

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY :
: No. 11-_____
Tariffs and charges submitted pursuant to :
Section 16-108.5 of the Public Utilities Act :

Direct Testimony of
KATHRYN M. HOUTSMA, CPA
Vice President,
Regulatory Projects
Commonwealth Edison Company

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1 **I. Introduction**

2 **A. Witness Identification**

3 Q. **Please state your name and business address.**

4 A. My name is Kathryn M. Houtsma. My business address is Commonwealth Edison
5 Company, Three Lincoln Centre, Oakbrook Terrace, Illinois 60181.

6 Q. **By whom and in what position are you employed?**

7 A. I am the Vice President, Regulatory Projects, of Commonwealth Edison Company
8 (“ComEd”).

9 **B. General Context and Purpose of Testimony**

10 Q. **What is the general context of your direct testimony?**

11 A. I address the new performance-based formula rate structure and process for setting
12 delivery service base rates. In summary, delivery service costs will be recovered through
13 a performance-based formula rate approved by the Illinois Commerce Commission
14 (“ICC” or “Commission”). The formula will specify the cost components that form the
15 basis of the rate and that will be updated annually with transparent and standardized
16 information to determine costs to be recovered during a “rate year,” which is a calendar
17 year.

18 Q. **What is the purpose of your direct testimony?**

19 A. The purpose of my direct testimony is to describe the overall concept of the formula rate
20 and the delivery service revenue requirement calculation formula that ComEd is
21 proposing. I also describe the formula rate template that we use in this case and intend to
22 use in future formula rate filings, and explain the rationale for the template and how it is

23 similar to the calculations we have used in prior cases and, in the limited respects when it
24 is different, explain why. The direct testimony of ComEd witness Martin Fruehe
25 (ComEd Ex. 4.0) presents and supports the specific data for 2010 and where appropriate
26 projected data for 2011 that “populate” ComEd’s proposed formula rate and from which
27 the revenue requirement for the first rate year is derived. Further support for the delivery
28 service revenue requirement’s components is provided in the direct testimony of Scott
29 Vogt (ComEd Ex. 3.0), Michelle Blaise (ComEd Ex. 5.0), Ronald Donovan (ComEd
30 Ex. 6.0), Michael Born (ComEd Ex. 7.0), and John Hengtgen (ComEd Ex. 8.0), as
31 identified in the direct testimony of Ross Hemphill (ComEd Ex. 1.0).

32 **C. Summary of Conclusions**

33 **Q. Please summarize the conclusions of your direct testimony.**

34 **A.** ComEd’s proposed formula rate, attached to my testimony as ComEd Ex. 2.1 and which
35 develops a delivery service revenue requirement template to be used in setting rates, both
36 in this case and in future filings, is reasonable and should be approved. We are asking
37 that the Commission, as part of its Order in this case, approve this formula rate template,
38 comprised of the attached Schedules and Appendices, for use now and in the future.

39 **D. Attachment to Direct Testimony**

40 **Q. What is the attachment to your direct testimony?**

41 **A.** The attachment to my direct testimony is the formula that is ComEd’s proposed formula
42 rate, set forth as ComEd Ex. 2.1.

43 **E. Background and Qualifications**

44 **Q. What are your responsibilities at ComEd?**

45 A. As Vice President, Regulatory Projects, my responsibilities include providing financial
46 expertise and support in various regulatory proceedings, including at the Commission.

47 Q. **What were your prior positions with ComEd and its affiliates?**

48 A. I began my employment with ComEd in 1979, and have held a variety of staff and
49 managerial positions in the financial, accounting, and regulatory areas for ComEd and
50 certain of its affiliates. Those positions include Director of Revenue Requirements and
51 Director of Regulatory Affairs (both with ComEd), Director of Investor Relations
52 (Unicom Corporation, ComEd's former parent company), Manager of Financial
53 Reporting, Vice President of External Reporting (Exelon Corporation, ComEd's ultimate
54 parent company), Vice President and Controller (ComEd), and Vice President – Finance
55 (Exelon Energy Delivery Company, LLC, ComEd's immediate parent company).

56 Q. **What is your educational background?**

57 A. I was awarded a Bachelors of Business Administration in Accounting from St. Mary's
58 College in 1979 and a Masters of Management from Northwestern University's Kellogg
59 Graduate School of Management, with a concentration in Finance, in 1983. In 1979, I
60 became a Certified Public Accountant in the State of Illinois.

61 **II. ComEd's Proposed Formula Rate**

62 Q. **Does ComEd's proposed formula rate develop a delivery service revenue
63 requirement?**

64 A. Yes. The formula rate template is set forth in ComEd Ex. 2.1.

65 Q. Does the proposed formula rate utilize a well-established revenue requirement
66 formula?

67 A. Yes, ComEd's formula rate follows the well-established revenue requirement formula:
68 Revenue Requirement = (Rate of Return x Rate Base) + Operating Expenses, and
69 incorporates the added directives set forth in Section 16-108.5(c) of the Public Utilities
70 Act.

71 Q. What are the "added directives" incorporated into the formula rate?

72 A. In addition to the traditional ratemaking requirements that provide for the recovery of a
73 utility's actual prudent costs, Subsections 16-108.5(c)(2) through (4) mandate a number
74 of inputs to the revenue requirement calculation. More particularly, those sections
75 require that the formula rate utilize the utility's actual capital structure (excluding
76 goodwill) for the year in question and a cost of equity calculated using a specific
77 methodology (the sum of the applicable calendar year average of 30-year U.S. Treasury
78 Bonds and 600 basis points, or 580 basis points if House Bill 3036 (the "Trailer Bill")
79 becomes law. Those sections also specify directives regarding: (A) recovery of incentive
80 compensation expense, pension and other post-employment benefits expense supported
81 by an actuarial study, severance costs, investment return on pension assets, formula rate
82 case expenses, and existing regulatory assets; (B) amortization of costs resulting from
83 workforce reduction program severance, changes in accounting rules, changes in law,
84 compliance with Commission-initiated audits, and single storm or other expenses; (C) the
85 use of historical weather normalized billing determinants; and (D) allocation methods for
86 common costs.

87 Q. **Does Section 16-108.5(c) contain other requirements?**

88 A. Yes. Section 16-108.5(c)(5) sets forth a return on equity collar (“ROE collar”) to be
89 implemented in the event that the utility actually earns a rate of return more than 50 basis
90 points higher or lower than the rate determined utilizing the specific methodology set
91 forth in Section 16-108.5(c)(3) and described briefly above. In addition,
92 Section 16-108.5(c)(6) provides for an annual reconciliation between the revenue
93 requirement determined pursuant to the formula rate and the revenue requirement that
94 would have been determined if actual cost information from the rate year itself had been
95 available at the filing date. The formula, in conjunction with Rate DSPP – Delivery
96 Service Pricing and Performance, incorporates all of these features of the statute, as more
97 specifically described in Section III of my testimony and by the testimony of Sharon
98 Kelly (ComEd Ex. 9.0).

99 Q. **Other than what you have discussed above, is determination of the formula rate
100 revenue requirement consistent with ComEd’s previous delivery service revenue
101 requirement determinations?**

102 A. Yes. For the most part, the revenue requirement is determined in the same manner as in
103 ComEd’s other delivery service rate cases. ComEd has identified a few limited changes
104 to the allocation of costs, however, and these changes are discussed in Section IV of my
105 testimony.

106 Q. **What is the starting point for determining the revenue requirement?**

107 A. Historical actual costs, plus projected plant additions and correspondingly updated
108 depreciation reserve and depreciation expense for the relevant calendar year.

109 Q. **Can you provide a summary of how the formula works?**

110 A. Yes. It reflects:

111 (1) costs recorded in the applicable FERC Form 1¹ in Distribution Accounts (plant
112 and operating expense), Customer Accounts (operating expense), and Customer
113 Service and Information Accounts (operating expense);

114 (2) the portions of costs of offering and providing distribution and customer service
115 recorded in the applicable FERC Form 1 in other Accounts;

116 (3) ratemaking adjustments to remove costs that are recovered through other tariffs or
117 are otherwise not recoverable through delivery service rates and to reflect
118 ratemaking reclassifications to provide for recovery of costs not recorded in the
119 referenced Accounts but that are recoverable through rates (e.g., charitable
120 contributions);

121 (4) net operating income representing the return on the utility's rate base, *i.e.*, the
122 application of the rate of return to its rate base; and

123 (5) appropriate adjustments to remove costs attributable to the transmission function.

124 All of the above is largely consistent with ComEd's prior practice in its five previous
125 delivery service rate cases.

126 Q. **Does ComEd's proposed formula rate have a general structure?**

127 A. Yes. The proposed formula rate is a workbook with two separate components. The first
128 component is a calculation of the revenue requirement based on historical data for the

¹ Federal Energy Regulatory Commission ("FERC") Form No. 1: Annual Report of Major Electric Utilities, Licensees and Others.

129 calendar year immediately prior to the year in which the rate is filed, plus an adjustment
130 for the projected capital additions and change in accumulated depreciation and
131 depreciation expense for the current year. The second component is a reconciliation
132 calculation that compares the actual revenue requirement for the rate year after it is
133 concluded to the revenue requirement that was reflected in the formula rate and used to
134 set rates for the rate year (which would have utilized prior year historical data plus the
135 projected data described above). If the reconciliation shows that the actual revenue
136 requirement for the rate year was more or less than the revenue requirement reflected in
137 rates for that period, the differential is added to or subtracted from the calculation
138 resulting from the next year's filing.² The workbook itself is an Excel spreadsheet, in
139 which the tabs are Schedules and supporting Appendices. The Schedules and
140 Appendices are described in more detail in Section III below and are attached as ComEd
141 Ex. 2.1.

142 **Q. Are the sources of the data in ComEd's proposed formula rate spreadsheets**
143 **standardized and transparent?**

144 **A.** Yes. Each of the spreadsheet tabs plainly identifies the sources of its data points, which
145 are either derived from data in ComEd's FERC Form 1, or are reconciled to the FERC
146 Form 1 by the application of clearly identified and supported data. To the extent that the
147 ILCC Form 21 has adopted reporting requirements that differ from FERC, those

² Thus, for example, proposed rates to be effective in June 2012 (filed in 2011) are based on 2010 costs plus 2011 projected plant additions, depreciation reserve and depreciation expenses for 2011. Proposed rates for 2013 (filed in 2012) will include: (1) 2011 costs plus 2012 projected plant additions and depreciation reserve and depreciation expenses for 2012 plus (2) adjustments reflecting a reconciliation between the revenue requirement in effect in 2011 and actual 2011 costs.

148 differences are reflected as well. In certain instances the data are drawn from ComEd's
149 General Ledger, in which case a clearly labeled supporting workpaper is provided. The
150 rate of return component uses certain data from the U.S. Department of the Treasury.

151 FERC Form 1 reports are publicly available on FERC's web site and are certified
152 by a company officer. Financial statement data is independently audited. The Treasury
153 Department data is also publicly available. ComEd's General Ledger data is the source
154 of the FERC Form 1 data as well as the utility's quarterly and annual reports with the
155 Securities and Exchange Commission, which are also publicly available.

156 **Q. Are costs automatically recoverable through the formula rate by virtue of their**
157 **inclusion in FERC Form 1?**

158 **A.** No. Costs that would otherwise not be recoverable through delivery service rates do not
159 become recoverable solely by their inclusion in FERC Form 1. As described in
160 Section III of my testimony, the formula continues to make the typical adjustments to
161 FERC Form 1 data that are customarily made in rate proceedings to remove costs that are
162 transmission related, are recovered through other tariffs or have historically not been
163 recovered through delivery service rates. In addition, all costs included in the formula
164 rate are subject to prudence and reasonableness reviews just as they would be in a
165 traditional rate proceeding.

166 **Q. Have any normalization adjustments been made to the data ComEd has presented**
167 **in the formula rate?**

168 **A.** No, Section 16-108.5(d)(3) specifically states that normalization adjustments are not
169 required. Moreover, normalization adjustments are not necessary in the context of a

170 formula rate. Because costs included in the formula rate will be reset each year, the need
171 to establish “normal” costs is not the same as it is when setting a traditional rate that will
172 remain in effect for several years or more.

173 Q. **What documentation has ComEd provided in support of its filing?**

174 A. We have included the kind of documentation and data that is ordinarily submitted in
175 connection with rate cases.

176 **III. Description of Formula Rate Template and Individual Components**

177 Q. **Please describe the formula rate template and the individual components.**

178 A. As discussed above, the formula rate template has been developed as a spreadsheet in
179 which the tabs are Schedules and Appendices. The Schedules used are A, B, C, and D.

180 A. **“A” Schedules**

181 Q. **Please list the formula rate “A” Schedules.**

182 A. The FR “A” Schedules are as follows:

- 183 • Schedule FR A-1 is summary “Net Revenue Requirement Computation.”
- 184 • Schedule FR A-1-REC is “Revenue Requirement Reconciliation Computation.”
- 185 • Schedule FR A-2 is “Allocators Computation.”
- 186 • Schedule FR A-3 is “Return on Equity (ROE) Collar Computation.”
- 187 • Schedule FR A-4 is “Reconciliation Calculation.”

188 Q. **What are the contents of Schedules FR A-1 and Schedule FR A-1 - REC?**

189 A. Schedule FR A-1 is a summary level calculation of the revenue requirement that will go
190 into effect in the year following the filing. The calculation utilizes the well established

191 formula: Revenue Requirement = (Rate of Return x Rate Base) + Operating Expenses,
192 using the components from supporting Schedules, and is based on the prior year historical
193 data plus projected plant additions, depreciation reserve and depreciation expense for the
194 year in which the filing is made. The Revenue Requirement is also adjusted, where
195 applicable, for the amount resulting from the reconciliation of the prior year to actual.
196 Schedule FR A-1 REC performs the calculation of the revenue requirement for the
197 reconciliation. FR A-1 REC is identical to FR A-1, except that it does not include the
198 projected data, and additionally provides for the application of the ROE Collar
199 adjustment.

200 Q. **What are the contents and data sources of Schedule FR A-2?**

201 A. Schedule FR A-2 sets forth the calculation of various allocators used in other Schedules
202 and Appendices to allocate common costs between functions (transmission, delivery
203 service, and, to a limited extent, supply). The specific allocators included on this
204 Schedule are:

- 205 • **Wages and Salaries Allocator**, which calculates delivery service wages as a
206 percentage of total wages. The data are derived from a filed report of the distribution
207 of salaries and wages by business function. The wages and salaries allocator is used
208 in supporting Schedules and Appendices to allocate portions of General and
209 Intangible (“G&I”) Plant, Administrative and General expenses, and other costs.
- 210 • **Net Plant Allocator**, which calculates the proportion of distribution net plant to total
211 net plant. The data are principally derived from a functionalization of plant and

212 accumulated depreciation. The net plant allocator is used to allocate plant-related tax
213 components between functions and for certain Other Revenues items.

214 • **Revenue Allocator**, which calculates the portion of total delivery service-related
215 retail customer revenues. The ratio is used to allocate uncollectible accounts between
216 functions.

217 • **Communications Equipment Allocator**, which represents the portion of total
218 communications equipment that is distribution-related based on a locational specific
219 study.

220 • **Easement Allocator**, which calculates the portion of distribution-related easements.
221 This ratio is then used to allocate to delivery service the revenues received from those
222 easements.

223 Q. **Were the allocators presented on Schedule FR A-2 used in prior ComEd rate cases?**

224 A. Yes. These allocators were used in prior ComEd rate cases and are calculated consistent
225 with the previous proceedings. In a limited number of instances the allocators are applied
226 to different cost elements, and those deviations are discussed in Section IV of my
227 testimony.

228 Q. **What are the contents and data sources of Schedule FR A-3?**

229 A. This is the calculation of the ROE collar that I referred to earlier. If the actual earned
230 return on common equity (after reflecting prudence and reasonableness disallowances)
231 for a rate year is more than 50 basis points (“bps”) higher than the ROE calculated under

232 the formula for that year (after reflecting penalties imposed for failure to meet metrics
233 and performance goals), then a credit in the amount of the excess will be given to
234 customers in the next formula rate. Similarly, if the actual earned ROE (after reflecting
235 prudence and reasonableness disallowances) is more than 50 bps lower than the formula
236 ROE (after reflecting penalties imposed for failure to meet metrics and performance
237 goals), a charge will be added to the next formula rate to recover the deficiency.
238 Schedule FR A-3 contains the methodology to calculate the earned ROE for the prior
239 calendar year. This calculation utilizes the actual delivery service revenues for the rate
240 year and the operating expenses, rate base, and capital structure determined consistent
241 with the other Schedules in the tariff for that year, and accordingly reflects any
242 ratemaking adjustments and Commission disallowances. This Schedule is completed as
243 part of the reconciliation calculation in Schedule FR A-1 REC.

244 Q. **What is the purpose of Schedule FR A-4?**

245 A. Schedule FR A-4 calculates the amount to be added/credited to the revenue requirement
246 to reflect the results of the reconciliation calculation. The calculation includes the
247 differential between (1) the revenue requirement in effect for the rate year, based on the
248 historical data and projected capital additions and (2) the revenue requirement calculated
249 for the rate year using actual data for that year. (The first reconciliation (*i.e.*, the
250 reconciliation filed in May 2012) will compare the revenue requirement for 2011
251 determined using the formula rate and 2011 actual costs to the revenue requirements in
252 rate orders approved by the ICC and in effect in 2011, on a weighted average basis). The
253 differential amount will be added/credited to the revenue requirement for the current

254 period, along with an interest charge/credit. Schedule FR A-4 also computes the interest
255 on the overage/underage based on monthly over or under recoveries.

256 **B. "B" Schedule**

257 Q. **Please list the formula rate "B" Schedules.**

258 A. The sole FR "B" Schedule is Schedule FR B-1, "Rate Base Summary Computation".

259 Q. **What are the contents and data sources of Schedule FR B-1?**

260 A. Schedule FR B-1 is the summary rate base Schedule. The Schedule has three primary
261 sections. The first section calculates net plant investment as of the end of the prior
262 calendar year, the second section summarizes other components of rate base that are
263 calculated in the supporting appendices, and the third section summarizes the projected
264 plant additions for the year in which the filing is made. Schedule FR B-1 aggregates all
265 of these components to compute total rate base.

266 Q. **What are the components of net plant investment, and how is it calculated?**

267 A. Net Plant in Service includes the following components:

- 268 • **Distribution Plant** as reported in the FERC Form 1 for the year preceding the filing.
269 This amount is adjusted to remove asset retirement costs (an accounting accrual that
270 is typically not reflected in rate base); costs that have been disallowed in prior rate
271 cases for reasons other than timing (principally disallowed capitalized incentive
272 compensation costs), but have not been written off for accounting purposes; and
273 Distribution Plant costs recovered through other tariffs (*e.g.*, Rider EDA – Energy
274 Efficiency and Demand Response Adjustment).

275 • **G&I Plant** as reported in the FERC Form 1 for the year preceding the filing, adjusted
276 to remove asset retirement costs, costs disallowed in prior cases, and costs recovered
277 through other tariffs. Because G&I Plant includes items such as office equipment,
278 software, and communications equipment that support both the delivery service and
279 transmission functions, an allocation of these costs to delivery service is necessary.
280 The wages and salaries allocator from Schedule FR A-2 is used to allocate G&I Plant,
281 except that Communications Equipment recorded in Account 397 is allocated on the
282 basis of a location-specific study that is provided as a supporting workpaper to the
283 filing. The allocators for G&I Plant differ in some respects from the allocators used
284 in prior ComEd rate cases. I discuss the differences and the rationale for them in
285 Section IV of my testimony.

286 • **Accumulated Depreciation** is calculated in a manner consistent with Plant in
287 Service, *i.e.*, the balances reported in the FERC Form 1 related to Distribution Plant
288 and G&I Plant are the starting point, and adjustments are made that correspond with
289 the adjustments to the related plant balances. For example, G&I Plant-related
290 accumulated depreciation is allocated using allocators used for the G&I Plant
291 balances.

292 Q. **What are the components of the second section of Schedule FR B-1?**

293 A. This section includes thirteen other rate base components, including Accumulated
294 Deferred Income Taxes, Construction Work in Progress, and Materials and Supplies. All
295 of these items are supported in an Appendix.

296 Q. **What do the Projected Plant Additions and Accumulated Reserve Adjustments in**
297 **the final section of Schedule FR B-1 represent?**

298 A. These represent the projected additions to Distribution Plant and G&I Plant for the year
299 in which the filing is made, and the roll forward of the depreciation reserve through the
300 end of the same period. These calculations are set forth in Appendix 1.

301 Q. **Please list the Appendices that support Schedule FR B-1.**

302 A. The Appendices for Schedule FR B-1 are: Appendix 1 – Capital Information, Appendix 2
303 - Customer Deposits Information, Appendix 3 - Cash Working Capital Information,
304 Appendix 4 - Accumulated Deferred Income Taxes Information, Appendix 5 - Deferred
305 Charges Information, and Appendix 6 - Property Held for Future Use in Rate Base
306 Information.

307 Q. **What are the contents and data sources of Appendix 1 - Capital?**

308 A. Appendix 1 - Capital includes the details of several items that feed into Schedule FR B-1,
309 including the following:

- 310 • Itemized ratemaking adjustments to Plant in Service and the accumulated
311 depreciation reserve to remove costs recorded in Distribution or G&I Plant and either
312 recovered through other tariffs or disallowed from rate base (for reasons other than
313 timing) in prior rate cases. Itemized adjustments to the depreciation reserve for Asset
314 Retirement Obligations are also included in this section.
- 315 • The calculation of Customer Advances for Construction included in rate base. This
316 amount begins with the total amount of Customer Advances for Construction, and

317 removes the portion of those advances associated with projects not related to delivery
318 service investment included in rate base.

- 319 • Projected capital additions and depreciation reserve change for the year in which the
320 filing is made, including an allocation of projected G&I Plant amounts using the same
321 allocators utilized for historical plant additions on Schedule FR B-1.

322 Q. **What are the contents and data sources of Appendix 2 - Customer Deposits?**

323 A. Appendix 2 - Customer Deposits provides the calculation of the thirteen month average
324 balances for customer deposits. The December 31 balances are derived from the FERC
325 Form 1, and the interim monthly balances are calculated in a manner consistent with the
326 December 31 balances. Pursuant to the ICC's order in Docket No. 10-0467, the entire
327 amount of customer deposits is applied as a rate base reduction (*i.e.*, a jurisdictional
328 allocation is not applied). The thirteen month average balance is reduced by the amount
329 of interest accrued on the customer deposits.

330 Q. **What are the contents and data sources of Appendix 3 - Cash Working Capital?**

331 A. Appendix 3 - Cash Working Capital presents the calculation of the cash working capital
332 ("CWC") allowance. The CWC calculation is based upon a lead/lag methodology
333 consistent with ICC practice and prior orders, and in this case is supported by the
334 testimony and workpapers of ComEd witness John Hengtgen (ComEd Ex. 8.0). The
335 critical assumptions in the analysis are largely consistent with the ICC's findings in
336 Docket No. 10-0467, except for a limited number of discrete issues discussed in further
337 detail by John Hengtgen.

338 Q. **Will a new lead/lag analysis be prepared each year?**

339 A. The basic structure of the CWC analysis is an analysis of the payment leads and revenue
340 lags for all of ComEd's revenues and expenses. The analysis of lead/lag days is detailed
341 and time intensive, and in general dramatic movement in this aspect of the analysis is not
342 expected on an annual basis. Therefore, in my opinion, absent a change in law that has a
343 significant impact on the lead/lag days, a reasonable approach would be to update the
344 CWC analysis annually to reflect current revenue and expense data and perform an
345 updated study of the lead/lag days only every three years.

346 Q. **What are the contents and data sources of Appendix 4 - Accumulated Deferred
347 Income Taxes ("ADIT")?**

348 A. This Appendix provides the components of the reduction to rate base for ADIT. The
349 Appendix is supported by a workpaper that provides a detailed itemization of all of the
350 components of the ADIT balance and the nature of the associated tax timing difference.
351 The Appendix then performs a jurisdictional allocation by applying an allocation factor
352 from Schedule FR A-2. The Appendix provides a jurisdictional allocation of each
353 component, again supported by the associated work paper.

354 Q. **What are the contents and data sources of Appendix 5 - Deferred Charges?**

355 A. Appendix 5 - Deferred Charges itemizes the various regulatory assets and deferred
356 charges that are delivery service related and included in the determination of rate base,
357 and the manner in which those items have been allocated to delivery services. Similar to
358 Appendix 4, Appendix 5 is supported by a workpaper that reconciles the amounts
359 included in rate base to the total amount included on ComEd's balance sheet.

360 Q. **What are the contents and data sources of Appendix 6 - Property Held for Future**
361 **Use in Rate Base?**

362 A. This Appendix provides a listing of all of the properties reported as Property Held for
363 Future Use, and states whether the intended use of those properties is for transmission or
364 distribution facilities. This Schedule would be applicable only if Property Held for
365 Future Use is requested in rate base, and as Martin Fruehe testifies, ComEd is not
366 requesting the inclusion of Property Held for Future Use in this initial filing.

367 **C. "C" Schedules**

368 Q. **Please list the formula rate "C" Schedules.**

369 A. The FR "C" Schedules are as follows:

- 370 • Schedule FR C-1 is "Expense Summary Computation."
- 371 • Schedule FR C-2 is "Depreciation and Amortization Expense Computation."
- 372 • Schedule FR C-3 is "Pension Funding Costs Computation."
- 373 • Schedule FR C-4 is "Taxes Computation."

374 Q. **What are the contents and data sources of Schedule FR C-1?**

375 A. Schedule FR C-1 is a summary of the operating expenses and taxes other than income
376 included in the revenue requirement. Operating expenses include distribution and
377 customer related O&M expenses and Administrative and General (A&G) expenses.
378 These expenses are then adjusted to remove items recovered through other tariffs or
379 customarily not recovered through rates. These adjustments are itemized in Appendix 7
380 and described in greater detail later in this section of my testimony. After making these
381 adjustments, a portion of A&G expenses is allocated to the transmission function using a

382 wages and salaries allocator. Taxes Other than Income are also summarized on this
383 Schedule, and allocated between functions using the allocators from Schedule FR A-2.
384 Appendix 7 provides further itemization of Taxes Other than Income.

385 Q. **What are the contents and data sources of Schedule FR C-2?**

386 A. Schedule FR C-2 calculates depreciation and amortization expense. Adjustments to
387 historical data for depreciation of Distribution and G&I Plant are made to remove
388 amounts recovered through other tariffs or that represent disallowed plant costs as
389 described above. Schedule FR C-2 also includes the forecasted change in depreciation
390 expense, which is calculated in further detail in Appendix 8.

391 Q. **What are the contents and data sources of Schedule FR C-3?**

392 A. This Schedule shows the calculation of pension funding costs, consistent with the
393 directive that the pension asset should be allowed an investment return based on the
394 weighted average cost of long-term debt as of the end of the applicable calendar year.
395 Schedule FR C-3 reflects the pension asset, reduced for the related accumulated deferred
396 income taxes. The wages and salaries allocator is applied to the balance to determine the
397 jurisdictional pension asset. This amount is then multiplied by the weighted average cost
398 of long-term debt from Schedule FR D-1, Line 14 to determine the annual pension
399 funding cost.

400 Q. **What are the contents of Schedule FR C-4?**

401 A. Schedule FR C-4 calculates the effective income tax rate and the tax effect of the interest
402 deductions. The income tax rate is based on statutory income tax rates for the same year

403 as the historical cost data, in this case 2010. Permanent tax differences and amortization
404 of Investment Tax Credits are also summarized on this Schedule.

405 Q. **Please list the Appendices for the FR “C” Schedules.**

406 A. The Appendices for the FR “C” Schedules are: Appendix 7 – Expense Information,
407 Appendix 8 – Depreciation Information, Appendix 9 - Permanent Tax Impacts
408 Information, Appendix 10 - Other Revenues Information, and Appendix 11 - Franchise
409 Delivery Service Value Information.

410 Q. **What are the contents and data sources of Appendix 7 - Expense?**

411 A. Appendix 7 - Expense supports Schedule FR C-1 and has the following components:

- 412 • Operating Expense Adjustments itemizes each of the adjustments to O&M expense
413 on Schedule FR C-1 to remove items typically not recovered through delivery service
414 rates (such as industry memberships and non-recoverable advertising expense), or to
415 reclassify costs recorded in below-the-line accounts but historically recovered
416 through delivery service rates (such as charitable contributions). This section of the
417 Appendix also removes O&M costs recorded in Distribution, Customer, and A&G
418 Accounts recovered through other tariffs, such as energy efficiency costs recovered
419 through Rider EDA. Finally, this section of the Appendix itemizes and removes costs
420 for which ComEd has voluntarily elected not to seek recovery, such as certain
421 executive compensation costs.
- 422 • Regulatory Commission Expenses recorded in Account 928 and determined to be
423 related to delivery service are included in this section, and supported by a workpaper

424 that itemizes the various proceedings to which the costs relate. Rate case expenses
425 related to this initial proceeding will be amortized over 3 years.

426 • Uncollectible costs are identified and allocated to delivery service based on a revenue
427 allocator.

428 • Adjustment is made to amortize over 5 years statutorily-specified expenses greater
429 than \$10 million, consistent with subsections (c)(4)(C) and (F) of Section 16-108.5.

430 • Amortization of regulatory assets. This section itemizes all of the components of
431 regulatory asset amortization recorded in Account 407.3, and describes which of
432 those items are delivery service related.

433 • Taxes Other than Income – itemizes all of the taxes other than income by type, and
434 sets forth the manner in which each tax is allocated to the delivery service function.

435 Q. **What are the contents and data sources of Appendix 8 - Depreciation?**

436 A. Appendix 8 itemizes ratemaking adjustments to depreciation and amortization expense to
437 remove amounts recovered through other tariffs, as well as depreciation related to plant
438 costs that have been permanently disallowed from rate base but have not been written off
439 of ComEd's books (e.g., capitalized incentive compensation costs disallowed in prior
440 cases). Appendix 8 also calculates the projected change in depreciation expense for the
441 current calendar year.

442 Q. **How is the projected change in depreciation expense calculated?**

443 A. The Appendix calculates an average depreciation rate for each functional class of plant
444 (*i.e.*, Distribution, G&I) for the prior historical year by dividing the depreciation expense
445 as reported in the FERC Form 1 by the average Plant in Service balances for the prior
446 historical year. The resulting average rate is then applied to the projected plant additions
447 for the current calendar year to estimate the increase in depreciation expense.

448 Q. **What are the contents of Appendix 9 - Permanent Tax Differences?**

449 A. This Appendix itemizes adjustments to taxable income that are not normalized (*i.e.*, are
450 permanent rather than timing differences). The adjustments are allocated to delivery
451 service using one of the allocators from A-2, and applied as an adjustment to income
452 taxes on Schedules FR C-4 and FR A-1.

453 Q. **What are the contents of Appendix 10 - Other Revenues?**

454 A. Appendix 10 itemizes all of the sources of revenue other than from retail sales of
455 electricity and how each item is allocated to the delivery service function.

456 Q. **What are the contents of Appendix 11 - Franchise Service?**

457 A. Appendix 11 calculates the value of delivery service provided to municipalities under the
458 terms of municipal franchise agreements. The cost of this service is recovered under
459 Rider FCA – Franchise Cost Additions. Appendix 11 estimates the costs of the franchise
460 service by multiplying the kilowatt hours (by rate class) provided to municipalities per
461 the franchise agreement by the average delivery service charge for each rate class.

462 **D. “D” Schedules**

463 Q. **Please list the formula rate “D” Schedules.**

464 A. Schedule FR D-1 is the “Cost of Capital Computation” and Schedule FR D-2 is “Average
465 Yield on Treasury Securities Computation.”

466 Q. **What are the contents and data sources of Schedule FR D-1?**

467 A. Schedule FR D-1 is a summary Schedule reflecting the calculation of ComEd’s overall
468 weighted average cost of capital. It has two sections. The first outlines ComEd’s sources
469 of capital and calculates the percentage of capital attributable to short- and long-term debt
470 and common equity. The second section provides the cost of common equity, the cost of
471 short- and long-term debt, weights each according to the capitalization ratios calculated
472 in the first section of the Schedule, and adds the cost of ComEd’s credit facilities to
473 derive the overall weighted average cost of capital. The data in this section are generally
474 derived from the FERC Form 1 and the ILCC Form 21. The equity balance is calculated
475 directly from those sources, and is adjusted to remove the portion associated with
476 goodwill. The balances and costs of short- and long-term debt are calculated in
477 accordance with the provisions of Subpart G, Sections 285.4020 and 285.4030 of the
478 Commission’s rules.

479 Q. **How is the cost of common equity calculated?**

480 A. The cost of common equity is calculated as the sum of the monthly average yields of 30-
481 year Treasury bonds provided on FR D-2 plus 600 basis points, except that for purposes
482 of the first reconciliation (*i.e.*, for calendar year 2011) the cost of equity will be the
483 weighted average cost of equity approved by the Commission for the rate orders that
484 were in effect in 2011. If the Trailer Bill becomes effective the cost of common equity is
485 calculated as the sum of the monthly average yields of 30-year Treasury bonds provided

486 on FR D-2 plus 580 basis points, except that for purposes of the first reconciliation (*i.e.*,
487 for calendar year 2011) the cost of equity will be the sum of the 30-year Treasury Bond
488 yields plus 590 basis points. Pursuant to the performance metrics provision of Section
489 16-108.5, schedule FR D-1 also provides for a reduction to the ROE in the event the
490 performance metrics are not achieved.

491 Q. **What are the contents and data sources of Schedule FR D-2?**

492 A. Schedule FR D-2 shows the calculation of the average monthly market yield on the
493 30-year Treasury bill, the rate used to calculate the cost of common equity in the formula.
494 The Schedule provides the average of the daily yields for each month and then averages
495 those monthly averages. The data used in this calculation are available from the H.15
496 Selected Interest Rate report, available on the website of the Board of Governors of the
497 Federal Reserve Board.

498 Q. **What are the contents and data sources of Appendix 12 – Short-term Debt?**

499 A. Appendix 12 calculates the balances and costs of short-term debt and the cost of
500 maintaining ComEd's lines of credit. These costs and balances of short-term debt are
501 calculated according to the Commission's prescribed methods. The methodology for
502 calculating short-term debt amount and cost and the cost of maintaining ComEd's lines of
503 credit is identical to that presented in ComEd's most recent rate case, Docket No. 10-
504 0467. The monthly debt balances and interest cost data are from ComEd's General
505 Ledger.

506 Q. **What are the contents and data sources of Appendix 13?**

507 A. Appendix 13 calculates the balance and cost of ComEd's long-term debt. These are also
508 calculated in accordance with the Commission's prescribed methods, and the
509 methodology is again identical to that presented in Docket No. 10-0467. The detailed
510 itemization of long-term debt issuances in Appendix 13 comes from the ILCC Form 21.

511 **E. Specific Provisions of the Formula**

512 Q. **Has ComEd attempted to include the directives set forth in Subsections 16-108.5 (c)**
513 **and (d) in its proposed formula rate?**

514 A. Yes.

515 Q. **Does the formula rate provide for recovery of incentive compensation expense that**
516 **is based on the achievement of operational metrics, including metrics related to**
517 **budget controls, outage duration and frequency, safety, customer service, efficiency**
518 **and productivity, and environmental compliance, but not for the recovery of**
519 **incentive compensation that is based on net income?**

520 A. Yes. Incentive compensative expense is recorded in various operating expense accounts
521 included in FR C-1. Each year ComEd will provide the amount of the incentive
522 compensation expense included in the formula rate, and the goals upon which the
523 incentive compensation is based. The amounts of incentive compensation expense for
524 2010 and the respective goals are included in the testimony of Mr. Fruehe (ComEd Ex.
525 4.0). Similar schedules will be provided in future updates. Additionally, the exclusion of
526 any amounts related to net income goals is provided for in Appendix 7 of the formula
527 (see line 12).

528 Q. **Does the formula rate provide for the recovery of pension and other post-**
529 **employment benefits expense that are supported by an actuarial study?**

530 A. Yes. Pension and other post-employment benefits expense (*e.g.*, retiree health care
531 expenses) are recorded in Administrative and General Expenses and are included in the
532 formula rate on Schedule FR C-1, Line 1, column (F). The amount of pension and post-
533 retirement health care expenses included in the rate for 2010 are provided in the
534 testimony of Mr. Fruehe (ComEd Ex. 4.0), along with the supporting actuarial study and
535 the reconciliation of the expense amounts to the study. Similar schedules will be
536 provided in future updates.

537 Q. **Does the formula rate provide for recovery of severance costs, to be amortized over**
538 **5 years if greater than \$10 million?**

539 A. Yes. Severance expenses are recorded in the various operating expense accounts shown
540 in Appendix 7. Line 27 on Appendix 7 provides for amortization over 5 years if the
541 severance expense in any year is greater than \$10 million

542 Q. **Does the formula rate provide for an investment return on the pension asset based**
543 **on the weighted average cost of long-term debt as of the end of the applicable**
544 **calendar year?**

545 A. Yes. Schedule FR C-3 calculates an investment return on the pension asset (net of
546 accumulated deferred income taxes) based on the weighted average cost of long-term
547 debt as of the end of the year calculated in Schedule FR D-1.

548 Q. **Does the formula rate provide for recovery of expenses related to this ICC**
549 **proceeding and to future proceedings to update the rate?**

550 A. Yes. Appendix 7 provides for the recovery of Regulatory Commission Expenses related
551 to distribution, which would include these proceedings and the subsequent proceedings to
552 update the formula rate (see line 22). Appendix 7, Line 29 also provides that the cost of
553 this initial proceeding be amortized over 3 years. The costs of this proceeding will be
554 incurred in 2011 and 2012, and will be reflected in the update filings for each of those
555 years. Costs incurred in 2011 for this proceeding will be amortized over the years 2011-
556 2013, and costs incurred in 2012 for this proceeding will be amortized over the years
557 2012-2014. A detailed itemization of the actual costs incurred will be provided in
558 support of those costs as part of the filing that includes cost recovery. As described by
559 Mr. Fruehe (ComEd Ex. 4.0), the initial calculation of the revenue requirement is based
560 on 2010 expense data and accordingly does not include any expenses associated with this
561 proceeding.

562 Q. **Does the formula rate provide for the amortization over a 5 year period of certain**
563 **charges that are greater than \$10 million as specified in 16-108.5(c)(4)(F)?**

564 A. Yes. Appendix 7 provides for the amortization of these types of costs over a 5 year
565 period.

566 Q. **Does the formula rate provide for the recovery of existing regulatory assets over the**
567 **periods previously authorized by the Commission?**

568 A. Yes. Appendix 7 sets forth an itemization of the regulatory asset amortization included
569 in the formula rate. The period over which each of the assets is being amortized will be

570 provided in a supporting workpaper along with the order authorizing recovery over the
571 specified period.

572 Q. **Does the formula rate provide for the use of historical weather normalized billing**
573 **determinants?**

574 A. Yes. The formula rate spreadsheet that my testimony supports does not utilize billing
575 determinants, however, as described by Sharon Kelly (ComEd Ex. 9.0), Rate DSPP
576 provides for the use of historical weather normalized billing determinants.

577 Q. **Does the formula rate provide for the allocation of common costs?**

578 A. Yes. As described earlier in my testimony, Schedule FR A-2 provides cost allocators that
579 are used to allocate costs that are attributable to both the transmission and distribution
580 portions of ComEd, such as General and Intangible Plant, and Administrative and
581 General Expenses. Additionally, virtually every schedule in the Appendix is designed to
582 remove any costs that are not applicable to the delivery services function so that only
583 those costs that support the delivery services function are included in Rate DSPP.

584 IV. **Non-Statutory Allocation Changes**

585 Q. **How do the calculations set forth in the formula compare to the calculation of a**
586 **revenue requirement in ComEd's traditional rate cases?**

587 A. Overall, the methodology used to calculate the revenue requirement under the formula is
588 very similar to the revenue requirement calculation utilized in traditional rate cases and
589 the vast majority of the components are calculated as in prior cases.

590 Q. **What are the differences in the calculations?**

591 A. I would note four differences in allocation of costs:

592 • G&I Plant: The formula rate uses a direct assignment study for Communications
593 Equipment, the largest component of G&I Plant, and a wages and salaries
594 allocator for the remainder. In ComEd's Article IX rate cases, Communications
595 Equipment was also allocated via direct assignment while the remainder of G&I
596 Plant was allocated using a variety of methodologies and allocators. For example,
597 Accounts 389 and 390 (Land and Structures and Improvements) were previously
598 allocated through a combination of a Property Usage analysis and the wages and
599 salaries allocator. However, the Property Usage analysis applied to only about
600 15% of the amounts recorded in those accounts, with the remaining 85% being
601 allocated through the use of a general allocator. Preparation of the Property
602 Usage analysis is very time consuming, subjective, and subject to change over
603 time as departments relocate; therefore I believe that application of a salaries and
604 wages allocator for the entirety of Accounts 389 and 390 provides a reasonable
605 alternative without sacrificing accuracy. Similarly, Account 394 (Tools, Shop
606 and Garage Equipment) was previously allocated by use of a gross plant allocator,
607 and while it is not unreasonable to assume that the usage of this equipment will
608 vary in proportion to the type of plant investment, it also is reasonable to assume
609 that the usage of tools will correlate to a labor-based allocator because the tools
610 and equipment are used by employees. Neither method is perfect, although both
611 can be considered reasonable. The wages and salaries allocator is also used by
612 FERC in the determination of the transmission rate, resulting in consistency

613 between jurisdictions and ensuring that the costs are neither over-recovered nor
614 under-recovered.

615 • Real Estate Taxes: In prior rate cases real estate taxes were allocated using a
616 variety of methods; in the formula they are allocated using a net plant allocator.
617 This is consistent with how that allocation is made in determining transmission
618 rates and provides a reasonable allocation to delivery service.

619 • Revenues received from finance charges: In prior rate cases these revenues
620 received from customers were allocated based upon a revenue allocator; because
621 these revenues are similar in nature to late payment charges, the formula applies
622 nearly 100% of these revenues to delivery service consistent with the
623 Commission's treatment of late payment charges in Docket No. 10-0467. The
624 formula reduces the amount of late payment charges and finance charges by the
625 small amount included in the Transmission Formula rate.

626 • Depreciation Expense for projected plant additions is estimated by applying
627 historical class average depreciation rates to the plant additions, rather than on a
628 project by project basis.

629 Q. **Does this complete your direct testimony?**

630 A. Yes.