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this report, Staff concluded that “the revenue requirement calculations reflected in the filing are consistent with the provisions of Public Act 98-15.” *Id.* at 4. The Commission concurred with Staff’s conclusions.

On June 5, 2013, the Commission entered an Order approving ComEd’s formula rate in Docket No. 13-0386. In that Order, the Commission determined that ComEd’s formula rate and the resulting revenue requirements fully complied with PA 98-0015, and directed ComEd to “submit the same Filed Rate Schedule Sheets, with updated revision numbering, and an effective date of June 6, 2013.” *Commonwealth Edison Co.*, ICC Docket No. 13-0386 (Order June 5, 2013) at 3. No party sought rehearing of that Order, no party appealed, and no party sought a stay.

Petitions to Intervene were filed in the instant proceeding by the Citizens Utility Board (“CUB”), the Illinois Attorney General’s Office (“AG”) and the Illinois Industrial Energy Consumers (“IIEC”). The ALJs granted these petitions. In addition, the City of Chicago (“City”) filed an appearance. Counsel for the Commission Staff (“Staff”), ComEd, CUB, AG, IIEC and the City appeared at these hearings.

Various parties presented testimony. ComEd presented the testimony of Christine M. Brinkman, Director, Rates & Revenue Policy, and Martin G. Fruehe, Manager, Revenue Policy.

Staff presented the testimony of Richard W. Bridal, Accountant, Accounting Department, Financial Analysis Division.

The People of the State of Illinois (“AG”) presented the testimony of Michael L. Brosch, Principal of Utilitech, Inc., and David J. Efron, Consultant.

The City of Chicago (“City”), the Citizens Utility Board (“CUB”), and the Illinois Industrial Energy Consumers (“IIEC”) (collectively, “CCI”) presented the testimony of Michael P. Gorman, Managing Principal at Brubaker & Associates, Inc.

An evidentiary hearing was convened in this docket at the Commission’s Chicago Office before duly authorized Administrative Law Judges (“ALJs”) on October 24, 2013.

II. PA 98-0015 COMPLIANCE

A. Do the Tariffs Filed on May 30, 2013 by ComEd Correctly Calculate Interest on ComEd’s Reconciliation Balance as Authorized by the Public Utilities Act?

ComEd’s Position

It is ComEd’s position that its approved formula rate and tariffs filed on May 30, 2013 comply with the requirements of the PUA and correctly calculate interest on its reconciliation balances. ComEd states that the reconciliation adjustment is a regulatory

asset or liability that reflects the difference between the revenue requirement used to establish the initial rates for a given rate year (in the current FRU proceeding, 2012) and the revenue requirement that recovers the actual costs that were incurred in that calendar year. ComEd asserts that PA 98-0015 recognizes that there is a time value of money and that, when there is an under-recovery, ComEd must finance that under-recovery – the difference between its actual costs and the amounts reflected in delivery service charges for a given rate year – until it is included in charges two years later.

ComEd further states that prior to PA 98-0015, that interest rate was set based on a two-year, and then on a short-term, debt cost. *Commonwealth Edison Co.*, Docket No. 11-0721 (Rehearing Order Oct. 3, 2012) at 36; *Commonwealth Edison Co.*, Docket No. 12-0321 (Order Dec. 19, 2012) at 86. ComEd asserts that the aim of the previous interest rates was to enable ComEd to finance the shortfall with only debt and, most recently, with only short-term debt rather than with all the components of ComEd's capital structure, as ComEd financed its other assets. *Commonwealth Edison Co.*, Docket No. 11-0721 (Rehearing Order Oct. 3, 2012) at 33-36; ComEd Init. Br. at 4. ComEd notes that PA 98-0015 rejected that premise, legislatively voided the Commission decisions based on that premise, and directed that the time value of money was to be based on ComEd's whole capital structure. 220 ILCS 5/16-108.5(d)(1) and (k); ComEd Init. Br. at 4. PA 98-0015 directed that the interest rate (*i.e.*, the time value of money) applicable to the delay in receiving (or refunding) the reconciliation adjustment is “to be calculated at a rate equal to” ComEd's WACC. 220 ILCS 5/16-108.5(d)(1)¹; *see also* 220 ILCS 5/16-108.5(k)(2) and (3). ComEd argues that the law legislatively confirms that ComEd finances these under-collections with its full capital structure, and that any continued suggestions that ComEd either can or actually does do something else is not only contrary to the evidence, but inviting an unlawful decision. ComEd Init. Br. at 5.

ComEd further argues that to recover any financing costs, it is necessary to recognize the added tax costs associated with the equity component of the capital financing that portion of the reconciliation balance. *Id.* In ComEd's view, this includes taxes that will need to be paid as a result of the cash collected for the reconciliation, as any revenue that ComEd receives for the interest on the reconciliation balance is subject to income taxes, and must be recovered in addition to the actual carrying costs related to the reconciliation. *Id.*; ComEd Ex. 1.0 CORR. at 14. ComEd asserts that if the interest rate is not grossed up for this added tax cost, the additional revenues will not be grossed up for the impact of income taxes and ComEd will be unable to recover or refund its full carrying costs related to reconciliation. ComEd Ex. 1.0 CORR. at 19. ComEd submits that the straightforward principle that WACC must be adjusted for this tax effect has been recognized for decades in the context of WACC applied to rate

¹ The relevant portion of Section 16-108.5(d)(1) provides *in toto* as follows: “Any over-collection or under-collection indicated by such reconciliation shall be reflected as a credit against, or recovered as an additional charge to, respectively, with interest calculated at a rate equal to the utility's weighted average cost of capital approved by the Commission for the prior rate year, the charges for the applicable rate year.”

base, and its critical importance is no different in this context. *Id.* at 16-17; ComEd Ex. 2.0 at 4.

ComEd observes that Staff, the AG, and CCI argue that because the language of Section 16-108.5(d)(1) does not explicitly provide for “*earnings or return* on the reconciliation balance,” but instead specifically addresses the calculation of interest at a prescribed interest rate, ComEd cannot recover income tax costs. Staff Init. Br. at 5; AG Init. Br. at 11-12; CCI Init. Br. at 6-7. In contrast, ComEd asserts that the legislature in Public Act 98-0015 made clear that setting the reconciliation interest at a rate other than a utility’s weighted average cost of capital was inconsistent with the original provisions and intent of EIMA, and emphasized that in specifying interest was to be calculated at a rate equal to WACC it was giving binding effect to the provisions of House Resolution 1157, adopted by the House of Representatives of the 97th General Assembly, and Senate Resolution 821, adopted by the Senate of the 97th General Assembly:

(k) The changes made in subsections (c) and (d) of this Section by this amendatory Act of the 98th General Assembly are intended to be a restatement and clarification of existing law, and intended to give binding effect to the provisions of House Resolution 1157 adopted by the House of Representatives of the 97th General Assembly and Senate Resolution 821 adopted by the Senate of the 97th General Assembly that are reflected in paragraph (3) of this subsection.

220 ILCS 5/16-108.5(k)²; ComEd Init. Br. at 6. Moreover, ComEd notes that the House and Senate Resolutions make absolutely clear that the intent of requiring the reconciliation to be “with interest” was to ensure that the utility and customers are made whole when a reconciliation adjustment is necessary:

WHEREAS, The Energy Infrastructure Modernization Act further provides in subsections (c) and (d) of Section 16-108.5 that those amounts to be credited or charged to customers following the annual reconciliation process under the performance-based formula rate shall be “with interest” *so the utility will be made whole for unrecovered amounts that were prudently and reasonably incurred and customers will be made whole for amounts they overpaid, if any; and*

WHEREAS, Such interest is intended to be set at the utility’s weighted average cost of capital, determined in accordance with the statute, which represents the reasonable cost and means of financing a utility’s investments and operating costs, *so that the utility and customers are made whole when charges or credits are necessary to reconcile to actual prudent and reasonable investments and costs.*

² Paragraph (3) of subsection (k) includes a specific reference to “interest calculated at a rate equal to the utility’s weighted average cost of capital.” *Id.*

Senate Resolution 821, 97th General Assembly, at 2-3; House Resolution 1157, 97th General Assembly, at 2-3 (emphasis added); ComEd Init. Br. at 6-7. In light of this legislative evidence, ComEd argues that the proposals to exclude the tax effects of receiving or paying interest on the reconciliation balance in calculating interest equal to a utility's WACC would prevent the utility and customers from being made whole when charges or credits are necessary to reconcile to actual prudent and reasonable investments and costs; as such, these proposals are contrary to EIMA and must be rejected.

ComEd further argues that Staff asks the Commission to read into the statute a prohibition not expressed, or intended, by the General Assembly, and to read out of the law words carefully inserted. ComEd Reply Br. at 3-4; *People ex rel. Birkett v. Dockery*, 235 Ill. 2d 73, 81 (2009) (It is a cardinal rule of statutory construction that courts "cannot rewrite a statute, and depart from its plain language, by reading into it exceptions, limitations, or conditions not expressed by the legislature."); *Solich v. George & Anna Portes Cancer Prevention Ctr. of Chicago, Inc.*, 158 Ill. 2d 76, 83 (1994) (Court not at liberty to depart from the plain language and meaning of the statute by reading into it exceptions, limitations or conditions that the legislature did not express.). ComEd submits that PA 98-0015 specifically directs utilities and the Commission to "calculate" an interest rate applicable to the reconciliation balance that is equivalent to WACC – the weighted average cost of the utility's capital structure. WACC has a tax cost, which no one can deny. Moreover, ComEd asserts that the General Assembly could have directed utilities to collect interest at the same annual percentage value as is set for its WACC, but it did not. ComEd Reply Br. at 4. It specifically directed that the utility "calculate" the collected interest rate at a rate which is equivalent to the WACC. According to ComEd, tenets of statutory interpretation require that the language must be given meaning; it cannot be read out of the statute simply because the General Assembly did not spell out that the calculation necessarily includes equity, debt, and taxes. *Id.*; *Hill v. Relyea*, 34 Ill. 2d 552, 555 (1966) ("Absolute criteria whereby every detail necessary in the enforcement of a law is anticipated need not be established by the General Assembly."). ComEd argues that even though the law does not specifically use the word tax, if taxes are ignored the interest rate and the WACC rate will not be equal. *Id.*

ComEd asserts that because its full capital structure includes both debt and equity components, ComEd must calculate a WACC-based interest to recover its costs – one of these financing costs, according to ComEd, is taxes. ComEd Init. Br. at 7; ComEd Ex. 4.0 at 6. Staff witness Bridal acknowledges that "the Commission routinely grosses up for income taxes the revenues it authorizes utilities in a rate case to recover from ratepayers ... [and this] allow[s] the utilities to earn the authorized return even after they have paid income taxes owed." Staff Ex. 2.0 at 3. ComEd argues that the genesis of these tax costs is plain: the portion of the interest that pays the equity cost component of the WACC will be fully taxable without any related deduction; in contrast, the portion that covers the debt cost component of WACC results in no taxable income. ComEd Init. Br. at 7. ComEd notes that when assets and/or liabilities are financed through the capital structure as a whole, *i.e.*, at a rate equal to the corresponding

WACC for that capital structure, the debt portion of WACC recovers an equal amount of interest expense which is deductible for tax purposes. ComEd Ex. 1.0 CORR., at 14. ComEd asserts that just as in every rate case where the full cost of the capital that finances utility assets must be recovered, the portion attributable to equity results in taxable income that must also be recovered, while the portion attributable to debt does not. ComEd Init. Br. at 7.

Staff witness Mr. Bridal claims that the gross-up of the WACC for the effect of income taxes is not necessary because the reconciliation amount is the difference between two revenue requirements that were already grossed-up for taxes. Staff Ex. 1.0 at 3. ComEd does not dispute that the reconciliation amount is the difference between the two revenue requirements that include a gross-up for taxes. However, ComEd argues that the difference between the two revenue requirements is recorded as additional revenues (or, conversely, a reduction of revenue) to ComEd, which has separate tax impacts. ComEd Init. Br. at 8. ComEd further clarifies its point, stating that the fact that the principal amount on which interest will be earned reflects taxes related to that principal does not affect the fact that the interest itself will result in still greater tax that is not reflected in the separate gross-up. *Id.* Mr. Bridal's claim that the revenue requirements already consider taxes completely disregards the tax effects related to the interest. According to ComEd, without the income tax gross-up on the equity portion of the WACC, these additional revenues are not grossed up for the impact of income taxes and ComEd will be unable to recover or refund its full carrying costs related to the reconciliation; such a result conflicts with EIMA's intent to allow ComEd the opportunity to recover its actual costs. *Id.* at 5.

ComEd argues that Staff's view that recognizing EIMA tax costs is inconsistent with Commission practice in rider reconciliations (Staff Ex 1.0 at 3, 4-5) is inapposite, as traditional reconciliation proceedings and the EIMA reconciliation process are not similar. ComEd Init. Br. at 8. EIMA ratemaking is aimed at providing accurate recovery of rate year revenue requirements. According to ComEd, other "reconciliations" do not involve a reconciliation of a utility's full delivery services revenue requirement or provide for the recovery of interest set at the WACC. *Id.* A better example in ComEd's case is the cash working capital calculation in ComEd's purchased electricity adjustment rider. There, the cost of capital is grossed up for taxes to account for the full cost of financing the lag (or lead) related to procuring electricity supply for ComEd customers. The rate year reconciliation balance is similar in that it is a lag (or lead) on recovery of ComEd's net revenue requirement for an individual rate year and the full cost of its financing should be recovered (or refunded). *Id.* at 8-9.

ComEd further notes that the reconciliations Staff points to are not efforts to ensure complete recognition in rates of a utility's full revenue requirement, which EIMA not only intends but mandates. ComEd Ex. 3.0 at 8-9. For example, Staff focuses on rider recovery of Water/Sewer Qualified Infrastructure Plant Surcharges ("QIPS") in support of its claim. While QIPS involves recovery of specific additional plant investments (Staff Ex. 1.0 at 5), ComEd notes that it does not reconcile the revenue requirement and does not provide for full recovery of all reasonable and prudent costs

of service (including tax costs). ComEd Init. Br. at 9. According to ComEd, the only situation that is truly comparable to the instant situation is the application of WACC in the context of establishing a utility's full revenue requirement; it is not contested that WACC is grossed up for income tax effects in that context. *Id.*

Finally, Staff witness Mr. Bridal points to the Commission's decisions in Docket Nos. 11-0721 and 12-0321. While those dockets did not approve an interest rate that had an equity component and thus had no occasion to consider taxes, Staff makes much of the fact that ComEd did not gross-up the proposed interest rate in those dockets. Staff Ex. 1.0 at 6. ComEd does not dispute this fact, but instead points out that the evidence shows that to have been an oversight, not a conscious decision. ComEd Ex. 2.0 at 2-4. As ComEd explained, there was no actual reconciliation involved in Docket No. 11-0721, and, therefore, all balances would have been zero. ComEd Reply Br. at 6. Moreover, ComEd has consistently argued that it could not change the formula in Docket No. 12-0321, as that was an update docket. ComEd Init. Br. at 9; ComEd Ex. 2.0 at 3-4. ComEd asserts that its actual and longstanding position on this issue is quite clear. In previous rate cases stretching back decades, ComEd consistently grossed-up the equity return component of WACC for purposes of recovering the costs of assets financed with its full capital structure. *Id.*

ComEd argues that the AG simply defies the statute and the resolutions, claiming that they do not "require consideration of the Company's incurred actual incremental financing costs or incremental income taxes arising from specific financing decisions that may be made by the utility." ComEd Init. Br. at 10; AG Ex. 1.0 REV. at 7. According to ComEd, the AG's argument contradicts the purpose of EIMA as a whole, which is to "reflect actual costs as if they were known when rates charged during each rate year were set" and the specific language of the resolutions, quoted above, that ComEd be made whole. ComEd Init. Br. at 10; ComEd Ex. 3.0 at 10. Moreover, ComEd notes that EIMA directs that the rate formula use the WACC approved by the Commission that reflects the utility's actual capital structure, and argues that because ComEd's capital structure is comprised of both debt and equity financing, using divergent financing, as the AG suggests, would contravene this capital structure. ComEd Init. Br. at 10.

Similarly, the AG argues that ComEd "will not actually pay income taxes when it collects interest as part of the recovery of the reconciliation balances," and that ComEd is "free to actually finance any changes in the reconciliation balance using any form of capital it desires, including a mix of debt or equity." AG Init. Br. at 15-16. However, ComEd asserts that it finances the reconciliation balance with its approved capital structure, and that it would be improper to treat all of ComEd's financing costs as if they resulted from debt, because: (1) the reconciliation balance does not represent discrete assets that can be financed, but instead is a mathematical share of the total final reconciliation revenue requirement that is financed by all of the financing elements included in the WACC; and (2) prior findings that ComEd could finance its reconciliation balance with debt alone were rejected by PA 98-0015. ComEd Init. Br. at 10; ComEd Ex. 1.0 CORR. at 15.

Finally, ComEd argues that Staff, the AG, and CCI ask the Commission to commit reversible error by arguing that the Commission should rely on whether Ameren Illinois Company grosses-up the interest rate to be applied to the reconciliation balance. ComEd Init. Br. at 11. ComEd notes that it is not a party to that proceeding, and emphasizes that the facts and circumstances of ComEd's Commission-approved formula rate are neither an issue in that proceeding nor within the scope of that proceeding. According to ComEd, the Commission must decide this case "exclusively on the record for decision" in this case. 220 ILCS 5/10-103; ComEd Init. Br. at 11. ComEd asserts that it should not be denied the right to recover its costs here simply because Ameren's formula appears not to consider these tax impacts. ComEd Init. Br. at 11.

ComEd states that the legislature made it absolutely clear that the purpose of EIMA was to "[p]rovide for the recovery of the utility's *actual costs* of delivery services that are prudently incurred and reasonable in amount consistent with Commission practice and law." 220 ILCS 5/16-108.5(c)(1) (emphasis added); ComEd Init. Br. at 11. ComEd states that the statutorily specified "intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates ... with what the revenue requirement determined using a year-end rate base for the applicable calendar year would have been *had the actual cost information for the applicable calendar year been available at the filing date.*" 220 ILCS 5/16-108.5(d)(1) (emphasis added). Interest calculated at a utility's WACC without accounting for tax effects in the calculation does not place the utility in the position it would have occupied "*had the actual cost information for the applicable calendar year been available at the filing date.*" *Id.* (emphasis added).

Staff and Intervenor Positions

[INSERT]

Commission Conclusion and Analysis

The Commission concurs with ComEd that the legislature clearly expressed that interest was intended to be set at WACC under EIMA because it "represents the reasonable cost and means of financing *a utility's investments and operating costs*, so that the utility and customers are made whole when charges or credits are necessary to reconcile to actual prudent and reasonable *investments and costs.*" Senate Resolution 821, 97th General Assembly, at 2-3; House Resolution 1157, 97th General Assembly, at 2-3 (emphasis added). Nor can it be disputed that the statutorily specified "intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates ... with what the revenue requirement determined using a year-end rate base for the applicable calendar year would have been *had the actual cost information for the applicable calendar year been available at the filing date.*" 220 ILCS 5/16-108.5(d)(1) (emphasis added). The Commission agrees with ComEd that calculating interest on the reconciliation balance equal to a utility's WACC without accounting for tax effects in the

calculation does not place the utility in the position it would have occupied had the initial revenue requirement been determined using the subsequently available actual cost for the applicable calendar year. The law is clear that a utility and its customers are to be made whole through the reconciliation process when charges or credits are necessary to reconcile to actual prudent and reasonable investments and costs. This can be accomplished only by taking income tax effects into account in calculating interest at a rate equal to the utility's WACC. The Commission concludes that ComEd's approved formula rate and tariffs filed on May 30, 2013, comply with the requirements of the PUA and correctly calculate the interest on its reconciliation balances.

B. Do the Tariffs Filed on May 30, 2013 by ComEd Correctly Calculate the Section 16-108.5(c)(5) Return on Equity ("ROE") Collar as Authorized by the Public Utilities Act?

ComEd's Position

It is ComEd's position that its formula rate and tariffs filed on May 30, 2013, comply with the requirements of Section 16-108.5(c)(5) of the PUA and correctly calculate the ROE collar. ComEd argues that the approved rate formula uses a year-end capital structure based on ComEd's FERC Form 1 balances for all purposes, including calculating the ROE Collar. ComEd further argues that the approved rate formula also uses rate base components, including plant in service, uniformly based on those year-end balances. This approach is internally consistent, financially sensible, and produces meaningful results. ComEd Init. Br. at 12. ComEd submits that the AG's and CCI's argument that an average rate base should be utilized for purposes of making the ROE Collar calculation is contrary to law. ComEd Reply Br. at 10-11. Moreover, ComEd notes that in its briefs, Staff did not support the use of an average rate base for the calculation of the ROE collar. Staff Init. Br. at 10-11.

In support of its position, ComEd submits that the use of a year-end rate base in calculating the applicable revenue requirements and reconciliation is required by Public Act 98-0015, including the following codified as Section 16-108.5(d)(1):

The filing shall also include a reconciliation of the revenue requirement that was in effect for the prior rate year (as set by the cost inputs for the prior rate year) with the actual revenue requirement for the prior rate year (determined using a year-end rate base) that uses amounts reflected in the applicable FERC Form 1 that reports the actual costs for the prior rate year."

220 ILCS 5/16-108.5(d)(1). ComEd notes that PA 98-0015 superseded prior rulings on use of an average rate base, and argues that PA 98-0015 clearly established that the year-end rate base is the only permissible rate base to use when calculating the applicable revenue requirements and reconciliation. ComEd Init. Br. at 12.

Although the words "year-end" do not literally appear within the language of Section 16-108.5(c)(5) establishing an ROE Collar calculation, ComEd argues that they

are incorporated by reference through the requirement that the earned rate of return on common equity be calculated “consistent with this Section” – which refers to Section 16-108.5 of the Act. 220 ILCS 5/16-108.5(c)(5); ComEd Init. Br. at 12. Section 16-108.5(c)(5) provides, in part,³ as follows:

If the participating utility's earned rate of return on common equity related to the provision of delivery services for the prior rate year (calculated using costs and capital structure approved by the Commission as provided in subparagraph (2) of this subsection (c), *consistent with this Section*, in accordance with Commission rules and orders ...) is more than 50 basis points less than the return on common equity calculated pursuant to paragraph (3) of this subsection (c) ... then the participating utility shall apply a charge through the performance-based formula rate that reflects an amount equal to the value of that portion of the earned rate of return on common equity that is more than 50 basis points less than the rate of return on common equity calculated pursuant to paragraph (3) of this subsection (c) ... for the prior rate year, adjusted for taxes.

220 ILCS 5/16-108.5(c)(5) (emphasis added); ComEd Init. Br. at 13.

Section 16-108.5(c)(2) requires that the formula rate reflect a year-end capital structure:

(2) Reflect the utility's actual *year-end* capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law

Id. at (c)(2) (emphasis added). Section 16-108.5(d)(1) provides that the reconciliation and reconciliation revenue requirement shall be determined using a year-end rate base:

The filing shall also include a reconciliation of the revenue requirement that was in effect for the prior rate year (as set by the cost inputs for the prior rate year) with the actual revenue requirement for the prior rate year (*determined using a year-end rate base*) that uses amounts reflected in the applicable FERC Form 1 that reports the actual costs for the prior rate year.

Id. at (d)(1) (emphasis added). ComEd argues that this section of the PUA further specifies that the intent of the reconciliation is to reconcile the revenue requirement

³ The quoted language addresses the scenario where the utility's earned rate of return on common equity is more than 50 basis points *less* than its authorized return on common equity. This same language is repeated in Section 16-108.5(c)(5) with one minor change to address the scenario where the utility's earned rate of return on common equity is more than 50 basis points *higher* than its authorized return on common equity. *Id.*

initially included in rates with the actual revenue requirement determined using a year-end rate base:

Notwithstanding anything that may be to the contrary, *the intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates* for each calendar year, beginning with the calendar year in which the utility files its performance-based formula rate tariff pursuant to subsection (c) of this Section, *with what the revenue requirement determined using a year-end rate base for the applicable calendar year would have been* had the actual cost information for the applicable calendar year been available at the filing date.

Id.; ComEd Init. Br. at 13-14.

According to ComEd, the law is clear: the ROE collar calculation would not be consistent with the requirements of Section 16-108.5 if it were based on anything other than a year-end rate base. ComEd Init. Br. at 14. ComEd submits that, in light of this solid statutory basis for use of a year-end rate base for the ROE collar, AG witness Mr. Efron's argument that EIMA does not specifically *reject* use of an average rate base is unconvincing at best. *Id.*

ComEd observes that the AG continues to argue that an average rate base should be utilized for purposes of making the ROE collar calculation, a position that is similarly supported by CCI. AG Init. Br. at 19-29; CCI Init. Br. at 11-15. In response, ComEd notes that even aside from the statutory provisions supporting use of the year end rate base, the AG's advocacy of an "average rate base" when calculating the earned ROE for the purpose of the ROE Collar calculation (AG Ex. 2.0 REV. at 4) would create a mismatch when calculating ComEd's earned ROE. ComEd Init. Br. at 14. In contrast, according to ComEd, there is no average rate base in the approved formula, in ComEd's FERC Form 1, or in the statute, and the average rate base does not equate to the year-end rate base for any year. *Id.* ComEd submits that the AG's proposal would have *the financial effect* of replacing the year-end rate base in both the collar calculation and the reconciliation revenue requirement, and that the use of an average rate base would result in an artificially inflated earned ROE by reducing the amount of rate base financed by both debt and equity resulting in both a higher net income due to a reduction in long-term interest expense and higher ROE given the higher income (numerator) and the lesser amount of equity (denominator), which would create an artificial impression that ComEd's earnings were further outside the ROE Collar band than they actually were. *Id.* at 14-15; ComEd Reply. Br. at 12; ComEd Ex. 1.0 CORR. 11-12; Brinkman, Tr. at 64:3-15. Alternatively, if ComEd's average rate base is higher than its year-end rate base, the ROE is artificially deflated when compared to the value calculated utilizing a year-end rate base. ComEd Init. Br. at 14.

AG witness Mr. Efron claims that his proposal would not modify the rate base used to establish the initial revenue requirement or the rate base used in the reconciliation. AG Ex. 4.0 at 1-2. However, according to ComEd, this disregards the ultimate effect that this change would have. ComEd Init. Br. at 15. According to

ComEd witness Ms. Brinkman, “it makes no sense to base an earnings test like the ROE Collar on a method of measuring rate base at odds with the method used to set the initial revenue requirement, the actual-cost reconciliation revenue requirement, and ultimately the charges applicable to customers.” ComEd Ex. 3.0 at 4. ComEd emphasizes that the real and practical effect of Mr. Effron’s proposal would achieve the same result clearly rejected by PA 98-0015 – to replace the year-end rate base in both the collar calculation and the reconciliation revenue requirement. ComEd Init. Br. at 15.

ComEd observes that AG witness Mr. Effron claims that PA 98-0015 nowhere expressly rejects the use of an average rate base in the ROE collar calculation, and uses this as a justification for his reliance on the use of the average rate base. AG Ex. 6.0 at 1-2. In contrast, ComEd submits the House and Senate Resolutions incorporated in part by reference in PA 98-0015, which addressed the legislature’s intent with respect to certain language in EIMA – including the application, scope, and authority related to the legislature’s provision for the use of a final year-end rate base under EIMA. ComEd Init. Br. at 15-16; ComEd Reply Br. at 11. ComEd asserts that the House and Senate Resolutions make clear that nothing other than a year-end rate base may be used with respect to EIMA:

WHEREAS, The Energy Infrastructure Modernization Act also provides that the final *year-end* cost data filed in FERC Form 1 should generally be used to determine rates; and

WHEREAS, No statutory authority was given to the Illinois Commerce Commission to set rate base and capital structure using average numbers that do not represent final *year-end* values reflected in the FERC Form 1, and the Illinois Commerce Commission's use of such average is contrary to the statute;

RESOLVED ... that we express serious concerns that the Illinois Commerce Commission Order, entered on May 29, 2012 in Commission Docket No. 11-0721, fails to reflect the statutory directives and the intent of the Illinois General Assembly by: ... (3) determining rate base and capital structure using an average, rather than the *year-end* amounts as reflected in FERC Form 1;

Senate Resolution 821, 97th General Assembly, at 3, 4-5; House Resolution 1157, 97th General Assembly, at 3, 4-5 (emphasis added); 220 ILCS 5/16-108.5(k); ComEd Reply Br. at 11.

ComEd concludes that the AG’s and CCI’s argument that there is no statutory requirement to use year-end rate base in performing the ROE collar calculation under EIMA is contrary to law and must be rejected in view of the clear statutory language and the specific legislative pronouncements to the contrary. ComEd further finds the AG’s and CCI’s proposal unreasonable in that it suggests the legislature required use of a

year-end rate base methodology to calculate the revenue requirements to be included in rates and utilized for reconciliations, only to undo and undermine that requirement by requiring an ROE collar adjustment each year that would be based on an average rather than a final year-end rate base. ComEd submits that the AG's argument on this issue is obviously contrary to law, and it must be rejected.

Staff and Intervenor Positions

[INSERT]

Commission Conclusion and Analysis

The Commission concurs with Staff and ComEd that the AG's and CCI's proposal to use an average rate base rather than a year-end rate base in calculating the ROE Collar adjustment is inconsistent with and contrary to EIMA. As Staff noted, a year-end rate base "is the only rate base specifically prescribed anywhere in Section 16-108.5 of the Act." Further, as ComEd observes, Section 16-108.5(c)(5) provides for the ROE Collar calculation to be consistent with Section 16-108.5, and Section 16-108.5 specifically requires use of a year-end rate base in multiple contexts. Further, as ComEd notes, the legislature made clear in giving effect to House Resolution 1157 and Senate Resolution 821 through Public Act 98-0015 that the intent of EIMA was to provide for the general use of final *year-end* cost data to determine rates, and no authority was provided under EIMA that set rate base using average numbers that do not represent final *year-end* values reflected in a utility's FERC Form 1. Accordingly, the Commission rejects the AG's and CCI's proposal to use an average rate base rather than a year-end rate base in calculating the ROE Collar adjustment.

C. Do the Tariffs Filed on May 30, 2013 by ComEd Correctly Reflect the Appropriate Tax Treatment in Calculating Interest on the Reconciliation Balance in the Formula Rate Tariff as Authorized by the Public Utilities Act?

ComEd's Position

It is ComEd's position that its formula rate and tariffs filed on May 30, 2013, comply with the requirements of the PUA and correctly reflect the appropriate tax treatment for calculating interest on reconciliation balances.

According to ComEd, it would be improper to net deferred income taxes related to the reconciliation balance against the reconciliation balance *before* interest is calculated, as prior to collecting the reconciliation balance ComEd has received no tax benefit. *Id.* The cash receipts, as well as the tax payment, are deferred. *Id.*

ComEd observes that witnesses for the AG and CCI propose an unlawful and improper reduction to the reconciliation balance for purposes of calculating the interest on that balance. AG Ex. 1.0 REV. at 9-17; AG Ex. 2.0 REV. at 7-11; CCI Ex. 1.1 at 5-9. Specifically, the AG and CCI propose that the accumulated deferred income tax

(“ADIT”) related to the reconciliation balance be netted against the reconciliation balance before calculating the interest amount. ComEd Init. Br. at 17. ComEd argues that this proposal is inconsistent with and violates the existing formula and would result in a reconciliation balance dramatically different from that specified by the formula’s calculations. *Id.*; ComEd Ex. 1.0 CORR. at 19-28. ComEd notes that the Commission rejected that same argument in Docket No. 11-0721, asserts that nothing has changed since that time to warrant a departure from the Commission’s prior decision, and further submits that nothing in PA 98-0015 would support any change in the disposition of this ADIT argument. *Id.*

ComEd argues that no party does, or can, dispute the fact that ComEd did not receive any cash from ratepayers in 2012 related to the underlying reconciliation balance. *Id.* However, according to ComEd, it has incurred carrying costs – that is, the time value of money – related to the full 2012 reconciliation balance. *Id.* ComEd claims that because the rates in effect did not recover the reconciliation balance or its carrying costs, ComEd should earn an interest rate on its full cost of financing that balance until it is able to collect the revenues related to those costs in 2014. *Id.*; ComEd Ex. 1.0 CORR. at 23. ComEd rephrases its position, stating that taxes related to the reconciliation are deferred because the revenue is deferred, and that deferral provides no tax benefit to ComEd. ComEd Init. Br. at 17. ComEd asserts that, as a result, this deferred tax liability represents an amount that ComEd must pay in the future, and is an amount that ComEd has not recovered from customers through rates – therefore, ComEd has no offsetting tax benefit with which to fund these carrying costs. *Id.*; ComEd Ex. 3.0 at 12.

ComEd observes that the AG argues that ComEd receives a real cash benefit from the deferral of income taxes, and that changes in ADIT provide incremental cash flow to utilities through the change in timing of the payment of cash income taxes associated with such tax deferrals. ComEd Reply Br. at 13. In response, ComEd argues that it is not sufficient for the AG to conclude that deferred taxes should reduce the revenue requirement simply because, generally, accumulated deferred income taxes are deducted from a utility’s rate base. ComEd Init. Br. at 18. ComEd distinguishes the deferred taxes at issue here from “typical” ADIT, noting that although the ICC does routinely recognize ADIT liability balances as rate base reductions, this only occurs when the ADIT liability results in a cash benefit to the utility in lower taxes paid in the current year. ComEd Init. Br. at 18; ComEd Ex. 3.0 at 13. According to ComEd, the lower taxes associated with “typical” ADIT create a tax benefit to the utility, which then results in cash available to fund rate base investments. *Id.* ComEd argues that, in contrast to the AG’s claims, the reconciliation amount is not recovered by the utility until a later year and thus produces no current cash benefit; in simple terms nothing exists against which to “net” the deferred taxes. ComEd Init. Br. at 18; ComEd Ex. 3.0 at 13.

Witnesses for the AG and CCI argue that the ADIT liability on the reconciliation is a tax benefit, and that taxes currently payable are lower because of the reconciliation. AG Ex. 4.0 at 5; CCI Ex. 2.0 at 4. In contrast, ComEd asserts that the ADIT liability

does not represent a current cash tax benefit. Instead, it represents a future tax liability. ComEd Reply Br. at 13. Moreover, according to ComEd, taxes that are currently payable are not impacted by the reconciliation – they are simply lower than they would have been had ComEd received more revenue and been paid the reconciliation balance earlier. *Id.*

The AG further argues that changes in ADIT provide incremental cash flow to utilities through the change in timing of the payment of cash income taxes associated with such tax deferrals. AG Ex. 1.0 REV. at 15. According to the AG, even when utilities are in a Net Operating Loss (“NOL”) carryforward position, the size of the NOL in each tax year is directly impacted by changes in the reconciliation balance regulatory asset, and the resulting NOL deferred tax asset is included in rate base to directly impact utility rates. *Id.* ComEd submits that this argument wrongly interprets the effect of the NOL and should be rejected. According to ComEd, the NOL carryforward was generated primarily by the 50% bonus depreciation deduction allowed under the Tax Relief Act of 2012. ComEd Init. Br. at 19. Among other things, the Tax Relief Act allowed companies to accelerate depreciation expense treatment on the tax return, which led to lower taxes for those companies in the near term. ComEd asserts that the purpose of the Act was to create an opportunity for companies to use their tax savings to stimulate the economy. *Id.* ComEd notes that the AG correctly states that ComEd is currently in a NOL carryforward position, but emphasizes that the AG misinterprets the effect of this tax benefit. *Id.* In briefing, ComEd describes the effect of the NOL carryforward position:

Without 50% bonus depreciation in 2012, ComEd would have reflected taxable income. Because it will reduce taxes in a future period, by applying this net operating loss to future taxable income, the NOL carryforward is a deferred tax asset. Under the GAAP Accounting Standards Codification (“ASC”), specifically ASC 740, ComEd has reflected a deferred tax asset of \$25 million (jurisdictional portion) for the NOL on WP 4, line 20 of ComEd’s 2013 formula rate template (Docket 13-0318, ComEd Ex. 14.02). The bonus depreciation itself, however, creates a deferred tax liability because there is a temporary difference related to accelerated depreciation, under the bonus depreciation rules, and is included on ComEd Ex. 14.02, WP 4, line 51. For book purposes, ComEd is recording depreciation expense at a slower rate than for tax purposes, thus ComEd is receiving a benefit on its tax return now before reflecting the full expense on its books. The NOL deferred tax asset nets against the bonus depreciation deferred tax liability. Once the NOL is utilized this deferred tax asset is eliminated.

ComEd Init. Br. at 19-20; ComEd Ex. 3.0 at 14. As a result, ComEd argues that its NOL carryforward in the current year is not directly impacted by changes in the reconciliation balance regulatory asset. *Id.* at 20. Further, in ComEd’s response to an AG data request in Docket No. 13-0318, ComEd expressly stated that the “deferred tax asset related to the Federal NOL does not affect the deferred income tax position related to

the regulatory asset for the under-recovery of reconciliation amounts.” ICC Docket No. 13-0318, AG 4.03(d).

ComEd notes that the AG argues that “[t]he reconciliation reveals an under-recovery during the 2012 calendar year *because ComEd collected fewer revenues than the revenue requirement authorized by the Commission’s Order in Docket No. 12-0321.*” AG Init. Br. at 31 (emphasis added). ComEd asserts that this is incorrect. ComEd Reply Br. at 14. According to ComEd, while the reconciliation for the 2012 Rate Year does reveal an under-recovery of the revenue requirement to be reflected in rates, it occurs because the Reconciliation Revenue Requirement based on actual costs for the 2012 Rate Year (submitted in Docket 13-0318) was higher than the Initial Revenue Requirement authorized by the Commission for the 2012 Rate Year⁴, not because ComEd collected less than the Initial Revenue Requirement authorized by the Commission for the 2012 Rate Year. *Id.* ComEd argues that during 2012, contrary to the AG’s assertion in its brief, ComEd has not been allowed to reflect in rates the additional costs resulting in the higher Reconciliation Revenue Requirement. *Id.* As a result, those costs (and their resulting revenues) will not be reflected in rates until 2014 – at which time ComEd will also pay income taxes associated with those additional revenues. *Id.* In light of the foregoing, ComEd asserts that this relationship (that both the revenues and related taxes will occur in the future) is why ComEd receives no current tax benefit from the deferral of taxes on the reconciliation balance. *Id.*

ComEd argues that the AG’s argument that its proposal is consistent with the language of Section 16-108.5(d)(1) misreads and misapplies the statutory language. ComEd Reply Br. at 15. According to ComEd, EIMA provides that interest is to be paid on the reconciliation balance, not on the reconciliation balance less deferred taxes: “Any ... under-collection indicated by such reconciliation [“of the revenue requirement that was in effect for the prior rate year (as set by the cost inputs for the prior rate year) with the actual revenue requirement for the prior rate year”] shall be ... recovered as an additional charge to, ... with interest calculated at a rate equal to the utility’s weighted average cost of capital approved by the Commission for the prior rate year, the charges for the applicable rate year.” 220 ILCS 5/16-108.5(d)(1); ComEd Reply Br. at 15. ComEd further argues that where EIMA intended that adjustments be made, to an amount or a balance, it has done so specifically, as in the case of projected plant additions which are to be included on a net basis considering updated depreciation reserve and expense. ComEd Reply Br. at 15; 220 ILCS 5/16-108.5(c)(6). ComEd submits that its method of calculating the allowed interest on the entire reconciliation balance – instead of the AG’s (fictional) net of tax reconciliation amount – permits ComEd to earn the allowed interest on only the lost *net* cash flow. *Id.*

ComEd further notes that the same relationship exists where the reconciliation results in an over-recovery. If less than the full reconciliation balance accrued interest,

⁴ Moreover, the revenue requirement used to set charges for 2012 was not the revenue requirement established in Docket 12-0321, but rather the 2012 Rate Year Initial Revenue Requirement approved in Docket No. 11-0721 plus other pre-EIMA revenue requirements in effect for portions of 2012 established in Docket No. 10-0467.

then customers – in cases where the utility over-collected prior to reconciliation – would receive interest on only about 60% of the money they would have “advanced” to the utility. Brinkman, Tr. 61:20 – 62:7. According to ComEd, that approach would not fully credit to customers the interest on funds that they have provided, just as the intervenors ADIT argument would deprive ComEd of recovering interest on a major portion of its deferred revenues. ComEd Init. Br. at 20.

ComEd asserts that CCI’s example and related discussion, as presented in its Initial Brief, reinforces the correctness of ComEd’s approach. ComEd Reply Br. at 15-16. CCI’s example assumes a reconciliation balance of \$100,000 and an effective tax rate of 41%. CCI posits that the inability to recover that \$100,000 in the current year (2012 in the example) results in a net-of-tax investment of \$59,000. *Id.* at 16. ComEd submits that all parties agree that ComEd “should only be allowed to recover carrying costs on its out-of-pocket net cash investment of \$59,000” as this will make ComEd “whole” for the delayed recovery of the \$100,000 reconciliation balance. *Id.* However, ComEd argues that it will not be made whole unless the carrying charges are applied to the full reconciliation balance as opposed to only the “net of cash” investment. *Id.* Assuming a 10% interest rate and a one-year delay of recovery, ComEd submits that the amount the utility company will need to recover to be made whole is \$64,900, which is the net cash investment plus interest thereon at 10% ($\$59,000 \times 110\% = \$64,900$). *Id.* According to ComEd, the only way this will happen is if the interest rate is applied to the full \$100,000 reconciliation balance, as shown below:

| | |
|-------------------------------------|-----------|
| Undercollection = | \$100,000 |
| Plus interest on undercollection | \$ 10,000 |
| Less taxes at 41% | \$ 45,100 |
| Net of tax recovery = | \$ 64,900 |

ComEd argues that recovery of anything less than the \$64,900 in the example will prevent the utility from being made whole. *Id.* However, according to ComEd, that is precisely the result of the AG and CCI proposal. If, in calculating the net cash to the utility in the example, interest is applied only to the net cash investment instead of the full reconciliation balance, the utility will recover less than the \$64,900 needed to make it whole, as shown below:

| | |
|------------------------------|-----------|
| Undercollection = | \$100,000 |
| Plus interest on \$59,000 | \$ 5,900 |
| Less taxes at 41% | \$ 43,419 |
| Net of tax recovery = | \$ 62,481 |

Id. at 16-17. Accordingly, ComEd argues that it ought to be allowed to recover interest, at the allowable rate (WACC), on the full reconciliation balance, not on only the balance net of deferred income taxes. ComEd further submits that the proposals of the AG and CCI are inconsistent with EIMA and the approved rate formula, and should be rejected.

Staff and Intervenor Positions

[INSERT]

Commission Conclusion and Analysis

AG and CCI propose that ComEd's reconciliation balance be reduced by netting ADIT with the reconciliation balance in calculating interest on the reconciliation balance. The proposed adjustment, however, contravenes the language and intent of EIMA.

We agree with ComEd that Section 16-108.5(d)(1) of EIMA provides that participating utilities be paid interest on the reconciliation balance and not the reconciliation balance less deferred taxes. See 220 ILCS 5/16-108.5(d)(1). The proposed adjustments violate this provision by inserting conditions that do not appear in the Act. The record shows that the proposed adjustments would also violate this provision because they would prevent ComEd as a participating utility from being made whole by the reconciliation, which is the clearly expressed intent of Section 16-108.5(d)(1). On the other hand, the record shows that ComEd's method of calculating interest on the full reconciliation balance, which Staff supports, would allow ComEd to earn the amount of the lost net cash flow. Neither of the examples that the AG and CCI provide in their reply briefs provide any support for the proposed adjustment. The record shows that CCI's example falls short because it will not make ComEd whole.

Additionally, we agree that the fact that ADIT is generally deducted from a utility's rate base is irrelevant in this context. Unlike other investments to which ADIT relates, the reconciliation amount produces no current cash benefit because it is not recovered by ComEd until a year later.

For all of the above reasons, we decline to adopt AG and CCI's proposed adjustment relating to the ADIT on ComEd's reconciliation balance.

III. IMPLEMENTATION OF RATE FORMULA CHANGES, IF ANY

ComEd's Position

ComEd maintains that there is no basis for the Commission to make any change in ComEd's approved rate formula. However, in the event that there were to be any changes made, all parties agree with ComEd's proposal that those changes should be given effect both prospectively and retrospectively back through the decision in Docket No. 11-0721, in the form of a single rolled-up credit or charge (as the case may be) applicable in 2014. ComEd Reply Br. at 17; Staff Init. Br. at 13; AG Init. Br. at 48. CCI did not opine on this topic.

The evidence on this subject is unanimous. The only other witness who testified on this subject, AG witness David Efron, concurred with ComEd's position. AG Ex. 6.0 at 2-3. AG witness Mr. Efron also made clear in his agreement that the effect of any charges or credits "including any retroactive effect on the ROE collar calculation and on the reconciliation, should be reflected in the Company's rates as of January 1, 2014." *Id.* at 3.

Staff and Intervenor Positions

[INSERT]

Commission Conclusion and Analysis

We agree with the positions expressed and supported by ComEd, Staff, and intervenors in this docket. In the event that any changes are to be made to ComEd's rate formula, those changes will be given effect both prospectively and retrospectively back through the decision in Docket No. 11-0721, in the form of a single rolled-up credit or charge (as the case may be) applicable in 2014. However, as noted above, no changes to ComEd's rate formula are required or appropriate.

IV. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having considered the entire record herein and being fully advised in the premises, is of the opinion and finds that:

- (1) Commonwealth Edison Company is an Illinois corporation engaged in the transmission, distribution, and sale of electricity to the public in Illinois and is a public utility as defined in Section 3-105 of the Public Utilities Act;
- (2) the Commission has jurisdiction over the parties and the subject matter herein;
- (3) the recitals of fact and conclusions of law reached in the prefatory portion of this Order are supported by the evidence of record and are hereby adopted as findings of fact and conclusions of law;

- (4) Commonwealth Edison Company's filed formula rate and tariffs correctly calculate interest on its reconciliation balance;
- (5) Commonwealth Edison Company's filed formula rate and tariffs correctly calculate the Section 16-108.5(c)(5) return on equity collar; and
- (6) Commonwealth Edison Company's filed formula rate and tariffs correctly reflect the appropriate tax treatment in calculating interest on the reconciliation balance.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that Commonwealth Edison Company's filed rate formula, as filed on May 30, 2013 and approved by the Commission on June 5, 2013, complies with Public Act 98-0015 and this investigation is closed.

IT IS FURTHER ORDERED that, subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the Administrative Review Law.

By Order of the Commission this ____ day of November, 2013.

(SIGNED) DOUGLAS P. SCOTT

Chairman