STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY	:	
	:	No. 11-0721
Formula rate tariff and charges authorized by	:	
Section 16-108.5 of the Public Utilities Act	:	

PRE-TRIAL MEMORANDUM OF COMMONWEALTH EDISON COMPANY

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PRE-TRIAL MEMORANDUM OF
COMMONWEALTH EDISON COMPANY

Commonwealth Edison Company ("ComEd"), by its counsel and in accordance with the scheduling order of the Administrative Law Judges, submits this Pre-Trial Memorandum.

I. INTRODUCTION / STATEMENT OF THE CASE

This proceeding is the initial rate-setting Docket for ComEd under new Section 16-108.5 of the Public Utilities Act (the "Act"), 220 ILCS 5/16-108.5. In this proceeding, ComEd seeks to establish a standardized, transparent method for determining its Illinois-jurisdictional revenue requirement and setting its delivery services charges that fully preserves the Illinois Commerce Commission's (the "Commission" or "ICC") role in reviewing the prudence and reasonableness of costs, and the accuracy of cost and revenue data.

A. The Formula Rate Framework

On October 26, 2011, Senate Bill 1652 became effective as Public Act 97-0616. Among its key provisions was the addition to the Act of Section 16-108.5. On December 30, 2011, Section 16-108.5 and certain other statutory provisions were modified in certain respects when a trailer bill, House Bill 3036 (the "Trailer Bill"), became effective as Public Act 97-0646.

The formula rate framework and the associated timing and processes are discussed in the direct testimony of ComEd witness Ross Hemphill, Ph.D., Vice President, Regulatory Policy & Strategy, Hemphill Direct ("Dir."), ComEd Exhibit ("Ex.") 1.0, 4:64-76, 6:118 – 9:169, and in

one of the attachments thereto, a detailed white paper, ComEd Ex. 1.2. A copy of the white paper is attached hereto. They were prepared when the Trailer Bill still was pending, and, thus, when applicable, discuss the different scenarios depending on its enactment. The following brief discussion is based primarily on the law and the white paper.

Under Section 16-108.5, a "participating [electric] utility" may elect to establish, by means of a tariff filing with the Commission, formulae that mathematically calculate the utility's Illinois-jurisdictional revenue requirement and corresponding delivery service charges. In the event of such a filing, an initial proceeding is held in which the Commission (1) establishes the formulae and (2) determines the resulting revenue requirement and charges for the initial period under the formula rate. Under Section 16-108.5, the revenue requirement formula is to provide for determination of the utility's revenue requirement based primarily on its most recent annual "FERC Form No. 1", with adjustments for its capital additions and changes in its depreciation reserve and depreciation expense in the filing year. Section 16-108.5 also mandates certain protocols regarding the formulae. Initially, the utility's delivery services charges formula is to be based on the cost of service (allocation across customer classes) and rate design determinations in its most recent delivery services rate case Order. Once established in the initial proceeding, the formulae remain fundamentally unchanged until modified by subsequent Commission action. 220 ILCS 5/16-108.5(c).

B. <u>ComEd's Filing</u>

On November 8, 2011, ComEd made the filing that initiated this Docket, and confirmed that it was making the commitments required it under Section 16-108.5. ComEd's filing, where

applicable, included alternative versions of the items that depended on enactment of the then still-pending Trailer Bill. Hemphill Dir., ComEd Ex. 1.0, 4:77 – 5:88.[1]

ComEd's November 8, 2011, filing included a performance-based formula rate tariff, Rate DSPP – Delivery Service Pricing and Performance ("Rate DSPP"), that set forth the formulae for determining ComEd's cost-based Illinois-jurisdictional revenue requirement and delivery services charges consistent with Section 16-108.5. Rate DSPP also provides for the subsequent annual updates and reconciliations discussed in the white paper. The formulae in Rate DSPP are sufficiently specific for the rate-setting and reconciliation processes to operate in a standardized and transparent manner. ComEd's filing also included the initial cost data that populate the formulae for purposes of determining the revenue requirement and setting the charges for the initial period, and the resulting figures and charges for the initial period. The filing was supported by testimony, exhibits, and other materials and information.[2]

The revenue requirement data filed by ComEd for purposes of setting the initial delivery services charges are based on its applicable costs and revenues from calendar year 2010 as recorded in its 2010 FERC Form 1, plus projected plant additions and correspondingly updated depreciation reserve and depreciation expense for 2011. *E.g.*, Hemphill Dir., ComEd Ex. 1.0, 6:119-127, 20:381 – 22:430. The population of the revenue requirement formulae for purposes of setting the initial delivery services charges was described primarily by the direct testimony of

[1] On January 11, 2012, ComEd gave notice to Commission Staff ("Staff") and the intervenors in this Docket that, as to those alternative version items, ComEd intends to offer into evidence only the versions reflecting the Trailer Bill. Staff and intervenors did not object.

[2] *E.g.*, Hemphill Dir., ComEd Ex. 1.0, 6:119-127, 10:178 – 15:280; ComEd Ex. 9.1 (Rate DSPP with the delivery services formulae as such but not populated by data); ComEd Ex. 9.2 TB (Rate DSPP as populated for the initial period and reflecting the Trailer Bill); ComEd Ex. 10.4 TB (exemplar delivery service charges informational sheets as populated for the initial period and reflecting the Trailer Bill). The detailed operation of the formulae was explained by the direct testimony of ComEd witness Kathryn Houtsma, C.P.A., Vice President, Regulatory Projects (ComEd Ex. 2.0). The rate design and the cost allocation reflected in Rate DSPP were addressed by the respective direct testimony of ComEd witnesses Sharon Kelly, P.E., Analyst, Retail Rates (ComEd Ex. 9.0), and Charles Tenorio, Principal Rate Analyst, Retail Rates (ComEd Ex. 10.0).

ComEd witness Martin Fruehe, Manager, Revenue Policy Department (ComEd Ex. 4.0). The direct testimony of a number of witnesses supported the revenue requirement.[3]

ComEd's direct testimony presented a revenue requirement, in the Trailer Bill scenario, of $2,030,391,000, which was $53,681,000 less than the revenue requirement approved by the Commission's Order in ComEd's most recent delivery services rate case, Commonwealth Edison Co., ICC Docket No. 10-0467 (Order May 24, 2011) (" *ComEd 2010*"). Fruehe Dir., ComEd Ex. 4.0, 3:66-69. The rate design and cost allocation across customer classes in Rate DSPP used to determine the delivery services charges are consistent with the Commission's Order in *ComEd 2010*. *E.g.*, Hemphill Dir., ComEd Ex. 1.0, 7:131-137, 15:293-297.

C. <u>Staff and Intervenor Positions and Proposals</u>

Staff and intervenors, in their direct testimony, addressed and made a number of proposals regarding the proposed revenue requirement formula and particular inputs into that formula for purposes of setting the initial delivery services charges. They also addressed the compliance of Rate DSPP with the rate design and cost of service determinations in the Commission's Order in *ComEd 2010* as well as some other subjects.

ComEd's rebuttal testimony agreed with or, in the interests of narrowing the issues, accepted certain of the Staff and intervenor direct testimony adjustments. Fruehe Rebuttal ("Reb."), ComEd Ex. 13.0, 4:84-88. The remaining Staff and intervenor direct testimony

[3] The testimony of Ms. Houtsma, Mr. Fruehe, and ComEd witnesses Michelle Blaise, P.E., Vice President, Engineering & Project Management (ComEd Ex. 5.0), Ronald Donovan, P.E., Vice President, Customer Business Transformation and Technology (ComEd Ex. 6.0), and Michael F. Born, P.E., Principal Engineer, Distribution Capacity Planning (ComEd Ex. 7.0), supported the prudence and reasonableness, and functionalization, of ComEd's costs. The direct testimony of John Hengtgen, independent Consultant (ComEd Ex. 8.0) presented and supported ComEd's cash working capital ("CWC") requirement. Finally, with respect to the revenue requirement, the testimony of Scott Vogt, Director, Financial Planning and Analysis (ComEd Ex. 3.0) presented ComEd's capital structure and cost of capital, including a cost of equity calculated as provided for by 220 ILCS 5/16-108.5(c)(3).

revenue requirement proposals, however, were improper. ComEd's rebuttal testimony refuted those other proposals, as discussed in later sections of this Pre-Trial Memorandum.

Staff's three largest proposed revenue requirement reductions in direct testimony were: (1) **eliminating all pension asset cost recovery**, an adjustment of $34,358,000; (2) **reducing 2011 plant additions** by a net amount of $59,992,000, with an associated depreciation expense reduction of $8,128,000, together yielding a revenue impact of $14,961,000; and (3) **reducing** ComEd's **cash working capital** (CWC) requirement by $63,874,000 in rate base, with a revenue impact of $7,208,000. Those three adjustments together accounted for $56,464,000 of Staff's $67,809,000 of proposed adjustments in direct testimony.[4]

ComEd's rebuttal showed that **all three of those reductions are improper**. First, Staff's pension funding costs recovery adjustment is based on the fallacious premise that ComEd has no pension asset. The Commission rejected that same Staff theory in its Order in Rehearing in ComEd's 2005 delivery services rate case, *Commonwealth Edison Co.,* ICC Docket No. 05-0597, p. 28 (Order on Rehearing Dec. 20, 2006). Staff did not renew that theory in *ComEd 2007* nor in *ComEd 2010*. The Commission approved ComEd's recovery of its pension contributions in all three Dockets, and the pension contribution recovery ruling in the Order in the 2005 Docket was affirmed by the Appellate Court, *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 398 Ill. App. 3d 1065, 924 N.E.2d 1065 (2d Dist. 2009), *app. den*., 237 Ill. 2d 554, 938 N.E.2d 519 (2010). Staff's "no pension asset" theory is contrary to fact, is wrong under Generally Accepted Accounting Principles, as confirmed by the rebuttal testimony of independent accounting expert William Graf, Partner, Deloitte & Touche LLP (ComEd Ex. 14.0), and is contrary to the Act.

[4] Staff also proposed to move Illinois-jurisdictional uncollectibles expense of $16,672,000 out of base rates and into ComEd's uncollectible cost recovery rider, Rider UF – Uncollectible Factors ("Rider UF"). That proposal was in addition to the $67,809,000 in adjustments.

Second, Staff's 2011 plant additions reduction was unreasonable because, among other things, the 2011 plant additions forecast was more than amply supported, Staff's position was supported in part by a misreading of a data request response, and Staff included an aberrational year in a multi-year average that is inappropriate to apply in any event. Moreover, ComEd's actual total 2011 plant additions now are known, and they were higher, not lower, than the forecast. By getting it wrong now, Staff's 2011 plant additions reduction unnecessarily would require an equal offsetting adjustment (with interest) in the first reconciliation.

Finally, Staff's CWC adjustment also improperly and unfairly sought to supplant fact with theory. Theory cannot alter the facts regarding ComEd's cash out-flows and in-flows.

Staff's rebuttal sought to rehabilitate, and in some instances recalculated, their contested adjustments, but they remained improper, and some of the recalculations included significant errors. Staff made a major calculation error related to the roll forward of the depreciation reserve, which understated the revenue impact of Staff's adjustments by approximately $14 million. Staff also made an error that overstated its proposed CWC adjustment.

The Illinois Attorney General's Office (the "AG") jointly with AARP, plus the Citizens Utility Board ("CUB"), submitted revenue requirement proposals in their direct testimony. To a limited degree, the Illinois Industrial Energy Consumers ("IIEC") also submitted positions. For the most part, intervenors' significant adjustments, too, were improper and/or would require offsetting adjustments in the first reconciliation, as shown in ComEd's rebuttal testimony. Those intervenors, in their rebuttal, also sought but failed to rehabilitate their contested adjustments, some of which they modified and/or recalculated. However, they failed to provide revised revenue requirement and net adjustment figures.

The Staff and intervenor direct testimony proposals related to rate design and/or cost of service, for the most part were improper, but some had merit or at least could be accepted in the interests of narrowing the issues, as discussed in ComEd's rebuttal testimony.

ComEd is not able, in this Pre-Trial Memorandum, to anticipate fully the responsive material, including calculation corrections, that will be contained in its surrebuttal testimony. Staff and intervenors filed their rebuttal testimony on Friday, February 24, 2012, three business days before the due date of this Pre-Trial Memorandum, Wednesday February 29, 2012. ComEd's surrebuttal testimony is due on Friday, March 2, 2012, and is currently the subject of ongoing substantive analysis, research, and drafting work. While ComEd's analysis to date has determined that all of the significant contested revenue requirement proposals remain improper, ComEd's review is continuing, and it is complicated by the Staff and intervenor calculation errors and/or incomplete presentations.

The Commission should approve ComEd's initial filing, subject to the revisions reflected in its rebuttal testimony. ComEd's initial filing, with those revisions, carefully and correctly implements and applies Section 16-108.5, and results in a just and reasonable Illinois-jurisdictional revenue requirement and delivery services charges for the initial period.

II. OVERALL REVENUE REQUIREMENT

ComEd's overall Illinois-jurisdictional revenue requirement is $2,027,035,000, reflecting corrections and Staff and Intervenor direct testimony adjustments with which ComEd agreed or was willing to accept in order to narrow the issues. Fruehe Reb., ComEd Ex. 13.0, 4:83-88.

III. RATE BASE

A. Overview

ComEd's direct testimony presented and supported a rate base, in the Trailer Bill scenario, of $6,647,036,000. Fruehe Dir., ComEd Ex. 4.0, 2:43-45. That figure was based on 2010 FERC Form 1 balances, functionalization, applicable ratemaking adjustments, and the addition of the estimated 2011 plant additions and the 2011 change in depreciation expense less the applicable roll forward of the depreciation reserve through 2011. *Id.*, 10:197 – 11:220. ComEd's rebuttal testimony, which reflected corrections and agreed or accepted adjustments, presented and supported a revised figure of $6,625,375,000. Fruehe Reb., ComEd Ex. 13.0, 4:91-95.

In addition to the overall figures and support in the direct testimony of ComEd witness Mr. Fruehe (ComEd Ex. 4.0, 10:197 – 19:386), ComEd's rate base was supported by the direct testimony of Ms. Blaise, ComEd Ex. 5.0, 4:82 – 44:930 (Distribution Plant, General and Intangible ("G&I") Plant, Materials and Supplies inventory, "non-AFUDC" Construction Work in Progress ("CWIP"), 2011 plant additions, major capital investments); Mr. Donovan, ComEd Ex. 6.0, 2:25-35, 4:77 – 9:170, 9:177 – 10:207, 11:228 – 13:277, 18:376 – 19:400) (rate base assets supporting customer service); Mr. Born (ComEd Ex. 7.0, 7:142 – 10:215) (functionalization of Distribution Plant versus Transmission), Mr. Hengtgen, ComEd Ex. 8.0 (cash working capital requirement); and Ms. Houtsma, ComEd Ex. 2.0, 29:591 – 30:614, 30:626-628 (G&I Plant functionalization, depreciation reserve).

Staff and intervenors in their direct testimony proposed a number of rate base adjustments, and generally adhered to those adjustments in rebuttal, with some modifications. Those proposals were addressed by the rebuttal testimony of several of the aforementioned witnesses, and Mr. Hemphill, plus, with respect to the Pension Asset issue, independent expert

Mr. Graf LLP (ComEd Ex. 14.0). The remaining contested adjustments as of Staff and intervenors' rebuttal testimony will be addressed by ComEd's surrebuttal testimony. The contested proposed adjustments of Staff and intervenors, including all of their major adjustments and some of their other adjustments, are improper, as discussed in the remainder of this Section III of this Pre-Trial Memorandum.

B. Potentially Uncontested Issues

1. Materials & Supplies Inventories

ComEd's materials and supplies inventory in rate base is uncontested. Fruehe Dir., ComEd Ex. 4.0, 14:289 – 15:296; ComEd Ex. 4.3 at Sch FR B-1, line 39.

2. Regulatory Assets & Liabilities

a) Regulatory Assets

ComEd's rate base includes certain regulatory assets. They are uncontested. *E.g.*, Fruehe Dir., ComEd Ex. 4.0, 15:299-304. *See also* Ostrander Dir., Staff Ex. 4.0, 7:139 – 8:152.

b) Asset Retirement Obligation

ComEd subtraction of asset retirement obligations from rate base is uncontested. Fruehe Dir., ComEd Ex. 4.0, 15:312 – 16:316.

c) Deferred Credits

ComEd subtracted deferred credits from rate base. Fruehe Dir., ComEd Ex. 4.0, 15:312 – 16:316. The sole proposed adjustment was that of AG/AARP relating to ComEd's leasing of its fiber optic equipment. AG/AARP was correct that there should be an additional deferred credit related to this item, but AG/AARP's proposed method of functionalizing the distribution portion of the credit, the net plant allocator, was incorrect. The communications equipment allocator should be used. ComEd reflected the credit, calculated with that allocator, in its rebuttal

testimony. Fruehe Reb., ComEd Ex. 13.0, 14:297 – 320. ComEd also made a parallel correction to the lease revenues credited against the revenue requirement. *Id*., 15:321-327. AG/AARP's rebuttal accepted ComEd's modification, so this item now is uncontested. Effron Reb., AG/AARP Ex. 4.0, 8:172-177.

d) Other Deferred Charges

ComEd included deferred charges (positive and negative) in its rate base, but amortized these items over five years as required by 220 ILCS 5/16-108.5(c)(4)(C) and (F). Fruehe Dir., ComEd Ex. 4.0, 17:337-354. Those items are uncontested.

3. Customer Deposits, Including Staff Proposal

ComEd included customer deposits as a subtraction from rate base. Fruehe Dir., ComEd Ex. 4.0, 17:356 – 18:362. Staff and AG/AARP proposed that interest on customer deposits, which were treated as a reduction to the customer deposits balance, instead be treated as an operating expense item. ComEd accepted and reflected that proposal in its rebuttal testimony. Fruehe Reb., ComEd Ex. 13.0, 16:329-336. No other adjustment was proposed. *See also* Section V.B.6.b of this Pre-Trial Memorandum.

4. Customer Advances

ComEd subtraction of customer advances from rate base is uncontested. Fruehe Dir., ComEd Ex. 4.0, 18:364-370.

C. Potentially Contested Issues

1. Plant-in-Service

a) Original Cost Finding 2010 Plant

ComEd's rebuttal testimony's original cost finding figure of $14,426,332,000 as of December 31, 2010, is correct. ComEd's rebuttal made a number of corrections to its original

figure, all of which Staff accepted in its rebuttal testimony (subject to reservation of potential issues in future Dockets). Staff's rebuttal testimony proposed a figure of $14,398,674,000, which was calculated by subtracting $27,658,000 based on Staff's proposed 2010 plant adjustments. Bridal Reb., Staff Ex. 16.0, 18:381 – 20:433. Staff's proposed 2010 plant reductions are without merit, as discussed in Section III.C.1.d of this Pre-Trial Memorandum. ComEd's corrected figure of $14,426,332,000 should be approved. Fruehe Reb., ComEd Ex. 13.0, 16:338 – 17:370.

b) <u>2010 Distribution Plant</u>

ComEd's 2010 Distribution Plant in rate base should be approved. ComEd Ex. 13.1, Sch FR B-1. Staff and intervenors did not propose any adjustments to ComEd's 2010 Distribution Plant, other than the derivative impacts on plant of their proposed adjustments to restricted stock, incentive compensation, and perquisites and awards, which should not be adopted, as discussed in Sections VI.C.1.b, c, and d of this Pre-Trial Memorandum.

c) 2010 General and Intangible Plant, <u>Including Functionalization</u>

ComEd showed that its 2010 General and Intangible Plant costs are prudent, reasonable, and used and useful. Neither Staff nor any intervenor disagreed. The only issue is the functionalization of these costs. ComEd functionalized General Plant Account 397 based on a direct assignment study, and functionalized the remaining G&I Plant Accounts based on the general labor allocator, also known as the wages & salaries ("W&S") allocator. Staff's direct testimony proposed two adjustments: (1) for those Accounts where ComEd is proposing a change from the methodologies approved in ComEd's 2007 and 2010 rate cases, to stick with the former methodologies; and (2) to revise the calculation of the W&S allocator. AG/AARP's and CUB's direct testimony also proposed the first of those two adjustments.

ComEd's proposal should be approved. ComEd's combination of methodologies (1) is cost-based, (2) simplifies and streamlines the splitting of these costs, and (3) aligns the methodologies for functionalization of these Accounts with the methodologies used to functionalize these same Accounts for purposes of its FERC-approved Transmission Formula Rate ("TFR"). If the methodologies continue not to be aligned (between FERC and ICC rates), that will mean that, in any given year, the split between distribution and transmission will be inconsistent, and that will lead either to over-recovery or under-recovery of ComEd's G&I Plant costs. Houtsma Dir., ComEd Ex. 2.0, 29:592 – 30:614; Houtsma Reb., ComEd Ex. 12.0, 4:69-71, 22:499-504, 24:529 – 31:669.

In contrast, Staff's primary proposal, echoed by AG/AARP and CUB, will deprive ComEd recovery of a net $18,197,000 of costs that all agree are prudent, reasonable, and used and useful, and would also deny recovery of the associated annual $492,000 of depreciation expense. Even AG/AARP witness Mr. Brosch agreed that if this adjustment is approved, then ComEd will not be allowed to recover all of its prudent costs of G&I Plant so long as the methodology under the FERC formula rate is unchanged. Moreover, the direction of the adjustment (a rate base reduction rather than an increase) is driven entirely by the difference in Accounts 390 and 394. ComEd's approach as to Account 390 does not sacrifice accuracy and avoids a time-consuming, subjective study previously used to functionalize 15% of the Account (the other 85% already was functionalized with the W&S allocator). As to Account 394, ComEd's approach simply moves from a different general allocator, the T&D gross plant allocator, to the W&S allocator, and the latter makes at least as much sense from a cost-causation standpoint. The Order in *ComEd 2010* ruled in favor of Staff on this issue, but in that Docket the Commission only had one side of the facts before it because ComEd's testimony was stricken on

timeliness grounds. This case should be decided based on the facts in the record here. Houtsma Reb., ComEd Ex. 12.0, 4:69-71, 21:483 - 31:669; ComEd Ex. 12.7; Houtsma Dir., ComEd Ex. 2.0, 29:591 – 30:614.

Staff, AG/AARP, and CUB adhered to their positions in their rebuttal testimony, but they failed to refute the facts in ComEd's rebuttal, and instead relied on arbitrary and conclusory arguments. Staff reiterated past points, asserted that ComEd was trying to shift the burden of proof, rejected the significance of the FERC-approved TFR, and, remarkably, claimed that ComEd's testimony that its proposal aligns state and federal methodologies was insufficient evidence, even while Staff presented no evidence to the contrary. AG/AARP and CUB presented no new substantive points, apart from suggesting that ComEd could seek to change the functionalization under the FTR. AG/AARP went so far as to indicate that even if ComEd's proposal is as reasonable as the current methodologies and aligns with the FTR, AG/AARP still would oppose it, without identifying any good reason, *See* Rukosuev Reb., Staff Ex. 21.01, 2:32 - 12:288; Brosch Reb., AG/AARP Ex. 3.0, 28:623 – 31:690; Smith Reb., CUB Ex. 3.0, 35:761 – 38:830.

ComEd's uncontradicted testimony regarding the alignment of methodologies is sufficient proof, as a matter of law, absent inherent improbability or impeachment. *Bazydlo v. Volant*, 164 Ill. 2d 207, 215, 647 N.E.2d 273, 277 (1995); *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 322 Ill. App. 3d 846, 849, 751 N.E.2d 196, 199 (2d Dist. 2001). ComEd is not shifting the burden of proof. ComEd proved its factual points. They have not been refuted. A utility bears the burden of proof that its proposed rates are just and reasonable, 220 ILCS 5/9-201(c), but once it makes out a *prima facie* case, the burden of going forward with the evidence shifts to the other parties that challenge its costs. *Illinois Bell Tel. Co. v. Illinois*

Commerce Comm'n, 327 Ill. App. 3d 768, 776, 762 N.E.2d 1172, 1173-1174 (3d Dist. 2002); *City of Chicago v. People of Cook County*, 133 Ill. App. 3d 435, 442-443, 478 N.E.2d 1369, 1375 (1st Dist. 1985).

The Staff, AG/AARP, and CUB position improperly and unfairly seeks to trap the costs in question between the federal and state tariffs, meaning they cannot be recovered. ComEd has a right to rates that allow it the opportunity to recover fully its costs of delivery services. 220 ILCS 5/16-108(c) ("Charges for delivery services shall be cost based, and shall allow the electric utility to recover the costs of providing delivery services through its charges to its delivery service customers that use the facilities and services associated with such costs. Such costs shall include the costs of owning, operating and maintaining transmission and distribution facilities.") "Delivery services" includes both transmission and distribution services. 220 ILCS 5/16-102 (definition of "Delivery services").

Such trapping of costs by a state public utility commission based on rulings inconsistent with FERC determinations is improper under federal law as well. In *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986), the Supreme Court of the United States reversed a decision of the North Carolina Supreme Court that was inconsistent with an earlier FERC determination. Nantahala and a sister utility each purchased power from the Tennessee Valley Authority. FERC previously had established the allocations of low-cost purchased power and high-cost purchased power between the two utilities. Nantahala made retail and wholesale electric sales. The North Carolina Supreme Court rejected FERC's allocation and substituted its own allocation, thereby reducing the costs of purchased power for purposes of establishing rates for retail sales. The North Carolina Supreme Court reasoned that it has jurisdiction regarding retail sales, and that it therefore could look at the cost allocation issue *de novo*. The United

States Supreme Court reversed, holding that states must respect the filed rate doctrine, that FERC's determination of the purchased power costs was an integral part of the determination of rates, and that the Supremacy Clause of the United States Constitution, Article VI, § 2, required preemption of the North Carolina Supreme Court's findings. The United States Supreme Court held that trapping of costs, such that a wholesale seller could not recover fully the FERC-approved rate, was prohibited. In *Mississippi Power & Light Co. v. Moore*, 487 U.S. 354 (1988), the Supreme Court of the United States reversed a decision of the Supreme Court of Mississippi that was inconsistent with a prior FERC determination. FERC had established a formula to allocate the costs of operating a nuclear power plant among the operating subsidiaries of a holding company. The Supreme Court of Mississippi held that it was free to disallow some of those costs on the theory that they were imprudent. The Supreme Court of the United States, reversing, held that (1) where FERC has allocated costs, the states must treat those costs are reasonable; (2) FERC's cost allocation preempted the state's reasonableness review; and (3) the preemption did not turn on whether any particular issue was raised before FERC.

Staff also incorrectly proposes to reduce ComEd's G&I plant by another net $3,247,000, and to deny recovery of the associated $343,000 of depreciation expense, based on Staff's recalculation of the W&S allocator to allocate a slice of costs to the production function. Staff's proposal is incorrect because the costs that would be moved to the production function are not really production costs, and because the proposal is unnecessary and would serve no purpose other than to push these costs from being recovered through base delivery services charges to ComEd's Rider PE – Purchased Electricity. If Staff's proposal nonetheless were to be approved, then the Commission's Order should find that these costs are prudent and reasonable, which ComEd showed and no one disputes, and that they shall be recovered through Rider PE.

Houtsma Reb., ComEd Ex. 12.0, 19:435 – 21:481; Hemphill Reb., ComEd Ex. 11.0, 14:279 – 15:298. *See also* Section V.C.1.e of this Pre-Trial Memorandum. Staff's rebuttal testimony adhered to these proposed adjustments based on the allocator, but took no position as to recovery under Rider PE. *See* Knepler Reb., Staff Ex. 14.0, 3:48 – 6:118. Staff's proposal should not be adopted, but, if it were to be approved, then the Order should find as suggested above.

d) <u>2011 Plant Additions</u>

ComEd's forecasted plant additions in rate base should be approved. The forecast was supported by a great deal of reliable data. Plus, now that the record has full 2011 plant additions total actuals data provide in ComEd's rebuttal testimony, we know that ComEd's forecast actually was low. *E.g.*, Blaise Dir., ComEd Ex. 5.0, 20:405 – 23:474; ComEd Exs. 5.1, 5.2; Donovan Dir., ComEd Ex. 6.0, 8:167 – 9:170, 9:177 – 10:207, 11:28 – 13:277; ComEd Ex. 6.1; Fruehe Dir., ComEd Ex. 4.0, 18:372-377; ComEd Ex. 4.3 at Sch FR B-1 TB, lines 50 and 52, and Appendix 1, lines 38-46.

Staff's direct testimony nonetheless proposed to reduce the additions by a net $34,368,000, and to deny recovery of the associated $8,128,000 of depreciation expense. Staff's adjustment had two bases: (1) a net $8,900,968 of the plant reduction is attributable to removing projects that were cancelled or had a revised completion date after 2011; while (2) the remaining net $25,467,032 (reduced by Staff to avoid double-counting with the first portion) was based on Staff's supplanting 2011 data with a five year average historical comparison of budget and actual additions, which suggested a 6% average variance of actuals below budgets. Staff's proposed adjustment is improper in both respects. The first part of the adjustment is improperly one-sided, because it fails to take into account new projects and projects that have been moved up. When both sides are taken into account, ComEd's projected plant additions figure remains reasonable.

Moreover, we now have full 2011 total actuals data, and we now know that 2011 total actual plant additions were approximately $753.6 million, instead of ComEd's projected amount of $684,431,000 (these are gross amounts, not net plant amounts). As to the second portion of Staff's adjustment, Staff claimed that through October 2011, plant additions were only tracking at 90%, but that was 90% of the amount for all of 2011, not the first 10 months. In fact, if 2011 actual results were included, a four year variance average would be minimal, with the average actuals being 99.44% of the budget. Moreover, it is not reasonable to blindly apply a five year historical variance average without taking into account changes in cost drivers. Furthermore, the Staff average is thrown off by the inclusion of 2009, which had an aberrational decline in the level of new business additions due to the economy. The additional support for this portion of the adjustment that was based on Staff's analysis of 30 major projects also suffered from numerous flaws, and even then only showed a 1.33% variance, not the 6% variance that this portion of Staff's adjustment applies. Finally, Staff's proposal is pointless, because the fact that actual 2011 plant additions were greater than the forecasted amount that ComEd included in rate base means that Staff's adjustment would only artificially suppress delivery services charges in the initial period and as a result require an ever larger adjustment in the other direction in the reconciliation proceeding. Blaise Reb., ComEd Ex. 17.0, 2:31 - 11:219; Hemphill Reb., ComEd Ex. 11.0, 10:185 – 11:213; Fruehe Dir., ComEd Ex. 4.0, 18:372-377.

Staff's rebuttal testimony unpersuasively tried to rationalize both parts of its adjustment, even while admitting that ComEd's 2011 plant additions were higher than forecasted. Staff's argument, that its position should be adopted because, while actual additions in the year at issue here were higher than forecast, the forecast might be too high in future years, is untenable. The time to assess the reasonableness of forecasted plant additions in future filings is in those

Dockets. Making an incorrect adjustment here, and/or altering the formulae to assume future incorrect forecasts, is improper and unreasonable. Moreover, Staff recalculated both parts of its adjustment, but Staff's calculations in part are incorrect, apparently resulting in overstatement of the adjustment by $14,755,000, although ComEd's review continues. *See* Bridal Reb. Staff Ex. 16.0, 3:51 – 9:199 and Schedule 16.01; *see also* Rashid Reb., Staff Ex. 19.0. Staff's adjustment remains wrong and should be rejected.

e) <u>Derivative: Restricted Stock</u>

The plant adjustments that are derivative of Staff's, AG/AARP's, and CUB's proposed restricted stock deferred compensation adjustments should not be approved, for the reasons stated in Section VI.C.1.b of this Pre-Trial Memorandum.

f) <u>Derivative: Incentive Compensation</u>

The plant adjustments that are derivative of Staff's, AG/AARP's, and CUB's proposed restricted incentive compensation adjustments should not be approved, for the reasons stated in Section VI.C.1.c of this Pre-Trial Memorandum.

g) <u>Derivative: Perquisites and Rewards</u>

The plant adjustments that are derivative of Staff's, AG/AARP's, and CUB's proposed perquisites and rewards adjustments should not be approved, for the reasons stated in Section VI.C.1.d of this Pre-Trial Memorandum.

2. <u>Accumulated Depreciation & Amortization</u>

Because ComEd's rate base includes 2011 plant additions, its depreciation reserve must be rolled forward to 2011 as well. 220 ILCS 5/16-108.5(c)(6). ComEd rolled forward the depreciation reserve by adding a full year of depreciation expense on the 2011 plant additions, as a reasonable proxy for the sum of (1) the increase in depreciation in 2011 associated with 2010

plant additions (the 2010 year-end depreciation reserve would reflect only approximately half of the increase in depreciation associated with 2010 plant additions because they occurred over the course of 2010) plus (2) the increase in depreciation in 2011 associated with 2011 plant additions (the 2011 year-end depreciation reserve similarly would reflect only approximately half of the increase in depreciation expense associated with 2011 plant additions because they occurred over the course of the year). This added $16,565,000 to the depreciation reserve. *E.g.*, Houtsma Reb., ComEd Ex. 12.0, 14:315 – 16:350; ComEd Ex. 12.4.

There is only one non-derivative proposed adjustment to ComEd's figure for its depreciation reserve. Staff's direct testimony proposes a different calculation of the 2011 change in accumulated depreciation, although Staff, inconsistently, does not propose a parallel adjustment to 2011 depreciation expense. ComEd responded on the merits, including identifying miscalculations in Staff's proposal as well as the improper omission of a parallel depreciation expense adjustment. ComEd also presented two alternative calculations, one resulting in a $16,612,000 figure, and the second found in ComEd Ex. 12.5, resulting in a $16,773,000 figure. Houtsma Reb., ComEd Ex. 12.0, 14:304 – 16:376; ComEd Ex. 12.5.

Staff's rebuttal testimony withdrew its original proposal and agreed to the alternative calculation in ComEd Ex. 12.5. *See* Bridal Reb., Staff Ex. 16.0, 15:329 – 16:354. However, Staff incorrectly implemented that method, resulting in a miscalculation that led to an understatement in the depreciation reserve. ComEd, in order to narrow the issues, is willing to agree to the alternative calculation in ComEd Ex. 12.5, provided that it is correctly implemented.

With respect to proposed changes to the depreciation reserve that are derivative of Staff's and intervenors' respective proposed plant adjustments, the derivative changes rise or fall with

the plant adjustments. Their contested plant adjustments should be rejected, as discussed in the applicable sections of this Pre-Trial Memorandum.

3. Construction Work in Progress

Section 9-214(e) of the Act, 220 ILCS 5/9-214(e), authorizes inclusion of CWIP in rate base. ComEd's rate base appropriately includes $6,225,000 of CWIP not accruing AFUDC, using the December 31, 2010, balance as a reasonable proxy for amounts to be expended in future periods. Fruehe Dir., ComEd Ex. 4.0, 13:257-268; Blaise Dir., ComEd Ex. 5.0, 18:373 – 19:403.

Staff's direct testimony proposed to remove all non-AFUDC CWIP from rate base, based on the erroneous theory that it double-counts the 2011 plant additions.[5] Non-AFUDC CWIP is not included in rate base as a means of including the specific projects that happen to be in progress and not accruing AFUDC as of the non-AFUDC CWIP measurement. Non-AFUDC CWIP is included in rate base as a proxy for the non-AFUDC amount that will exist in future periods. ComEd's approach is consistent with how it accounted for, and what the Commission approved, in its 2005, 2007, and 2010 rate cases. The projects in CWIP as of December 31, 2010, may be in service now, but the projects in CWIP constantly roll over and are replaced by new projects. The exact same proposal that Staff now makes was made by CUB, the AG, and the Cook County State's Attorney's office in ComEd's 2005 rate case. By the time of the evidentiary hearing in that case, those parties, Staff, and ComEd all agreed that it was appropriate to include a normalized level of non-AFUDC CWIP in rate base, and their respective witnesses each testified in support of the normalized amount. Houtsma Reb., ComEd Ex. 12.0, 18:407 – 19:433.

[5] IIEC proposed to amend formula rate Sch FR B-1 to remove all CWIP from rate base, but IIEC did not explicitly provide any facts or argument in support of that proposal. *See* Gorman Dir., IIEC Ex. 1.0, 24:536. That unsupported proposal is erroneous for the same reasons that Staff's proposed adjustment is erroneous.

Staff's rebuttal provides only unconvincing responses, including an unpersuasive attempt to distinguish the contrary Staff position and Order in ComEd's 2005 rate case. Staff nonetheless agrees, however, that, in the reconciliation, ComEd will be allowed to include non-AFUDC CWIP in rate base. *See* Bridal Reb., Staff Ex. 16.0, 9:201 – 13:291.

Nonetheless, in the interests of narrowing the issues, ComEd's is willing to accept Staff's proposal to remove non-AFUDC CWIP from rate base, provided that the Commission's Order provides, as Staff agrees, that non-AFUDC-CWIP shall be included in the reconciliation. Otherwise, Staff's proposed adjustment should not be adopted, because it is erroneous.

CUB proposed an adjustment to non-AFUDC CWIP that was derivative of its proposed adjustment to Restricted Stock. Smith Dir., CUB Ex. 1.0, 21:469-473. That underlying adjustment lacks merit, as discussed in Section V.C.1.c of this Pre-Trial Memorandum.

4. Cash Working Capital, Including ComEd Proposal Regarding Timing of Future Lead/Lag Study

ComEd's direct testimony presented and supported a cash working capital requirement of $49,705,000, which was updated in its rebuttal testimony to a figure of $39,805,000. ComEd's CWC requirements are based on a proper lead/lag study similar to that approved in *ComEd 2010*, except ComEd made three changes, one ordered by the Commission in that Docket, and the other two involving improving the accuracy of the lags and leads for certain pass-through items. ComEd's revised CWC figure of $39,805,000 represents its real CWC requirement resulting from the applicable actual cash outflows and inflows and should be approved. Hengtgen Dir., ComEd Ex. 8.0; ComEd Ex. 8.1; Hengtgen Reb., ComEd Ex. 16.0; ComEd Ex. 16.6.

Staff, AG/AARP, CUB, and IIEC direct testimony each proposed various revisions to ComEd's lead/lag study. Their rebuttal testimony was highly similar, except Staff withdrew a portion of its proposal and recalculated it (nonetheless resulting in an increase of its proposed

adjustment from $63,874,000 to $74,888,000 despite the partial withdrawal and ComEd's figure already having been reduced), AG/AARP also revised its calculations (resulting in an increase of its proposed adjustment from $78,893,000 to $86,564,000), and CUB indicated some alternative positions (but did not provide a recalculation of its $60,033,000 adjustment). (IIEC never presented a dollar adjustment.) *See* Kahle Reb., Staff Ex. 15.0, 2:26 – 9:169; Brosch Reb., AG/AARP Ex. 3.0, 2:34-44, 3:54 – 4:68, 12:271 – 28:619; Smith Reb., CUB Ex. 3.0, 2:31 – 13:255; Gorman Reb., IIEC Ex. 2.0, 14:311 – 18:421. As in past cases, their proposals predominately consist of efforts to substitute theory for fact. In brief:

- ComEd's collections lag of 34.23 days is correct. The shorter collections lags proposed by AG/AARP and CUB are incorrect, and, in AG/AARP's case, miscalculated. They improperly disregard that ComEd, by incorporating grace periods into its calculation, significantly understated the collections lag. AG/AARP's attempt to turn that fact into an argument against the reliability of ComEd's lead/lag study is absurd. They also improperly ignore that ComEd loses the time value of money with respect to receivables that ultimately are not collected. AG/AARP's and IIEC's proposals for more study on this subject are unwarranted.

- ComEd's revenue lag of 51.25 days for pass through taxes is correct. ComEd's respective leads for pass-through taxes also are correct. The various proposals of Staff, AG/AARP, CUB, and IIEC are incorrect. (Staff's rebuttal withdrew its expense lead adjustment for certain pass-through taxes.) Their attempts to substitute theory for fact on this subject should end.

- ComEd's intercompany expense lead of 30.55 days is correct. The Staff, AG/AARP, and CUB leads also substitute theory for fact and are incorrect.

- ComEd's revenue lag of 51.25 days for revenues associated with pension and OPEB is correct. The zero lags proposed by AG/AARP and CUB are yet another attempt to substitute theory for fact and are incorrect. The Commission rejected these very arguments in *ComEd 2010*.

- ComEd plans in its surrebuttal testimony to present a correct revised calculation of the CWC requirement associated with non-AFUDC CWIP. The amounts proposed by AG/AARP and CUB are incorrect. Moreover, if non-AFUDC CWIP is not included in rate base (*see* Section III.C.3 of this Pre-Trial Memorandum), then no CWC adjustment for non-AFUDC CWIP is appropriate.

- ComEd's rebuttal testimony expense lead of 228.50 days for incentive pay is correct. ComEd's rebuttal accepted in part the AG/AARP and CUB position.

- ComEd's use of the base payroll lead for vacation pay is correct. The AG/AARP proposal regarding vacation pay are incorrect. They have the timing wrong. ComEd in rebuttal revised the presentation of this portion of the lead/lag study, to show it had correctly handled this item.

- ComEd plans to file surrebuttal with the correct amount and expense lead for 401(k) matching. ComEd anticipates that its surrebuttal will accept in part the AG/AARP position.

- ComEd's rebuttal testimony appropriately updates the calculations relating to state and federal income taxes and deferred income taxes.

Hengtgen Reb., ComEd Ex. 16.0; ComEd Ex. 16.6; Fruehe Reb. ComEd Ex. 13.0, 12:254 – 14:295. *See also* the discussion of intervenor proposals relating to incentive and vacation pay in Section III.C.6.a of this Pre-Trial Memorandum.

ComEd's proposal to annually update the inputs to the lead/lag study, but, absent a change in law that has significant impact on the lead/lag study, to update the study methodology once every three years, is reasonable and should be adopted. Houtsma Dir., ComEd Ex. 2.0, 17:338-345; Hengtgen Dir., ComEd Ex. 8.0, 20:390 – 21:398.

5. <u>Accumulated Deferred Income Taxes</u>

ComEd has correctly calculated the Accumulated Deferred Income Taxes ("ADIT") deduction from rate base. Fruehe Dir., ComEd Ex. 4.0, 14:280-287; Fruehe Reb., ComEd Ex. 13.0, 5:98 – 12-251.

Setting aside derivative impacts of proposed plant adjustments, various substantive adjustments to ADIT were proposed by AG/AARP, CUB, and IIEC in direct testimony. The AG/AARP and CUB proposal to include the ADIT associated with ComEd's "SERP" (Supplemental Executive Retirement Plan) in the calculation of the return on ComEd's Pension Asset is correct, and was accepted in ComEd's rebuttal. The AG/AARP, CUB, and IIEC rebuttal

as to the other proposals is similar to their direct, except the AG/AARP witness added some alternative positions and he and the CUB witnesses did not address some items. Effron Reb., AG/AARP Ex. 4.0, 1:14 – 3:64; Smith Reb., ComEd Ex. 3.0, 13:259 – 15:293; Gorman Reb. IIEC Ex. 2.0, 10:230 – 12:276. Staff's rebuttal adopted the AG/AARP and CUB adjustment for ADIT associated with the bad debt reserve. Bridal Reb., Staff Ex. 16.0, The contested proposals lack merit, and in part are one-sided.

- They each propose to add the ADIT associated with the 2011 plant additions to rate base. While it is correct that adding ADIT for the 2011 plant additions would make the rate base closer as to this one item to the actual 2011 rate base, the proposal ignores all other changes in 2011 ADIT. The proposal also is unnecessary, because the reconciliation will capture the difference between 2011 ADIT and ADIT approved in the instant Docket. Moreover, on the other hand, if the actual revenue requirement determined in the reconciliation is higher than the revenue requirement determined in this Docket, then all the proposal will do is to increase the size of the reconciliation adjustment. Finally, Section 16-108.5(c)(6) of the Act, 220 ILCS 5/16-108.5(c)(6), requires rolling forward the depreciation reserve and depreciation expense along with the plant additions, but it contains no such provision as to ADIT. Staff's rebuttal opposed this adjustment.

- AG/AARP and CUB propose to eliminate the ADIT balance associated with what was identified as employee litigation. ComEd's direct testimony did mislabel certain ADIT amounts as attributable to employee litigation, when they actually related to renewable energy credits ("RECs") and 401(k) matching, and the former should not have been included because it related to purchased power expenses. ComEd's rebuttal corrected the labeling and removed the RECs item. AG/AARP's and CUB's proposal as to the 401(k) item lacks merit. Staff's rebuttal opposed that proposal.

- AG/AARP and CUB proposed to functionalize the ADIT associated with the bad debt reserve, and to remove the non-distribution portion. Staff's rebuttal adopted this proposal. The proposal is in direct contrast to AG/CUB's proposal in *ComEd 2010* to credit distribution rates with all late payment charges revenues because the non-distribution portion was not credited in other rates, which proposal the Commission adopted. The non-distribution portion of ADIT associated with the bad debt reserve is not captured in other rates, either.

- CUB proposes to adjust ADIT relating to incentive pay and vacation pay, but at the same time reduces rate base for the operating reserves for these two items. CUB's calculation is incorrect, but, more importantly, the proposal is wrong because ComEd's lead/lag study as revised in rebuttal appropriately accounts for these two items. Staff's rebuttal opposed these proposals.

- CUB proposes to remove the ADIT associated with "FIN 47" (FASB Interpretation No. 47), on the sole basis that this would be consistent with the ratemaking treatment in *ComEd 2010*. This ADIT is properly included in rate base, however. Moreover, CUB conveniently ignores that ComEd included the ADIT associated with holiday pay, thereby reducing rate base, even though that also was inconsistent with the ratemaking treatment in *ComEd 2010*. CUB's proposal is one-sided. Staff's rebuttal opposed this proposal.

Fruehe Reb., ComEd Ex. 13.0, 5:98 – 12:251.

6. Regulatory Assets & Liabilities

a) Operating Reserves

ComEd included certain operating reserves, both assets and liabilities, in rate base. Fruehe Dir., ComEd Ex. 4.0, 15:313 – 16:316.

The only proposed operating reserves adjustments are AG/AARP's and CUB's vacation and incentive pay proposals. Their rebuttal is similar to their direct testimony. Effron Reb., AG/AARP Ex. 2.0, 3:67 – 8:169; Smith Reb., CUB Ex. 3.0, 13:259 – 14:283. Staff's rebuttal adopted these proposals. Bridal Reb., Staff Ex. 16.0, 27:591 – 31:676. The proposals are improper. The current liability associated with vacation pay is short term in nature, and is not a source of funds that is financing rate base. Moreover, customers have not yet paid for the vacation pay, so there is no basis for a rate base reduction.[6] As to the current liability related to incentive pay, incentive pay is paid in February, and at that time the liability for the prior year decreases to zero. Similar to the current liability for vacation pay, this item cannot finance rate base. The proposed adjustments should be rejected. Fruehe Reb., ComEd Ex. 13.0, 12:254 – 14:295.

7. Other

[6] ComEd's rebuttal did revise its CWC analysis relating to vacation pay, as discussed in Section III.C.4 of this Pre-Trial Memorandum.

II. REVENUES

A. Potentially Uncontested Issues

1. Correction to Lease/Rental Revenues

ComEd's rebuttal made a correction to its figure for lease/rental revenues. Fruehe Reb., ComEd Ex. 13.0, 44:951-961. This correction is uncontested.

B. Potentially Contested Issues

1. Late Payment Charges Revenues

ComEd has allocated all late payment charges revenues, other than the portion credited to customers under its FERC-jurisdictional Transmission Formula Rate (TFR), to the other revenues credited against its revenue requirement, consistent with the Commission's Order in *ComEd 2010*. Fruehe Dir., ComEd Ex. 4.0, 30:624-626. AG/AARP has proposed that, if its positions on functionalization as to other issues are rejected, then as an "offset" 100% of late payment charges revenues be credited here, even though that would be a double count with the portion credited to customers under the TFR. That proposal has no principled basis, and is contrary to the ruling in *ComEd 2010*. AG/AARP's witness himself subtracted the late payment charges revenues credited against the TFR in his testimony in *ComEd 2010*. ComEd's allocation should be approved. Fruehe Reb., ComEd Ex. 13.0, 42:900 – 44:949. AG/AARP's rebuttal addresses this issue in an unclear manner that does nothing to rehabilitate its position. *See* Brosch Reb., AG/AARP Ex. 3.0, 3:50-53, 32:698-711.

2. New Business and Billing Determinants

ComEd's proposed Rate DSPP uses historical weather-normalized billing determinants in accordance with Section 16-108.5(c)(4)(H) of the Act, 220 ILCS 5/16-108.5(C)(4)(H). Houtsma Dir., ComEd Ex. 2.0, 4:71-86, 28:572-576; Fruehe Reb., ComEd Ex. 13.0, 44:964 – 45:967.

AG/AARP, for purposes of the initial period, proposes to cherry pick among 2011 data, by modifying the billing determinants to reflect 2011 growth in the number of customers but not the 2011 decrease in kWh delivered. AG/AARP's proposal is inconsistent with the Act, and with proper ratemaking practices. Also, the delivery services charges set for the second year under the formula rate will be determined using updated billing determinants. AG/AARP's one-sided proposal must be rejected. Fruehe Reb., ComEd Ex. 13.0, 44:968 – 46:991. AG/AARP's rebuttal did not respond to any of the above points, other than arguing that the annual re-setting of rates will not capture customer growth in prior years. *See* Effron Reb., AG/AARP Ex. 4.0, 9:203 – 10:215. AG/AARP's rebuttal cannot alter that its proposal is one-sided and improper.

3. Other

III. OPERATING EXPENSES

A. Overview

ComEd's original operating expenses total, before income taxes, in the Trailer Bill scenario, was $1,422,689,000. Fruehe Dir., ComEd Ex. 4.0, 3:51-56. That figure was based on 2010 FERC Form 1 balances, functionalization, applicable ratemaking adjustments, and the addition of the estimated 2011 plant additions and the 2011 change in depreciation expense less the applicable roll forward of the depreciation reserve to 2011. *Id*., 19:389 – 29:617. ComEd's rebuttal testimony, which reflected corrections and agreed or accepted adjustments, presented and supported a revised figure of $1,422,421,000. Fruehe Reb., ComEd Ex. 13.0, 18:374-375.

In addition to the overall figures and support in the direct testimony of ComEd witness Mr. Fruehe (*id*., 19:389 – 29:617), ComEd's operating expenses were supported primarily by the direct testimony of Ms. Blaise, ComEd Ex. 5.0, 44:932 – 55:1163; and Mr. Donovan, ComEd Ex. 6.0, 2:25-35, 4:77 – 6:112, 6:121– 8:164, 10:208 – 11:226, 14:279 – 19:400.

Staff and intervenors in their direct testimony proposed a number of operating expense adjustments. Those proposals were addressed by the rebuttal testimony of the above witnesses, Mr. Hemphill, and Ms. Houtsma. The contested proposed adjustments of Staff and intervenors, including all of their major adjustments and some of their other adjustments, are incorrect, as discussed in the remainder of this Section III of this Pre-Trial Memorandum.

B. Potentially Uncontested Issues

1. Distribution

ComEd's Distribution Operating and Maintenance ("O&M") expenses were $313,141,000 for 2010. After reflecting adjustments, a total of $312,853,000 in distribution O&M expenses recorded in FERC Accounts 580-598 is included in the revenue requirement. Fruehe Dir., ComEd Ex. 4.0, 20:421 – 21:430; Blaise Dir., ComEd Ex. 5.0, 45:952 – 46:965. There are no objections to ComEd's 2010 Distribution O&M expenses. Moreover, Staff witness Mr. Rashid testifies that he does not object to ComEd's proposed electric distribution O&M expenses for 2010. Rashid Dir., Staff Ex. 8.0, 11:232-34.

2. Customer Accounts Expenses Other Than Uncollectibles

Customer Accounts expenses other than uncollectibles expense are expenses recorded in FERC Accounts 901-903 and -905, and include the costs of maintaining and servicing customer accounts, *e.g.*, meter reading, record-keeping, and billing. Fruehe Dir., ComEd Ex. 4.0, 21:431 – 22:454; Donovan Dir., ComEd Ex. 6.0, 4:76 – 6:120. After adjustments to the 2010 FERC Form 1 balances, $179,197,000 of these expenses should be included in the revenue requirement. ComEd Ex. 13.3, Schedule C-1 Revised, p. 1, line 9; Donovan Dir., ComEd Ex. 6.0, 8:171-176, 10:208-226. There are no objections to the amount of these customer accounts expenses.

3. Uncollectibles Expense and Staff Rider Proposal

Uncollectible accounts expense is generally a function of revenues billed and has been assigned to the delivery services function by applying a revenue allocator to ComEd's total uncollectible expense recorded in the 2010 FERC Form 1, Account 904. $16,671,000 of uncollectible accounts expenses are included in the revenue requirement. Fruehe Dir., ComEd Ex. 4.0, 22:455 – 23:472; Donovan Dir., ComEd Ex. 6.0, 14:278 – 18:374.

Staff witness Mr. Knepler proposes that all uncollectible costs be recovered through incremental uncollectible cost factors, which are described in Rider UF-Uncollectible Costs ("Rider UF"), rather than having a base portion of uncollectible costs recovered through the application of delivery service charges and supply related base uncollectible cost factors. As part of this proposal, no uncollectible costs would be included in the delivery services revenue requirement. Knepler Dir., Staff Ex. 2.0, 3:48-52.

As for the recovery of delivery service uncollectibles, ComEd does not object to Mr. Knepler's proposal, provided that the Commission determines that such a change does not affect interclass cost allocation and is consistent with the rate design approved in *ComEd 2010*. Fruehe Reb., ComEd Ex. 13.0, 38:806 – 40:862; Hemphill Reb., ComEd Ex. 11.0, 31:639-54; Knepler Reb., Staff Ex. 14.0, 2:34 – 3:46. Mr. Fruehe proposes an additional adjustment to the reconciliation, which will be required if this proposal is accepted, to ensure that uncollectibles will be removed from the reconciliation calculations. Fruehe Reb., ComEd Ex. 13.0, 38:806 – 40:862.

ComEd witness Dr. Hemphill testifies that Mr. Knepler's proposal as it relates to supply uncollectibles should be addressed outside of this proceeding, as supply uncollectibles are collected through tariffs not at issue in this proceeding. Hemphill Reb., ComEd Ex. 11.0,

31:643-54. In his rebuttal, Mr. Knepler agrees that supply related uncollectibles are properly addressed outside of this proceeding. Knepler Reb., Staff Ex. 14.0, 2:34 – 3:46.

4. Customer Service and Informational Expenses

Customer service and informational expenses are recorded in FERC Accounts 906-910. Fruehe Dir., ComEd Ex. 4.0, 21:431-22:454; Donovan Dir., ComEd Ex. 6.0, 4:76 – 6:120. After adjustments to the 2010 FERC Form 1 balances, $10,535,000 of customer service and informational expenses should be included in the revenue requirement. ComEd Ex. 13.3, Schedule C-1 Revised, p. 1, line 10; Donovan Dir., ComEd Ex. 6.0, 8:171-176, 10:208-226. There are no objections to the amount of customer service and informational expenses.

5. Adjustments for Ratemaking, Other Tariffs, Past Orders, and Other

ComEd has voluntarily made downward adjustments to its 2011 operating expenses. The costs ComEd has removed from its operating expenses include rate-making adjustments, costs recovered through other tariffs, and voluntary exclusion. ComEd also reduced its operating expenses for costs recovered through other tariffs, and has reduced its operating expenses for expenses such as a portion of compensation costs of certain executives, half of its corporate jet costs, and certain lease expenses. It has also reduced its Other Revenues by removing the amounts applicable to transmission services. Fruehe Dir., ComEd Ex. 4.0, 32:662-677. There are no objections to these adjustments.

6. **Administrative and General Expenses**

a) Regulatory Commission Expense

ComEd accepts the proposal by Staff witness Knepler to remove $91,000 in procurement regulatory costs from ComEd's revenue requirement. Knepler Dir., Staff Ex. 2.0, 11:201-209; Fruehe Reb., ComEd Ex. 13.0, 41:871. Staff's rebuttal acknowledges that ComEd accepted

Staff's adjustment in ComEd's rebuttal revenue requirement. Knepler Reb., Staff Ex. 14.0, 7:127-129.

b) <u>Customer Deposits</u>

ComEd agrees with Staff's and AG/AARP's proposal to include $866,000 of interest on customer deposits in operating expenses rather than as a reduction to the balance of customer deposits included in rate base. Ostrander Dir., Staff Ex. 4.0, 2:34 – 3:44; Brosch Dir., AG/AARP Ex. 1.0, 52:1163-1168; Fruehe Reb., ComEd Ex. 13.0, 16:329 – 36, 42:890. AG/AARP's rebuttal acknowledges that ComEd accepted AG/AARP's adjustment as stated in ComEd's rebuttal testimony. Brosch Reb., AG/AARP Ex. 3.0 34:717 – 35:719. *See also* Section III.B.3 of this Pre-Trial Memorandum.

c) <u>Research & Development</u>

ComEd accepts the proposal by Staff witness Mr. Knepler to remove $14,000 in R&D expense that was found to be related to transmission from ComEd's revenue requirement. Knepler Dir., Staff Ex. 2.0, 12:220-226; Fruehe Reb., ComEd Ex. 13.0, 41:874. Staff's rebuttal acknowledges that ComEd accepted Staff's adjustment in ComEd's rebuttal revenue requirement. Knepler Reb., Staff Ex. 14.0, 7:130-132.

d) <u>Sporting Event Activities</u>

ComEd accepts the proposal by Staff witness Mr. Tolsdorf to remove $56,000 in professional sporting expenses from ComEd's revenue requirement. Tolsdorf Dir., Staff Ex. 6.0, 8:180 – 9:184; Fruehe Reb., ComEd Ex. 13.0, 41:872. Staff's rebuttal acknowledges that ComEd accepted Staff's adjustments in ComEd's rebuttal revenue requirement. Tolsdorf Reb., Staff Ex. 17.0, 1:20 – 2:23.

e) Outside Services

In order to narrow the issues in dispute, ComEd agrees with the Staff, AG/AARP, and CUB proposal to remove $692,000 in legal costs associated with the IRS dispute, which are related to generation, from its revenue requirement. Tolsdorf Dir., Staff Ex. 6.0, 9:188-191; Brosch Dir., AG/AARP Ex. 1.0, 49:1102-1104; Smith Dir., CUB Ex. 1.0, 46:1057-1059; Fruehe Reb., ComEd Ex. 13.0, 41:873. Staff's rebuttal acknowledges that ComEd accepted Staff's adjustment in ComEd's rebuttal revenue requirement. Tolsdorf Reb., Staff Ex. 17.0, 1:20 – 2:24.

f) Correction of Error Relating to Rider EDA

In order to narrow the issues in dispute, ComEd accepts the proposal by Staff witness Mr. Tolsdorf to remove $24,000 in Rider EDA legal costs from ComEd's revenue requirement. Tolsdorf Dir., Staff Ex. 6.0, 9:194-199; Fruehe Reb., ComEd Ex. 13.0, 41:873. Staff's rebuttal acknowledges that ComEd properly reflected the adjustment in ComEd's rebuttal revenue requirement. Tolsdorf Reb., Staff Ex. 17.0, 1:20 – 2:27.

g) Photovoltaic Pilot Costs

In order to narrow the issues in dispute, ComEd accepts the proposal by CUB witness Mr. Smith to remove $580,000 in Photovoltaic Pilot Costs from ComEd's revenue requirement. Smith Dir., CUB Ex. 1.0, 47:1080 – 48:1087; Fruehe Reb., ComEd Ex. 13.0, 42:891.

7. Regulatory Asset Amortization

ComEd witness Ms. Houtsma testifies that Appendix 7 provides an itemization of all of the components of regulatory asset amortization and describes which of those items are delivery services related. Houtsma Dir., ComEd Ex. 2.0, 21:430-32. Other than objections to ComEd's amortization of IEDT, discussed below under Potentially Contested Issues, there are no objections to ComEd's proposed amortization of regulatory assets. Moreover, Staff witness

Mr. Ostrander recommends that the Commission find the amount ComEd has proposed to include as an Unusual Operating Expense for the June 18, 2010 storm to be prudent and reasonable. Ostrander Dir., Staff Ex. 4.0, 6:114-121.

8. Pension Asset Funding – SERP ADIT Component

As discussed in Section III.C.5 of this Pre-Trial Memorandum, CUB witness Mr. Smith and AG/AARP witness Mr. Effron recommend that the ADIT associated with ComEd's Supplemental Employee Retirement Plan (SERP) be included in the calculation of the return on the pension asset rather than in rate base. The related adjustment to expense is an increase of $323,000. Effron Dir., AG/AARP Ex. 2.0 Rev., 7:136-146; Smith Dir., CUB Ex. 1.0, 57:1310-1312. ComEd agrees with this recommendation, and has reflected this change in ComEd 13.1, Sch. FR C-3 and Appendix 4. Fruehe Reb., ComEd Ex. 13.0, 11:220-225; Effron Reb., AG/AARP Ex. 4.0, 3:57-64.

9. Income Taxes Other Than Interest Synchronization

The amount of income taxes included in the revenue requirement is $196,201,000, which includes the impact of the 2011 plant additions. ComEd Ex. 13.3, Schedule C-1, p. 1, line 24. Income taxes have been calculated based on the expenses and miscellaneous revenues assigned or allocated to the delivery services function. Fruehe Dir, ComEd Ex. 4.0, 29:609-613. Setting aside a proposed interest synchronization adjustment that is derivative of other proposed adjustments, discussed below, there are no non-derivative objections to ComEd's amount of income taxes, in the event that ComEd's rebuttal revenue requirement otherwise is approved. To the extent that adjustments are approved, income taxes must be recalculated, but there is no dispute regarding the method of the calculation.

10. Depreciation & Amortization Expense, Including Staff's Withdrawn Proposal Regarding A Future Study

ComEd's depreciation expense as calculated in its rebuttal testimony was $405,551,000. ComEd Ex. 13.3, Schedule C-1 revised, p. 1, line 13. Staff witness Mr. Bridal originally proposed adjustments to ComEd's proposed method of calculating projected depreciation expense in conjunction with an adjustment to the calculation of projected accumulated depreciation, and he proposed that a new depreciation study be undertaken and submitted with the next formula rate filing following the order in this proceeding. Bridal Dir., Staff Ex. 5.0, 10:203 – 14:293. *See also* Section III.C.2 of this Pre-Trial Memorandum. In response to Mr. Bridal's concerns, Ms. Houtsma's rebuttal explained that a new depreciation study is unnecessary in light of the Commission's Order in ComEd's 2005 rate case that ComEd complete a depreciation study every five years, which ComEd has followed, with an upcoming depreciation study already planned for 2013. Houtsma Reb., ComEd Ex. 12.0, 18:395-405. Ms. Houtsma also proposed an alternate method of calculating depreciation expenses, set forth at ComEd Ex. 12.5. This calculation uses the depreciable bases in the most recent FERC Form 1 and the depreciation rates supported by the most recent deprecation study. Houtsma Reb., ComEd Ex. 12.0, 17:391 – 18:394. Mr. Bridal's rebuttal accepts ComEd's proposed new method of calculating depreciation expense as described in Ms. Houtsma's rebuttal and set forth in ComEd Ex. 12.5. Staff's adoption of this proposal is reflected in Staff Ex. 16.0, Schedule 16.04, although there are calculation errors in Staff's schedule. Mr. Bridal's rebuttal withdrew his recommendation that ComEd complete a new deprecation study, although he continued to recommend that ComEd consider the results of the most recent deprecation study completed prior to filing in all future formula rate or general rate filings. Mr. Bridal also recommended that ComEd Ex. 12.8 be updated to reflect changes set

forth in ComEd Ex. 12.5. Bridal Reb., Staff Ex. 16.0, 15:328 – 17:367. ComEd, in the interests of narrowing the issues, agrees to use the alternative depreciation calculation in ComEd Ex. 12.5, and is willing to update ComEd Ex. 12.5 with appropriate minor technical modifications.

11. Staff Proposal for Finding Regarding Non-Inclusion of Rate Case Expense in Initial Rates

ComEd agrees with Staff witness Mr. Ostrander's recommendation that the Commission not include any rate case expenses for this Docket in recovery in this proceeding, because they were not incurred in 2010. As Mr. Ostrander explains, rate case expenses incurred in 2011 and 2012 will be considered as part of the proceedings related to the recovery of costs for those years. Ostrander Dir., Staff Ex. 4.0, 5:89-106.

12. Gross Revenue Conversion Factor

ComEd's proposed Gross Revenue Conversion Factor ("GRCF") is 1.660. Fruehe Dir., ComEd Ex. 4.0, 32:679-681. Staff calculated the number to more decimal places, and differentiated it between the scenario of Illinois-jurisdictional uncollectibles expense being included in base delivery services charges versus included in Rider UF – Uncollectible Factors, 1.659750 versus 1.659613. Ebrey Dir., Staff Ex. 1.0, Sched. 1.07. ComEd does not object to Staff's calculations. The applicable Staff figure should be used, depending on whether the Commission approves Staff's rider position.

C. Potentially Contested Issues

1. Administrative and General Expenses

a) Total

ComEd's total Administrative and General ("A&G") Expenses that should be included in its revenue requirement are $340,673,000. ComEd Ex. 13.1, Schedule C-1 Revised, p. 1, line 12. Staff's and intervenors' contested adjustments to A&G expenses are incorrect.

b) <u>Restricted Stock</u>

ComEd's Key Manager restricted stock program is not an incentive compensation program. It is a deferred compensation program, designed to attract and retain key employees, under which Key Managers receive a portion of their compensation pro-rated over a three-year period in the form of shares of Exelon stock. Fruehe Reb., ComEd Ex. 13.0, 18:381-91.

AG/AARP witness Mr. Brosch, CUB witness Mr. Smith and Staff witness Ms. Ebrey propose that restricted stock payment amounts should not be included in ComEd's revenue requirement. Mr. Brosch argues that the award is driven by financial considerations rather than service quality and that ComEd has not adequately described the goals associated with the program. Mr. Smith argues that the program is incurred to improve the financial performance of Exelon and ComEd for the benefit of shareholders which is generally in opposition to minimizing costs to ratepayers. In addition to arguing that ComEd has not shown how the program benefits customers and that the payment is made in Exelon restricted stock units, Ms. Ebrey claims that the program is incentive compensation based upon net income or an affiliate's earnings per share. Their positions are incorrect. Retaining key managers that understand that the quality of service is key to ComEd's success is critical to achieving and maintaining a high level of customer service and reiterates that the goal of the program is retention of key individuals. Moreover, the program is in line with industry practices, the form of compensation is irrelevant, the payment is not entirely dependent on achieving the individual goals of each key employee, and the compensation is not dependent upon net income or an affiliate's earnings per share. Fruehe Reb., ComEd Ex. 13.0, 20:427 – 22:460. In rebuttal, Staff and the intervenors reiterate the arguments they made in their direct testimony in support of their proposals. Ebrey Reb., Staff Ex. 13.0, 17:378-394; Brosch Reb., AG/AARP Ex. 3.0 35:723 – 36:762; Smith Reb., CUB Ex. 3.0, 15:298 – 18:351. The Staff and intervenor proposals should be rejected.

c) **Incentive Compensation**

ComEd has two basic incentive compensation programs: the Annual Incentive Program ("AIP") and the Long Term Incentive Program ("LTIP"). Fruehe Dir., ComEd Ex. 4.0, 23:475-476.

AG/AARP witness Mr. Brosch and CUB witness Mr. Smith challenge the inclusion of 75% of Exelon Business Services Company ("BSC") AIP costs in ComEd's revenue requirement. In rebuttal, Staff adopts this proposed disallowance. Ebrey Reb., Staff Ex. 13.0, 18:400 – 20:451. BSC should be viewed in the same light as any other vendor, and its total costs for services should be based on the overall reasonableness of the charges without regard to individual components. No party to this proceeding has challenged the overall reasonableness of BSC's charges to ComEd. ComEd also disagrees with the interpretation of the Act espoused by Mr. Brosch, Mr. Smith, and Ms. Ebrey that the Act specifically excludes recovery of incentive compensation *of an affiliate* that is based on net income or earnings per share of an affiliate. Fruehe Reb, ComEd Ex. 13.0, 22:463 – 24:507; 220 ILCS 5/16-108.5(c)(4)(A).

Mr. Smith also proposes that the amount of AIP recovered through rates should be reduced by $2.248 million (jurisdictional) to limit the amount recovered through rates to 100% of target. In rebuttal, Staff adopts this proposal. Ebrey Reb., Staff Ex. 13.0, 18:400 – 20:451. While in the past the Commission approved adjustments that brought the test year AIP costs to 100% of target level, those filings were based upon historic test years and included "normalization" adjustments. The current filing differs because the rates will reflect actual costs incurred during the year and normalization adjustments are not required. AIP amounts above 100% of target are reasonable and prudent because if results are better than the target then the AIP award is higher but if the target is not met, then the AIP award is lower, thus providing a proper balance between achievement and award. The Commission determined in *ComEd 2010*

that ComEd's AIP metrics do benefit customers and payments based thereon are recoverable in rates. In addition, the adjustment in the plan's net income limiter did not result in any award payout greater in amount than if the net income limiter had not been in place and that ComEd Ex. 4.9 was created when ComEd was filing a traditional, as opposed to a formula, rate case. CUB's proposal should be rejected. Fruehe Reb., ComEd Ex. 13.0, 24:509 – 27:576. In rebuttal, CUB erroneously asserts that holding the net income limiter at 102.9 percent will result in a $1.564 million reduction in AIP costs. Smith Reb., CUB Ex. 3.0, 18:354 – 22:457.

IIEC witness Mr. Gorman proposes that ComEd's incentive payments included in the formula rate should be tied to the metrics ComEd has agreed to meet during the regulation period, and if ComEd fails to meet those metrics, no incentive payments be included in the formula. Gorman Dir., IIEC Ex. 1.0, 18:404 – 20:443. Such an advance cap on incentive compensation costs is improper. Such a cap is inconsistent with the annual formula rate structure and is not a valid means of measuring the prudently incurred and reasonable *actual* costs in that category. Moreover, price cap regulation is not reflective of the annual performance-based formula rate structure and it would be improper price cap regulation to cap only certain costs in isolation. Also, suggestions about future proceedings and measurements such as those of rate changes, and comments concerning costs that will be proposed and supported for the first time in the reconciliation process are not part of this proceeding. Hemphill Reb., ComEd. Ex. 11.0, 32:662-680.

d) <u>Perquisites and Awards</u>

ComEd provides performance based awards to employees for performing above expectations and providing excellent customer service and "other stock awards" are typically off-

cycle awards provided to certain executives as a sign-on incentive or as a retention award as a means to attract talent. Fruehe Dir., ComEd Ex. 13.0, 30:652-53, 31:662-665.

AG/AARP witness Mr. Brosch, CUB witness Mr. Smith and Staff witness Ms. Ebrey recommend that ComEd reduce the amount of perquisites and awards included in the revenue requirement through the application of the same adjustments that were applied in the Commission's Order in *ComEd 2010*. The adjustments include a four year normalization of retention awards, a 50% reduction to performance based awards and a complete removal of other stock awards. They claim that ComEd failed to provide evidence that could persuade the Commission to make a different determination here, that there is no evidence that shareholders do not benefit from these costs and that the stock awards and other perquisites include amounts allocated from affiliates and are excessively high.

However, it is unnecessary to normalize the 2010 amount of retention awards based on a four year average, because each year may include a higher or lower amount of a particular cost and as long as the amount is deemed prudent and reasonable by the Commission, the costs of the awards will tend to even out over time. Furthermore, there is no principled basis to limit recovery of performance based awards costs to 50% because customers ultimately benefit from a higher level of service. If the normalization adjustment is accepted by the Commission, ComEd proposes that certain revisions be made to App 7 of the formula rate template. Fruehe Reb., ComEd Ex. 13.0, 30:638 – 31:661.

The rebuttal testimony of Staff and intervenors largely reiterates arguments in support of their proposed disallowances that were made in their in direct testimony. Ebrey Reb., Staff Ex. 13.0, 21:455-464; Brosch Reb., AG/AARP Ex. 3.0 36:746-762; Smith Reb., CUB Ex. 3.0, 24:495 – 26:559. AG/AARP incorrectly claims that adjusting (rather than amortizing) what they

characterize as "excessive" retention awards paid in 2010 will set inception rates at a reasonable and normalized level. Brosch Reb., AG/AARP Ex. 3.0 36:746-762. Staff's rebuttal accepts ComEd's proposed revisions to App 7 of the formula rate template in the event the Commission approves the normalization adjustment. Ebrey Reb., Staff Ex. 13.0, 21:455-464.

e) <u>W&S Allocator</u>

A variety of costs, including Administrative and General expenses, certain components of General and Intangible plant, and certain components of ADIT are allocated using the Wages and Salaries ("W&S") allocator. Houtsma Reb., ComEd Ex. 12.0, 20:454-59. Staff witness Knepler proposes that ComEd's calculation of the W&S allocator be modified to allocate a portion of common costs to the production function. Staff's proposal is unnecessary because it would only push costs from being recovered in base delivery service charges to Rider PE and it is also improper because the costs Staff proposes to move to production are not production-related. Moreover, Staff does not explain how the costs allocated using the proposed revised W&S allocator that would be disallowed under his proposal would be recovered. If the Commission were to adopt Staff's proposal, then its Order should indicate that the costs are prudent and reasonable and shall be recovered through Rider PE. Houtsma Reb., ComEd Ex. 12.0, 20:439 – 21:481; Hemphill Reb., ComEd Ex. 11.0, 14:279 – 15:298. Staff's rebuttal testimony is similar to its direct testimony. Concerning whether costs Staff proposes to move to production are truly production related costs, Staff adds that in formulating its W&A allocator it relied on ComEd's 2010 FERC Form 1. Staff also states that while it is possible that some costs could be shifted to Rider PE, as ComEd suggests, the supply charges recovered through Rider PE are not at issue. Knepler Reb., Staff Ex. 14.0, 3:51 – 6:118. *See also* Section III.C.1.c of this Pre-Trial Memorandum.

f) **Charitable Contributions**

ComEd's charitable contributions should be approved. Staff witness Mr. Tolsdorf, joined by AG/AARP witness Mr. Brosch and CUB witness Mr. Smith propose disallowance of portions of ComEd's $5.9 million of charitable contributions relating to the University of Wisconsin and organizations that they do not believe provide for the public welfare. Mr. Brosch also claims that the information provided in ComEd's schedule listing ComEd's charitable contributions that exceed $5,000 is insufficient to determine whether the listed donations meet the Commission's statutory standard and he recommends that the Commission determine information about comparable levels of charitable contribution among Exelon affiliates to be relevant to the issue of the overall reasonableness of ComEd's proposed spending. In rebuttal, CUB adopts Staff's proposed disallowance. Smith Reb., CUB Ex. 3.0, 43:939 – 51:1121. The Act allows for the recovery of charitable contributions made for educational purposes and does not limit the recovery to only Illinois institutions. Moreover, Mr. Tolsdorf's definition of public welfare is incorrect, the cultural organizations excluded by Mr. Tolsdorf provide service to the public because they further cultural endeavors, and ComEd's donations support organizations that provide benefit to customers and the community. Most of the donations to community and economic development organizations for which ComEd is seeking recovery have been deemed reasonable and prudent by the Commission in prior Dockets. Fruehe Reb., ComEd Ex. 13.0, 31:337 – 35:749; Hemphill Reb., ComEd. Ex. 11.0, 11:215 – 14:277; 220 ILCS 5/9-227.

In rebuttal, Staff rejects the definition of "public welfare" presented by ComEd and argues for an improperly narrow definition of the term in its rebuttal. Tolsdorf Reb., Staff Ex. 17.0, 2:36 – 5:97.

g) Advertising Expense

The advertising expenses included in ComEd's revenue requirement should be approved. Staff witness Mr. Tolsdorf proposes a disallowance of $2.65 million of advertising expense that he considers promotional. He also claims that ComEd is trying to circumvent the Total Resource Cost test associated with energy efficiency and demand response programs found in Section 8-103 of the Act, 220 ILCS 5/8-103, and that recovery of the advertising costs through the base rate avoids the cap set forth under Rider EDA and could cause the energy efficiency programs to appear more cost effective than they actually are. Staff's claims are incorrect. The advertisements in question provide the reader with a message regarding energy efficiency or direct the reader to ComEd's website for money saving ideas. The advertising costs are recoverable because Section 9-225 of Act, 220 ILCS 5/9-225, allows for recovery of advertising that is related to safety, customer information, and energy efficiency. Finally, assuming that the advertising expenses were included in Rider EDA calculations for Plan Year 2 ("PY2"), the Total Resource Cost calculation for PY2 would not have been significantly affected. Fruehe Reb., ComEd Ex. 13.0, 35:756 – 36:780. In rebuttal, Staff erroneously asserts that the advertising costs it seeks to disallow are goodwill in nature and incremental to ComEd's historical expenditures of energy advertising. Mr. Tolsdorf also states that he did not testify that ComEd circumvented the TRC test as set forth in Rider EDA but that if the costs are allowed there is the potential that the TRC test could be circumvented. Tolsdorf Reb., Staff Ex. 17.0, 5:100 – 7:152.

h) Pension Expense

See Section V.C.4.b of this Pre-Trial Memorandum.

2. Taxes Other Than Income

The level of taxes other than income included in the revenue requirement is $109,085,000. ComEd Ex. 13.1, Schedule C-1 Revised, p. 1, line 14. In general, these include real estate taxes, the Illinois Electric Distribution Tax ("IEDT"), payroll taxes, and several other taxes. Fruehe Dir., ComEd Ex. 4.0, 29:599-606. Contested issues pertaining to IEDT are discussed in Section V.C.3 of this Pre-Trial Memorandum.

Whereas in prior rate cases real estate taxes were allocated using a variety of methods, in the formula they are allocated using a net plant allocator. That is consistent with how that allocation is made in determining transmission rates under ComEd's FERC-jurisdictional Transmission Formula Rate and provides a reasonable allocation to delivery services. Houtsma Dir., ComEd Ex. 2.0, 30:615-618. CUB witness Mr. Smith claims that this proposed jurisdictional allocation of property taxes should be rejected, recommending that the jurisdictional allocation method and findings of *ComEd 2010* should be used instead, thereby reducing ComEd's proposed jurisdictional allocation of property taxes by $3.345 million. Smith Dir., CUB Ex. 1.0, 14:286-305; Smith Reb., CUB Ex. 3.0, 39:832-853. AG/AARP witness Mr. Brosch testifies that ComEd's proposed allocation should not be approved without a showing by ComEd that previously submitted and approved cost allocation procedures for real estate taxes were otherwise inappropriate. Brosch Dir., AG/AARP Ex. 1.0, 43:958 – 44:967; Brosch Reb., AG/AARP Ex. 3.0, 31:694 – 32:697. In response to those recommendations, ComEd witness Ms. Houtsma explains that the allocation method chosen by ComEd is consistent with ComEd's FERC allocation and results in correct full cost recovery, neither over- nor under-recovery. The real estate tax allocation method applied in *ComEd 2010* did not necessarily produce a more accurate jurisdictional allocation, and the overall net plant allocator is a more reasonable measure for allocating real estate taxes as it portrays the overall relationship between the investments

made in transmission and distribution. ComEd's taxes other than income taxes should be approved. Houtsma Reb., ComEd Ex. 12.0, 31:671-690.

3. Regulatory Asset Amortization: IEDT

As noted under Section V.B.7 of this Pre-Trial Memorandum, most of ComEd's proposed regulatory asset amortization is not contested. Furthermore, Staff has not contested ComEd's recommendations pertaining to the Illinois Electric Distribution Taxes ("IEDT"), and Staff witness Mr. Ostrander recommends that the Commission find the amortized amount, unamortized balance, and deferred tax impact of ComEd's IEDT prudent and reasonable. Ostrander Dir., Staff Ex. 4.0, 6:123 – 7:137. However, Mr. Smith opposes ComEd's proposal, arguing that Section 16-108.5(c)(4)(f) does not mandate that the expense be amortized over five years and that it does not make sense to amortize the expense over five years. Mr. Smith proposes that IEDT should be amortized over three years. Mr. Smith also argues that ComEd is incorrect that under Mr. Smith's proposal that the IEDT should be amortized over three years the 2011 reconciliation will not reflect the continuing amortization of the IEDT and argues that, regardless of whether a three- or five-year amortization period is applied, the amortizations of the IEDT must be recognized in the Formula Rate Plan reconciliations for 2011 and 2012. Smith Reb., CUB Ex. 3.0, 26:561 – 30:640. Because the IEDT is well in excess of $10 million and involves a one-time unusual adjustment, it meets the spirit of Section 16-108.5(c)(4)(f) of the Act, 220 ILCS 16-108.5(c)(4)(f), and for purposes of this initial proceeding only, amortization reflecting a five year period should be applied. If the Commission agrees with Mr. Smith's suggestion, however, then only the first year of the three-year amortization is relevant to this initial proceeding, and the amortization would not be reflected in ComEd's 2011 reconciliation, because the IEDT credit was incurred in 2010. 2011 actual costs will be reconciled to the

weighted average of the revenue requirements in effect in 2011, making this issue moot. Fruehe Reb., ComEd Ex. 13.0, 37:784 – 38:804. Mr. Smith's proposal is incorrect as the actual figures from 2011 will be reflected in the reconciliation.

4. Pension Asset Funding

a) Pension Asset

As discussed in introductory Section I.C of this Pre-Trial Memorandum, ComEd's inclusion of $34,871,000 for recovery at a debt rate of return of its Pension Asset is authorized by the Act as well as past Commission practice and should be approved. ComEd Ex. 13.3, Schedule C-1 Revised, p. 1, line 16; 220 ILCS 5/16-108.5(c)(4)(B). Staff witness Ms. Ebrey recommends an adjustment to remove $34.4 million of pension funding costs from the revenue requirement, arguing that ComEd has no pension asset as it is defined by accounting literature. As a preliminary matter, ComEd requests recovery of pension funding costs in the amount of $34,871,000. Ms. Ebrey's total reflects a reduction of $193,000 due to a separate allocation adjustment that she proposes. Ms. Ebrey's recommended downward adjustment is based on an overly-narrow definition of the term "pension asset" that is incorrect under the financial accounting standards governing pensions, is contrary to prior Commission decisions, and is contrary to both the statutory language on pension cost recovery established by the Act and the legislative intent of the Illinois General Assembly. Houtsma Reb., ComEd Ex. 12.0, 4:86 – 12:262.

ComEd witness independent expert William Graf testifies that ComEd has properly recorded a pension asset even though the Exelon plan in which it participates is not overfunded, and the accounting method used by Exelon and ComEd is common within the utility industry

and consistent with well-accepted accounting practices for companies with one pension plan covering several subsidiaries. Graf Reb., ComEd Ex. 14.0, 3:53 – 7:135.

Ms. Houtsma testifies that because ComEd has contributed more to its pension plans than it has recovered through rates, a pension asset exists even under Ms. Ebrey's definition of the term. Houtsma Reb., ComEd Ex. 12.0, 4:86 – 12:262. Moreover, as described by Mr. Graf, it is neither appropriate nor necessary to "push down" ComEd's portion of the pension liabilities recorded on Exelon's books as Ms. Ebrey suggests. However, even if these liabilities were "pushed down" according to Ms. Ebrey's suggestion, that would have no impact on ComEd's pension asset on its balance sheet because the two "pushed down" accounting entries (the liabilities and the equal regulatory asset) would offset each other, and ComEd would still have made $1.039 billion more in pension contributions than it had incurred in periodic pension costs. Houtsma Reb., ComEd Ex. 12.0, 4:86 – 12:262; Graf Reb., ComEd Ex. 14.0, 3:54 – 5:106.

Moreover, the pension contributions that resulted in a pension asset have significantly lowered annual pension expense, bringing a benefit to customers, and as the Commission has correctly recognized in the last three ComEd distribution rate case orders, ComEd should be able to recover the funding costs of those contributions. ComEd's proposal to recover $34,871,000 in costs related to its pension funding should be approved for that reason and because the asset is appropriately accounted for, is reflected on its audited financial statements, would be unchanged even if pension liabilities recorded on the balance sheet of its parent were "pushed down," and the proposed cost recovery is in accordance with the provisions of the Act and consistent with prior Commission ratemaking decisions dating to 2006. Indeed, the Order on Rehearing in ComEd's 2005 rate case expressly approved recovery of a debt rate of return on ComEd's "Pension Asset." Houtsma Reb., ComEd Ex. 12.0, 4:86 – 12:262.

In her rebuttal, Ms. Ebrey testifies that although the Commission has approved ratemaking adjustments based on pension contributions in ComEd rate cases since Docket No. 05-0597, the Commission has not accepted the Company's requests for recovery of a pension asset in those rate cases. Ms. Ebrey argues that her definition of the term "pension asset" is not overly narrow but takes a broader view of the overall status of the pension plan and its components as it relates to the utility on a stand-alone basis, including 1) the current fair value of the assets; 2) the pension benefit obligation; and 3) the overall funded status of the plan. Ms. Ebrey argues that the pension plan should be considered on a stand-alone basis consistent with the treatment of other ratemaking issues, and further testifies that although she takes no issue with ComEd's accounting treatment of its pension plan, the fact that something is accounted for using generally accepted accounting principles does not make it automatically recoverable in base rates. Ebrey Reb., Staff Ex. 13.0, 4:72 – 14:326.

b) <u>Pension Expense</u>

The pension expense level included in ComEd's revenue requirement, $69,022,000, is correct and should be approved. Staff witness Ms. Ebrey proposes that if the Commission determines that it is appropriate for ComEd to recover pension funding costs, the correct level of 2010 pension expense should be $9.977 million lower than the amount included in the revenue requirement. $9.977 million is the jurisdictional reduction in pension expense resulting from special contributions made by ComEd in August and September of 2010 to improve the funded status of ComEd's pension plans. Staff's proposed adjustment reflects a misapplication of the pension accounting principles. The reduction in pension costs caused by pension contributions is reflected when the plan sponsor next measures pension costs. ComEd's independent actuary measures ComEd's pension costs every year reflecting census data and known contributions as

of December 31, and finalizes the cost determination for the current year in March. Known pension contributions prior to December 31 are included by the company's actuarial measurement of net periodic pension costs, and contributions not certain as of December 31 are not. Exelon's practice, which is appropriate under authoritative accounting guidance, is to utilize this actuarial valuation for the year, rather than re-measure pension costs throughout the year to incorporate additional contributions made at a later date. Staff's proposed adjustment to 2010 pension expense would artificially reduce 2010 costs and would result in under recovery of 2010 pension expense which would be inconsistent with the Act. Staff's adjustment is inconsistent with the statutory language relating to recovery of pension expense because the language states that a utility is entitled to recover pension expense if the costs are supported by an actuarial study and ComEd provided an actuarial report supporting jurisdictional pension expense of $69,022,000. Staff in substance is asking the Commission to make a *pro forma* adjustment to pension expense that is not justified on grounds of unreasonableness or imprudence nor on any other basis. Houtsma Reb., ComEd Ex. 12.0, 12:263 – 14:302.

In her rebuttal, Ms. Ebrey testifies that Ms. Houtsma's argument that Staff's proposed adjustment reflects a misapplication of the pension accounting principles is not valid, because the recommendation concerns a ratemaking adjustment, not an accounting adjustment. Ms. Ebrey also objects to the argument that her recommended adjustment would result in under recovery of 2010 costs, because the argument assumes that a reconciliation of 2010 FERC Form 1 data would occur at some point, but it will not. She argues that the rates that will result from the current formula rate proceeding will be used in the reconciliation of the revenue requirement based on the 2012 FERC Form 1 data and a weighted average of the revenue requirements that form the basis for rates charged to ComEd ratepayers during 2012. Ms. Ebrey testifies that her

proposed adjustment is based on the 2010 actuarial study, but that if the Commission does not agree that the adjustment to the 2010 actuarial study is consistent with the statute, the most current actuarial study (that of 2012) should be used as the basis for pension expense in the revenue requirement. Ebrey Reb., Staff Ex. 13.0, 14:327 – 15:354.

5. Income Taxes: Interest Synchronization

Interest synchronization is a key component of the revenue requirement, and was accurately calculated by ComEd in its filing and updated in rebuttal. Fruehe Dir., ComEd Ex. 4.0, 9:177 – 10:185, 33:685-689; ComEd Ex. 13.1, Schedules FR A-1, FR C-4. CUB witness Mr. Smith presented a derivative interest synchronization adjustment based on CUB's proposed rate base adjustments. CUB's derivative proposed adjustment should be rejected because its underlying rate base adjustments are incorrect. ComEd does agree that, to the extent that Commission approves any contested rate base adjustments, the interest synchronization figure will need to be recalculated.

6. Other

IV. RATE OF RETURN

A. Overview

The following chart summarizes the rate of return recommendations of ComEd and Staff, showing the individual components on which the overall weighted average cost of capital is based. No Intervenor witnesses proposed specific adjustments to ComEd's capital structure.

Party	Capital Structure	LTD Cost	STD Cost	ROE	ROR
ComEd	LTD 53.89% STD 0.57% Common Equity 45.54% Other 0.00%	6.37%	0.72%	10.05%	8.11%
Staff	LTD 53.35% STD 0.53% Common Equity 46.12% Other 0.00	6.42%	0.72%	10.05%	8.16%

B. Capital Structure

ComEd correctly proposes to use its actual capital structure as of December 31, 2010, adjusted as in past proceedings to remove goodwill. Staff witness Ms. Phipps proposes to use an average capital structure instead of a year-end capital structure. Ms. Phipps' recommendation is not appropriate and does not comply with the directive in 220 ILCS 5/16-108.5(c)(2) to use an actual capital structure. Moreover, Ms. Phipps' claims that average capital structures are not as easily manipulated and produce a more accurate measurement of ComEd's earned return on equity are incorrect. Vogt. Dir., ComEd Ex. 3.0, 2:33-36; Vogt Reb., ComEd Ex. 15.0 3:57 – 5:91.

Ms. Phipps also proposes using an average daily balance of long-term debt. That is inconsistent with the Act for the same reasons discussed above regarding use of an average capital structure. Vogt Reb., ComEd Ex. 15.0 5:92-107. In rebuttal, Ms. Phipps maintains that use of an average daily balance of long-term debt is appropriate, but states that Staff does not object to calculating that cost using monthly data. Phipps Reb., Staff Ex. 18.0 13:172-182.

Ms. Phipps also proposes removing $31,992,000 of long-term debt and $27,656,000 of equity from the capital structure based on her assessment of average monthly amounts of long-term debt and equity included in the CWIP accruing AFUDC rate. That is inappropriate because Ms. Phipps is directly assigning components of debt and equity and because her concern over

double counting is not warranted. If the Commission nonetheless were to accept this adjustment, then it would also need to make similar adjustments such as removing the $542,360,000 of long-term debt equal to the net pension asset which by statute (220 ILCS 5/16-108.5(c)(4)(D)) is required to earn a return equal to the weighted average cost of debt. Ms. Phipps does not argue with the principles supporting this corresponding adjustment. Rather, she opposes it solely on the basis that it would increase the cost of capital and ultimately the revenue requirement. Phipps Reb., Staff Ex. 18.0 19:287 – 20:306. Finally, Ms. Phipps' suggested change would have a *de minimus* effect on the revenue requirement and would unnecessarily complicate the formula rate equation. Vogt Reb., ComEd Ex. 15.0 5:108 – 7:148.

Last, Ms. Phipps proposes to remove approximately $10 million dollars of equity equal to ComEd's investment in Commonwealth Edison of Indiana ("ComEd of Indiana"), a wholly owned subsidiary of ComEd, on the basis that this adjustment is in accordance with Section 9-230 of the Act, 220 ILCS 5/9-230, in that it removes any incremental increase in cost of capital resulting from affiliation with non-utility companies. However, the proposal should not be adopted, because ComEd of Indiana is a utility, does not incrementally increase ComEd's risk, and does not increase ComEd's equity percentage. Vogt Reb., ComEd Ex. 15.0, 7:149 - 9:183.

In addition to the proposed adjustments described above, three witnesses raise additional issues for discussion that do not currently result in adjustments to ComEd's capital structure. Staff witness Kight-Garlisch discusses the prudence and reasonableness of ComEd's capital structure in light of Section 16-108.5 of the Act, 220 ILCS 5/16-108.5, and asks the Commission to order ComEd to "work with Staff to explore more leveraged capital structures for future years and provide a report to the Commission with its 2013 formula rate filing." Although Mr. Vogt

testifies that it is not reasonable to conclude that ComEd's capital structure could result in a rate of return that is "unreasonably high given the substantial decline in operating risk to which ComEd is exposed under section 16-108.5" as Ms. Kight-Garlisch proposes, ComEd is committed to work with Staff outside of this proceeding on this issue to understand these concerns. Vogt Reb., ComEd Ex. 15.0, 10:209 - 12:247; *see also* Hemphill, ComEd Ex. 11.0, 15:301-11. CUB witness Mr. Hempling raises similar issues as those discussed by Ms. Kight-Garlisch. In addition, IIEC witness Mr. Gorman proposes setting a common equity ratio limit of 55%. Mr. Vogt testifies that both of these issues should be addressed contemporaneously with the issues raised by Staff. Vogt Reb., ComEd Ex. 15.0, 11:248-265. In rebuttal, Ms. Kight-Garlisch rejects ComEd's offer to work with Staff voluntarily and instead reiterates that the Commission should *order* ComEd to work with Staff *and* submit a report to the Commission with its 2013 formula rate filing. Kight-Garlisch Reb., Staff Ex. 23.0 2:35 – 3:41. Mr. Gorman reiterates his proposal for a 55% equity cap in this proceeding and states that the appropriate common equity ratio cap to be included in the formula rate in the future should be addressed in a subsequent proceeding. Gorman Reb., IIEC Ex. 2.0 12:277 – 13:308.

C. <u>Cost of Short-Term Debt</u>

Ms. Phipps proposes changing the cost of short-term debt to the weighted average cost presented in ComEd's 2010 10-K, 0.72%. Although this proposal deviates from the method prescribed in the Commission's general rate case information requirements, 83 Ill. Adm. Code Part 285, Subpart G, ComEd is willing to accept this adjustment and, with the Commission's approval, to modify the formula prospectively. Vogt Reb., ComEd Ex. 15.0, 9:184-192.

D. Cost of Credit Facilities

Ms. Phipps also proposes to adjust the arrangers' fees for the community and minority owned bank credit facilities to 34% of total arrangers fees based on the presumption that ComEd participates in an Exelon wide community and minority-owned bank credit facility. That presumption is incorrect. Moreover, in the absence of a finding that these fees were unreasonable or imprudent, and they are not claimed to be, they should be fully recoverable on a jurisdictional basis in ComEd's rates. Vogt Reb., ComEd Ex. 15.0, 9:193 - 10:208. In rebuttal, Ms. Phipps argues that her proposed disallowance is not based on reasonableness or prudence, but rather on allocation between affiliated entities. Phipps Reb., Staff Ex. 18.0 24:382-392.

E. Cost of Long-Term Debt

ComEd presented the correct calculation of its cost of long-term debt. Staff witness Ms. Phipps suggests a cost of long-term debt based on the number of days outstanding for each debt issuance. That is not appropriate nor consistent with the Act, for reasons discussed in Section IV.B of this Pre-Trial Memorandum regarding use of averages. Even if the use of an average was permissible under the Act, the method of determining averages should be consistent when determining equity or debt, but Staff's proposal violates this principle by mixing and matching averages: daily for long-term and short term debt and monthly for equity, although as discussed above, Ms. Phipps partially addresses this mismatch in her rebuttal. Vogt Reb., ComEd Ex. 15.0 5:92-107.

F. Cost of Common Equity

The cost of common equity, or return on equity ("ROE"), is set by statute and no party contests this issue. As Mr. Vogt testifies and as Staff witness Ms. Phipps agrees, ComEd's ROE in this proceeding is 10.05%. By statute, this is calculated by taking the sum of (1) the average

for the applicable calendar year (2010) of the monthly average yields of 30-year U.S. Treasury bonds published by the Board of Governors of the Federal Reserve System in its Statistical Release of Selected Interest Rates – H.15; and (2) 580 basis points. Because the average treasury yield was 4.25%, the total allowed return on equity is 10.05%. The calculation of the 2010 average yield and the resulting ROE can be found on Schedules FR D-1 TB. Vogt Dir., ComEd Ex. 3.0, 4:65-76.

G. Overall Cost of Capital (Derivative)

The positions of the parties on ComEd's overall weighted average cost of capital, its rate of return ("ROR"), are shown on the chart included in Section IV.A of this Pre-Trial Memorandum.

V. COST OF SERVICE AND RATE DESIGN

A. Studies Submitted Pursuant to 2010 Rate Case Order

In direct testimony, ComEd proposed cost allocations and a rate design consistent with those approved by the Commission in ComEd's last rate case, ICC Docket No. 10-0467 ("2010 Rate Case"). For informational purposes, ComEd also presented the various studies and additional data (including illustrative Embedded Cost of Service Studies ("ECOSSs")) pursuant to Commission directives in the 2010 Rate Case Order. However, Dr. Hemphill testified that as these studies are related to rate design, they are not at issue in this proceeding. Hemphill Dir., ComEd Ex. 1.0, 7:131-137, 15:293-17:337. Staff and Intervenors did not disagree; however, Staff witness Mr. Peter Lazare raised a concern as to when these studies would be addressed and recommends that ComEd be ordered to integrate the studies into the cost of service study to be submitted for the revenue neutral cost of service and rate design proceeding. Lazare Dir., Staff Ex. 9.0, 5:114-8:196. ComEd disagrees, as the Commission directed ComEd to provide the

information and studies allowing parties to address and permitting the Commission to decide these issues in a subsequent rate design proceeding. The Commission *did not* order ComEd to propose those studies as ComEd's position. Hemphill Reb., ComEd Ex 11.0, 22:448-23:468.

In rebuttal testimony, Staff witness Mr. Lazare continues to improperly recommend that ComEd be ordered to integrate the studies into the cost of service study to be submitted for the revenue neutral cost of service and rate design proceeding. Mr. Lazare's arguments that Dr. Hemphill does not correctly characterize all ICC directives and that Dr. Hemphill's direct and rebuttal testimonies are inconsistent and without merit.

Further, Staff witness Mr. Rockrohr noted concerns regarding Study Report #3, the Distribution System Loss Study that segregates secondary and service conductor losses, and Study Report #5, the report that analyzes the use of Railroad customers' traction power facilities. However, he acknowledges that this is not the proceeding to review these reports. Rockrohr Dir., Staff Ex. 11.0, 4:71-76, 12:236-245. ComEd responded to these concerns and agrees that this is not the proceeding to address these reports. Blaise Reb., ComEd Ex. 17.0, 11:220-14:288; Born Reb., ComEd Ex. 18.0, 3:60-4:69.

In direct and rebuttal testimony, CTA and Metra also raised concerns about Study Report #2, regarding allocation of primary voltage costs for Railroad Class and Extra Large Load Class customers, but acknowledged that this is not the proceeding to address that study. However, CTA/Metra ask the Commission to direct ComEd to provided quarterly reports regarding the progress of Study Report #2. ComEd has worked and will continue to work with CTA/Metra regarding this study; thus, such a requirement is unnecessary.

B. **Rate Design**

Staff witness Mr. Lazare argues that ComEd incorrectly implemented the Straight Fixed Variable ("SFV") rate design. He concludes that ComEd's currently effective and proposed rates following the 2010 Rate Case Order are noncompliant. Lazare Dir., Staff Ex. 9.0, 8:205-13:308. Staff's arguments are untimely, unfounded and incorrect for several reasons. First, ComEd's compliance rates were fully and timely filed following the 2010 Rate Case Order. Pursuant to Commission rules, Staff reviewed and investigated the rates and informed ComEd that the rates were compliant with the 2010 Rate Case Order. No objection was made; no notice of any objection was given to the Commission or to ComEd; thus, the rates were deemed approved and became effective. Second, Mr. Lazare's argument that only 50% of fixed costs are to be recovered through fixed charges is based on a single sentence of the 2010 Rate Case Order, which is not placed in context, is read inconsistently with the Order's approval of a design that moves away from recovery of fixed costs through volumetric charges, and is ascribed an incorrect meaning to that sentence standing alone. The sentence in the 2010 Rate Order upon which Mr. Lazare relies, standing alone, says nothing about the recovery of *total* costs, and thus cannot form the basis of an argument that a rate design that recovers 50% of total costs through fixed charges incorrectly implements the SFV rate design. Further, to move the prior non-SFV rate design to Mr. Lazare's proposed rate design, the volumetric distribution facilities charge would have to be increased, just opposite of what the sentence actually states. Hemphill Reb., ComEd Ex. 11.0, 23:469-30:637.

Mr. Lazare, in rebuttal testimony, maintains that ComEd has incorrectly implemented SFV. Staff's arguments are without merit. ComEd does provide compelling argument supporting SFV. Staff relies on a strained reading of the Commission's Order in *ComEd 2010*.

C. Embedded Cost of Service Study

The proposed delivery service charges employ cost allocations that are consistent with the cost allocations employed in the development of delivery service charges in compliance with the 2010 Rate Case Order, which is the most recent Commission Order regarding a ComEd request for a general increase in its delivery service rates. Specifically, cost data used in this proceeding are from the ECOSS developed in accordance with the provisions of Part 285.5110 of 83 Illinois Administrative Code updated with 2010 data and with modifications that are consistent with directives in the 2010 Rate Case Order. Tenorio Dir., ComEd Ex. 10.0, 8:149-160. CTA and Metra raised certain concerns with regard to the allocation of the AMI costs to the Railroad customers. Bachman Dir., CTA/Metra Joint Ex. 1.0, 4:64-72. In rebuttal testimony, ComEd made certain corrections to the ECOSS, including adjustments to address the allocation of AMI costs. Tenorio Reb., ComEd Ex. 19.0, 2:35-5:104.

With regard to the Distribution System Loss Study, Staff witness Greg Rockrohr argues that ComEd's proposed Study, ComEd Ex. 7.1, should be rejected because it does not incorporate the updated Transmission System Loss Study filed on e-Docket by ComEd in December 2010 pursuant to the 2010 Rate Case Order. Instead Mr. Rockrohr recommends the Commission approve Study Report #7B, the Distribution System Loss Study submitted by ComEd for informational purposes in December 2010 (which incorporated the updated Distribution System Loss Study), or in the alternative, approve the Distribution System Loss Study approved in the 2010 Rate Case[7]. Rockrohr Dir., Staff Ex. 11.0, 2:31-8:159. Staff errs. First, Study Report #7 is a rate design issue that must be addressed in a later proceeding. Hemphill Reb., ComEd Ex. 11.0, 32:681-33:695. Second, ComEd's proposed Distribution

[7] ComEd Ex. 7.1 and Distribution System Loss Study approved in the 2010 Rate Case are identical except that ComEd Ex. 7.1 has been updated for 2010 class load.

System Loss Study, ComEd Ex. 7.1, is superior to the study approved in the 2010 Rate Case Order, because it is updated for the 2010 class load data, which reflects the year at issue in this proceeding. *Id.* at 2:20-3:59.

In rebuttal testimony, Staff, joined by DOE, continue to recommend the approval of the Distribution System Loss Study identified as Study Report #7B. ComEd does not agree with the Staff and DOE recommendation. However, ComEd plans to present Study Report #7B in surrebuttal testimony should the Commission approve the use of Study Report #7B.

Finally, Staff witness Rukosuev comments on and objects to the manner by which general and intangible plant is functionalized in ComEd's ECOSS. Rukosuev Dir., Staff Ex. 10.0, 8:171-19-459. Mr. Tenorio testified that ComEd's ECOSS functionalizes general and intangible plant in the same manner used in the development of the overall revenue requirement. Tenorio Reb., ComEd Ex. 19.0, 5:105-6:113. *See also* Section III.C.1.c. *supra* of this Pre-Trial Memorandum.

VI. OTHER FORMULA / TARIFF ISSUES

A. Reconciliation

1. Average rate base proposals

CUB witness Mr. Smith, AG/AARP witnesses Messrs. Effron and Brosch, and IIEC witness Mr. Gorman argue that the revenue requirement calculation for the reconciliation on Schedule FR-A-1 REC should use an average, rather than year-end rate base. ComEd demonstrated that this argument should be rejected for several reasons. First, use of a year-end rate base is consistent with the statute, which provides that the reconciliation be calculated consistently with the initially established revenue requirement to which it is reconcile. *See* 220 ILCS 5/16-108.5. The statute also is clear that the reconciliation rely on FERC Form 1 data for

the current year and not an average calculated using the prior and current calendar years. Second, the use of year-end rate base is consistent with traditional ratemaking principles as the timeline associated with the formula rate process is more akin to a historical test year. Third, regulatory lag is only reduced and not eliminated by the formula rate process. Finally, concerns that rates are expected to increase in future years and year-end rate base will cause ComEd to over earn the intended return on equity are unfounded. Houtsma Reb., ComEd Ex. 12.0, 32:691 - 35:776. The AG/AARP, CUB, and IIEC rebuttal as to this proposal is similar to their direct. Brosch Reb., AG/AARP Ex. 3.0, 6:128-11:244; Smith Reb., CUB Ex. 3.0, 40:854 - 43:930; Gorman Reb., IIEC Ex. 2.0, 1:17-6:140. In rebuttal, Staff has agreed with these intervenors. Bridal Reb., Staff Ex. 16.0, 32:704-37:823.

2. <u>Interest rate proposals</u>

Staff witness Ms. Ebrey, AG/AARP witness Mr. Brosch, and CUB witness Mr. Smith recommend alternatives to the proposed use of weighted average cost of capital to apply to the unrecovered/refunded reconciliation amount. These alternatives should be rejected as they would not compensate ComEd for the cost of capital during the reconciliation period. AG/AARP argument to use short term debt interest rate should be rejected. Short term debt matures in less than one year; however, the receipt of true up revenues for any given calendar year will not be complete until approximately three years after the start of the calendar year. Staff's proposal to use Commission-ordered customer deposits rate should also be rejected. There is no evidence that ComEd is able to finance any revenue shortfall at the customer deposit interest rate, which is currently 0%, other than through the availability of customer deposit balances, and the customer deposits available to ComEd are already assumed to be financing rate base and are a reduction to rate base. If Staff's proposal is adopted, the rate base reduction

should be reduced by unrecovered true-up amount in the applicable year. Finally, CUB's proposal to use the larger of weighted average cost of capital or the short term debt rate on over collections, and the smaller of the two on under collections should be rejected. CUB's asymmetrical proposal is one-sided and unprincipled. Houtsma Reb., ComEd Ex. 12.0, 35:777 - 37:812.

AG/AARP, CUB, and IIEC rebuttal as to this proposal is similar to their direct. Brosch Reb., AG/AARP Ex. 3.0, 11:246-12:269; Smith Reb., CUB Ex. 3.0, 35:748-757; Gorman Reb., IIEC Ex. 2.0, 6:141-8:195. In rebuttal testimony, Ms. Phipps disagreed with ComEd's proposal to apply an interest rate that equals the rate of return on rate base assets to reconciliation amounts because it incorrectly assumes that reconciliation amounts are subject to the risks as rate base assets. Instead, Ms. Phipps argues that an AAA-rated bond yield would be a fair and reasonable benchmark for establishing the interest rate on reconciliation amount. However, this argument must be rejected. Phipps Reb., Staff Ex. 18.0, 25:408-28:468. ComEd could not secure financing at such a rate; thus, such a benchmark would not allow ComEd to recover its carrying costs.

3. <u>After Tax Recommendation</u>

In direct and rebuttal testimony, AG/AARP witness Mr. Brosch recommends that the Commission direct ComEd to record a regulatory asset deemed to be a deferral of operating expenses, and that the deferred tax liability associated with that regulatory asset be applied as an offset to the basis on which reconciliation interest be calculated. This recommendation is unreasonable and should be rejected. The simple recording of a deferred income tax liability for accounting purposes does not provide a source of cash to ComEd to fund the revenue shortfall. Cash would only be provided if the deferred tax expense had simultaneously been recovered

through rates, which would not be the case here. Further, the fact that the operating expenses, which Mr. Brosch suggests be deemed to be deferred, are tax deductible when incurred is taken into consideration in the determination of the reconciliation amount, and therefore no further adjustment to the revenue requirement shortfall is appropriate. Houtsma Reb., ComEd Ex. 12.0, 37:813-824.

4. IIEC proposal re exclusion of earnings collar from reconciliation calculations

In direct and rebuttal testimony, IIEC witness Mr. Gorman proposes to remove the impact of the earnings collar from Schedule FR A-1 REC to Schedule FR A-1 because he does not believe it is part of the reconciliation determination. The proposal should be rejected as unnecessary. The earnings collar impact is appropriately presented in Schedule FR A-1 REC because the reconciliation in Schedule FR A-1 REC considers the actual results for the applicable calendar year, and the purpose of the collar is to determine how those actual results compare to the earnings collar thresholds. To the extent there is a collar adjustment, the results are plainly visible on Schedule FR A-1 REC, and they are appropriately carried forward to Schedule FR A-1 as part of the reconciliation value. Houtsma Reb., ComEd Ex. 12.0, 37:825 - 38:839.

B. Other proposals and positions regarding formula, tariff schedules and attachments, and processes

1. Staff

Staff witnesses Ms. Ebrey, Mr. Tolsdorf, Ms. Phipps, and Mr. Rukosuev made a number of recommendations to change the Formula Rate template. ComEd accepted some but not others. Houtsma Reb., ComEd Ex. 12.0, 38:840-39:867; ComEd Ex. 12.9.

Further, Staff had no objections to ComEd's for protocols regarding weather normalized billing determinants and allocation of common costs to customer classes. Lazare Dir., Staff Ex. 9.0, 13:310-14:339.

2. <u>IIEC</u>

IIEC witness Mr. Gorman makes many arguments concerning the formula rate tariff, including that it is too detailed, wholesale incorporation of workpapers into the formula rate should be eliminated, and that Commission should direct that all Part 285/286 information be provided in formula rate and reconciliation filings. He also makes other recommendations including, (1) the Commission maintain an open formula rate docket and that all Part 285/286 information be provided in that docket as soon as available; (2) an "ongoing or conditional intervention to all intervenors in this case for all future filings …."; and (3) the Commission commence general investigation of formula rates after in effect for 3 years. He also expressed concern that 2.5% residential rate increase threshold presents an incentive for ComEd to shift costs to other rate classes. Thus, he recommends that the Commission should exclude the effects of changes in class rate design in assessing 2.5% threshold.

Mr. Gorman's recommendations are not necessary and should be rejected. The definition of a formula rate is a rate that itself contains formulae that set charges in a standardized manner based on defined inputs transparently set out in the tariff itself. IIEC is asking the Commission to do the very opposite. ComEd's proposed Rate DSPP specifies the cost components that form the basis of the rate charged to customers with sufficient specificity to operate in a standardized manner and be updated annually with transparent information that reflects the utility's actual costs. Further, the specificity of Rate DSPP would aide and not hinder the Commission's ability to review ComEd's costs. Further, the EIMA already specifies the type of data to be provided in advance, and specifically addresses data of the type called for under Part 285. With respect to

IIEC's remaining recommendations, IIEC provides no authority for such recommendations, nor explains how as a practical matter they could be squared with the law, including the requirement that periodic cases be initiated and terminated by final Commission Orders. Hemphill Reb., ComEd Ex. 11.0, 16:312-20:398, 31:655-32:680.

VII. OTHER

VIII. CONCLUSION

For all reasons appearing of record and herein, the Commission should approve ComEd's filing, subject to those corrections and revisions made in its rebuttal testimony and any corrections and revisions that may appear in its forthcoming surrebuttal testimony.

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Respectfully submitted,

COMMONWEALTH EDISON COMPANY

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