end balance. In any event, ComEd believes that the final Order needs to clarify which balance should be used. It is ComEd's view that the thirteen month balance is most appropriate for several reasons.

First, the variations in the accounts payable balances throughout the year are much more profound than the variations in the inventory balances. Use of the year-end accounts payable balance is unsupported by any evidence in the record. Staff claims that use of the year-end balance is necessary because of its "concerns" about debit balances in ComEd's accounts payable calculations (Staff BoE at 25) and because the inventory has demonstrated "large fluctuations" (Staff Init. Br. at 31). Staff however, cites no evidence demonstrating that the debit balances represent an abnormal variation or any evidence as to exactly what those "large fluctuations" are that Staff references in its Initial Brief, and made no attempt to question the variations during discovery or cross-examination. No such evidence exists in the record, and in the absence of such a showing, the use of a year-end accounts payable balance cannot be supported. Moreover, the evidence shows that the accounts payable at the end of the year, which Staff suggests should be used in order to coincide with a year-end inventory balance, is the second highest balance of the year and is not representative of ComEd's normal level of payables throughout the year. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 31:669-671; ComEd Ex. 55.6. Nothing in the record supports the use of a year-end account payable balance, and thus Staff's exception should be rejected.

II. OPERATING EXPENSES

A. Incentive Compensation Cost and Expenses

The Proposed Order (at 64) reduces ComEd's incentive compensation cost recovery but (1) rejects AG/CUB's proposals for further reductions in the recovery of costs of ComEd's Annual Incentive Plan ("AIP") and Long-Term Incentive Plan ("LTIP") and (2) rejects Staff's proposal to disallow LTIP costs associated with emissions reduction and Smart Grid measures. CUB (BoE at 15-17) and Staff (BoE at 27-28) take Exception as to the respective rulings. Their Exceptions should not be adopted.

1. CUB's Exception

CUB (BoE at 16) argues that high unemployment means that ComEd does not have to pay "such hefty" incentive compensation. The record evidence is directly to the contrary: "The total compensation ComEd pays its employees is the amount *needed in the marketplace to attract and retain qualified personnel.* Rather than pay the entire amount of an employee's compensation through base salaries, ComEd makes a portion of each employee's pay subject to achievement of operational metrics specified in incentive compensation plans." Trpik Dir., ComEd Ex. 4.0 Rev., 24:458-62 (emphasis added). "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 ComEd's plan and the compensation payouts resulting from it to evaluate the program in light of incentive compensation offered by peer companies and relevant research on incentive compensation plans generally. The results of the recent benchmarking study completed in October, 2010 show that the company continues to be aligned with the peer group on incentive pay." Trpik Reb., ComEd Ex. 28.0, 3:51-58. The Commission cannot lawfully disregard ComEd's uncontradicted evidence on this point. ComEd Reply Br. at 73, n. 16.

CUB (BoE at 15-16) also argues for an adjustment based on the AIP "net income limiter". However, as the Proposed Order (at 64) recognizes, 2010 aggregate operating metric performance exceeded the "Target" level of the AIP, resulting in an expected actual AIP payout of 100%, equivalent to the costs submitted in ComEd's rate filing. Trpik Reb., ComEd Ex. 28.0, 4:68-70.

Finally, CUB (BoE at 15, 16-17) argues that the AIP and LTIP costs should be disallowed on the theory that they benefit shareholders more than customers. CUB's argument is an improper attempt to apply outdated facts to the instant case. One of the issues the Commission has had with portions of ComEd's incentive plans in prior cases has been that some of the plan "metrics" are thought to primarily benefit shareholders, not customers. Mindful of those issues, ComEd has revised its plans to accommodate those concerns. The terms of both the AIP and the LTIP have been established specifically to comply with the Commission's standards for incentive compensation cost recovery as set forth most recently in the Order in Docket No. 07-0566. For the 2009 test year, ComEd revised the AIP to eliminate the net income metric that the Commission disapproved in Docket No. 07-0566, and, therefore, all of the costs incurred under the AIP during the 2009 test year are attributable to meeting operational goals of the type approved by the Commission in that case. Similarly, ComEd addressed the concerns identified in Docket No. 07-0566 with the LTIP metrics by eliminating the net income and legislative / regulatory goals from the plan for 2010, thereby insuring that all LTIP costs ComEd will incur in the future meet the Commission's cost recovery standards. Trpik Dir., ComEd Ex. 4.0 Rev., 24:448-27:530.

2. **Staff's Exception**

Staff (BoE at 27-28) continues to argue against recovery of LTIP incentive compensation costs associated with emissions reductions and Smart Grid metrics. The Proposed Order (at 64) appropriately rejects Staff's positions on these costs, stating:

> 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.

Mr. Trpik testified that these two metrics are specific operational metrics of the type the Commission has repeatedly approved as appropriate bases for recoverable incentive compensation expenses. Both provide benefits to customers and are appropriate goals for a delivery services company to aspire to achieve. Trpik Sur., ComEd Ex. 54.0, 6:112-17.

Staff's BoE (at 27) seems to be contending that even though customers benefit from the emissions reduction benefit, the benefit is related to supply, and, therefore, should be ignored in applying the Commission's customer benefits standard for incentive compensation costs. Staff cites no prior Commission decision that amounts to denying recovery of incentive compensation costs (or any other costs) that benefit customers based on what amounts to the functionalization of the benefits. Moreover, the Commission approved incentive compensation costs associated with reducing the costs of gas supply in the 2007 rate cases of North Shore and Peoples Gas, North Shore Gas Co., Docket Nos. 07-0141, 07-0242 Cons., pp. 57-58, 66 (Order Feb. 5, 2008) ("Further there is a measure of 10% associated with gas expenses and Gas Charges that we also believe should be counted."), even though gas supply costs are not recovered through the base rates that are before the Commission in a gas rate case. In addition, Staff's position is inconsistent with its position supporting inclusion of non-delivery services customer deposits as

a subtraction from rate base. *E.g.*, Staff Reply Br. at 25. Finally, if the Commission is going to create a new customer benefits functionalization standard, then it should be prospective only.

Staff's BoE (at 27-28) as to denial of incentive compensation costs associated with the Smart Grid metric does not make sense. Staff appears to complain that the Smart Grid is new, that the newness means that the costs are not ordinary and necessary, that the benefits of Smart Grid are unproven, and that the Commission has not yet approved recovery of Smart Grid costs in delivery services rates. A benefit is not less of a benefit because it is new. Furthermore, Mr. Marquez's direct testimony provided uncontradicted evidence of the likely benefits of one important aspect of the Smart Grid, advanced metering infrastructure ("AMI"), and he pointed out that the benefits and costs of the AMI Pilot were addressed in detail in Docket No. 09-0263, in which the Commission ordered ComEd to conduct the AMI Pilot. Marquez Dir., ComEd Ex. 10.0, 12:225-233, 16:304 – 17:324; *Commonwealth Edison Co.*, Docket No. 09-0263 (Order Oct. 14, 2009). Moreover, the costs of the AMI Pilot, with a limited exception, are uncontested in this Docket. PO at 11, 105-106. None of the straws at which Staff grasps here is a reasonable ground for disallowance even on its face, much less in light of the evidentiary record and the Commission's actions with respect to the Smart Grid.

B. <u>Rate Case Expenses and Fees</u>

ComEd has met its burden of proof of its rate case expenses, although the PO (at 69-70, 73-75) incorrectly reduces certain amounts. ComEd BoE at 47. Staff, AG, and CUB each hope, thereby, to get large additional portions of ComEd's empirically reasonable rate case expenses disallowed. Staff BoE at 33; AG BoE at 48; CUB BoE at 20 and 23. ComEd has proceeded according to the applicable and unchanged cost recovery standard under Section 9-229 of the PUA, 220 ILCS 5/9-229, which is no different than the cost recovery standard for all other

expenses and for rate case expenses in prior dockets. *See* ComEd BoE at 47. Section 9-229 has no effect on that standard and on ComEd's ability to recover its rate case expenses. Staff, AG, and CUB's implications to the contrary cannot be reconciled with the applicable law and their own positions rejecting the proposed rulemaking, discussed *infra*.

As illustrated below, ComEd has met its burden of proof in this case in the same manner that it met its burden in previous cases. It also appears that ComEd has met or exceeded the standard used in the other post-Section 9-229 cases cited by Staff. *See* Staff BoE at 32.[14] Indeed, the Commission did not hold those utilities to a higher standard of proof than general cost recovery, and it does not appear that the utilities in those cases made a greater showing of proof than ComEd has offered here. *See e.g. Consumers Gas Co.*, ICC Docket No. 10-0276, (Final Order, Oct. 6, 2010) at 4 (utilizing forecasted amounts that were slightly less than prior rate case); *Aqua Illinois, Inc.*, ICC Docket No. 10-0194, (Final Order, Dec. 2, 2010) at 13 (allowing amounts consistent with prior rate case); *Illinois-American Water Co.*, ICC Docket No. 09-0319, (Final Order, April 13, 2010) at 76-80 (projected fees reasonable based on data request responses and utilities used cost control measures such as fixed fee arrangements); *Apple Canyon Utility Co. and Lake Wildwood Utilities Corp.*, ICC Docket Nos. 09-0548 / 09-0549 (cons.) (Final Order, Sept. 9, 2010) at 20-21 (intervenors' argument that monthly statements did not contain enough detail was not convincing); *MidAmerican Energy Co.*, ICC Docket No. 09-0312, (Final Order, March 24, 2010) at 43 (containing less fulsome discussion).

[14] Staff's citation to no less than 10 cases applying Section 9-229 likewise shows that CUB's proposed exception stating that Section 9-229 has never been tested before is incorrect and should be rejected. *See* CUB BoE at 23.

1. Costs of the General Rate Case Proceeding

a. ComEd Witnesses Hewings and Andrade, and Other Economic Development Evidence

ComEd has already detailed its exceptions to the PO's conclusions regarding the testimony of Drs. Hewings and Andrade. *See* ComEd BoE at 47-49. ComEd continues to believe that the expenses associated with these witnesses should be allowed in full. *Id.* In the event that the Commission disagrees with ComEd, however, ComEd addresses several problems with Staff's, AG's, and CUB's proposed exceptions seeking a larger disallowance than that set forth in the PO.

Staff states that there is no basis in the evidentiary record for the PO's conclusion disallowing only half of the recommended adjustment, and therefore the PO's conclusion is not legally sustainable. First, Staff's position on this issue is inconsistent with its proposal in its BoE to disallow 25% of ComEd's directors' fees in light of the PO's rejection of its argument for a 50% disallowance. *See* Staff BoE at 40.

Second, Staff's position is inaccurate as a matter of law. In *ComEd v. Ill. Commerce Comm'n*, 405 Ill. App. 3d, 389 (2d Dist. 2010), the Appellate Court addressed this exact issue. That court deferred to the Commission's finding disallowing 25% of ComEd's labor costs for certain employees that were associated with a proposed merger with PSEG, even though AG/CUB had proposed that labor costs associated with those employees be disallowed entirely. *Id.* at 398-402. The court rejected ComEd's argument that the Commission's decision to exclude 25% of the labor costs was not supported by substantial evidence and held that the Commission has wide latitude to reach pragmatic solutions by filling gaps in the record as long as the Commission does not act in an arbitrary or capricious manner. *Id.* at 400-02. Thus, the

Commission need not accept Staff's larger disallowance in order to create a legally sustainable order.

ComEd also disagrees with CUB's argument that the Proposed Order *inadvertently* reduced the disallowance for Dr. Andrade, and that the proper disallowance should be half of $42,000, or $21,000. *See* CUB BoE at 20. CUB does not include any citations in support of this argument or these figures, and ComEd has been unable to find any evidentiary support for CUB's arbitrary deduction. The Commission should therefore reject this exception.

In addition, the Commission should reject the AG's "bottom up" approach to Economic Development and Jobs testimony, including its suggested application to Dr. Andrade and Dr. Hewings. *See* AG BoE at 38-41. Because ComEd's rate case expenses are calculated at the beginning of ComEd's rate case and extend beyond the time that the record is marked heard and taken, they are necessarily based on estimates. Obviously some individual components of the estimates come in under budget, and likewise certain individual elements end up being over budget. The AG's "bottom up" approach would penalize ComEd for those items that come in under budget, but not compensate ComEd for those items that exceed the budget. This approach raises concerns akin to concerns about single issue ratemaking and should be rejected by the Commission. Indeed, the evidence shows that ComEd is on track to incur the entire amount requested in rate case expenses. *See* Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 18:366-19:397; ComEd Ex. 56.3 Rev. The AG's proposal is thus contrary to the evidence in the record. Moreover, a bottom up standard would be procedurally unworkable in a rate case where significant expenses are incurred in the months after the record is marked heard and taken.

b. Normalization vs. Amortization

CUB takes exception to the Proposed Order's rejection (at 67-68) of the AG/CUB argument to "normalize" rate case expenses. AG/CUB attempted to justify their proposal on grounds that it is allegedly necessary to avoid "double counting" of rate case expenses. CUB BoE at 18-19. The reality is that this professed concern about "overpayment" is simply another variant of AG/CUB's 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. The focus on costs that might continue to be reflected in rates after they have been "recovered" simply ignores the equally if not more likely possibility that a great number and variety of new costs arising after a rate order is entered will not be reflected in rates set in this or any other rate case. Further, as Mr. Fruehe has testified, Mr. Smith's proposal is somewhat vague (*e.g.*, how does a three-year "normalization" differ from a three-year amortization?). Moreover, such "normalization" has not been the practice in Illinois and, perhaps most importantly, no showing has been made (or even attempted) that the practice of amortizing rate case expenses has resulted in any over-recovery of costs. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 19:389-403. Staff also opposes Mr. Smith's proposal as unsupported and unclear. Staff Init. Br. at 42-43. The Proposed Order correctly concludes that this proposal is vague and untested, and this Exception should therefore be rejected. PO at 67.

c. General Reductions for Supposed "Overestimation"

The Proposed Order (at 79-80) correctly rejected AG/CUB's proposal to disallow rate case expenses based on overestimation. *See* Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 18:366-19:397; ComEd Ex. 56.3 Rev.; PO at 79-80. As Mr. Fruehe demonstrated and as the Proposed Order correctly concludes, data through the end of November 2010 show that the amount

ComEd has paid to consultants and expert witnesses for the direct case is relatively close to the estimate. *See* ComEd Ex. 56.3 Rev., p.2. It is not at all surprising that the "post-direct case" is likely to cost more than the "direct case," inasmuch as that phase of the case includes the preparation and filing of both rebuttal and surrebuttal testimony, preparation of hundreds of Data Request Responses, preparation and presentation of the witnesses at the hearing, preparation for and cross-examination of Staff and intervenor witnesses and preparation and filing of four rounds of post-trial briefs as well as a proposed order and pretrial memorandum. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 18:366-79.

The AG's rehashed argument in its BoE (at 43-52) that ComEd overestimated direct case costs and it can logically be inferred that ComEd therefore overestimated post direct case costs is belied by the fact that ComEd is on track to incur all of its rate case expenses. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 18:380-19:397. Indeed, the chart on page 45 of the AG's BoE showing invoices paid is not based on the most recent data in the record (*see* ComEd Ex. 56.3 Rev., p.2) and does not include major portions of the case, including rebuttal, surrebuttal, hearing testimony, and briefing. It also fails to consider that "the timing of when accruals are made and invoices are actually received can vary depending upon the witnesses' and consultants' internal billing processes." Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 19:395-97. In addition, the AG's assumption that the costs represented in its chart would have been incurred at the beginning of the case is not supported by any record evidence and should not be considered by the Commission.

Mr. Fruehe showed that five months after the filing of its 2007 rate case ComEd had incurred $7.1 million of rate case expenses, or about 68% of the total $10.5 million allowed (and about 62% of the $11.5 million without the ComEd/Staff Stipulation). Over the same time

period in this case, ComEd has incurred just over $5 million, or about 59% of its estimated $8.5 million. This shows not only that ComEd's actual costs so far have been reduced by about $2 million compared to its last rate case, but also that ComEd is on track to incur the estimated $8.5 million. *Id.*, 18:380-19:397. The AG's argument concerning categorization of expenses as direct or post-direct elevates form over substance and ignores the record evidence. *See* AG BoE at 43-47.

All in all ComEd has presented extensive data and other information more than sufficient to show that its requested rate case expenses are reasonable under applicable law, including Section 9-229 of the Act. As to CUB's contention that ComEd has failed to provide sufficient documentation showing details of services provided (CUB BoE at 21), Mr. Fruehe pointed out that through discovery ComEd provided on-going status updates regarding its rate case expenses with invoices and descriptions, and only privileged information was redacted. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 13:268-79. CUB has not, with few exceptions, voiced any objection to any of that detailed information.[15] ComEd certainly bears the burden of proof, but it has met that burden. ComEd does not bear the burden of rebutting every intervenor's assumptions and inferences, as discussed in Section III.E of this RBoE. The Commission should allow the full $8.5 million requested, amortized over three years.

[15] The case the AG cites in support of its argument that the overall rate case expenses are not reasonable because they are not adequately itemized or explained and because they include legal fees for the Alt. Reg. docket does not support its position. *See* AG BoE at 50 n.7. The *Rexam* court noted that "terse" and "concise" bills are adequate, and the court need not conduct a line by line reasonableness determination – the fact that a client pays the bills is a strong indication that they are reasonable. *Rexam Beverage Can Company v. Bolger*, 620 F.3d 718, 739 (7th Cir. 2010). Moreover, the court upheld the award of attorneys fees even though the bills did not indicate whether the services were for covered or non-covered claims, because the trial court used a practical approach by awarding all reasonable fees incurred after the date the covered claim was asserted, and excluding those costs that were clearly related to only non-covered claims. *Id.* at 737, 739.

2. **Deduction for Alleged Alternative Regulation Case Costs**

ComEd has already thoroughly discussed its exceptions to the Proposed Order regarding its Alt. Reg. expenses. *See* ComEd BoE at 52-54. AG and CUB also take exception to the PO, and propose a greater disallowance of rate case costs – in the amount of 50% of ComEd's total rate case expenses. AG BoE at 50; CUB BoE at 25. This proposal should be rejected.

The AG and CUB argue that ComEd has not met its burden of proof regarding the amount of these expenses, and therefore it is reasonable to assume that 50% of ComEd's total expenses should be disallowed. CUB BoE at 25. The AG also introduces a new assumption (that must also be inferred) that because the Alt. Reg. docket was innovative, it was necessarily expensive. AG BoE at 49-50. As discussed above, ComEd bears the burden of proof, but not a burden to disprove intervenor assumptions. ComEd met its burden here with the same level of proof it has always offered in rate cases and with undisputed evidence that the Alt. Reg. docket did not increase ComEd's costs. Alternatively, ComEd provided evidence that the Alt. Reg. docket could account for at most 11% of ComEd's rate case expenses, including "overlapping expenses." Fruehe Reb., ComEd Ex. 30.0 Public, 14:301-06. AG/CUB's proposed 50% disallowance is contradicted by record evidence and should not be adopted.

3. **A Rulemaking on the Issue of Rate Case Expenses is Unnecessary**

No party to this rate case has voiced an opinion in favor of the PO's proposed rulemaking regarding rate case expenses. Staff, AG, and CUB (along with ComEd) all oppose such a proceeding on the grounds that it is unnecessary because the cost recovery standards under Section 9-229 are not new or different (ComEd BoE at 47; Staff BoE at 30-32; AG BoE at 48-49), and/or that a rulemaking could prohibit the fact specific inquiry that is necessary in each rate

case (Staff BoE at 32; AG BoE at 51, CUB BoE at 21-22). The Commission should therefore adopt ComEd's Exception Nos. 11, 12, 16, and 19.

C. Administrative and General (A&G) Expenses

1. "Exelon Way" Severance Amortization

The AG's and CUB's exception seeking to disallow recovery of Exelon Way severance costs should be rejected, as the Proposed Order (at 86) finds. AG and CUB for the third case in a row propose that the Commission terminate any further recovery of the Exelon Way severance costs. The proposal would reduce ComEd's revenue requirement by $18.8 million and would deny ComEd recovery of more than $56 million[16] of these prudently incurred costs that were designed to produce savings of $70 million annually, savings reflected in the revenue requirement proposed in this case. In addition, the unrecovered amount will need to be written off, causing a seriously adverse financial outcome to ComEd. The Proposed Order (at 86) thus properly rejects the AG's and CUB's inequitable repudiation of the decisions the Commission reached in Docket Nos. 05-0597 and 07-0566.

AG and CUB rehash their claim that amortization of the costs should have commenced when the costs were incurred in 2003 and 2004, instead of in January 2007, the effective date of the rates approved in Docket No. 05-0597. CUB BoE at 28; AG BoE at 59. As both AG and CUB concede, however, the simple and undeniable fact is that ComEd could not have recorded the costs as a regulatory asset and begun to amortize them before January 2007 because the Commission had not previously granted any authorization for it to do so, nor could it have done so given the statutory rate freeze that was in effect at the time.

[16] Based on the amortization period allowed in Docket No. 05-0597, about three years of cost recovery still remain after the rates approved in this case go into effect, 3*18.8 = 56.4.

AG and CUB attempt to avoid this dispositive fact by claiming that the "matching principle," requires that cost recovery be matched with the realization of benefits, and because the benefits began in 2003 the Commission should calculate the amortization of the expenses from 2003. CUB BoE at 28; AG BoE at 59. Neither AG nor CUB provides any citation for the novel principle that the period of cost recovery must be co-extensive with the period during which any related benefits exist. Moreover, the benefits of the Exelon Way severance program will continue long after the previously-allowed amortization of the related costs terminates, at which time customers will receive the entire benefits of the program.

The related argument that cost recovery in effect began in 2003 and 2004 when the Exelon Way program was initiated, because ComEd began realizing the savings resulting from the Exelon Way program at that time, also does not suggest that the actual recovery of the costs of the program should be terminated prematurely. CUB BoE at 28; AG BoE at 59. This is the same argument that Staff, AG, and CUB adopt to support reduced recovery of ComEd's 2009 severance expenses, and the Proposed Order (at 99) properly rejects the argument as applied to those expenses as well. The argument is conceptually unsound because it focuses on only a single element of ComEd's costs and revenues, disregarding all the rest, including those that increased and were not reflected in rates in effect in 2003 and 2004; thus, the argument is akin to prohibited single-issue ratemaking. The argument is factually unsound because ComEd was never allowed to recover the increased costs that it experienced in 2003 and 2004 and that were not reflected in rates that were in effect during those years. That such unrecovered costs were experienced by ComEd is evidenced by the fact that in Docket No. 05-0597 ComEd was authorized to increase its rates by approximately $83 million based on a 2004 test year.

Full recovery of the Exelon Way severance costs was approved in Docket No. 05-0597, and was reaffirmed in Docket No. 07-0566. Nothing has changed since either order was entered. Accordingly, the Proposed Order properly allowed recovery of these prudently incurred costs. AG and CUB's proposed exceptions to disallow this recovery should be rejected.

2. <u>2010 Pension / OPEB Costs</u>

CUB's Exception seeking disallowance of $37.4 million of ComEd's recovery of its actuarially-determined 2010 pension costs, based on a 2006-2008 average, should be rejected, as the Proposed Order (at 88-89) finds.

CUB repeats its claim that March 2010 pension value report prepared by Tower Watson, a leading actuarial firm, to determine ComEd's 2010 pension and OPEB costs should be tossed aside and replaced with the subjective judgment of AG/CUB witness Mr. Smith. CUB BoE at 28-30. The Proposed Order properly rejected this argument.

As AG/CUB witness Mr. Smith conceded (Tr. 527) and the Proposed Order recognizes (PO at 89), no evidence suggests that the Tower Watson report contained any errors. He further conceded that economic conditions have not returned to the pre-recession conditions (Tr. 540-41). Mr. Smith's opinion that ComEd's pension costs are "abnormally high" and "unreasonable" (CUB BoE at 29) and therefore should be based on a 2006-2008 average should be disregarded inasmuch as he, unlike Towers Watson, has no demonstrated expertise in estimating pension costs.

Moreover, CUB fails to explain why use of a 2006-08 average, as it proposes (*id.*), is appropriate at all, much less the "most reasonable," given the total dissimilarity between market conditions before and after 2008. Use of a 2006-08 average appears to be chosen simply because it results in a lower revenue requirement, not because of any principled reason.

The Proposed Order's approval of ComEd's actuarially-determined pension costs, as supported by the March 2010 report, is consistent with the Commission's past acceptance of valuation reports as providing known and measurable, and objective, verification of ComEd pension and post-retirement benefit costs. Houtsma Reb., ComEd Ex. 29.0, 32:684-33:691. In this regard, it should be noted that CUB was willing to accept the actuarially-determined decrease in OPEB costs contained in the same report, without regard to how those compared with some prior years' average.

Finally, CUB's effort to reduce the actuarially-determined pension costs on grounds of "normalization" is completely inappropriate here. Normalization adjustments that substitute prior year(s) average data are appropriate only if the test year expenses are not representative of costs levels expected to be in effect during the period in which new rates are in effect, and the prior year averages are expected to be more representative of future costs. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 21:454-22:460. As already stated, CUB has presented no evidence to support its bald assumption that pension expense levels will revert to those that existed in 2006-08. For all of the above reasons, CUB's exception should be rejected.

3. <u>2005 Pension Contribution Costs</u>

Staff's Exception seeking disallowance of ComEd's recovery of its 2005 pension funding costs should be rejected, as the Proposed Order (at 92) finds. In the Order on Rehearing in Docket No. 05-0597, the Commission allowed ComEd recovery of a limited return, based on ComEd's then cost of long-term debt, on the pension contribution it made in 2004. *Commonwealth Edison Co.*, Docket No. 05-0597 (Corr. Order on Rehearing, Dec. 20, 2006) at 26-28. The amount of the recovery established by the Commission in that order was $25.5 million. That 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, ComEd included the same $25.5 million in its revenue requirement in this case and the Proposed Order properly approved the amount in its entirety.

Staff's BoE reiterates the claim that this twice-approved recovery should be cut by $6.329 million. Staff BoE at 38-39. Staff's stated rationale is that hypothetically "the cost of debt service would decline as portions of the underlying debt mature (as detailed in Alternative 3) and with it, the amount of ComEd's regulatory debit." Staff BoE at 37. This rationale is not supported, and is in fact contradicted, by the evidence of record. First, this contribution was not financed by debt, but instead by equity, which does not "amortize." Second, even if the contribution had been financed by debt, virtually all of ComEd's debt securities do *not* amortize over time[17]; instead ComEd pays interest periodically and the principal balance remains outstanding in its entirety until the maturity date, at which point the debt is either paid off in its entirety or is re-financed. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 13:258-76.

Furthermore, Staff's claim that its "proposal is not based on assumptions outside of Alternative 3" (Staff BoE at 37) is simply beside the point. The question is whether anything in the Order in Docket No. 05-0597 supports what Staff is arguing here, and the answer to that question is clearly "no." The "maturing" of the hypothetical debt relied on by Staff is purely speculative, and not justified by either the facts or by the Commission's Order on Rehearing in Docket No. 05-0597 which first approved this recovery. Nevertheless, in its BoE, Staff once again argues that the recovery allowed in Docket No. 05-0597 was based on the issuance of fictitious 5, 10, and 30 year bonds, and that by the time the rates in this case go into effect, the 5

[17] Only 0.7% is amortizing debt, sinking fund debentures issued in 1961. Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 13:263-65; Schedule D-3.

year bond series reflected in Alternative 3 could be assumed to be paid off around the end of 2011, and therefore "it appears improper to reflect the entire cost of these 5 year bonds in the 2009 test year." Staff Init. Br. at 47. Staff's arguments take the Commission's Order in Docket No. 05-0597 far beyond anything the Commission did or said in that order. The Commission granted recovery based on an assumed and hypothetical weighted cost of debt that would have been incurred had ComEd issued debt at that time. The Commission did not, however, order ComEd or others to pretend that such hypothetical debt was really issued, and more importantly the Commission did not intimate that in future cases it would pretend further that ComEd "retired" these hypothetical "bonds." The fact that the Commission did not so state makes perfect sense; doing so would have denied ComEd even debt-rate cost recovery based on a make-believe scenario that is foreign to ComEd's actual financial situation. Yet that is precisely what Staff recommends. Staff's pretense would deny ComEd cost recovery on pension assets that still exist and that still carry a cost. Finally, even if the Commission intended to create this type of "fantasy financing," the reality is that, just as with all other ComEd bond issuances, once a debt issue matures, the capital need does not disappear; instead ComEd would have re-financed the maturing bonds with new debt securities. That would also have an associated cost.

Contrary to the unfounded speculation in Staff's BoE, GAAP accounting outlines a method whereby the funding cost will decrease. Under this method, the pension asset will decline over time as accruals exceed contributions, as discussed in connection with the 2009 pension contribution, and as shown on ComEd Ex. 55.4. The evidence shows that ComEd has applied pension accruals to the pension asset other than that reflected in the 2004 contribution, which results in a lower revenue requirement than if the accruals had been applied ratably because the remaining pension asset earns a higher return. As the pension asset declines with

annual accruals, the cost of the return on that balance will decline as well. But until such time as the pension asset has completely diminished, the capital remains in the pension trusts earning returns used to satisfy future benefits, and ComEd should be compensated for the cost of that remaining capital.

By seeking to recover the full $25.5 million that the Commission authorized in its Order on Rehearing in Docket No. 05-0597, ComEd does not "disregard" the provisions (Staff BoE at 38) of that order, but instead, acts in accordance with the order. The Proposed Order properly approved ComEd's recovery of the costs of its 2005 pension contribution in the annual amount of $25.5 million and Staff's exception should therefore be rejected. Pearce, Tr. 2544-2566.

4. Directors' Fees and Expenses

Staff takes exception to the Proposed Order's finding (PO at 94-95), stating that ComEd failed to produce evidence regarding the amount of time ComEd's board devotes to shareholder activities. Staff BoE at 39-40. Staff's argument is illogical, however, because "[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." PO at 51. ComEd met its initial burden of proof regarding directors' fees and expenses. *See* ComEd Init. Br. at 70-72, Fruehe Reb., ComEd Ex. 30.0 Public, 17:370-18:378. ComEd did not have the burden to show that directors' fees and expenses solely benefit customers. The Proposed Order simply and correctly finds that Staff did not sufficiently rebut ComEd's proof and there is no support for a disallowance.

Moreover, it is undisputed that a utility operating as a corporation is required by law to have a board of directors to manage its business and affairs (805 ILCS 5/8.05) and the costs of a board of directors are therefore a necessary, non-discretionary expense associated with the

business of operating a public utility. Likewise, Staff does not contend that the fees are unreasonable in amount. Fruehe Reb., ComEd Ex. 30.0 Public, 17:363-18:381; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 20:405-15. These costs are, in short, reasonable and necessary costs of providing utility service to customers. The Supreme Court has rejected requiring a utility to share reasonable amounts incurred in light of legal requirements. *Citizens Util. Bd. v. Ill. Commerce Comm'n*, 166 Ill. 2d 111, 121 (1995) (reversing ICC Order directing the sharing of costs incurred by utilities under environmental laws). That is the end of the inquiry.

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

5. **Perquisites and Awards**

ComEd has already filed an Exception related to the ruling of the PO (at 97) regarding perquisites and awards. *See* ComEd BoE at 103. Staff also takes exception to the PO's determination regarding perquisites and awards on the basis that "they are similar in nature to incentive compensation costs" and thus "in Staff's view, must meet the additional test of providing ratepayer benefit." Staff BoE at 41. Staff's recommendation should be rejected. The Proposed Order explicitly states that "[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." PO at 51. While perquisites and awards do represent rewards to employees, they are not the same as incentive compensation and the customer benefits test is not appropriately applied here.

Even if the customer benefits test is appropriately applied to perquisites and awards, however, ComEd has satisfied the requirements of that test. As discussed in ComEd's pre-filed testimony as well as its Initial Brief and BoE, the perquisites and awards at issue reward improvements in job performance and directly benefit ratepayers. Trpik Reb., ComEd Ex. 28.0, 6:117-19; ComEd Init. Br. at 72-73; ComEd BoE at 56-57. The Commission should therefore reject Staff's proposed exceptions on this issue and instead adopt ComEd's Exception No. 23. This is consistent both with the PO's conclusion that the customer benefits test should not be expanded, and with the PO's conclusion that when customers benefit from certain of ComEd's operating expenses, they should be allowed fully.

6. **2009 Severance Expenses**

Staff's, CUB's, and the AG's exceptions seeking to disallow recovery of ComEd's 2009 severance expenses should be rejected, as the PO (at 99) finds. In the test year ComEd incurred

$12.8 million in jurisdictional severance costs, and proposed to amortize that amount over a three-year period, including $4.277 million in its revenue requirement. The Proposed Order properly approved ComEd's severance cost amount in its entirety as well as ComEd's proposal to amortize these costs over a three-year period. Staff, in its BOE, again recommends a reduction of these severance costs to approximately $ 1.1 million. Staff BoE at 43. The result of Staff's proposal is a total annual disallowance in the amount of $3.867 million. CUB and the AG advocate an even more extreme disallowance, reiterating their position that the $12.8 million jurisdictional severance cost amount should be disallowed in its entirety. CUB BoE at 30; AG BoE at 62. These exceptions should be rejected for the following reasons.

No party ever argued, and the Proposed Order does not find, that the costs actually incurred by ComEd were not prudently incurred or reasonable in amount. Moreover, these costs are expected to save delivery service customers more than $6 million annually, savings that have been reflected in ComEd's revenue requirement in this case. CUB and the AG in their BoEs confuse the undisputed fact that savings have been and will be realized as a result of the severance costs with the issue of whether ComEd's severance costs can and should be deemed "recovered" through the savings. The AG, for example, argues that the Proposed Order is incorrect because "to the extent that the severance costs are 'reasonable and prudent costs' they must create savings that…offset the cost of the program" and so the proposed adjustments "[do] not create any risk of non-recovery." AG BoE at 61. The conclusion that costs incurred in a test year are "recovered" through savings experienced before they are passed on to customers through new rates is unprecedented, and properly so because that presumption will ensure that utilities will never have an opportunity to recover fully their prudently incurred costs. It ignores the fact that at the same time savings not reflected in rates are experienced, so are cost increases

of other types. Taking account of only the savings but not the increases will prevent full cost recovery.

Staff concedes that the Commission has never before 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)). In fact, the closest applicable Commission precedent is in stark opposition to the argument asserted by Staff, CUB and the AG, and recognizes the impropriety of focusing exclusively on a single element of ComEd's costs and ignoring how other costs during the same period may have *exceeded* those reflected in existing rates. The Commission rejected a similar argument proposed by the AG in Docket No. 08-0312 (ComEd's Original Cost Audit docket), and Staff there opposed the kind of disallowance its witness advocates here.

In that case, the AG claimed that a change in ComEd's accounting policy in 2002, pursuant to which ComEd would capitalize certain cable fault repair costs instead of expense them, led to double recovery of those costs, first as an expense (under then-existing rates) from the time of the change, and then as an element of ComEd's rate base established effective January 2, 2007, in Docket No. 05-0597. This is virtually identical to the "double recovery" premise underlying Staff's, CUB's and the AG's proposed treatment of the 2009 severance costs. *See, e.g.*, Effron Dir., AG/CUB Ex. 2.0, 24:538. In that case, however, Staff opposed the AG/CUB proposal, arguing (according to the Commission's order) that "[a] single element of a revenue requirement should not be viewed in isolation as a matter of ratemaking policy. All the elements of a revenue requirement should be viewed in the aggregate so that changes in one element are netted against changes in all other elements." *Commonwealth Edison Co.*, Docket No. 08-0312, Final Order (Jan. 12, 2010) at 4. Here, for example, the evidence shows that in

2009 ComEd's earned ROE was 8.5%, well below the 10.3% authorized in Docket No. 07-0566, indicating that any savings from the severance initiative were more than offset by other cost increases relative to the test year in that case, and hence that revenues were not available for the "recovery" of severance costs. *See also* Houtsma Sur., ComEd Ex. 55.0 2nd Rev., 27:584-30:639; Houtsma Reb., ComEd Ex. 29.0, 44:928-47:1010. That ComEd did not "recover" these 2009 severance costs through "savings" in the test year is conclusively shown by the fact that, as the Proposed Order concludes, ComEd experienced a severe revenue deficiency based on a 2009 test year.

The Order in Docket No. 08-0312 reached the right result in rejecting an argument strikingly similar to the logic underlying the severance cost reduction proposed by Staff, CUB and the AG. For the same reason, the Proposed Order properly rejected Staff's, CUB's and the AG's conclusion that ComEd has "recovered" its 2009 severance costs through the savings in employee compensation costs.

The AG, unsuccessfully, attempts to base the disallowance of the severance costs on the ground that it is consistent with the same, unidentified version of the novel "matching" principle that it claims applies to the Exelon Way severance costs (AG BoE at 61-62) and that has been implicitly rejected by the Commission with respect to those costs, and that is discussed in Section C.1., *supra*, of this RBoE. By this, the AG appears to argue that because the savings have pre-dated the time they will be passed on to customers, the benefits and costs have somehow not matched. But that is true in later years as well, to the exclusive benefit of customers: the savings will continue to be realized by customers long after the costs have been amortized, just as is the case with the Exelon Way costs and benefits. In other words, cost recovery will be" matched" – and in fact be outlived – by customer realization of savings.

The Proposed Order also properly rejected the 7.5 year amortization period proposed by AG and CUB in the alternative. PO at 99. The three-year amortization period proposed by ComEd produces only $4.277 million in annual revenues for ComEd, compared to the more than $6 million in annual savings enjoyed by customers. A 7.5-year amortization period widens the gap between ComEd's cost recovery and the customer savings: ComEd would recover only about $1.71 million per year compared to the $6 million in customer savings. As the Proposed Order correctly recognized, that greater disparity cannot be justified.

For all of these reasons, Staff's, CUB's, and the AG's exceptions should be rejected by the Commission.

7. <u>Charitable Contributions</u>

Staff takes exception to the Proposed Order (at 102-03), arguing that the charitable contributions at issue are actually not charitable contributions governed by Section 9-227 of the Act, 220 ILCS 5/9-227, but are instead advertising governed by Section 9-225, 220 ILCS 5/9-225. Staff BoE at 44-45. Staff's main concern appears to be that ComEd does not make the contributions anonymously, and that ComEd receives benefits from the donations, although Staff provides no support for that assertion. *Id.* Staff also reiterates its position that donations made by Exelon Business Services Company ("EBSC") on behalf of ComEd should be disallowed. *Id.* Indeed, Staff takes this argument one step further in its BoE and makes the unsupported assertion that the EBSC donations are not made on behalf of ComEd. *Id.* The AG adopts these arguments for the first time in its BoE. *See* AG BoE at 66-67. Staff also relies on an interpretation of Section 9-227 that is facially incorrect and in direct conflict with *BPI II*. In addition, the AG and CUB renew their proposition that the Commission disallow half of ComEd's charitable

contributions so that ratepayers and shareholders share the costs equally. AG BoE at 68; CUB BoE at 34.

As discussed in ComEd's BoE, with the exception of charitable contributions to organizations outside ComEd's service territory, the Proposed Order correctly decided these issues and Staff and AG/CUB's arguments should be rejected. *See* ComEd BoE at 57-58. Neither Staff nor AG/CUB submitted evidence showing that the recipients of the amounts in question are not *bona fide* charitable organizations, or even that the overall contributions are excessive. As ComEd explained in testimony and in its briefs, ComEd's total charitable contributions for which it seeks recovery in this case – $6.3 million – is lower than the $6.8 million (both amounts before jurisdictional allocation) of contributions approved in Docket No. 07-0566. Fruehe Reb., ComEd Ex. 30.0 Public, 8:163-66; ComEd Init. Br. at 76; ComEd Reply Br. at 87. ComEd also submitted evidence 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. Fruehe Reb., ComEd Ex. 30.0 Public, 8:166-71.

The undisputed evidence shows that the contributions made in conjunction with EBSC are made on behalf of ComEd and are functionally equivalent to the donations made by ComEd in its own name. *Id.*, 8:157-158. It is nearly certain that had ComEd made those donations directly, no question would have been raised about the propriety of those contributions (to such organizations as the United Way of Metropolitan Chicago, the Kellogg School of Management, the Chicago 2016 Committee, and the Field Museum). *Id.*, 8:158-160; ComEd Init. Br. at 77. Moreover, the fact that ComEd may receive some positive recognition for its contribution is no reason to characterize the contribution, to an admittedly *bona fide* charity as "promotional" or

"goodwill" in nature. As Mr. Fruehe pointed out, such contributions are quite different from, for example, a promotional billboard at U.S. Cellular Field. Fruehe Reb., ComEd Ex. 30.0 Public, 9:177-86.

Additionally, staff makes the unsupported statement that ComEd requests recognition for its charitable contributions. *See* Staff BoE at 44. In some instances, ComEd does receive recognition for its contributions, but calling this a request for recognition is a mischaracterization. Indeed, as ComEd has explained, "One reason charitable organizations display the names and logos of contributors is to encourage others also to contribute." ComEd Ex 56.0 3rd Rev., 7:136-37. There is no contrary evidence.

As ComEd also explained in its testimony and briefs, the only proper tests are whether the donation is made for "charitable, scientific, religious or educational purposes" and whether it is "reasonable in amount." Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 6:123-28; 220 ILCS 5/9-227. ComEd's $6.3 million of charitable contributions qualify on both counts and should be approved in their entirety. Fruehe Reb., ComEd Ex. 30.0 Public, 7:143-9:195; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 6:110-8:166; ComEd Ex. 6.1, Sched. C-7 (details of contributions). Staff's unsupported inference – from the mere existence of Section 9-227 – that the legislature doubted the "legitimacy of these expenses being recovered through rates" is contrary to the plain terms of Section 9-227. Plus, Staff's argument that Section 9-227 simply "allows for the *consideration* of donations" (Staff BoE at 44) is in direct conflict with *BPI II*, which mandates that the Commission allow charitable contributions that are reasonable in amount. *BPI II*, 146 Ill. 2d at 254.

Likewise, CUB and the AG's reliance on *BPI II* for its 50% disallowance of donations across the board (CUB BoE at 32-33; AG BoE at 64-65) is directly contrary to both the terms of

9-227 and the same holding in *BPI II*. The *BPI II* court held that the Commission must look at the *total amount* of charitable contributions in order to determine whether the contributions are reasonable in amount. *BPI II*, 146 Ill. 2d at 254. "When this burden of proof is considered, the Act merely states that the Commission shall not disallow any portion of that amount *which Edison has shown to be reasonable in amount.*" *Id.* (emphasis in original). As discussed above, ComEd met its burden of proof on this issue by showing that the total amount of contributions was reasonable. The Commission therefore cannot disallow these expenses and must reject Staff and AG/CUB's exceptions.

8. <u>Legal Fees – IRS Dispute</u>

ComEd has provided an exception to the Proposed Order regarding this operating expense. *See* ComEd BoE at 58. That exception obviates the need to make Staff's correction. However, in the event that the Commission rejects ComEd's exception, ComEd agrees with Staff's proposed correction.

D. <u>AMI Pilot</u>

The Proposed Order (at 106) correctly rejects Staff's unreasonable proposal to disallow as not known and measurable $1,108,000 of ComEd's expenses incurred pursuant to the Commission's Order in Docket 09-0263 requiring ComEd to conduct the AMI Pilot.

Staff's BoE (at 47-48) is devoted to arguing that the known and measureable standard applicable to *pro forma* adjustments (under 83 Ill. Admin Code § 287.40) applies to the AMI Pilot expenses (notwithstanding the Commission's later approval of the "bridge tariff" that allowed ComEd to seek to recover in this Docket operating expenses that it previously was going to recover through the AMI Pilot rider).

What Staff's BoE does not do, however, is present any grounds for concluding that the challenged AMI Pilot expenses actually fail to meet the known and measureable standard. The costs meet the standard. Staff's Exception is irrelevant.

In his rebuttal testimony, Staff witness Tolsdorf proposes to disallow all costs ComEd expected to incur in connection with the AMI Pilot program between December 2010 and June 2011, claiming that ComEd has not produced sufficient documentation to establish that they are "known and measurable." Tolsdorf Reb., Staff Ex. 19.0, 11:244-12:278. This means Mr. Tolsdorf would allow $130,000 for November 2010 and disallow the remaining $2,706,000 for December 2010 through June 2011. *Id*., Sched. 19.05.

The costs in question are those incurred in connection with an AMI Pilot that the Commission ordered ComEd to conduct, as noted above. ComEd has subsequently proceeded with the pilot. However, because an Appellate Court decision precluded rider recovery of these costs going forward, the Commission approved a separate tariff (the bridge tariff) providing that any costs not recovered through the tariff would be included "in a general rate case …. There, they would be recovered … like any other operating expenses." Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 27:564-28:583. Mr. Tolsdorf recognizes that the "rate case" referenced in the tariff language quoted above is the instant case. Tr. 1290.

ComEd Ex. 56.6 provides a detailed list of ComEd's latest estimate of the AMI Pilot expenses it will incur through June 2011, along with a list and description of the activities and the service providers. Tr. 1293-95. The Commission's *pro forma* adjustments rule (83 Ill. Admin Code § 287.40) requires projects proposed as "known and measurable" adjustments to be "individually identified". Mr. Tolsdorf agrees that ComEd Ex. 56.6 "individually identifies" the projects associated with the AMI pilot project through June 2011. *Id.*, 1295.

Mr. Tolsdorf's position boils down to an assertion that a project cannot be known and measurable unless it is covered by a contract or purchase order. Tr. 1297. The Commission's rule does not contain any such requirement, and Mr. Tolsdorf acknowledges that he has not cited any authority for such an interpretation. In fact, under a similar prior Commission rule, the absence of such documents as purchase orders, written contracts, and invoices did not by itself justify a conclusion the projects were not known or measureable. *Commonwealth Edison Co. v. Ill. Commerce Comm'n*, 322 Ill. App. 3d 846, 851-852 (2nd Dist. 2001) (reversing the Commission's disallowance of certain *pro forma* adjustments on this ground).

The AMI project is one the Commission specifically approved in Docket No. 09-0263, and ordered to be completed. Mr. Tolsdorf has never suggested nor does the record reflect anywhere that ComEd will or may not complete this project. The Commission has further provided for the recovery of the costs in question in this Docket. This is another example of Staff's adherence to an unusually and unreasonably rigid standard for allowing recovery of the costs of post-test year costs. Combining all of those facts with Mr. Tolsdorf's unprecedentedly strict (and unlawful) interpretation of the *pro forma* rule means that Mr. Tolsdorf's proposed disallowance should and must be rejected, as the Proposed Order provides.

E. New Business Revenue Credit

See Section VII.B of this RBoE.

F. Tax Repair Methodology – New IRS Procedures

The Proposed Order (at 108) correctly rejects AG/CUB's proposal that ComEd create a reserve account and be subject to certain recordkeeping requirements, and be subject to a revenue requirement adjustment, with carrying charges, in its next rate case, because of a

possible future change in ComEd's accounting as a result of an IRS change in procedures. CUB's BoE (at 35) takes Exception, but CUB's proposal lacks merit.

CUB's BoE (at 35) tries to make it sound like money is growing on trees and ComEd simply is refusing to look up at the branches, but, of course, those are not the actual facts. AG/CUB have never identified even a single utility that has made the accounting change and then had it audited by the IRS.

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

The IRS has not issued any guidelines, and considerable uncertainty exists over how a unit of property should be defined for transmission and distribution property. ComEd is collaborating with the Edison Electric Institute and other electric utilities to obtain specific implementation guidance from the IRS. Although some utilities have filed a request for change in the method of accounting (AG/CUB identified three by name), a significant number are awaiting the IRS guidelines before implementing the change. Once guidelines for the new method are issued and can be implemented by ComEd, customers will benefit immediately, because any resulting cash flows will help finance new plant investment. In addition, the cumulative accelerated tax benefits that may ultimately result from the change in policy will be

reflected as a reduction to rate base in future rate cases, and thereby be flowed through to customers just like all other tax benefits. Houtsma Reb., ComEd Ex. 29.0, 38:816 - 40:856.

Not only would it be unnecessary to create a separate account as Mr. Effron proposes to "preserve" the tax benefits for customers, but it would be inappropriate to do so. ComEd presently records all of its accumulated deferred income taxes in separate accounts, and the Uniform System of Accounts requires that tax timing differences be recorded in separate asset/liability accounts. ComEd's records track the various categories of tax differences. Upon implementation of the new repair guidelines, ComEd will record the tax deductions separately within the existing, proper accounts reflecting tax timing differences. Houtsma Reb., ComEd Ex. 29.0, 40:857 - 41:872.

Mr. Effron's suggestion that "carrying charges" be accumulated on these tax benefits would be inappropriate single-issue ratemaking when implemented in the next rate case, particularly in light of the fact that no mechanism exists (or has been suggested by Mr. Effron) by which "carrying charges" on the investment made between rate cases that starts to accrue depreciation before inclusion in rate base can be similarly deferred and recovered in future rate cases.

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

G. IEDT – Illinois Electricity Distribution Tax

The Proposed Order (at 110) correctly concluded that calculating Illinois Electric Distribution Taxes ("IEDT") using a weather normalized credit is appropriate because a normalized credit smoothes out year to year fluctuations. However, AG (BoE at 73-78) and CUB (BoE at 36-37) continue to argue that the IEDT expenses should be reduced based on 2009 actual IEDT taxes paid reduced by the estimated IEDT credit for 2009. This argument must be rejected as it is without merit.

As ComEd explained in its Initial Brief (at 85-86), the AG/CUB methodology should be rejected as faulty for several reasons. First, the AG/CUB methodology is based solely on 2009, which was an abnormally cool summer, having the fewest cooling degree days since 1992. The tax for that year will not be representative for the period in which the rates set in this proceeding will be in effect. Under its methodology, which is supported by Staff (*see* Hathhorn Reb., Staff Ex. 17.0, 10:204-11:213), ComEd accounts for this data by weather normalizing the tax over a six year period. AG claims that ComEd has performed no analysis "to determine which of the six historical years that were averaged had abnormally mild or severe weather and correspondingly large or small taxes to the revenue cap." AG BoE at 75. This argument is a red herring. ComEd applied the weather normalization methodology just as it weather normalizes billing determinants to develop rates that will best reflect normal conditions expected during the period rates set in this case will be in effect (a practice no party has opposed). ComEd also makes weather normalized adjustments to storm costs, which can also vary year to year. Fruehe Reb., ComEd Ex. 30.0, 12:249-61; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:196-210.

Second, the AG/CUB methodology improperly mixes the 2009 tax with a credit that is not applicable to 2009 because the credit lags the tax by three years (resulting in a mismatch between the tax and the credit). Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:207-08. Thus, CUB's

claim (CUB BoE at 36) that the AG/CUB methodology best matches the credit and tax for the test year fails. ComEd's use of the six-year average of the credit will smooth out year-to-year fluctuations and will provide a better estimate of the net amount of the tax ComEd will pay in a given year. Fruehe Reb., ComEd Ex. 30.0, 11:240-12:248; Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 10:208-10.

Finally, the AG's claim that the AG/CUB approach is supported by the statutory cap (AG BoE at 74) is incorrect and ignores the facts. Fruehe Sur., ComEd Ex. 56.0 Public, 10:196-215; *see also* Fruehe Reb., ComEd Ex. 30.0, 11:231 – 12:261. The AG's additional argument that Mr. Brosch's approach is the one that properly accounts for the statutory cap (AG BoE at 75) is wrong. This argument wholly ignores the fact that the credit lags payment of the tax by three years and, more importantly, that the credits ComEd included in the average calculation are all a product of the cap.

For these reasons, the AG/CUB exception language regarding the IEDT calculation method should be rejected.

H. <u>Medicare Part D Regulatory Asset</u>

The AG's and CUB's exception to the findings of the Proposed Order (at 112), which seek to amortize the regulatory asset relating to tax liability for Medicare Part D for 10 years should be rejected.

Until passage of the federal health care reform legislation in 2010, ComEd was entitled to receive a tax-free subsidy from the federal government for providing prescription drug coverage to retirees. During that time, ComEd passed on the benefit of the subsidy to customers even though payment from the federal government seriously lagged ComEd's provision of the coverage. The evidence showed that ComEd had received only about 13% of the subsidy from

the government. Houtsma Reb., ComEd Ex. 29.0, 27:572-74, 30:630-39; ComEd Ex. 29.9. Under the law as changed in 2010, ComEd will now be taxed for all subsidies ComEd receives even if those subsidies relate to years before 2010. ComEd thus will be faced with a substantial tax liability, and proposed the creation of a regulatory asset in the amount of the anticipated tax liability, with a three-year amortization period. ComEd proposed the three-year period because: (1) of the need to have sufficient funds available to pay this tax liability when it becomes due; and (2) customers have received and will retain the full benefit of the cash subsidies even though ComEd has received only a small fraction of those subsidies. Houtsma Reb., ComEd Ex. 29.0, 29:609-31:647. The Proposed Order accepted this reasoning.

AG and CUB restate their contention that ComEd's regulatory asset relating to tax liability for Medicare Part D should be amortized over ten years. CUB BoE at 37; AG BoE at 78. They argue first that "[t]he benefits of the subsidy received in 2009 will be realized over approximately eleven years." CUB BoE at 37. That contention is irrelevant to ComEd's cost recovery on numerous grounds, not least of which is the fact that it is ComEd's customers, not ComEd, who have realized the benefits of all subsidy amounts received to date. Moreover, the suggestion that ten years is a proper amortization period because that is the period over which subsidies will be received in the future is illogical because the amount ComEd seeks to collect relates to subsidies received for years prior to and including 2012, not ten years into the future. Houtsma Reb., ComEd Ex. 29.0, 26:536-31:647. A three-year amortization is thus much more closely aligned with the period for which future taxes are being recovered than is the AG/CUB ten-year period.

AG and CUB argue further that the Proposed Order's approval of a three-year period, even though it is not known with complete certainty when the tax will be due, is improper.

CUB BoE at 37; AG BoE at 78. This argument is unavailing. Neither the Proposed Order nor ComEd claims that the tax payment is "imminent." The Proposed Order only acknowledges that it is possible that payment of the tax is imminent. PO at 112. No evidence suggests that payment of this tax will be delayed indefinitely into the future. Simply because it is impossible to predict the exact timing as to when the tax will be due is no reason to choose a lengthy amortization period that could likely leave ComEd with insufficient funds to make required payments when they become due. This is especially true in that ComEd has already passed to its customers each year the full benefit of the cash subsidy even though ComEd received only a small portion of that amount. The three year amortization period approved in the Proposed Order is much more likely to allow this desirable outcome to be achieved than is the AG/CUB ten-year period. The AG's and CUB's exception to the Proposed Order should therefore be rejected.

III. RATE OF RETURN

A. Cost of Short-Term Debt

The Proposed Order's approval of ComEd's short-term debt balance and cost complies with all applicable requirements. Section 285.4020(d) of the Commission's rules (83 Ill. Admin. Code § 285.4020) provides that short-term debt balances shall be provided on "a 12 month average basis." The balance approved by the Proposed Order is calculated using a 12 month average basis. The 12 month period used for the calculation ends on March 31, 2010 – a date that complies with all requirements relating to capital structure measurement periods.

Staff contends that the Commission should approve a different 12 month average for a period ending in September, 2010. No legal requirement in any statute, regulation, or decision supports Staff's position. Here, the evidence shows that the measurement period adopted by

ComEd and approved by the Proposed Order is more representative and consistent. Where that data and evidence is present, it should be heeded, past practice in the absence of such evidence notwithstanding.

In sum, the Proposed Oder's resolution of this issue is supported by the evidence and Staff's Exception should be rejected.

B. <u>Cost of Common Equity</u>

The Proposed Order contains a well-reasoned discussion of the cost of equity issues presented in this proceeding, including citations to and analysis of the evidence in the record. It correctly found serious fault with the return on equity (ROE) calculations presented by witnesses for Staff, IIEC, and AG-CUB. Those errors, as the Proposed Order also correctly recognized, occurred in both their CAPM and DCF studies and resulted in both erroneous and downwardly biased results. By contrast, the Proposed Order found that Professor Hadaway's analysis employed accepted methodologies and used unbiased data and samples. His growth rates are based on actual historical long-term GDP data. His comparable company sample was not skewed by including companies that are not comparable to ComEd. His data was not measured at dates that were unrepresentative and unfair.

ComEd's Brief on Exceptions describes why that evidence – together with the evidence of the unique financial conditions utilities now face – support a base return on equity of 10.9%. *See* ComEd BOE at 63-66. A 10.9% ROE would be consistent with the Proposed Orders' detailed findings concerning the data, the studies, and the methodology presented, as well as the evidence showing the current ROEs are at the top end of the mathematically-calculated reasonable ranges. However, if the Commission nonetheless decides on a "mid-point" approach, the Proposed Order's detailed analysis unquestionably supports the award of 10.5%. It's

recommendation in that regard is unquestionably supported by substantial evidence and appropriate findings.[18] By contrast, the contentions by Staff that it "is unclear how [the ALJs] arrived at [their] result," by IIEC that the Proposed Order "fails to articulate a reasoned analysis" and is "arbitrary and unreasonable," by CUB that the Proposed Order "falls well short" of stating "the facts essential to its rulings," and by AARP that the decision is "not supportable," are simply without any basis.[19]

Underlying all of this rhetoric is the suggestion that 10.50% is too high of a return on equity because it is more than the Commission has authorized for ComEd in recent proceedings. IIEC (BoE at 6), for example, argues that the 0.2% increase (over the existing authorized return) the Proposed Order approves represents "a dramatic change of direction for ComEd's authorized equity returns," despite the fact that it is far less of a change than IIEC itself proposed. AARP complains that it would mean "a *dramatic* increase in Commission authorizations" (BoE at 2), raising the question of what adjective AARP would apply to the nearly *seven* times greater change in ComEd's ROE proposed by AG-CUB. Similarly, Staff characterizes the decision as "a 180 degree departure" (BoE at 56) from a prior Commission order, despite the Proposed Order's fidelity to the Commission's methodological decisions and its commitment to using unbiased data. All of this rhetoric ignores the fact that the 20 basis point increase the Proposed Order recommends is modest, representing an increase of less than 2% over ComEd's existing authorized return on equity.

In this market environment, a modest increase in the equity return is unquestionably appropriate and equally unquestionably supported by the evidence. In fact, the evidence shows

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[18] ComEd's proposed exceptions suggest additional language that would complement the analysis and findings already included in the Proposed Order.

[19] *See*, respectively, Staff BoE at 56, IIEC BoE at 5, 15; CUB BoE at 41; AARP BoE at 2.

that the current financial conditions and investor required returns clearly call for a return on equity above those approved in the most recent past. In arriving at a 10.50 % equity return, the Proposed Order properly addressed the evidence in this proceeding, rather than evidence in prior cases in which the circumstances were significantly different. As ComEd explained (with relevant citations to the record) in its Initial Brief:

> The economic and financial uncertainties generated by the credit crisis have significantly impacted the cost of equity for the capital intensive electric utility industry (Hadaway, ComEd Ex. 11.0, 19:409-30:616) testing the financial standing of the utility sector "like never before." Fetter, ComEd Reb. Ex. 45.0, 11:212-213. Unlike typical industrial firms, which make annual capital expenditures of approximately 35% of their operating cash flow, electric utilities often must devote 100% of operating cash flow to new capital expenditures. Seligson Dir., ComEd Ex. 12.0, 4:90-91. ComEd is no exception. Since its last rate case, ComEd has made more than $2 billion of new distribution infrastructure investments and continues to invest about $900 million each year to maintain and modernize its system.
>
> Electric utilities are in competition with all other firms seeking investor capital (Seligson Reb., ComEd Ex. 38.0, 3:47-48, Tr. 1764) but they face special challenges in the capital markets because of the critical impact of regulation on a utility's financial performance. Current and prospective investors are looking for assurance that allowed returns on equity, and the actual earnings that they produce, will be sufficient to attract new capital on reasonable terms. Seligson Dir., ComEd Ex. 12.0, 11:241-243. Investors value stable earnings and regular dividends supported by consistent and fair regulation. Seligson Dir., ComEd Ex. 12.0, 12:257-258.

> Although the capital needs of electric utilities are high, authorized returns on equity for utilities have been at extremely low levels for a number of years, prompted in part by a decline in interest rates to historically low levels. Seligson Dir., ComEd Ex. 12.0, 7:138-139. Higher risks facing utilities for major construction initiatives, the mounting need for external financing, increasing costs for medical, post-retirement, and pension benefits, and other factors require correspondingly higher returns on equity. Id., 7:141-147. Developments in the capital markets show that higher returns are warranted. While the index of S&P 500 common stock prices has increased significantly during the past year, utility prices have remained relatively flat, indicating that the cost of equity for utility companies has not declined to the same extent that interest rates have fallen or to the same extent that the cost of equity may have come down for the broader equity market. The relatively lower prices for utility shares indicate that the cost of capital for utilities is higher. Hadaway Dir., ComEd Ex. 11.0, 25:511-25:516.
>
> All of these factors call for a return on equity for ComEd in excess of the range the Commission has approved in recent proceedings.

ComEd Init. Br. at 95-96. The 10.50% return on equity recommended by the Proposed Order is, thus, strongly supported by the evidence, including the extraordinary economic environment and the challenges it presents for electric utilities facing the need to make enormous capital expenditures each year.

Focusing on the specific numerical analyses presented in this proceeding, the briefs on exceptions recognize that one of the most important factors in the determination of ComEd's return on equity is the appropriate growth rate to be used in the DCF analysis. IIEC refers to this

as the area in which the "most significant differences" exist between the parties. IIEC BoE at 8. CUB too acknowledges that, of all of the differences between the parties, "the most significant are related to company growth expectations." CUB BoE at 42. Contrary to the contentions about insufficient analysis and reasoning, the Proposed Order addresses the growth rate issue clearly and logically, explaining, for example, that Staff's proposed growth rate is inconsistent with the weight of the evidence and, in particular, inconsistent with actual experience:

> 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.

PO at 145.[20]

The Proposed Order (at 145) also addresses IIEC's proposed growth rate, finding it to be "negatively biased." Mischaracterizing this finding as "conclusory," IIEC seeks to leave the impression that there is "no evidence supporting" it or that it is merely a "baseless opinion." IIEC BoE at 10. The Proposed Order and the evidence it reviews shows those claim to be false. Page 120 of the Proposed Order explains exactly why IIEC's growth rate assumption is unreliable, and cites the specific evidence that proves it. The Proposed Order states:

> 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

[20] Staff's claim that the Proposed Order's findings regarding the DCF growth rate is inconsistent with its own sustainable growth "sv" analysis is contradicted by the evidence showing that "[t]he 'sv' term in that model accounts only for potential growth, or attrition, that may result from stock sales above, or below, book value. Mr. McNally's inclusion of that term does not reconcile the sustainable growth model's fundamental deficiencies, *e.g.*, its exclusion of growth from any other source (productivity improvements, changes in product markets, etc.). His application of that model to claim that [ComEd's] growth rates are not sustainable is not valid." Hadaway Sur., ComEd Ex 62.0, 4:70-76.

> 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.

In addition, the Proposed Order's conclusion that Staff's growth rate relies on an unreasonable estimate of future rate of inflation applies equally to IIEC's growth rate assumption. As the testimony demonstrated:

> The principal cause for [IIEC witness Gorman's] much lower forecast is the much lower projected inflation rates in his data. His projected inflation rates are only 2.0 percent to 2.1 percent, whereas [ComEd's] estimate includes long-term inflation of 3.1 percent. The data in … ComEd Ex. 11.3 show that over the past 60 years, the GDP price deflator has increased by an average of 3.5 percent per year. Even the most recent 10-year periods have shown average increases of 2.3 percent per year. Mr. Gorman's inflation rates are lower than even those associated with recently depressed economic conditions, and they are not at all consistent with the longer-term historical inflation rates that investors have experienced.

Hadaway Sur., ComEd Ex. 62.0, 7:149-8:157. Once again, efforts to reduce suppress ROEs rely on the use of unrepresentative periods and data that does not square with actual performance.

In summary, on the most important issue affecting return on equity issue – the growth rate used in the DCF analysis – the Proposed Order is supported by compelling evidence and appropriate findings.

Likewise, on the question of selecting comparable companies for the DCF analysis, the Proposed Order's findings that adjustments to competing models were required is supported by the evidence. On this point, the Proposed Order (at 144) concludes that Staff's comparable company selections contained "companies that are not that similar to ComEd." Once again, as reviewed by the Proposed Order (at 118), the evidence supporting that finding is compelling:

> 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 …. 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.*

Without a doubt, these two tiny natural gas companies should not have been included in the already small group of companies that Staff used to try to derive a fair estimate of ComEd's ROE. In accordance with the Proposed Order's findings, the evidence demonstrated that:

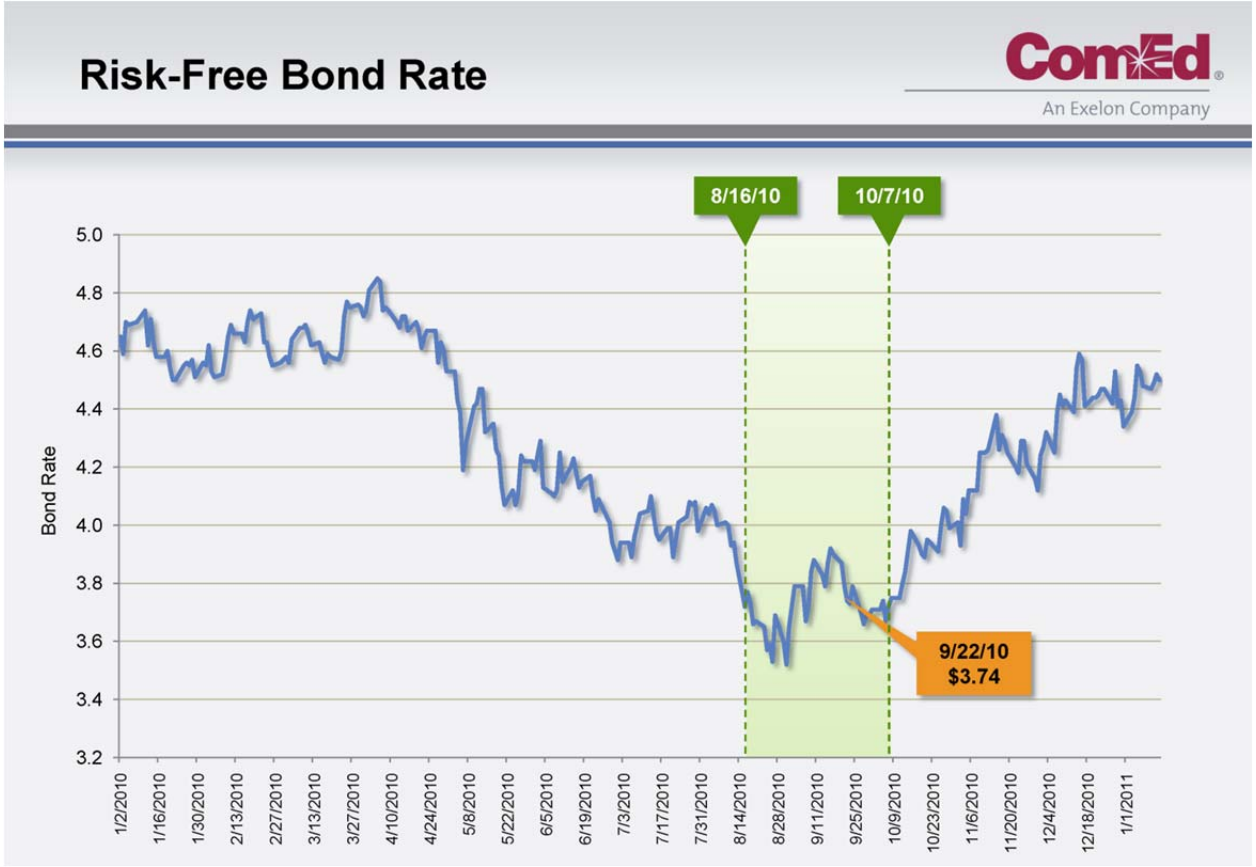
> New Jersey Resources receives only 38 percent of its revenues from regulated activities and South Jersey Industries has only 53 percent regulated revenues. Mr. McNally's lengthy attempt to rationalize his selections notwithstanding, the disparity in the size and percentage of regulated revenues for these companies relative to ComEd shows that they should not have been included, or, at best, they might have been part of a much larger comparable group so that their results were better blended with those for other more comparable utilities.

Hadaway Sur., ComEd Ex. 62.0, 2:41-3:48.

The Proposed Order also points out that Mr. McNally's CAPM used an extraordinarily biased and unfair sample date (9/22/2010) – a date falling within a short period when interest rates were at a historic low that was significantly atypical even for recent times. PO at 144-45; Hadaway Sur., ComEd Ex. 62.0, 9 n.1. Staff, among other things defends this date as a "normal day" and claims "the Company offers no evidence to suggest otherwise." Staff BOE at 66. Frankly, this is nonsense. September 22 falls in a short period in which there was a sharp dip in interest rates. Only by choosing a date in the narrow band between August 16 and October 7 is there any chance of getting a rate as low as Staff's – and even during this atypical period many of the day's had higher rates. This dip was not only short-lived, it was historic, with rates far below those prevailing before and after.[21] It was also a sharp dip. As the Proposed Order

[21] Staff's claim that ComEd introduced no evidence is inexplicable given that ComEd introduced into evidence, among other things, the official Federal Reserve Board data showing the relevant interest rates on every trading day from January 1, 2010 through January 13, 2011, the newest data available as of the day of the hearing. *See* ComEd Cross Ex. 20.

correctly notes, the rate was fully 67 basis points lower on September 22 than on the last trading day of the year. PO at 145. September 22 spot data is, thus, severely biased both when looking at typical 2010 rates and when looking at the latest available data. The Commission need only view the data graphically, as on the chart below, to see the reality of it.



This use of atypical "spot" data is exactly the type of flaw the Commission condemned in its *North Shore* decision. *North Shore Gas Co.*, ICC Docket Nos. 07-0241/07-0242 (Cons.) (Final Order, Feb. 5, 2008) at 92, 125-6. Staff argues that it is proper under *North Shore* to use their single measurement date, arguing that *North Shore* did not criticize the use of all spot data, but only spot data that ignored the "conditions or financial climate … in the surrounding days and times." *See* Staff BoE at 66-67 *quoting in part North Shore* at 126-27. One would be hard

pressed to think of less representative spot data than Mr. McNally used here, or data that more plainly ignored the "conditions or financial climate … in the surrounding days and times."

Staff (BoE at 65-66) makes much of the fact that one cannot arrive at a valid CAPM result by simply adding 67 basis points to Staff's calculation, as if ComEd's was relying on it. This is Staff's CAPM calculation, not ComEd's, and it is biased and flawed beyond repair. Neither ComEd nor the Proposed Order pretends a valid conclusion can be reached from it.[22] Rather, as acknowledged by the Proposed Order, the 67 basis points illustrates the sheer magnitude of the downward bias that Staff's use of unrepresentative data could introduce into the CAPM result. The Proposed Order (at 145) observes that this error alone is far more than sufficient to have cause Mr. McNally's CAPM to deviate from Dr. Hadaway's recommendation, pointing out that if an CAPM result without this bias were only 33 basis point higher (half of his error), it would "be more in the range of Dr. Hadaway's midpoint of 10.6%." PO at 145.

The remaining attacks on the Proposed Order are largely slinging adjectives. For example, notwithstanding IIEC's claim that the Proposed Order "fails to articulate a reasoned analysis" and is "arbitrary and unreasonable," (IIEC BoE at 5, 15), the order's reasoning is unassailable and supported by evidence it cites, as shown above. IIEC also complains (BoE at 5) that the adjustments the Proposed Order found to be required were rejected by "the expert sponsoring the analysis." While it might be called bold, that argument is hardly valid, nor a deficiency of the Proposed Order. Experts frequently oppose adjustments to their own models, especially when those adjustments expose their own use of biased data. Proposed Order evaluates the evidence objectively, as it should. The fact that an expert advocating a low cost of

[22] Ironically, Staff points the ComEd was clear about this, quoting the colloquy from the hearing, in both its post-Hearing briefs and, again, in its BOE. Tr. 1877-79.

equity disagrees is no reason to disturb the order's findings. CUB's claim that the Proposed Order "falls well short" of stating "the facts essential to its rulings," CUB BoE at 41, is plainly wrong because the Proposed Order's decision to reject unrealistically low growth rates is explained in detail. Far from proposing a decision that is "not supportable," as AARP maintains (BoE at 2), the Proposed Order reaches a reasonable conclusion, firmly grounded in the evidence in the record.

Finally, Staff, IIEC, CUB, and AARP contend that it is "unclear" how the Proposed Order's 10.50% recommended return on equity was determined, but no uncertainty exists. Staff (BoE at 56) itself recognizes and acknowledges that 10.50% is approximately "the average of the midpoint of Dr. Hadaway's estimate range (10.6%) and the results of Mr. McNally's capital asset pricing model (CAPM) after adjustment 'in the range of 10.50%'. (PO, p. 145)." Having acknowledged the 10.5% and 10.6% reference points, Staff's argument is reduced to the contention that something is improper about "rounding down" the result rather than adopting the precise average of the two rates. No such requirement can be found, and if one existed, it would *increase*, not decrease the allowed rate of return.

Moreover, the suggestion that no record evidence supports a 10.5% return is flatly contradicted by the evidence establishing that, after correcting Mr. McNally's analysis for the improper inclusion of two non-comparable companies, Staff's recommended return on equity would be 10.1%, without any adjustment for unreasonably low growth rates or the inappropriate "spot date" approach in Staff's CAPM analysis. ComEd Ex. 37.0 at 14; ComEd Ex. 37.2. The average of Staff's low growth rate DCF / spot date CAPM result of 10.1% and Dr. Hadaway's reasonable DCF growth rate – based on a comparable sample and actual historical growth rates –

result of 10.9% is 10.5%. The effort to characterize the Proposed Order's result as "arbitrary" and unsupported by the evidence is plainly wrong.[23]

In sum, the Proposed Order carefully analyzes the evidence concerning ComEd's cost of equity and correctly identifies the growth rate estimate as the most important issue for resolution. The briefs on exceptions agree that the growth rate estimate is critical, but argue in favor of lower rates premised on the assumption that inflation will average only 2% – a full percentage point less than the actual historical average. The Proposed Order correctly rejects that unrealistic prediction. That determination, which is supported by extensive record evidence, is by far the largest factor underlying the PO's 10.50% approved return on equity. Because the cost of equity estimates presented by Staff,[24] IIEC[25] and CUB[26] rely on unrealistic growth rate predictions, their extremely low recommended equity returns for ComEd were properly rejected by the PO. The Proposed Order corrects these and other errors in the estimates, considers all of the evidence and arrives at a fair and reasonable cost of equity of 10.50%. Nothing in the briefs on exceptions provides any basis for departing from that recommendation.

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[23] The strong record support for the Proposed Order's 10.5% result without any adjustment to Staff's CAPM analysis demonstrates that Staff's extensive criticism of the Proposed Order's discussion of Staff's flawed CAPM approach, Staff BOE at 65-69, is to no avail. Although Staff's reliance on the spot date approach and its selection of a date on which the risk free Treasury rate was at an exceptionally low rate are properly rejected in the Proposed Order, that determination is not <u>necessary</u> to the outcome. The 10.5% return on equity is supported independently by the findings that (1) it was error for Staff to include two small gas companies with low percentages of regulated activities in the comparable group and (2) that Staff's growth rates are "too low" and should be averaged with Dr. Hadaway's DCF growth rate, which is "a more reasonable proxy for investor's long-term expectations." PO at 145.

[24] Staff used a GDP growth rate of only 5.0%. Staff Ex. 5.0.

[25] IIEC used a GDP growth rate of only 4.7%. IIEC Ex. 1.0, 26:613-15.

[26] CUB used a GDP growth rate of only 4.86%. AG-CUB Ex. 4.3.

C. **Staff's Adjustments to Rate of Return**

The Proposed Order properly rejects Staff's proposed downward adjustment to ComEd's return on equity resulting from the approval of ComEd's SFV rate design. The bases for rejecting Staff's adjustment are clearly stated in the Proposed Order:

1. The Proposed Order concludes that 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. PO at 155.
2. Staff presents no evidence of its own quantifying any adjustment. The Proposed Order finds that Mr. McNally's reliance on Dr. Tierney's testimony in support of a 40 basis-point adder for energy efficiency risk does not support Staff's proposal. PO at ___.

In addition, Staff's brief on exceptions recognizes that a 20 to 40 basis point reduction is unjustified in any event because the Proposed Order only recommends approval of a 50/50 fixed variable rate design. Under those circumstances, Staff reduces its proposed downward adjustment to 10 basis points (Staff BoE at 79), which is still unwarranted. For the reasons stated in the Proposed Order, no downward adjustment is appropriate, regardless of the result on SFV.

The Proposed Order's conclusion on this issue is also correct for reasons described in ComEd's Reply Brief.

> Staff has presented no empirical evidence supporting [a downward ROE] adjustment [based on SFV] or its size. Indeed, NRDC witness Ralph Cavanagh questioned whether any deduction to ROE was warranted in the case of decoupling. Tr. 1507:17 – 1509:9. Moreover, Staff's deduction vastly overstates the deductions the Commission made in other cases where it approved a 80-20 SFV. In *Ameren*, the

> Commission made a 10 basis-point deduction. *Ameren Illinois Utilities,* ICC Docket No. 07- 0585 (consol.) (Order, Sept. 24, 2008), at 215. In the recent *Nicor* decision, the Commission made only a 6.5 basis-point deduction. *Northern Illinois Gas Co.*, ICC Docket No. 08-0363 (Order at 71.)

ComEd Reply Br. at 106. Given that the Commission approved deductions of only 6.5 to 10 basis points adjustments when it approved 80/20 straight fixed variable rate designs, Staff's suggestion that a 10 basis point reduction is appropriate for a greatly reduced 50/50 SFV design is obviously flawed. Proposed Order properly rejects any reduction in ComEd's approved 10.50% return on equity associated with the modest movement toward a straight fixed variable rate design. Staff's exception to this determination should be rejected.

D. <u>Other Exceptions Relating to Return on Equity Adders</u>

ELPC and the AG each request that the Proposed Order be amended to reflect the arguments made by those parties in opposition to ComEd's proposed 40 basis point adder to the base allowed return on equity. Each proposes the identical language to be added to the Order, including to the "Commission Analysis and Conclusion" section of the Order. ComEd does not object to the inclusion of a summary of the positions expressed by these parties, so long as the proffered language fairly reflects arguments and positions they have in fact advanced. ComEd does, however, object to their proposed revision of the Commission's Analysis and Conclusion section. In support of that objection, ComEd incorporates herein the arguments on this issue set forth in its Brief on Exceptions. In addition, the newly-suggested language is deficient for the following reasons.

The language concluding that the proposed adder "is contrary to Section 8-103 of the Act" is not justified by the text of Section 8-103. In fact, that Section supports ComEd's request

for an adder. Section 8-103 explicitly guarantees that the utility will be allowed "to *recover costs* for reasonably and prudently incurred expenses for energy efficiency and demand-response measures." 220 ILCS 5/8-103 (emphasis added). By distinguishing between "costs" and the direct "expenses" a utility incurs on efficiency and demand measures, the Section demonstrates that recovery is not limited to those direct expenses. Had the General Assembly intended that only such direct expenditures be recovered, it would have expressed that limitation in far narrower language: *e.g.,* "the utility will be allowed recovery for only the direct expenses incurred on energy efficiency and demand response measures." But the language is far broader, allowing recovery of all "costs" of those expenditures. One of the *costs* of ComEd's incurrence of expenses of demand response and energy efficiency is the *enhanced cost of capital* resulting from the increased risk of revenue loss threatened by these programs. That increased risk is the focus of Dr. Tierney's testimony and the basic justification for the adder. To the extent that Section 8-103 has any relevance to the issue, it supports, not contradicts, ComEd's position.

The remaining language AG and ELPC seek to add to the Order is either unsupported and/or inconsistent with established ratemaking principles. The conclusory language that the adder "is bad public policy" is not only unsupported, but contradicted, by the record. ComEd has explained in detail how Dr. Tierney's testimony established that the adder will serve a large number of important public policy goals, including aligning the interests of customers and shareholders with respect to efficiency measures, removing disincentives for less than aggressive utility participation in such measures, and reassuring the investment community that Illinois regulation will not require shareholders to bear the costs of energy efficiency. Dr. Tierney also refuted in detail the Staff and Intervenor testimony suggesting that the adder would not accomplish, or be necessary to accomplish, those goals. Of course the ultimate public policy

objective that the adder will further is the one that counts the most under the law - - compensating the utility for its costs of providing delivery service. For the same reasons, the proposed added language that the adder "does not provide any incentive for the Company to further promote energy efficiency" (AG BoE at 84) is unsupported by the evidence, and should not be included in the Order.

Finally, the added language that the adder "provides no customer benefit" is inappropriate as yet another attempt to make cost recovery dependent upon the identification of specific customer benefits for each item of utility cost. As ComEd has explained elsewhere in this case, and as the Proposed Order itself recognizes, the "customer benefit test" bears no relationship to the utility's prudently incurred costs, and has been restricted to "the context of incentive compensation payments and should not be expanded into other areas." PO at 51.

IV. COST OF SERVICE, ALLOCATION, AND RATE DESIGN ISSUES

A. Overview and Common Issues

As ComEd has previously emphasized in this proceeding, cost of service, cost allocation and rate design issues are revenue neutral for ComEd. ComEd Reply Br. at 110; Alongi, Tr. 2020-21. Once the Commission determines ComEd's revenue requirement, the objective then becomes how to allocate recovery of the revenue requirement among the customer classes. ComEd would gain nothing if it were to improperly allocate costs and design rates to unduly discriminate against a particular class of customers. Thus, to the extent that intervenor try to paint ComEd as attempting to advance its own interests at the expense of customers when addressing cost of service, allocation, and rate design issues (s*ee, e.g.*, REACT BoE at 2), those claims are baseless.

The Intervenors' Briefs on Exceptions reveal the ongoing battle between customer classes over cost allocation. For example, REACT continues to argue that ComEd improperly seeks "from its largest customers unjustified, massive million dollar-plus annual rate increases for individual customers." REACT BoE at 2. On the other hand, the Commercial Group takes exception to the Proposed Order's imposition of an unequal subsidy burden on the Small, Medium, Large and Very Large Load customer classes—which are comprised of Illinois commercial retailers, schools, homeless shelters, churches and smaller industrial customers—"even though no witness could justify why other classes, particularly those paying much lower rates, should not have to bear an equal share of the subsidy burden." CG BoE at 1. Kroger similarly supports moving away from the subsidy paid to the Extra Large Load and High Voltage customer classes. Kroger BoE at 1.

B. Cost of Service and Allocation Issues

3. Primary/Secondary Split

a. Functional Identification of Costs

The Proposed Order correctly rejects IIEC's arguments in support of its proposal to further segment certain costs of the primary distribution system by reallocating single-phase primary circuit costs and line transformer costs. PO at 162-63. Among other reasons, the Proposed Order correctly concludes that "at this time, these costs do not appear to be as neatly (and fairly) segregable as the IIEC asserts." *Id*. at 163.

IIEC's Exception 5 is broken into arguments relating to line transformers and single-phase primary wires. As to the former issue, IIEC repeats its argument that ComEd's primary/secondary analysis improperly defines facilities, "including line transformers, as primary or secondary based on their energized voltage level, rather than on the basis of a

functional definition as directed by the Commission." IIEC BoE at 34. And as to the latter issue, IIEC repeats its recommendation that ComEd should be ordered to "identify single-phase primary circuits/lines used to serve secondary customers…, assign those facilities to the secondary system, and allocate their costs accordingly." IIEC BoE at 37.

In essence, IIEC contends that certain facilities energized at primary voltages serve only secondary customers and, therefore, the cost of such facilities should be allocated only to secondary customers. ComEd demonstrated that IIEC's claim is unjustified and inequitable to other customers who do not use other parts of ComEd's distribution system. ComEd Init. Br. at 110-11. ComEd further demonstrated that IIEC's proposal is far more complex than IIEC claims if all customers are to be treated equitably. *Id.* Finally, ComEd demonstrated that the analysis proposed by IIEC, among others, would "be many times more complex and controversial than the segmentation of ComEd's distribution system into primary and secondary which ComEd has already performed," and that "[p]erforming such a complex multi-dimensional analysis is simply not necessary or reasonable" or appropriate where "performing the one-sided analysis … is inequitable to other customer classes." Alongi Rate Design Sur. Ex. 73.0 2nd Rev. 21:461-22:488.

Because the evidence supports the Proposed Order's rejection of IIEC's proposal to further segment ComEd's distribution system, IIEC's arguments do not warrant any amendment to the Proposed Order.

2. <u>Customer-Specific Cost Studies</u>

Because it has been advancing the cause for many years to no avail, REACT not surprisingly supports the Proposed Order's departure from past Commission orders in directing ComEd "to undertake a study of the distribution assets used to serve the Extra Large Load class."

REACT BoE at 3. REACT takes issue only with the Proposed Order's limitation of the study to the Extra Large Load customer class, contending that the study should include "all over-10MW customers – including the over-10 MW High Voltage class customers." *Id*. at 6. In evaluating REACT's claim for special treatment for an even larger group of customers, the Commission should consider facts identified during the evidentiary hearings, facts which at minimum go to the weight to be given REACT's arguments. For example, of the 12 purported entities that comprise the *ad hoc* organization called REACT, only four have customer premises in the Extra Large Load Customer Class.[27] Alongi, Tr. 2125-2126. To place this number in perspective, the Extra Large Load Customer Class is comprised of 57 customer premises. Terhune, Tr. 1627. Thus, the overwhelming majority of this customer class has not presented any evidence supporting REACT's position.

As set forth in ComEd's Brief on Exceptions, the Proposed Order's requirements for ComEd to conduct such studies are inappropriate. First, the conclusion that studies should be conducted to determine the facilities used to serve individual members of selected classes is unprecedented and nothing in Part 285.5110, or in any other Commission Rule or Order, establishes a requirement that a utility conduct a special investigation of the assets used to serve individual members of any particular customer class for the purposes of preparing a cost study.

Second, nothing has changed in the time since the Commission previously rejected customer-specific studies on numerous occasions, so they should be rejected again here. REACT accepts "credit" from the Proposed Order for "the persuasive evidence presented by REACT expert witness Harry Terhune." REACT BoE at 6. Yet, REACT conveniently glosses

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

over the fact that Mr. Terhune's testimony on which the Proposed Order explicitly relies is not in evidence. In particular, the Proposed Order relies upon Mr. Terhune's analysis of "documents regarding 45 of the total of 57 Extra Large Load customers." PO at 178. As ComEd pointed out in its Brief on Exceptions, this "analysis" provided by Mr. Terhune is not record evidence in this proceeding. The ALJs properly refused to allow any additional "direct" testimony to be given by Mr. Terhune at the evidentiary hearing in this proceeding. Tr. 1672-88. Accordingly, the "analysis" that the Proposed Order relies upon is found only within an offer of proof submitted by REACT, which states, in part, that "Mr. Terhune would have testified" as to certain matters based upon his analysis of documents provided by ComEd. REACT's Verified Offer of Proof in Response to the Administrative Law Judges' January 14, 2011 On-the-Record Ruling, at 3 (emphasis added). The Commission may not issue findings based upon evidence that is not in the record and as to which no other party was allowed to conduct discovery or cross examination. *See, e.g., Metropolitan Sanitary Dist. v. Pollution Control Bd.*, 62 Ill. 2d 38, 43 (1975). Had this "evidence" been proffered in a timely manner for admission into the record, ComEd would have responded with evidence showing that the actual facts are otherwise and that the limited information that Mr. Terhune considered was insufficient to support the conclusions he purported to reach.

Third, as the Commission has previously concluded, such studies are inappropriate:

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

Commonwealth Edison Co., Docket No. 07-0566 (Order, Sept. 9, 2008) at 210; *see also Commonwealth Edison Co.*, Docket No. 08-0532, Denial of REACT's Petition for Interlocutory

Review (Aug. 25, 2009 Commission Minutes, Tr. 15:10-16:19) ("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.").

Fourth, the Proposed Order's requirement of customer-specific cost studies is at odds with how costs are compiled and allocated in an ECOSS. Like all such studies, ComEd's ECOSS compiles ComEd's costs of providing distribution service and allocates such costs to the appropriate customer classes. Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 29:646-50; ComEd Init. Br. at 118. No ECOSS, including ComEd's, is conducted by compiling the costs to serve individual customers and then aggregating the costs to serve individual customers into class costs. *Id*.

Although the Proposed Order breaks with precedent in requiring the customer-specific cost study requested by REACT—and such study will not aid the ECOSS process—ComEd has committed to conducting the additional analysis if so required by the Commission. At a minimum, however, the study should be as limited as possible as indicated by the Proposed Order's limitation of the study to the Extra Large Load customer class.

3. Allocation of Illinois Electric Distribution Taxes

a. Response to IIEC Exception 3

The costs associated with the Illinois Electricity Distribution Tax in the ECOSS have been properly allocated based on kilowatt- hours ("kWh") delivered and this allocation should be approved by the Commission. The basis for this allocation is straightforward – this tax is imposed upon ComEd on the basis of kWh delivered. ComEd Init. Br. at 121; ComEd Rep. Br.

at 124-125; ComEd Exs. 75.1, 75.2, and 75.3; Alongi Dir., ComEd Ex. 16.0 3rd Rev., 18:392-394. The nature of the cost imposed and the nature of its allocation are symmetrical and reasonable. Staff agrees with the IEDT allocation. Staff Init. Br. at 141-44.

IIEC suggests that these tax costs should be allocated in a different manner. IIEC BOE at 19-31. IIEC's proposal is inappropriate because it does not reflect the basis on which ComEd *incurs* the costs. In particular, while mentioning another section of 35 ILCS 620, IIEC conveniently ignores the fact that the Illinois General Assembly, in 35 ILCS 620/1a, PA. 90-561 (eff. 1-1-98), decided to change the way the distribution tax is determined in replacing a tax based on invested capital with a tax determined by kilowatt-hours delivered. In essence, IIEC is asking that the Commission order ComEd to disregard current law. Therefore, IIEC's proposed exceptions should be rejected.

b. <u>Response to IIEC Exception 4 and REACT</u>

ComEd understands the Proposed Order to adopt its modification of rate design to provide a separate volumetric charge for the recovery of the IEDT and uncollectible costs associated with the application of the tax. PO at 270; *see* Alongi Dir., ComEd Ex. 16.0 3rd Rev., 18:392-94.

This conclusion is consistent with a recent Commission decision regarding the allocation methodology for recovery of the IEDT. *See Central Ill. Light Co., et al.*, Docket Nos. 09-0306 (cons.), Order dated Apr. 29, 2010 ("*Ameren Order*") at 243; *see also* Heintz Reb., ComEd Ex. 51.0, 6:129-32; Alongi Rate Design Reb., ComEd Ex. 49.0 Rev., 18:406-10. IIEC (BOE at 19-33) and REACT (BOE at 20) renew their support of an alternative calculation. These arguments should be rejected. Unlike Residential, watt-hour, and lighting customers where the IEDT is already recovered through per kWh DFCs, the tax is currently recovered through *per kW* DFCs

for demand-based nonresidential delivery classes. As a result, low load factor customers are currently subsidizing the high load factor customers with respect to recovery of this tax from these customers. Hemphill Rate Design Reb., ComEd Ex. 46.0, 6:133-7:140. By adopting ComEd's proposal, the Proposed Order eliminates this intraclass subsidy.

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 243-44. 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. Based on its analysis, the Commission found that:

> … the interpretation of the PURA by AIU and Staff more reasonable than that of IIEC. Adoption of the AIU and Staff position is also consistent with Docket No. 99-0117. … In the absence of any clear legislative intent to the contrary, AIU should recover PURA tax costs in base rates through the kWh-based Distribution Delivery Charge…

Ameren Order at 244. The Commission determined that IEDT should be collected based upon kWh DFC and nothing in the record refutes the Commission's analysis of the applicable statutes. Accordingly, IIEC and REACT proposed exceptions should be rejected in their entirety.

4. <u>Other Issues</u>

a. <u>Utilization of Railroad Facilities</u>

This issue arose as a tangent to ComEd's proposed Railroad Delivery Class cost allocation adjustment, which resulted from a Commission-ordered study of the extent to which ComEd uses or needs Railroad Delivery Class facilities to serve other customers. ComEd Reply Br. at 130-31. The study showed that flows through railroad owned equipment to other ComEd

customers do occur, but it did not show that the flows were necessary to serving customers under normal conditions or that restoration from power outages requires the railroad facilities. Hemphill Dir., ComEd Ex. 14.0 Rev., 24:486-25:496; ComEd Ex. 16.4.

In response to the study presented in ComEd Ex. 16.4, Staff recommended that the Commission order ComEd "to provide a plan to eliminate its current practice of supplying customers by using railroad customer facilities." Rockrohr Dir., Staff Ex. 6.0, 31:691-93. The evidence demonstrated that Staff's proposal was unnecessary as there are no operational, reliability or safety issues associated with the current configuration at railroad tracking substations. *See, e.g.*, Born Sur., ComEd Ex. 67.0 Rev., 3:65-66; Born, Tr. 1721:4-15; Staff BoE at 93. Importantly, all affected parties (*i.e.*, ComEd, CTA and Metra), while not opposing Staff's suggestion as a long term goal, rejected the elements of Staff's proposal setting a deadline for such modifications or that they be mandatory. ComEd Reply Br. at 131; CTA Init. Br. at 22-24; Metra Init. Br. at 18-21. Thus, the Proposed Order correctly concludes that the Commission should not require ComEd, CTA and Metra to pursue any particular avenue in addressing this issue or impose a deadline upon them as they further investigate the issue. PO at 259.

Staff takes exception to the Proposed Order's directive to commence workshops on this issue. Staff BoE at 93. In lieu of the workshops, Staff recommends that ComEd be required to file a report that identifies, among other things, "available solutions to eliminate its dependence on, and use of, each specific railroad traction power substation facility, including the estimated cost to implement each solution." Staff BoE at 93. Staff further recommends that this report be filed in this docket within one year of the date of the final order in this proceeding and that ComEd should file an updated copy of the report "at the time it files its next rate case." *Id.*

ComEd maintains its position that Staff's proposal should be rejected. ComEd Reply Br. at 131. However, to the extent the Commission determines that further analysis of this issue is necessary, ComEd generally agrees with Staff's recommendation to prepare a report in lieu of workshops to be issued within one year of the date of the final order. Further, ComEd agrees with Staff's proposal that the report contain a description of available solutions to eliminate ComEd's dependence on railroad-owned traction power substation facilities to supply other customers, including the estimated cost to ComEd to implement each solution. However, ComEd disagrees that any report it prepares can or should contain information about the costs that the railroad customers may incur with respect to any changes to their facilities as such information is confidential to the railroads. ComEd also disagrees that it should be required to file the report in this docket or file an updated copy of the report at the time it files its next rate case. Such steps are unnecessary in light of ComEd's commitment to prepare the report as directed in the final order. Moreover, as addressed above, linking completion of the report and ComEd's next rate case filing unlawfully and unwisely constrains ComEd's right to seek timely rate relief in the future. Finally, ComEd disagrees with Staff's proposal that ComEd provide annual reports quantifying "the amount of 'other customer load' that ComEd supplies through each railroad traction power substation during each billing cycle." Staff BoE at 94. To the extent that the Commission concludes additional reporting is needed beyond the initial report outlined above, ComEd suggests that it include a section in its annual reliability report to the Commission to provide the Proposed Order's contemplated "updates as to ComEd's use of the[se railroad] facilities." PO at 259.

C. <u>Customer Care Cost Allocation</u>

The Proposed Order correctly agrees with Staff and ComEd that the sound application of the principle of cost causation requires the Commission to adopt the Switching Study and reject

the Allocation Study. As reflected in the PO, both Staff and ComEd have clearly and concisely briefed the issues with regard to customer care cost allocation, and the Proposed Order comes to appropriate and rational conclusions. *See* PO at 190-99. ComEd's exceptions on this issue are minor and serve only to clarify the PO's conclusions and statements in this regard. *See* ComEd BoE at 88-89 and Exception Nos. 44-45.

In its BoE, REACT mainly rehashes its arguments in favor of the Allocation Study that the Proposed Order has already considered and rejected. *Compare* REACT BoE at 10-17 *with* PO at 190-99. ComEd, however, wishes to address three issues in REACT's BoE. The first is REACT's attempt to cast the Switching Study as inconsistent with the Commission's preference for an embedded cost approach to other cost allocation issues. *See* REACT BoE at 11-17. This is simply inaccurate. As stated in ComEd's pre-filed testimony:

> The Switching Study is not inconsistent or incompatible with ComEd's embedded cost of service study. The Switching Study is essentially just a means of determining and demonstrating what portion of the remaining, common costs are distribution related and which are not. It is merely an added step in the direct assignment of costs that are attributable to the delivery service function, like meter reading. As noted previously, direct assignments were the starting point for both the Switching Study and Allocation Study. Moreover, the direct assignment of costs is a common part of the development of an embedded cost of service study.

Garcia Supp. Dir., ComEd Ex. 24.0, 10:205-212. *See also* Garcia Reb., ComEd Ex. 50.0, 10:225-37. Staff concurs, and "consider[s] the Switching Study to be a subset of, and consistent with, ComEd's general ECOSS." Rukosuev Reb., Staff Ex. 28.0, 13:295-96. [28]

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[28] The results of the Switching Study are also consistent with prior Commission action on this issue dating back to ComEd's first delivery services rate case. *See e.g. Commonwealth Edison Co.*, ICC Docket No. 01-0423, Interim Order (April 1, 2002) at 62-63; *Commonwealth Edison Co.*, ICC Docket No. 01-0423, Final Order (March 28, 2003) at 71-72 (allocating customer services costs to delivery service rates); *Commonwealth Edison Co.*, ICC Docket No. 05-0597, Final Order (July 26, 2006) at 257 (July 26, 2006) (rejecting arguments "to allocate no less than one-fourth of call center costs to supply."); *Commonwealth Edison Co.*, ICC Dockets Nos. 07-0528/07-0531 cons., Final Order (Dec. 19, 2007) at 104, ComEd Reply Comments at 10, Staff Reply Comments at 11 (recognizing (cont'd)

Second, REACT has muddled the issues in its BoE by stating that "the entire Switching Study was ComEd's test to see whether Direct O&M costs somehow would be avoided under future switching scenarios; the purpose was not to allocate existing costs," and that "the entire Switching Study began by asking the wrong question. … As a result, the Switching Study simply cannot be used to properly allocate the total Customer Care Costs." REACT BoE at 12, 13. These propositions are not true, as both Staff and the Proposed Order correctly concluded.

As explained in ComEd and Staff's testimony and briefs, and as reflected in the PO, the Switching Study clearly allocated existing costs. ComEd Init. Br. at 123-24; ComEd Reply Br. at 127, n.24; Staff Reply Br. at 68-69; Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 8:165-71; Donovan Reb., ComEd Ex. 48.0, 5:91-110; Donovan Sur., ComEd Ex. 72.0, 2:25-33; Rukosuev Reb., Staff Ex. 28.0, 13:296-300; PO at 196. In addition, both the Switching Study and the Allocation Study as initially performed by ComEd examined Direct O&M customer care costs as opposed to total customer care costs, but both studies could also be used to allocate total customer care costs. Donovan Supp. Dir., ComEd Ex. 19.0 Rev., 4:73-5:110.

The question of the scope of the costs to be analyzed is unrelated to the Commission's basic decisions with regard to customer services. The Proposed Order correctly selects the Switching Study as supported by Staff and ComEd even though it concludes that the customer care costs at issue are properly measured looking to "total costs" and not just direct O&M costs. *See* ComEd BoE at 88-89. Moreover, as ComEd has explained several times, the Switching Study clearly concludes that no change in costs occurs at 1% switching, which is the current situation. *See* ComEd Ex. 19.1. This conclusion does not change whether the relevant pool of

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incentive for ComEd to classify common customer care costs as supply costs and approving revised tariffs limiting such classification).

costs is Direct O&M Costs as analyzed by ComEd or "total costs" as defined by Mr. Merola. As simply stated in ComEd's BoE, 0% of $176,231,365 (Direct O&M Costs) is the same as 0% of the sum of $176,231,365 plus $141.9 million (Direct O&M Costs plus total customer care costs). *See* ComEd BoE at 89; PO at 197.

Third, REACT attempts to make its position appear more reasonable by stating that "ComEd and REACT are less than three percentage points apart in their respective proposed embedded cost studies." REACT BoE at 17. The fact remains, however, that neither ComEd nor Staff – nor the Proposed Order – believe that ComEd's Allocation Study reflects actual cost causation. The Allocation Study presented by ComEd and as modified by Mr. Merola is an inappropriate method of cost allocation and is correctly rejected by the PO. *See generally* PO at 190-99.

E. Rate Design Issues

1. SFV / Decoupling

Staff and numerous Intervenors continue to oppose ComEd's Straight Fixed Variable ("SFV") proposal, taking the position that the Proposed Order errs in adopting a modified version of ComEd's proposal. These parties offer several arguments in support of this position, including that SFV discourages energy efficiency, that gas utility cases should not be used as a guide in electric rate design, and that SFV places an excessive burden on low use customers.

The Commission should reject these arguments and modify the Proposed Order to reflect adoption of ComEd's SFV proposal as originally proposed, which gradually moves to an 80% SFV because this rate design more closely reflects the correct division between fixed and variable costs. *See, e.g.*, ComEd BoE at 90-93; ComEd Init. Br. at 137-39; ComEd Reply Br. at 133-41. Moreover, the Proposed Order's analysis justifies a more rapid implementation of an SFV rate structure for all delivery costs than the limitation to a 50% SFV. Indeed, the

Commission implemented an 80% SFV structure without delay in the Ameren and Nicor Gas cases, and no party has presented evidence showing that the Commission should waver from the policy it embarked upon in these prior cases. ComEd's proposal to implement a 60% SFV now, a 70% SFV next year, and an 80% SFV in two years allows for gradualism and addresses concerns of potential rate shock. Finally, the 50% SFV approved in the Proposed Order represents a step backward from the SFV policy endorsed by the Commission in previous orders, and movement away from more accurate pricing, for the Watt-Hour Delivery Class. ComEd BoE at 92.

a. The Proposed Order Correctly Concludes That The SFV Proposal Does Not Reduce Consumers' Incentive To Conserve

Staff and Intervenors argue that the Proposed Order errs in finding that SFV does not reduce the incentive to conserve. Staff BoE at 82-83; AARP BoE at 6-8; City BoE at 11-13; CUB BoE at 49-50; ELPC BoE 9-18; NRDC BoE at 1-4. Staff goes so far as to argue that this lone error supports full reversal of the Proposed Order's adoption of SFV. Staff BoE at 82-83. This argument ignores the fact that, as a percentage of a typical customer's total bill for all electric services, the portion that will be subject to SFV is significantly less than the amount recovered through volumetric charges. Most costs on a customer's bill will still be recovered volumetrically because electric supply service is still priced volumetrically. Hemphill Rate Design Reb., ComEd Ex. 46.0, 12:282-13:300. Accordingly, the impact on a given customer from a shift to SFV will be small, if not negligible. The Proposed Order's analysis correctly recognizes this fact: "The actual commodity costs associated with the electric power and energy, which is the majority of the total electric bill … vary directly with usage." PO at 217.

Staff and Intervenors' argument about the purported disincentive to conserve accompanying SFV actually ignores the disincentive that volumetric distribution rates have on a

utility's promotion of energy efficiency. As Dr. Hemphill testified, "[a] non-SFV design makes a utility's ability to recover its fixed costs – costs that the utility incurs regardless of use and demand – dependent upon maintaining customer demand and/or use at test year levels. This is because with rates that misallocate fixed costs, like ComEd now has, efficiency and demand management programs generally reduce utility revenues far more than they reduce utility costs." Hemphill Dir., ComEd Ex. 14.0 Rev., 18:363-67. With volumetric pricing, Staff witness Boggs even acknowledged that "a larger customer charge and lower volumetric charge reduces the utilities [*sic*] profit from increased sales, reducing the utility disincentive to promote energy efficiency." Boggs Reb., Staff Ex. 13.0, 19:369-71. Thus, by reducing the volumetric delivery charge, a utility would be more likely to promote energy efficiency and reduced electricity usage because revenues are less sensitive to increases or decreases in electricity usage. Hemphill Rate Design Reb., ComEd Ex. 46.0, 12:273-275.

Finally, the Commission has spoken with respect to the impact of SFV on energy efficiency when it previously adopted an SFV rate design in other rate case dockets. In particular, the Commission stated that

> The Commission is not convinced that an SFV rate design reduces the incentive to conserve natural gas. These costs are in fact fixed costs, cannot be conserved, and result in an under-recovery of fixed costs for the utility during periods of milder than average weather and an over-recovery of fixed costs for the utility during periods of colder than average weather. 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 Rate 1 design that more accurately reflects a consumer's actual costs does not impede conservation.

Northern Illinois Gas Co. d/b/a Nicor Gas Co., Docket No. 08-0363, Order (Mar. 25, 2009), at 92. The Commission made similar statements when it directed the Ameren Illinois Companies to increase their respective monthly customer charges for certain classes "to recover more of its fixed delivery services costs." *Central Illinois Light Co., et al.*, ICC Docket Nos. 07-0585

(consol.) (Order, Sept. 24, 2008) at 237, *aff'd sub nom. People v. Ill. Commerce Comm'n*, Case No. 4-08-0895 (Ill. App. Ct. 4th Dist., Nov. 13, 2009) (affirming the Commission's decision adopting 80% fixed charge decoupling alternative).

Accordingly, the Commission should adopt the Proposed Order's conclusion that an SFV rate design does not reduce the incentive to conserve electricity, as well as the Proposed Order's related analysis.

b. **The Proposed Order Properly Relies Upon Prior Commission Decisions Adopting SFV**

The AG and CUB argue that the Proposed Order should not rely upon gas utility precedent as a guide to electric rate design. AG BoE at 96-97; CUB BoE at 51. On the contrary, the Proposed Order properly relied upon gas utility precedent because, regardless of the different physical properties of the delivered product, the cost characteristics of electricity are very similar to the cost of delivering gas. For example, ComEd witness Hemphill testified 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. 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 consistent pricing policies for both industries because they have similar underlying cost structures. Hemphill Rate Design Sur., ComEd Ex. 71.0, 3:52-63. Moreover, no party has offered a compelling reason why the outcome in this case should differ from the previous Commission decisions in the Ameren and Nicor Gas dockets.

c. SFV Does Not Unfairly Burden Low Use Customers Or Improperly Increase Costs

Several Intervenors continue to argue that the switch to SFV will have a disparate effect on low-use customers or improperly increase customer charges. AARP BoE at 3-6; AG BoE at 89-94; City BoE at 3-7; CUB BoE at 51-52. ComEd submits that the evidence shows otherwise.

It must be noted that the issue here is not about consumption of electricity by ComEd's customers, but whether changes in that consumption impact the costs of distribution. For that reason, consideration of a customer's usage in a vacuum is an incomplete analysis. 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). Hemphill Rate Design Reb., ComEd Ex. 46.0, 14:331-33. The Commission acknowledged this in the 2007 Rate Case Order, when it stated that "[t]he record shows that distribution facilities must be planned and built to meet customers' maximum loads, regardless of when those may occur." 2007 Rate Case Order at 217. In his rebuttal testimony, Dr. Hemphill provided two instructional examples. First, he considered two customers using electricity in the summer. One customer, using the electricity every day for air conditioning, might be using 1,000 kWh. The other customer, trying to be more energy efficient, might refrain from using air conditioning for the first three days of a four day heat wave and might be using only 500 kWh in the month. While their kilowatt-hour usage is different, Dr. Hemphill noted that the delivery service facilities ComEd must have in place for both customers could very well be identical, and therefore, the customers should be responsible for equal shares of ComEd's fixed delivery costs. Hemphill Rate Design Reb., ComEd Ex. 46.0, 14:337-15:344.

Dr. Hemphill then considered two customers that use identical amounts of electricity in the month, for example, 1,000 kWh. While using the same number of kilowatt-hours, they may

not be responsible for equal shares of ComEd's fixed costs because one might spread her usage out over the course of the month, while the other uses her electricity predominantly during peak periods. While their maximum usage at any given time is different, ComEd still has to have sufficient capability to deliver electricity to both at peak periods. *Id.*, 15:345-350.

Dr. Hemphill concluded that these examples show that it is quite possible for two customers to use different amounts of kilowatt-hours but be responsible for equal shares of fixed costs. Thus, regardless of load shape, ComEd must consider the maximum rate at which the electricity is used, not just the quantity of electricity used. Further, it is not appropriate for ComEd to assign cost responsibility or recover its costs for its delivery service facilities based simply on electricity usage. *Id.*, 15:351-356. 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. Hemphill Rate Design Sur., ComEd Ex. 71.0, 6:116-120.

The AG argues in favor of retaining the existing level of variable charges, as supported by ComEd's own ECOSS data reproduced in AG Ex. 6.01, which purportedly demonstrates that "there are substantial demand-related costs incurred to serve residential customers". AG BoE at 89-90. This argument does not advance the AG's opposition to SFV rate design. First and foremost, the AG is misreading the evidence and confusing demand with energy usage. As the AG concedes, AG Ex 6.01 is a reproduction of ECOSS data that ComEd submitted. AG BoE at 90. However, AG Ex. 6.01 simply shows overall costs and does contain any information about which costs are fixed and which costs are variable. While it shows that usage varies among customer classes, it does not show which costs actually vary. Thus, it is essentially irrelevant to the SFV issue at hand. Moreover, ComEd did provide evidence showing the amount of

ComEd's fixed and variable costs and demonstrated that ComEd's fixed costs represent over 97% of ComEd's distribution costs. Hemphill Rate Design Reb., ComEd Ex. 46.0, 12:285-87; ComEd Ex. 46.1; ComEd Ex. 46.3. Importantly, no party refutes this evidence showing that over 97% of ComEd's distribution costs are fixed.

d. The Proposed Order Correctly Concludes That SFV Is Not an Attempt to Recover Short Term Marginal Costs

The City and NRDC continue to argue that ComEd's SFV proposal is actually an attempt to recover short term marginal costs. City BoE at 11; NRDC BoE at 4-5. The Proposed Order's findings correctly reflect reality—*i.e.*, ComEd's rates are based on average embedded costs. PO at 217-18. This was demonstrated in ComEd witness Hemphill's testimony that ComEd is attempting to use its non-volumetric charges to recover 80% of its embedded total costs and, under ComEd's proposal, its volumetric rates will continue to recover a portion of its embedded fixed costs and all of its embedded variable costs. Hemphill Rate Design Reb., ComEd Ex. 46.0, 21:470-76. Further, as Dr. Hemphill testified, "[t]he notion that average variable embedded costs are equivalent to short-run marginal costs, or that average fixed embedded costs are equivalent to long run marginal costs is spurious and contrary to any economics text book." Hemphill Rate Design Sur., ComEd Ex. 71.0, 8:163-165.

ComEd further notes that NRDC appears to completely misunderstand ComEd's proposal. NRDC BoE at 4-5. Aside from its erroneous characterization of SFV as a Rider, which ComEd's proposal is not, NRDC fails to recognize that commodity charges are not zero and are priced volumetrically, which was demonstrated in ComEd's evidence. *See, e.g.*, Hemphill Rate Design Reb., ComEd Ex. 46.0, 12:282-13:300.

2. Class Definitions

a. Residential Rate Classes

ComEd concurs with the arguments set forth in Staff's Brief on Exceptions at pages 85-86. As noted by both Staff (*id.*) and ComEd (BoE at pp. 93-95), there is sufficient information in the record to support the consolidation of the residential delivery class from four classes to two classes without subjecting the residential class to rate shock. As noted by Staff, under the exemplar model submitted by ComEd and adopted in the Proposed Order, the differential in annual bill increases for the space heating customers and non-space heating customers would be relatively small. Staff BoE at 85. Further, ComEd demonstrated that it makes sense to consolidate the residential rate classes at the same time as the move to an SFV rate design (Alongi Dir., ComEd Ex. 16.0 3rd Rev., 17:368-72), and the Proposed Order correctly adopts SFV (albeit with an improper limitation to 50%). The impact of the Proposed Order's acceptance of a modified SFV rate design while rejecting the residential rate class consolidation proposed by ComEd are shown in the rate impacts provided in ComEd's response to the ALJs' post-record data request. For these reasons, and those discussed in ComEd's Brief on Exceptions, the Proposed Order should be modified as proposed by ComEd in its Exceptions at pp. 247-249.

b. New Primary Voltage Delivery Class vs. Primary Subclass Charges

Appendix A of IIEC's BOE contains language proposing modifications to the Proposed Order. IIEC BoE, Appendix A at 20-21. While the language proposed by IIEC is not conceptually inconsistent with the alternative language proposed by ComEd, ComEd recommends the adoption of its language as it more fully reflects the record evidence and properly puts all of the arguments raised by the parties into context in the Analysis and

Conclusions section of the Proposed Order. Therefore, ComEd recommends the adoption of the arguments and language contained in ComEd's Brief on Exceptions and Exceptions at pp. 95-97 and 254-255, respectively.

3. Movement towards ECOSS Rates

a. The Railroad Class and the Extra Large Load and High Voltage Customers

The Commercial Group and Staff both submitted Exceptions to the conclusions reached in the Proposed Order regarding the movement towards ECOSS affecting the Railroad Class and the Extra Large Load and High Voltage Customer Classes. *See* CG BoE at 5-11; Staff BoE at 86-89. Neither party has raised arguments sufficient to warrant revisions to the Proposed Order. ComEd (BoE at 95-97) and the IIEC (BoE at 53-55) agree that the Proposed Order has reached the proper conclusions. However, ComEd recommends the adoption of ComEd Exceptions 57 and 58 as corrected by Errata filed on April 14, 2011 to clarify and refine the language in the Commission's Analysis and Conclusions section of the Proposed Order.

4. Dusk to Dawn Street Lighting

The City of Chicago has submitted overly descriptive language in its Brief on Exceptions for the Commission's Analysis and Conclusions section of the Proposed Order. While the language submitted by the City is contained in the record, the proper placement of the proposed language would be in the City's Position section and not the Commission's Analysis and Conclusions. ComEd has offered clarifying analysis and language in its Brief on Exceptions at pp. 97-98 and 278-279, respectively, which more appropriately articulates a summary of the issue. ComEd recommends that its language be adopted.

5. **Distribution Loss Factors**

Staff had recommended in this proceeding that ComEd should update its distribution loss study after updating its transmission loss study, and "then file tariff revisions, as appropriate, to reflect its updated distribution loss factors" ("DLFs"). Rockrohr Reb., Staff Ex. 21.0, 19:396-402. Staff has now clarified that it did not intend that "ComEd's filed tariff revisions and distribution loss study would simply become effective automatically through a compliance filing several months after the final order in this docket." Staff BoE at 96. Accordingly, Staff recommends that the Proposed Order be modified to direct ComEd to "provide an updated distribution loss study to all parties of record in Docket No. 10-0467 by the end of 2011" and to decline to "adopt Staff's recommendation to require that ComEd also file tariff revisions, based on this updated information, prior to its next rate case." *Id*. ComEd agrees with Staff's recommended modifications to the Proposed Order as set forth in its Brief on Exceptions.

REACT continues to press its request that the Commission require ComEd to annually update and file its distribution loss factors, emphasizing in its Brief on Exceptions that the "best forum for resolving DLFs is through contested litigation." REACT BoE at 4, 20-21. Because of the sizeable efforts necessary in updating distribution losses and the resultant small changes in the value of the DLFs, the Commission should reject REACT's proposal for annual filings. ComEd Init. Br. at 151; ComEd Reply Br. at 150. Rejection of REACT's proposal is particularly appropriate as Staff and ComEd are in agreement on the best procedural mechanism for ComEd to update its DLFs.

6. General Terms and Conditions

a. Residential Service Station (Ownership of Non-Standard Residential Connections)

The Proposed Order correctly rejects Staff's proposal that ComEd take ownership of certain non-standard customer-owned facilities, and adopts ComEd's proposal to further study the issue before ordering any further action. PO at 279-80. Staff continues to recommend 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 BoE at 96-98.

This issue arose out of ComEd's straightforward proposal to add one word, "pole", to an existing section of General Terms and Conditions describing responsibilities for installation of a Residential Service Station (ILL. C. C. No. 10, 1st Revised Sheet No. 165) to further clarify ComEd's practice that has existed since at least 1955 whereby the residential customer "must furnish, install, own and maintain the remainder of the overhead primary service connection including the first support on private property" that already exists in ComEd's General Terms and Conditions (ILL. C. C. No. 10, Original Sheet No.160). Alongi Sur., ComEd Ex. 68.0, 2:42-3:53. In response to Staff's position, ComEd articulated a number of legal and operational flaws in Staffs proposal: (1) it is unclear how or when ComEd will "assume" ownership of property that is customer-owned; (2) the proposal does not grant ComEd the easement that would be needed to access a customer's property to perform necessary maintenance nor does it solve clearance issues relating to trees and other vegetation; (3) offering customers the ability to have ComEd assume ownership on a prospective basis would create a permanent dual system of those customers who own their own overhead primary facilities and those customers who have let ComEd assume ownership; (4) ComEd already offers residential customers who are willing to

pay the associated costs the option to replace customer-owned overhead primary facilities and the ComEd-owned overhead Residential Service Station transformer with ComEd-owned underground direct-buried primary facilities and a pad-mounted Residential Service Station transformer; and (5) there may be a labor jurisdiction issue regarding International Brotherhood of Electrical Workers labor union work. Alongi Reb., ComEd Ex. 41.0, 4:88-5:107; McMahan Reb., ComEd Ex. 33.0, 20:433-40.

ComEd also provided evidence of why Staff's proposal was unnecessary for any operational, safety or reliability reasons, and would be expensive and difficult (if even possible) to accomplish. McMahan Reb., ComEd Ex. 33.0, 18:404-21:458; Alongi Sur., ComEd Ex. 68.0, 4:74-5:88. Indeed, ComEd provided evidence that in order to even identify the residential customer-owned overhead primary lines at issue, "ComEd would have to query its systems to extract a list of transformers that serve only one residential customer, perform a preliminary review of ComEd maps to determine if those transformers identified in the query appear to be located on the residential customer's property or on public property, and conduct field reviews based on initial map review findings to confirm if the primary lines and transformers are located on the residential customer's property." Alongi Sur., ComEd Ex. 68.0, 4:77-83. There may be as many as 57,700 such connections requiring further analysis from ComEd. *Id*. at 4:83-5:88. ComEd agrees that safety issues are unquestionably important, emphasizes that it is committed to operating at an industry-leading level of safety, and points to its decades of experience on which to base a sound conclusion about the safety of its practices regarding customer-owned facilities. McMahan Sur., ComEd Ex. 60.0, 16:353-54, 16:357-63. Based on the evidence provided by ComEd, the Proposed Order correctly concludes that Staff's proposal "entails complicated legal issues" and, therefore, should be rejected. PO at 279. However, the Proposed Order found that

Staff had raised sufficient safety issues that should be further studied as proposed by ComEd. *Id*. at 279-80. Staff maintains that the results of a study, "regardless of what they are," will not change its position that ComEd should take ownership of these customer-owned facilities. Staff BoE at 97. Notwithstanding that it has already rejected the results of a future study, Staff recommends that certain information be included in the study to be prepared by ComEd. *Id*. at 97-99.

The Commission should reject Staff's proposed data points as such specifics are unnecessary.[29] ComEd has already provided evidence of the burden and expense involved in simply identifying the customer-owned overhead primary facilities, which is Staff's proposed point (a). Alongi Sur., ComEd Ex. 68.0, 4:74-5:88. ComEd has also already provided evidence that there are likely no ComEd-owned residential primary service connections, which is Staff's proposed point (b) and part of point (f). Alongi Reb., ComEd Ex. 41.0, 6:119-25. Further, there is no reason to include any non-residential primary service connections in the study as Staff has not taken issue with those facilities, which would takes care of Staff's proposed points (c), (d), and the remaining part of (f). As to the remaining point (e) proposed by Staff, ComEd has provided evidence showing that physical inspections of even a 10% sample of the customer-owned overhead primary facilities could be as many as 5,770 connections, which would be an onerous, excessive and expensive undertaking as it would involve field review primarily in ComEd's most rural areas, such as ComEd's Dekalb, Dixon and Freeport districts where overhead primary installations are most prevalent. Alongi Sur., ComEd Ex. 68.0, 4:83-5:88; Alongi Reb., ComEd Ex. 41.0, 6:119-25. Ordering physical inspection of any specific

[29] To the extent that the Commission adopts any of Staff's data points, they must be clarified to reflect that the only customer-owned facilities to be studied are customer-owned *overhead* primary facilities (not underground) and that any application of the National Electric Safety Code is as currently adopted in Illinois.

percentage or sampling size is simply not tenable based upon the information known to date, particularly where the Proposed Order contemplates that ComEd will provide a report on this issue by the end of 2011.

For all these reasons, the Commission should adopt the Proposed Order's conclusion that the contemplated study "examine the costs, benefits, and potential legal and practical obstacles to ComEd attempting to acquire ownership of these facilities." PO at 280. Finally, the final order should provide that any Operations & Maintenance costs ComEd incurs in conducting the contemplated study, whether with or without any of Staff's proposed data points, should be capitalized and deferred in a regulatory asset to be recovered in the Company's next rate case.

V. REVENUE ISSUES

A. Late Payment Charge Revenues

The Proposed Order (at 289-290) rejects Staff's and ComEd's testimony and arguments that only the $11.1 million of jurisdictional (delivery services) late payment charges revenues should be included in calculating ComEd's revenue requirement, and instead recommends that, in addition, the $13.986 million of non-jurisdictional late payment charges revenues also should be included. ComEd's BoE (at 99-102) supports an Exception to that ruling.[30]

The AG's BoE (at 103) states that the Proposed Order's Appendix A omits the late payment charges revenues adjustment. ComEd agrees. ComEd BoE at 100 n. 33.

B. New Business Revenue Credit

The Proposed Order, in an apparent attempt to be consistent with its limitation of ComEd's *pro forma* additions (with limited exceptions) to a cut-off of December 31, 2010,

[30] ComEd notes that on the subject of incentive compensation, Staff's BoE (at 28) argues that only delivery services-related costs should be recovered through delivery services rates. That principle supports ComEd's Exception here, which objects to the inclusion of non-delivery services late payment charges revenues.

adopts Staff's Reply Brief's calculation of the new business revenue credit as of December 31, 2010. The Proposed Order reduces ComEd's rebuttal figure of $3,457,000, which was based on approval of *pro forma* plant additions through June 30, 2011, by $1,389,000, to arrive at Staff's Reply Brief's figure of $2,068,000. Proposed Order, Appendix A, p. 2, col. (h), relying on Staff's Reply Brief, Appendix A, p. 20. The Proposed Order (at 292-293) correctly rejects the AG/CUB proposal to inflate the new business revenues credit by adding another $3,800,000.

The AG's BoE (at 1, 70-73, and 103-105) and CUB's BoE (at 55-57) take Exception, but their proposal to increase the credit by $3,800,000 is even more erroneous than the Proposed Order indicates. Staff's BoE (at 99-100 and Appendix A, p. 17) claims that, given the Proposed Order's rulings, the correct amount of the new business revenue credit is $3,273,000, rather than $2,068,000, but Staff's claim is erroneous.

1. <u>The Nature of the New Business Revenue Credit</u>

ComEd's new business revenue credit is intended to account for the estimated revenue from growth in customers during the *pro forma* adjustments period, because a portion of the *pro forma* adjustments is "new business". Houtsma Dir., ComEd Ex. 6.0 Rev., 46:920-927. In other words, ComEd offsets the cost recovery increase from inclusion of its *pro forma* additions in rate base with a credit on the revenue side for the revenues that it may receive from new customers in the *pro forma* period. Fruehe Reb., ComEd Ex 30.0, 21:454 - 22:462. To accurately determine the amount of the credit, ComEd must ascertain which customers are new, and thus ComEd must take into account customer migration between classes. Fruehe Sur., ComEd Ex. 56.0 3rd Rev., 21:429 - 22:456.

ComEd calculated the new business revenue credit consistent with the methodology approved by the Commission in Docket No. 07-0566, and, based on an update, increased the

figure to $3,457,000 in its rebuttal. Houtsma Dir., ComEd Ex. 6.0 Rev., 46:925-927; Fruehe Reb., ComEd Ex. 30.0, 24:524 – 25:530; ComEd Ex. 30.1, Sched. C-2.9 Rev.

If the *pro forma* adjustments period is shortened, however, from ComEd's proposed period end date of June 30, 2011, then the new business revenue credit must be reduced in a corresponding manner, because otherwise the calculation of its rates would include the revenues side of new business but exclude the cost side. Fruehe Reb., ComEd Ex. 30.0, 25:531-537.

2. <u>AG/CUB's Exceptions</u>

The AG's and CUB's BoEs seek to rehabilitate Mr. Effron's proposed adjustment, but, other than incorrectly and incompletely describing the evidence, they have nothing new of substance to say and the adjustment remains spurious.

AG/CUB witness Effron seeks to artificially inflate the new business revenue credit by only including growth in customer classes, without providing an offset to reflect a *decline* in customer classes due to customer migration. Fruehe Sur., ComEd Ex 56.0 3rd Rev., 21:429 - 22:456.; *see* Effron Reb., AG/CUB Ex. 8.0, 10:209-11:242. Mr. Effron's approach is flawed because under his approach, a migrating customer – who does not provide ComEd with any new revenue – is treated like a new customer who does provide ComEd with new revenue. Effron Reb., AG/CUB Ex. 8.0, 10:209-11:242. That is sort of like taking a class room with 20 students, asking 10 of them to move to empty seats closer to the front of the room, and then concluding there must be 30 students because 30 seats were occupied at one point or another.

The AG (BoE at 72) and CUB (BoE at 55-56) continue to claim that the offset is *de minimus*, no more than $49,000, but they are wrong. The example that they provided in support of this *de minimus* argument shows that they are wrong. In attempting to show that migration away from the Large Commercial and Industrial customer class ("LCI") is immaterial,

the AG adjusted the Small Commercial and Industrial customer class ("SCI") revenue credit down by $49,000. AG Init. Br. at 152-53. The problem with the AG's example is that it assumed that anticipated revenues from the LCI class will remain the same, which is simply not true due to the expected reduction in LCI customers due to both migration and business closings. ComEd Ex. 30.2, work paper WPC-2.9; *see also* ComEd Ex. 56.4 (providing updated customer statistics).

When the new business revenue credit was calculated in ComEd's rebuttal in manner that correctly reflected customer migration, the result was figure of $3,513,000, from which $46,000 of uncollectibles had to be removed, resulting in the figure of $3,457,000. ComEd Ex. 30.1, Sched. C-2.9 Rev.; ComEd Ex. 30.2, work paper WPC- 2.9.

The Proposed Order (at 293) is incorrect if it is intended to mean that the AG and ComEd agree that Mr. Effron's figure is *only* off by $49,000, as the AG and CUB seek to read it. The AG/CUB example is off by $49,000, as the AG and CUB apparently agree, but ComEd has shown that Mr. Effron's entire adjustment is erroneous. The next sentence of the Proposed Order (at 293) correctly indicates that Mr. Effron's calculations here generally are incorrect, although it uses the word "indicia" when it probably meant "indicated". Those two sentences of the Proposed Order should be revised accordingly.

Finally, the AG and CUB fail to mention that Mr. Effron's figure assumes that ComEd's *pro forma* additions are approved through March 30, 2011. Effron Reb., AG/CUB Ex. 8.0, 11:237-242. Thus, even if it were not wrong for the reasons shown above, it still would be overstated.

3. **Staff's Exception**

Staff's Exception (Staff BOE, Appendix A, p. 17) appears to reason that (1) the Proposed Order approved an aggregate amount of $181,612,000 ($114,761,000 plus $66,851,000) out of $191,819,000 of new business included in ComEd's *pro forma* plant additions, or, in other words, disallowed only 5.32% of the new business; and, therefore, (2) ComEd's new business revenue credit of $3,457,000, which was based on approval of its *pro forma* additions through June 30, 2011, should only be reduced by 5.32%, or $184,000; which means (3) the Proposed Order's reduction of the new business revenue credit by $1,389,000 should be changed to $184,000.

Staff cites "Staff Appendix B, p. 8" for the $114,761,000 and $66,851,000 figures. Staff's BoE does not have an Appendix B, but Staff appears to mean Staff's Initial Brief, Appendix B. Staff has not explained, however, how the $66,851,000 figure in Appendix B to its Initial Brief ties to the Proposed Order's recommendations.

At the time of Staff's rebuttal, when Staff's position was that the Commission should approve *pro forma* adjustments through December 31, 2011, plus certain additional projects, Staff was recommending that the new business revenue credit be reduced by $592,000, not $184,000. Ebrey Reb., Staff Ex. 16.0, Sched. 16.14.

Staff's position is unreasonable and unfair on the merits. ComEd is being denied approximately 81% of its capital investments for the first two quarters of 2011 under the Proposed Order. PO at 20-23; ComEd Ex. 55.2, work paper WPB-2.1a Support. Yet, Staff's starting point is ComEd's calculation of the new business revenue credit assuming its *pro forma* additions were approved through June 30, 2011. That, per Staff's calculation, ComEd is being allowed to include 94.68% of its new business additions does not alter that approximately 81%

figure. To factor in 94.68% of the revenue increase through June 30, 2011, while denying ComEd most of its investments for the first six months of 2011, is unwarranted.

VI. CONCLUSION

WHEREFORE, for the reasons set forth herein and in ComEd's Initial and Reply Briefs and Brief on Exceptions, ComEd respectfully requests that the Proposed Order be modified as set forth in the ComEd's Exceptions and, as modified, be adopted by the Commission.

Dated: April 18, 2011

Respectfully submitted,

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