

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Commonwealth Edison Company :
: :
Annual formula rate update and revenue : **15-0287**
requirement reconciliation under :
Section 16-108.5 of the Public Utilities Act. :

PROPOSED ORDER

October 19, 2015

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I. INTRODUCTION / STATEMENT OF THE CASE

A. Procedural History

On April 15, 2015, Commonwealth Edison Company (“ComEd”, “the Company” or “the Utility”) filed with the Illinois Commerce Commission (the “Commission” or “ICC”) ComEd’s annual formula rate update and revenue requirement reconciliation and requested the Commission to authorize and direct ComEd to make the compliance filings necessary to place into effect the resulting charges to be applicable to delivery services provided by ComEd beginning on the first day of ComEd’s January 2016 billing period, as authorized by Section 16-108.5(d) of the Public Utilities Act (the “Act” or “PUA”), 220 ILCS 5/16-108.5(d).

ComEd’s filing, consistent with Section 16-108.5(d)(1), included:

- updated inputs to the performance-based formula rate for the applicable rate year (2016) that are based on final historical data reflected in the Utility’s most recently filed annual FERC Form 1 (for 2014) plus projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the inputs are filed (2015).
- a reconciliation of the revenue requirement that was in effect for the prior rate year (2014) (as set by the cost inputs for the prior rate year) with the actual revenue requirement for the prior rate year (as reflected in the applicable FERC Form 1 (for 2014) that reports the actual costs for the prior rate year).

The filing, consistent with Section 16-108.5(d)(1), also included: (1) a corporate officer certification relating to reconciliation Schedule “Sch FR A-1 REC” and (2) the new delivery services charges corresponding to the updated costs and reconciled revenue requirement.

Statutorily, this docket must conclude by December 11, 2015. 220 ILCS 5/16-108.5(d)(3).

The following ComEd witnesses testified in this case: Christine M. Brinkman, Sandeep S. Menon, Kristine R. Farkas, John A. Fitterer, Michael F. Born, Michael C. Moy, John L. Leick, Chad A. Newhouse, and Cheryl M. Maletich.

The following Staff witnesses testified in this case: Daniel G. Kahle, Burma C. Jones, Rochelle M. Phipps, and Richard W. Bridal II.

In addition to ComEd and Staff, the following parties have submitted testimony in this case: the Illinois Attorney General's Office ("AG") and the City of Chicago ("City") (collectively, "AG/City"), and the Citizens Utility Board ("CUB") and the Illinois Industrial Energy Consumers ("IIEC") (collectively, "CUB/IIEC" or "C/I").

During the course of the proceeding, Staff and other parties proposed various adjustments and changes to the Company's proposed revenue requirements. ComEd accepted some of these adjustments and changes.

An evidentiary hearing was convened in this docket at the Commission's Chicago Office before duly authorized Administrative Law Judges ("ALJs") on August 27, 2015. The parties filed and served Initial Briefs on September 9, 2015. Reply Briefs were filed and served on September 16, 2015. A Proposed Order was issued on October 19, 2015.

II. OVERALL REVENUE REQUIREMENT

This formula rate update ("FRU") proceeding sets ComEd's distribution rates applicable during 2016. Those rates are set in order to recover the balance of ComEd's fully reconciled actual costs for rate year 2014 as well as the initial projection of ComEd's 2016 costs as provided for by EIMA.¹ The 2016 Rate Year Net Revenue Requirement used to set those rates derives from the following figures:

1. The 2014 Reconciliation Adjustment – the difference between ComEd's rates in effect in 2014 and the 2014 Reconciliation Revenue Requirement determined based on ComEd's actual 2014 costs as reported in its Federal Energy Regulatory Commission ("FERC") Form 1 for 2014, corrected for the lost time value of money;
2. The 2016 Initial Rate Year Revenue Requirement – a projection of 2016 costs based on ComEd's actual 2014 operating costs and rate base plus projected 2015 plant additions and the associated adjustments to accumulated depreciation (the associated change in the depreciation reserve), depreciation expense, and, per the Commission's prior Orders, accumulated deferred income taxes ("ADIT");

¹ "EIMA" refers to the Energy Infrastructure Modernization Act, Public Act ("PA") 97-0616, as amended by PA 97-0646 and PA 98-0015, and the changes and additions it made to the PUA.

3. The “Return on Equity (“ROE”) Collar” adjustment relating to 2014 and the “ROE Penalty Calculation” applicable to 2014.

E.g., ComEd Ex. 1.0 CORR. at 10-18.

ComEd presented evidence supporting its proposed 2016 Rate Year Net Revenue Requirement and the components thereof through the testimony of nine witnesses and the attachments, schedules, and exhibits they sponsored. Staff and intervenors presented evidence on the contested issues. The Commission’s determinations on the subject of rate base issues are reflected and set forth below in the applicable sections of this Order.

A. 2016 Initial Rate Year Revenue Requirement

ComEd presented evidence showing that its calculated 2016 Initial Rate Year Revenue Requirement as adjusted in its surrebuttal testimony is \$2,437,879,000. ComEd Ex. 12.01, SCH FR A-1, line 23. Staff recommends a 2016 Initial Rate Year Requirement of \$2,431,643,000, as presented on line 1 in Appendix A, Schedule FY of its Initial Brief (“Init. Br.”). The Commission’s determination regarding the 2016 Initial Rate Year Revenue Requirement is set forth later in this Order.

B. 2014 Reconciliation Adjustment

ComEd presented evidence that its calculated 2014 Reconciliation Adjustment (including interest), reflecting the difference between the rates in effect in 2014 and the actual 2014 Reconciliation Revenue Requirement as adjusted in surrebuttal is \$89,092,000. ComEd Ex. 12.01, Sch A-4, line 31. Staff recommends a 2014 Reconciliation Adjustment of \$81,920,000, as provided in Appendix A, Schedule 8 FY of its Initial Brief. Staff’s method of calculating the reconciliation adjustment presented on this schedule is identical to that included in the appendix to the Commission Orders in Docket Nos. 12-0321, 13-0318 and 14-0312. The Commission’s determination regarding the 2014 Reconciliation Adjustment is set forth later in this Order.

C. ROE Collar and ROE Penalty Calculation

ComEd presented evidence that its calculated ROE Collar adjustment is \$0. ComEd Ex. 12.01, Sch FR A-1, line 35. The ROE Penalty Calculation is set forth on workpaper (“WP”) 23 and is reflected in ComEd’s Cost of Capital Computation on Sch FR D-1. See ComEd Ex. 12.01, Sch FR D-1; see *also* ComEd Ex. 2.02, WP 23. ComEd has reflected a penalty of 5 basis points for the Reconciliation Year on Sch FR D-1, line 9, as a result of failing to meet a service reliability performance metric resulting in a reduction of the allowed ROE to 9.09%. ComEd Ex. 1.0 CORR. at 15; ComEd Ex. 12.01, Sch FR D-1, lines 9, 11.

Staff IB, Appendix A, Schedule 9 FY computes the adjustment necessary when the Company’s earned return on common equity falls outside of the parameters of the

earnings collar established by EIMA. Appendix A, Schedule 9 FY demonstrates that ComEd's Delivery Service ROE during 2014 falls within the ROE collar; therefore, Staff agrees that no ROE collar adjustment is necessary. The Commission approves ComEd's figure based on the detailed evidence in the record.

D. 2016 Rate Year Net Revenue Requirement

ComEd provided evidence that its calculated 2016 Rate Year Net Revenue Requirement, reflecting the adjustments made in rebuttal testimony, is \$2,526,971,000. ComEd Ex. 12.0 at 2; ComEd Ex. 12.01, Sch FR A-1, line 36. Staff's recommends 2016 Initial Rate Year Revenue Requirement presented in Staff Initial Brief, Appendix A, Schedule 1 FY, line 1 is \$2,431,126,000. The Commission's determination regarding the 2016 Rate Year Net Revenue Requirement is set forth later in this Order.

III. SCOPE OF THIS PROCEEDING

A. The Definition of Rate Year and the Reconciliation Cycle

ComEd states that EIMA establishes an annual process by which ComEd's rate year costs and revenue requirements are first estimated, and then finally fixed and reconciled when actual costs are known. The objective 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.

220 ILCS 5/16-108.5(d)(1).

ComEd explains that, to accomplish this objective, EIMA requires that each FRU involve both a final reconciliation of the revenue requirement "for the prior rate year," for which actual costs will be known by the time of filing, and a provisional projection of the revenue requirement for the following calendar year. That provisional Initial Revenue Requirement will be reconciled two years hence. EIMA requires ComEd to base that projection on "historical data reflected in the utility's most recently filed annual FERC Form 1 plus projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the inputs are filed." 220 ILCS 5/16-108.5(d)(1). ComEd states that EIMA thereby establishes a two-year cycle of before-the-fact estimation based on actual and projected costs for years earlier than the rate year and a subsequent after-the-fact reconciliation of that estimated Initial Rate Year Revenue Requirement with the actual data. Thus, in the end, and after adjustment for interest, the rates for each year should be based purely on actual cost. ComEd Init. Br. at 6-7.

ComEd states that it is using the reconciliation process specified by EIMA and that that process is conducted using the rate formula exactly as approved and found compliant with EIMA in Docket Nos. 11-0721, 13-0386, 13-0553, and 14-0316². 220 ILCS 5/16-108.5(d). ComEd further states that this structure replicates the structure used in Docket No. 14-0312 (which reconciled rate year 2013 and calculated an initial revenue requirement for rate year 2015 based on 2013 actual costs and 2014 projected plant additions), Docket No. 13-0318 (which reconciled rate year 2012 and calculated an initial revenue requirement for rate year 2014 based on 2012 actual costs and 2013 projected plant additions), Docket No. 12-0321 (which reconciled rate year 2011 and calculated an initial revenue requirement for rate year 2013 based on 2011 actual costs and 2012 projected plant additions), and, insofar as is possible given the special start up rules, also mirrors the process followed in Docket No. 11-0721 (which set the initial revenue requirement for rate year 2012 based on 2010 actual costs and 2011 plant additions). ComEd Init. Br. at 8-9.

B. Original Cost Finding

1. ComEd Position

ComEd requests that the Commission, as it has in past FRU Orders,³ approve ComEd's original cost of plant in service as of the end of the reconciliation rate year which, in this case, is as of December 31, 2014. See ComEd Ex. 2.0 at 14-15. ComEd states that the record shows that the original cost of gross investment in electric utility plant in service in ComEd's rate base as of December 31, 2014 is \$17,244,257,000. ComEd Ex. 2.0 at 14. ComEd explains that subtracting Asset Retirement costs, capitalized incentive compensation, costs recovered in riders, other costs disallowed in prior ICC orders, and such costs capitalized in 2014, from the total of ComEd's Distribution gross plant and Illinois jurisdictional General and Intangible gross plant results in the original cost of plant in service as of December 31, 2014, of \$17,202,460,000. ComEd Ex. 12.01, Sch FR B-1, line 6. ComEd requests that the Commission approve this amount.

ComEd further explains that per the 2014 Rate Case Order, the original cost calculation excludes assets that are recovered through Rider Energy Efficiency and Demand Response Adjustment ("Rider EDA"), Rider Purchased Electricity ("Rider PE"), and Rider Purchase of Receivables with Consolidated Billing ("Rider PORCB").

2. Staff Position

Staff recommends that the Commission include the following language in the Findings and Ordering paragraphs of its Order in this proceeding:

² *Commonwealth Edison Co.*, ICC Docket No. 11-0721, Final Order (May 28, 2012) ("2011 Rate Case Order"); *Commonwealth Edison Co.*, ICC Docket No. 12-0321, Final Order (Dec. 19, 2012) ("2012 Rate Case Order"); *Commonwealth Edison Co.*, ICC Docket No. 13-0318, Final Order (Dec. 18, 2013) ("2013 Rate Case Order"); *Commonwealth Edison Co.*, ICC Docket No. 14-0312, Final Order (Dec. 10, 2014) ("2014 Rate Case Order").

³ 2011 Rate Case Order at 178; 2012 Rate Case Order at 106; 2013 Rate Case Order at 88-89; 2014 Rate Case Order at 8.

#) The Commission, based on ComEd's proposed original cost of distribution plant in service as of December 31, 2014, before adjustments, of \$17,199,997,000, and reflecting the Commission's determination adjusting that figure, approves \$17,198,474,000 as the composite original cost of jurisdictional distribution services plant in service as of December 31, 2014.

Staff Ex. 5.0 at 8.

3. Commission Analysis and Conclusion

The Commission finds that ComEd's original cost of plant in service as of the end of the reconciliation rate year, December 31, 2014, is \$17,198,474,000, and, consistent with the 2014 Rate Case Order, the Commission will make separate original cost findings with respect to the excluded assets recovered through Rider EDA, Rider PE and Rider PORCB.

C. Issues Pending on Appeal

ComEd states that it has preserved several arguments, including the definition of the formula rate "structure" through appeal from the Commission's orders and that it does not waive any of those arguments. ComEd explains, however, that pending an Illinois Appellate Court decision regarding these arguments, ComEd's filing presents revenue requirements calculated in accordance with EIMA as it has been interpreted and applied by the Commission in prior ComEd FRU and related proceedings. ComEd Ex. 1.0 CORR. at 38; ComEd Init. Br. at 10. ComEd states that it does not intend to relitigate those legal issues on appeal in this proceeding as they are already before the courts and will be decided there. ComEd Ex. 1.0 CORR. at 38-39; ComEd Init. Br. at 10.

IV. RATE BASE

A. Overview

ComEd supported its 2014 Reconciliation Year rate base and its 2016 Initial Rate Year rate base through the testimony of multiple witnesses. There are three contested rate base issues, two relate to ADIT and one relates to Materials and Supplies.

B. 2014 Reconciliation Rate Base

ComEd submitted evidence that its calculated 2014 Reconciliation Year rate base, as adjusted in its surrebuttal testimony is \$7,081,566,000. ComEd Ex. 12.01, Sch FR B-1, line 28. Staff's proposed 2014 reconciliation Rate Base is \$7,078,308,000 as presented on Staff Initial Brief, Appendix B, Schedule 3 RY. The Commission's determination regarding the 2014 Reconciliation Rate Base is set forth later in this Order.

C. 2016 Initial Rate Year Rate Base

ComEd submitted evidence that its calculated 2016 Initial Rate Year rate base as adjusted in its surrebuttal testimony is \$8,277,117,000. ComEd Ex. 12.01 Sch FR B-1,

line 36. Staff's proposed 2016 initial rate year Rate Base is \$8,268,713,000 as presented on Staff IB, Appendix A, Schedule 3 FY. The Commission's determination regarding the 2016 Initial Rate Year Rate Base is set forth later in this Order.

D. Uncontested Issues

1. Plant in Service

a. Distribution Plant

ComEd demonstrated that its Distribution Plant for the 2014 Reconciliation Revenue Requirement was prudently acquired at a reasonable cost and was used and useful when placed into service. ComEd further demonstrated that its Distribution Plant for the 2016 Initial Rate Year Revenue Requirement is prudent and reasonable and the underlying assets are used and useful. ComEd Ex. 6.0 at 23-25. Neither Staff nor any intervenor disagreed. The Commission therefore approves the foregoing Distribution Plant costs.

b. General and Intangible Plant

ComEd demonstrated that its General and Intangible ("G&I") Plant for the 2014 Reconciliation Revenue Requirement was prudently acquired at a reasonable cost and was used and useful when placed into service. ComEd further demonstrated that its G&I Plant for the 2016 Initial Rate Year Revenue Requirement is prudent and reasonable and the underlying assets are used and useful. ComEd Ex. 6.0 at 23-25. Neither Staff nor any intervenor disagreed. The Commission therefore approves the foregoing G&I Plant costs.

2. Regulatory Assets and Liabilities

ComEd's Regulatory Assets are comprised of: (1) a regulatory asset representing the unamortized balance (as of year-end 2014) of capitalized incentive compensation costs, (2) the unrecovered costs related to ComEd's Advanced Metering Infrastructure ("AMI") pilot, and (3) the unrecovered balance of the accelerated depreciation associated with ComEd's AMI investment (apart from the AMI pilot). ComEd Ex. 2.0 at 21-22; ComEd Ex. 2.01, App. 5, line 4. The Regulatory Assets and Liabilities for the 2014 Reconciliation Revenue Requirement and the 2016 Initial Rate Year Revenue Requirement are uncontested. Therefore, the Commission approves this component of rate base.

3. Deferred Debits

a. ComEd Position

ComEd's Deferred Debits included in the rate base are comprised of: (1) Cook County Forest Preserve Fees related to licensing fees for distribution lines; (2) a Long Term Receivable from the Mutual Beneficial Association ("MBA") Plan related to ComEd's payments to the trust on behalf of union employees for short term disability and for which it is awaiting reimbursement; (3) a deferred debit associated with ComEd's capitalized

vacation pay not included in plant-in-service; (4) expected recoveries from insurance on claims made by the public against ComEd; and (5) payment to the Commission for fees related to purchasing new money as part of future long-term debt issuances. ComEd Ex. 2.0 at 22; ComEd Ex. 2.01, App. 5, lines 5-9.

AG/City witness Mr. David Efron proposed two adjustments concerning ADIT related to certain debits. AG/City Reply Br. at 3. The first related to “Stock Options: Other Equity Based Compensation.” ComEd accepted Mr. Efron’s proposal. *Id.*; ComEd Ex. 9.0 at 11. The second related to Other Current Liabilities. AG/City Reply Br. at 3. Although ComEd disagreed with this proposal, in order to limit the issues in this case and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd agreed to the adjustment. *Id.*; ComEd Ex. 8.0 at 24-25. Both adjustments were numerically reflected in ComEd’s rebuttal and surrebuttal revenue requirement calculations. *Id.*; ComEd Ex. 9.01; ComEd Ex. 12.01.

b. AG/City Position

AG/City state that two issues relating to accumulated deferred income taxes for deferred debits are uncontested. AG/City provide draft language for the Commission to adopt in the Order, which they recommend the Commission incorporate in its analysis and conclusion.

c. Commission Analysis and Conclusion

AG/City made two adjustment proposals ADIT related to certain deferred debits, which ComEd accepted in rebuttal testimony. First, Mr. Efron proposed a reduction to rate base related to ADIT for “Stock Options: Other Equity Based Compensation,” an ADIT item originally included in Account 190. Mr. Efron argued that the accrued reserve for the Stock Options item is not reflected in ComEd’s determination of the Company’s rate base, so the related ADIT should be excluded, reducing rate base in both the 2014 Reconciliation Year and 2016 Initial Rate Year by \$7.541 million. Second, Mr. Efron proposed a reduction to rate base related to Other Current Liabilities, based on certain miscellaneous accruals of liabilities that ComEd asserted should be included in the determination of its rate base. Mr. Efron argued that these accruals are not included in operating reserves or deferred credits or otherwise recognized in the determination of ComEd’s rate base, so the related ADIT should be excluded, reducing rate base in each of the 2014 Reconciliation Year and 2016 Initial Rate Year by \$1.434 million. The Commission hereby adopts these uncontested adjustments.

4. Other Deferred Charges

ComEd’s Other Deferred Charges relating to incremental distribution costs for storms greater than \$10 million are uncontested. ComEd included in its 2014 Reconciliation Revenue Requirement rate base and its 2016 Initial Rate Year Revenue Requirement rate base Other Deferred Charges relating to incremental distribution storm costs, which ComEd is amortizing over five years pursuant to Section 16-108.5(c)(4)(F).

In addition, ComEd removed certain merger expenses related to the Exelon/Constellation Energy Group merger from its operating expenses, and is amortizing them over a five-year period. ComEd Ex. 2.0 at 22-23. No party contested these issues. The Commission therefore approves this component of rate base.

5. Accumulated Provisions for Depreciation and Amortization

ComEd's Accumulated Provisions for Depreciation and Amortization related to ComEd's rate base are uncontested. ComEd Ex. 12.01, Sch FR B-1, lines 7-12. The Commission approves this component of rate base.

6. Accumulated Miscellaneous Operating Provisions

ComEd's Accumulated Miscellaneous Operating Provisions include Operating Reserves, Asset Retirement Obligations, and Deferred Credits for the 2014 reconciliation year and 2015 filing year. ComEd Ex. 2.02, WP 5; ComEd Ex. 2.0 at 23; ComEd Ex. 2.01, Sch FR B-1, lines 21-23. These items are uncontested. The Commission therefore approves this component of rate base.

7. Asset Retirement Obligation

ComEd's Asset Retirement Obligation is uncontested. ComEd Ex. 2.01, Sch FR B-1, line 22; ComEd Ex. 2.0 at 24. Therefore, the Commission approves this component of rate base.

8. Customer Advances

ComEd reduced its 2014 Reconciliation Revenue Requirement rate base and its 2016 Initial Rate Year Revenue Requirement rate base to reflect the customer deposits and advances that are related to projects that were included in the rate base as of December 31, 2014 as well as those deposits and advances related to projects included in its 2015 projected plant additions. ComEd initially reduced rate base for these deposits and advances related to projects included in rate base as of December 31, 2014 or in its 2015 projected plant additions by \$85,985,000. ComEd Ex. 2.0 at 25; ComEd Ex. 2.01, Sch FR B-1, line 26 and App. 1, lines 23-30.

AG/City witness, Mr. Efron, proposed reductions to customer advances in the amount of \$5,178,000, which included non-jurisdictional projects and projects not included in the reconciliation year rate base because these advances represent non-investor-supplied funds that are available to the Company regardless of the particular projects to which such advances apply. AG/City Ex. 2.0 at 3-5. ComEd disagreed with the adjusted amount proposed by AG/City but in order to limit the issues in this case and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd agreed to remove the jurisdictional amount of customer advances, approximately \$4.6 million, from rate base. ComEd Ex. 9.0 at 10. ComEd explained that the adjustment reduced rate base for both the reconciliation period and the initial rate

year and that it increased the projected plant additions for this same amount in order to ensure that the duplication of the reduction in rate base for the initial year did not impact the revenue requirement. ComEd stated that by making this adjustment, ComEd reduced the revenue requirement by \$527,000 in the reconciliation year. *Id.*; ComEd Ex. 9.01, App. 1, line 25; ComEd Ex. 9.02, WP 19, line 8a. For these reasons, ComEd's adjusted Customer Advances for the 2014 Reconciliation Revenue Requirement rate base and its 2016 Initial Rate Year Revenue Requirement rate base are uncontested. The Commission approves this component of rate base.

9. Customer Deposits

ComEd's Customer Deposits for the 2014 Reconciliation Revenue Requirement rate base and the 2016 Initial Rate Year Revenue Requirement rate base are uncontested. ComEd Ex. 2.0 at 25; ComEd Ex. 2.01, Sch FR B-1, line 25, and App. 2 "Customer Deposits Information." Therefore, the Commission approves this component of the rate base.

10. Cash Working Capital

ComEd states that the Cash Working Capital ("CWC") reflected in its rate base is the amount of cash that ComEd maintains in order to meet its expenses and other cash outflow obligations. ComEd Init. Br. at 16. ComEd explains that the amount of CWC is based on its lead/lag study, which is a specific analysis of the timing of applicable cash inflows to and cash outflows from a utility. ComEd Ex. 2.0 at 19. Staff and the Company agree on the methodology for CWC.

ComEd's rate base includes a deduction as adjusted in its surrebuttal testimony of \$47,098,000 for CWC that impacts both the 2014 Reconciliation Revenue Requirement and the 2016 Initial Rate Year Revenue Requirement. ComEd Ex. 12.01, Sch FR B-1, line 16. ComEd states that in accordance with the 2013 Rate Case Order, ComEd has adjusted the formula rate App 3 to include a calculation of CWC specifically for the 2016 Initial Rate Year Revenue Requirement. ComEd Ex. 2.0 at 19. ComEd further states that this 2016 Initial Rate Year Revenue Requirement adjustment was a deduction in the amount of \$2,639,000. ComEd Ex. 12.01, Sch FR B-1, line 34a. The leads and lags used to determine CWC were approved in 2014 Rate Case Order. ComEd Ex. 2.0 at 19.

Staff calculated an alternate CWC figure in accordance with Staff's proposed disallowances. ComEd notes that this calculation contains a discrepancy with regard to the amount for depreciation on projected plant additions. ComEd Reply Br. at 3. Staff agrees with ComEd's suggested correction.

Other than the impact of contested issues discussed below, the Commission finds that ComEd's CWC is uncontested and is approved.

11. Construction Work in Progress

ComEd's Construction Work in Progress ("CWIP") for the 2014 Reconciliation Revenue Requirement rate base is uncontested. ComEd demonstrated that its CWIP for the 2014 Reconciliation Revenue Requirement is prudent and reasonable. See ComEd Ex. 6.0 at 20. Neither Staff nor any intervenor disagreed. Therefore, the Commission approves this component of rate base.

E. Contested Issues

1. Accumulated Deferred Income Taxes

ComEd states that generally speaking ADIT reflects the temporary difference between when an expense (or revenue) is recognized in a company's financial and accounting records, commonly referred to as a company's "books," versus when the company recognizes that expense (or revenue) on its tax return. ComEd Init. Br. at 17; 2013 Rate Case Order at 10. According to ComEd, deferred income taxes relate to future tax effects and can be classified as either deferred income tax liabilities or deferred income tax assets. *Id.*

ComEd states that ADIT arises in several different manners, and the appropriate ratemaking treatment is not a function of a "blanket rule" but must correspond with how the ADIT is created and how it affects ComEd's costs. *Id.* at 18. In this proceeding, ComEd states that it has treated each type of ADIT both in accordance with prior Commission decisions, and appropriately given the nature of the ADIT and how it affects ComEd's actual costs. *Id.*; 2011 Rate Case Order at 59-60, 62; Housekeeping Order at 26-27. ComEd states that there is no basis, in law or in the record in this proceeding, to overturn that practice or artificially reduce ComEd's recoverable costs.

2. ADIT Related to Plant Additions

a. ComEd Position

ComEd states that C/I witness Mr. Gorman proposes an \$8 million rate base disallowance associated with ComEd's deferred tax liability related to projected plant additions, which would reduce ComEd's revenue requirement by \$0.8 million. ComEd Init. Br. at 18; C/I Ex. 1.0C at 13. ComEd states that although this adjustment falls under the heading of ADIT, no controversy exists about how this type of ADIT should be reflected in rates. ComEd Init. Br. at 18. Instead ComEd states, it is driven by the calculation of depreciation on projected plant additions, which then impacts the amount of ComEd's associated ADIT balance. *Id.* In calculating that ADIT balance, ComEd asserts that the Commission should reject Mr. Gorman's proposed disallowance based on his claim that the Commission should take into consideration only "half of a year of book depreciation on 2015 plant additions" instead of "a full year of book depreciation expense" in this calculation. *Id.*; C/I Ex. 1.0C at 12.

ComEd states that the Commission clearly addressed how ComEd should calculate depreciation related to projected plant additions in its recent Final Order in ComEd's Petition to Make Housekeeping Revisions and a Compliance Change to filed Rate Formula, Docket No. 14-0316, a determination which no party appealed. ComEd Init. Br. at 18-19. ComEd submits that in response to a Staff proposal concerning the calculation of that depreciation, the Commission stated:

Based on the evidence presented in this proceeding, the Commission finds that Staff's adjustment to reflect the impact of applying depreciation rates from ComEd's updated depreciation rate study, which was effective January 2014, to calculate depreciation expense as well as ADIT for the filing year is appropriate, and it is approved. Staff's adjustment provides the best projection of the depreciation expense for the filing year. The Commission agrees with Staff that this adjustment will limit the reconciliation adjustment that will be required in the formula rate proceeding for 2014, and it will minimize any interest that would impact customer rates subsequent to the reconciliation.

Id.; Housekeeping Order at 26.

ComEd states that the C/I proposal is at odds with that finding and that as Staff witness Mr. Kahle testified in this case: "No argument has been offered that any circumstance has changed to warrant adopting a different method for determining the amount of depreciation on projected plant additions to include in the calculation of ADIT." ComEd Init. Br. at 19; Staff Ex. 5.0 at 7. ComEd asserts that continually changing the formula erodes the simplicity and clarity intended by formula ratemaking. ComEd Init. Br. at 19.

In its Reply, ComEd states that the issue concerns the depreciation balance used to calculate the ADIT related to ComEd's projected 2015 plant additions and that no party disputes that ADIT related to plant additions is properly included in rate base or how that ADIT factors into the rate formula. ComEd Reply at 3. ComEd states that C/I simply claim that ComEd "failed to correctly calculate" the amount of that ADIT. *Id.*; C/I Init. Br. at 4. ComEd asserts that no other brief makes that claim, and that Staff affirmatively "recommends that the Commission reject this proposal." ComEd Reply Br. at 3; Staff Init. Br. at 7.

First, ComEd states, contrary to the C/I claim, ComEd calculated the ADIT balance as the Commission has directed. ComEd Reply Br. at 3. ComEd states that the Commission decided how book depreciation on projected plant additions should be calculated in its Order in Docket No. 14-0316. *Id.* at 3-4; Housekeeping Order at 26-27. ComEd submits that the Commission determined that "the 2014 depreciation rates from ComEd's updated depreciation rate study" should be used "to calculate depreciation expense as well as ADIT for the filing year." ComEd Reply Br. at 4; Housekeeping Order at 27 (emphasis added). ComEd states that it followed that direction, as to both depreciation and the resulting ADIT and that the C/I argument is premised on rejecting it. ComEd Reply Br. at 4. ComEd further states that Staff observes, "[t]he Commission

previously rejected the issue raised by Intervenors in its Order in Docket No. 14-0316.” *Id.*; Staff Init. Br. at 7. ComEd asserts that while C/I claim they made no ADIT argument last year (C/I Init. Br. at 6), the calculation of depreciation on projected plant additions was fully litigated and decided. ComEd Reply Br. at 4; Housekeeping Order at 26. ComEd contends that contesting that depreciation calculation is the basis of the C/I ADIT argument. ComEd Reply Br. at 4.

Further, ComEd states that it already explained that both ComEd and Staff agree that C/I cannot justify re-litigating that depreciation issue. *Id.*; Staff Init. Br. at 7. ComEd states that Commission decisions on litigated issues, especially in the context of a formula rate structure are expressly designed to promote rate stability, and should not be altered without good reason. ComEd Reply Br. at 4. According to ComEd, “Mr. Gorman’s proposal now reopens that calculation and adds further complications, without any corresponding benefit to customers or the formula ratemaking process.” *Id.*

ComEd also states that C/I’s claim that calculating depreciation as directed by the Commission will cause an “over-recovery” of costs that will “require[] resolution in some future reconciliation case” is in error. *Id.* at 5; C/I Init. Br. at 5. ComEd states that the depreciation was accurately calculated, as directed by the Commission and, in any event, ADIT on plant additions affects only the Initial Rate Year Revenue Requirement, so “customers are fully protected by the reconciliation process ...” ComEd Reply Br. at 4. ComEd contends that there is no risk of over-recovery. *Id.*

Finally, ComEd asserts that while C/I argue that reliance on the reconciliation process should be minimized regardless of its effectiveness in protecting customers, their proposal will likely increase, not reduce, the size of the future reconciliation required. *Id.* at 5. ComEd explains that under EIMA, projected Initial Rate Year Revenue Requirements tend to understate actual costs for obvious reasons (*e.g.*, the included operating expense is from two years earlier and the capital investment excludes the entire rate year itself). *Id.* According to ComEd, by including an ADIT balance less than that supported by the Commission-approved depreciation, the C/I proposal will *enlarge* the gap between ComEd’s actual and projected 2016 costs and push a *greater* share of ComEd’s actual 2016 costs into the reconciliation process. *Id.* ComEd concludes that if the Commission strives to minimize the size of the reconciliation balance, as it has in the past (*e.g.*, Housekeeping Order at 26), that is yet another reason to reject the C/I proposal. ComEd Reply Br. at 5.

b. Staff Position

C/I propose to change the amount of depreciation on projected assets used to calculate ADIT. C/I Ex 1.0 at 11-13. The Commission previously rejected the issue raised by Intervenors in its 2014 Rate Case Order. 2014 Rate Case Order at 26. No argument has been offered that any circumstance has changed to warrant adopting a different method for determining the amount of depreciation on projected plant additions to include in the calculation of ADIT. Staff Ex. 5.0 at 7. Accordingly, Staff recommends that the Commission reject this proposal.

c. C/I Position

C/I argue that ComEd failed to correctly calculate the ADIT associated with the 2015 plant additions.

ComEd calculated tax depreciation on the 2015 projected additions based on the first-year tax depreciation rates, which reflected approximately half of the full annual rates. However, C/I state ComEd then incorrectly calculated the book depreciation expense on 2015 projected additions using the current depreciation rates. According to C/I, this faulty calculation resulted in a full year of book depreciation expense on 2015 plant additions resulting in half of a year of tax depreciation being compared to a full year of book depreciation. C/I reason that ComEd's approach reduces the level of ADIT in the rate base and increases the revenue requirement.

According to C/I, the calculation of the future year component of the formula rate recognizes 2015 plant additions and the associated depreciation reserve, ADIT and depreciation. C/I Ex. 1.0C at 11. C/I claim that ADIT associated with 2015 plant additions should reflect the first year tax depreciation less the comparable first year book depreciation expense, multiplied by the combined effective income tax rate. *Id.* at 12. C/I showed that first year tax depreciation rates are less than the full-year rates, in recognition of the fact that the plant additions occur throughout the year. *Id.* Therefore, C/I state the amount should be compared to a book depreciation expense that also reflects the fact that 2015 plant additions occur throughout the year. The correct calculation and comparison proposed by C/I reduces rate base by approximately \$9.5 million and the Company's revenue requirement by approximately \$0.9 million. C/I Ex. 2.03. C/I observe that ComEd asserts the C/I proposal affects only the projected plant balances in the Initial Rate Year Revenue Requirement for 2016. ComEd Ex. 8.0R at 25. C/I state ComEd supports its rejection of C/I's proposal arguing that projected plant is an estimate, designed to be an estimate, and will ultimately be reconciled (with interest) in 2016 with actual costs, which ComEd believes fully protects both customers and utilities. *Id.*

C/I argue their proposal considers the protection of both customers and the utilities because the proposal results in a reduction to revenue requirement in the current proceeding resulting in a more accurate calculation of ADIT associated with the 2015 additions, allowing ComEd to recover its reasonable and prudent cost of service now, as opposed to permitting an over-recovery (recovery in excess of its prudent and reasonable cost of service) that requires resolution in some future reconciliation case. ComEd argues that C/I proposed to adjust the calculation of depreciation on projected plant additions when that calculation was modified by the Commission in the last ComEd formula rate case. *Id.* ComEd asserts that C/I's recommendation would change the methodology again, adding complexity in comparisons and general understanding of what is included in the revenue requirement. *Id.*; ComEd Ex. 11.0 at 10. However, C/I respond that their proposal is to calculate an amount of ADIT that accurately reflects the ADIT balance associated with 2015 plant additions. Furthermore, C/I observe their proposal would require changing one formula on one workpaper, making ComEd's complexity argument meritless considering the hundreds of calculations that are performed to determine the revenue requirement.

Staff also suggests that the Commission previously considered and adopted the appropriate method to determine the depreciation expense on the projected plant additions in Docket 14-0316. Staff Ex. 5.0 at 7. Staff asserts no argument has been offered in this case that any circumstance has changed to warrant adopting a different method for determining the amount of depreciation on projected plant additions to include in the calculation of ADIT. *Id.* However, C/I state the argument made here is that the ADIT associated with 2015 plant additions should reflect the first year tax depreciation less the comparable first year book depreciation expense, multiplied by the combined effective income tax rate. C/I Ex. 1.0C at 12. C/I reason that such an argument has not been previously considered by the Commission.

C/I opine that ComEd's calculation of ADIT is correct for tax depreciation, but incorrect for book depreciation. C/I observe that ComEd calculated the book depreciation expense on 2015 projected additions using the current depreciation rates resulting in a full year of book depreciation expense on 2015 plant additions. As a result of these faulty calculations, C/I state half a year of tax depreciation is being compared to a full year of book depreciation resulting in a reduced level of ADIT. This increases the Company's revenue requirement. C/I reason a correct calculation needs to reflect only half a year of book depreciation on 2015 additions. *Id.* C/I's proposal seeks to calculate an amount of ADIT that accurately reflects the ADIT balance associated with 2015 plant additions. C/I state this was not done in the previous ICC docket and should be corrected here.

d. Commission Analysis and Conclusion

Under EIMA, the initial (but not the reconciliation) revenue requirement for each rate year includes an estimate of plant additions made in the year prior to the rate year. Associated with those plant additions are an ADIT balance that the Commission has consistently included in rate base. Last year, the Commission addressed the questions of how this ADIT and the depreciation balance that affects it are to be calculated. Housekeeping Order at 26. In this proceeding, C/I propose an \$8 million rate base disallowance based on using a different measure of depreciation than the Commission directed. Both Staff and ComEd oppose this disallowance.

The Commission rejects this disallowance. The evidence shows that ComEd calculated its depreciation and ADIT balances in accordance with our direction. As the Commission determined last year in accepting our Staff's recommendation, the methodology that ComEd followed here "provides the best projection of the depreciation expense for the filing year," and the Commission agrees with Staff that no changed circumstance warrants adopting a different method for determining the depreciation or the ADIT balance. Nor is there any risk that ComEd will over-recover its costs. The Commission also observes that, while C/I claim that their method of measuring depreciation is more theoretically accurate, even that claim was made with respect to the depreciation balance in isolation. Customers, however, are affected by the revenue requirement as a whole and by the magnitude of any reconciliation adjustment on which interest must apply. The evidence establishes that the full-year measure of depreciation the Commission approved and ComEd uses will both "limit the reconciliation adjustment that will be required in the formula rate proceeding" and "will minimize any interest that

would impact customer rates subsequent to the reconciliation.” *Id.* The approved method is likely to result in a more accurate estimate of the rate year revenue requirement.

3. ADIT Related to Bad Debt

a. ComEd Position

ComEd states that AG/City witness Mr. Brosch proposes an \$18.5 million rate base disallowance of ComEd’s deferred tax asset related to bad debt, which would reduce ComEd’s revenue requirement by approximately \$4 million. ComEd Init. Br. at 19; AG/City Ex. 1.0 at 20. ComEd explains that ADIT reflecting a deferred tax *asset* like this arises when ComEd will receive a tax benefit in a period *after* it recognizes the item on its book income statement. ComEd Init. Br. at 19-20; 2013 Rate Case Order at 11. When this happens, ComEd states that it appropriately reflects the ADIT in rate base because its investors have lost the benefit and use of those additional funds until receipt of the tax benefit, and like any asset funded by investors, it is entitled to rate base treatment. ComEd Init. Br. at 20. Otherwise, according to ComEd, the calculated rate base will not be accurate, and ComEd will not recover its costs. *Id.*

ComEd asserts that Mr. Brosch’s bad debt ADIT disallowance errs first by ignoring the fact that ComEd has effectively pre-paid the taxes on collections and that ComEd will not receive the corresponding tax benefit until later and that the disallowance is unwarranted and inaccurate. *Id.* ComEd states that its “bad debt” balances reflect ComEd’s best estimate of the amount that customers ultimately will not pay. *Id.* ComEd explains that under generally accepted accounting principles (“GAAP”), it records its best estimate of bad debt in the current period for financial statement purposes, but ComEd cannot take a tax deduction related to that bad debt until a specific customer account is identified as worthless and written off, which does not happen until a future period. *Id.* ComEd states that in other words, there is a timing difference between when ComEd records the bad debt expense for book purposes and when ComEd is allowed to take a deduction on its tax return for this item. *Id.* ComEd asserts that the delay in the tax deduction causes ComEd to incur a greater tax liability in the current period than it actually will have in the future, and the related ADIT is therefore a deferred tax asset or a “pre-paid” tax using shareholder supplied funds. *Id.* at 20-21.

Moreover, ComEd asserts that while it is entitled to recover its delivery services costs, including bad debt costs, the customer account balances that are written off are only themselves ultimately socialized to all customers and recovered through ComEd’s Rider UF – Uncollectible Factor (“Rider UF”). *Id.* at 21. But, ComEd states, Rider UF does not include a mechanism to account for the deferred tax asset related to that bad debt, therefore if ADIT is artificially removed from rate base, ComEd asserts that it will not recover its legitimate delivery services costs. *Id.*

ComEd submits that the treatment of ADIT related to bad debt has also been addressed by the Commission in a prior docket and, unlike Mr. Brosch’s proposal, ComEd’s inclusion of this ADIT in rate base is consistent with that decision. *Id.* ComEd states that in ComEd’s initial 2011 formula rate case, the Commission directed ComEd to

include the jurisdictional portion of that deferred tax asset in ComEd's rate base. *Id.*; 2011 Rate Case Order at 62. And, ComEd states that this is the treatment the AG requested in ComEd's 2011 formula rate case. *Id.*

ComEd contends that the AG now requests instead that the Commission exclude this deferred tax asset from rate base. ComEd Init. Br. at 21; AG/City Ex. 1.0 at 20. According to ComEd, Mr. Brosch claims that ComEd cannot include this pre-paid tax in rate base without also *reducing* rate base with the underlying Account 144 – Allowance for Uncollectible Accounts balance sheet credit. ComEd Init. Br. at 21; AG/City Ex. 1.0 at 21-22; AG/City Ex. 3.0 at 4-5. ComEd states that aside from having the improper effect of eliminating this shareholder-funded asset from rate base, Mr. Brosch's argument conflates the treatment of the underlying balance sheet debits and credits with the treatment of the deferred tax assets and liabilities. *Id.* ComEd further states that the fact that a particular form of ADIT is included in rate base does not, and should not, imply that underlying balance sheet entries are offsetting deductions. ComEd Init. Br. at 21-22. ComEd explains that every ADIT asset or liability and its corresponding relationship to its underlying balance sheet debits and credits is different. *Id.* at 22. Here, ComEd states, it has essentially pre-paid the taxes with shareholder supplied funds, thus this ADIT asset should be included in rate base. *Id.* ComEd submits that the Commission has never previously directed that Account 144 be treated as a simple offset or deduction to ComEd's rate base. *Id.*

ComEd also contends that there are several problems with Mr. Brosch's argument that a better way to account for the underlying balance sheet credit would have been to adjust the revenue collection lag in ComEd's cash working capital calculation. *Id.*; AG/City Ex. 3.0 at 8-9. First, ComEd states that the Commission rejected this exact proposal in the 2011 Rate Case Order. *Id.* ComEd contends that there is no basis for relitigating that issue, or for reaching a different conclusion now. ComEd Init. Br. at 22. According to ComEd, the time to raise this issue again – if revisiting it was indeed warranted, and ComEd does not agree with this premise – was in the 2014 Rate Case Order, when the parties analyzed and updated ComEd's leads and lags consistent with the Commission's directive that the parties revisit ComEd's cash working capital study every three years. *Id.*; 2011 Rate Case Order at 56.

Second, ComEd contends that Mr. Brosch's theory that this would lead to a *decrease* in the collections lag is based on the false assumption that there is no revenue collections lag with uncollectibles. ComEd Init. Br. at 22. ComEd states that there is no basis for this assumption. *Id.* To the contrary, ComEd states that it has shown that even if uncollectibles were considered in the cash working capital or rate base calculations, they cannot be presumed to shorten the lag. *Id.* at 22-23. According to ComEd, since ComEd recovers its uncollectibles via Rider UF, “[i]f anything, the lag associated with uncollectible accounts is longer than regular accounts, rather than non-existent.” *Id.*, quoting the 2011 Rate Case Order, ComEd Ex. 16.0 at 6. In other words, ComEd states, it must wait longer to find out which accounts will not be paid – it does not know this when it issues the bills. ComEd Init. Br. at 23. ComEd submits this could actually *increase* the collections lag. *Id.*

ComEd states that C/I and AG/City argue that ComEd's rate base should exclude ADIT related to bad debt, at least unless it is reduced by an allowance for bad debt recorded in Account 144. ComEd Reply Br. at 5; see C/I Init. Br. at 6-7; AG/City Init. Br. at 10-12. ComEd contends that their argument, which has never been accepted by the Commission, relies on inaccurate over-generalizations about ADIT and an inaccurate portrayal of what the ADIT on bad debt and Account 144 actually represent. ComEd Reply Br. at 5-6; ComEd Init. Br. at 22-23. According to ComEd, it has accounted for this ADIT as directed by the Commission. ComEd Reply Br. at 6.

ComEd explains that ADIT on bad debt represents a prepaid tax and that it is a real investment by shareholders that must be included in rate base. *Id.* In contrast, ComEd states, the balance in Account 144 is a book entry that represents no offsetting source of funds. *Id.* ComEd contends that it does not lessen or offset the real investment ComEd shareholders make in the prepaid tax, or reduce ComEd's need to finance and that it has never been and should not be deducted from rate base. ComEd Reply Br. at 6. ComEd states that Account 144 simply recognizes delayed receivables which, if anything, relate to cash working capital, not rate base. *Id.*

Pointing to other types of ADIT created and funded in other ways, ComEd states that C/I argue that "[i]n general, the treatment of ADIT balances that relate to specific asset and liabilities should 'follow' the rate base treatment of the corresponding assets and liabilities." *Id.*; C/I Init. Br. at 7. ComEd further states that the AG/City make a similar, if lengthier, claim that "general principles" of GAAP provide a one-size-fits-all directive concerning the proper *ratemaking* treatment of this ADIT. ComEd Reply Br. at 6; AG/City Init. Br. at 8-10. ComEd submits that neither argument is accurate. ComEd Reply Br. at 6. ComEd states that there are many types of ADIT that arise in different ways and "every ADIT is different." *Id.* According to ComEd, correctly reflecting ADIT balances in ratemaking is not about any blanket rule or accounting convention, but requires consideration of what the ADIT represents and how it is funded. *Id.* And, ComEd states, "while GAAP dictates the methodology for recording revenue and expense items for accounting purposes, it does not purport to predict whether the accounting treatment results in a 'cash benefit' to the business" warranting a particular ratemaking treatment. *Id.* at 6-7; *People ex rel. Madigan v. Illinois Commerce Comm'n*, 2015 IL App (1st) 140275 at ¶42 ("*Madigan*"). ComEd states that for ratemaking purposes, "[e]ach case depends on the purpose of the asset and the related ADIT." ComEd Reply Br. at 7; ComEd Ex. 8.04 at 7.

In addition, ComEd states that AG/City also claim Ms. Brinkman "admitted" that she previously supported the notion of a general offset "accounting principle that Mr. Brosch advocates ..." ComEd Reply Br. at 7; AG/City Init. Br. at 14 (citing Tr. at 49). ComEd asserts that she did not. ComEd Reply Br. at 7. ComEd states that she also directly addressed the inaccurate inference of inconsistency the AG/City brief claims she accepted. ComEd Reply Br. at 7; Tr. at 52. ComEd submits that Ms. Brinkman's testimony reinforces why there is no such general principle and why the proposed reduction in ADIT on bad debt must be rejected. ComEd Reply Br. at 7.

ComEd further contends that AG/City anticipate and try to respond to the fact that the substance of this claim has already been rejected by the Commission. *Id.*; AG/City Init. Br. at 12-14. ComEd asserts that wading through the fine details of the attempt is unnecessary. ComEd Reply Br. at 7-8. ComEd states that AG/City acknowledge that Ms. Brinkman's testimony concerning the equivalent Cash Working Capital argument in Docket No. 11-0721 follows the Commission's decision (while they label her testimony "technically consistent," they point out no respect in which it is not *perfectly* consistent). *Id.* at 8. According to ComEd, AG/City then devolve into a discussion of their witness assignments in 2011, a question ComEd believes to be irrelevant to the Commission's decision, while ultimately acknowledging that "had his [Mr. Brosch's] position in Docket No. 11-0721 been adopted, ComEd's Accumulated Provision for Uncollectibles would have been considered in determining the utility's rate base, which is exactly the matching of ADIT with the associated asset/liability balances that he is proposing in this case." *Id.*; AG/City Init. Br. at 14. ComEd contends, however that the Commission, *rejected* Mr. Brosch's position in Docket No. 11-0721 and the argument AG/City make now is an attempt to undo that decision, which AG/City tacitly acknowledge by referring to the Commission's 2011 Order as having "erroneously rejected" their claim. ComEd Reply Br. at 8; AG/City Init. Br. at 13; see *also* AG/City Init. Br. at 14 (accepting ComEd's practice of following that decision would "perpetuate the error made in the prior case").

Finally, ComEd contends, C/I argue that ComEd's uncollectibles costs are recovered under Rider UF. ComEd Reply Br. at 8. But, ComEd states, Rider UF only recovers ComEd's uncollectibles costs themselves. *Id.* According to ComEd, the costs measured by the ADIT – the prepaid tax – are not recovered through Rider UF, and there is no evidence to the contrary. *Id.* ComEd states that the fact that those real costs are not recovered through Rider UF only reinforces why this ADIT must be included in rate base. *Id.*

In sum, ComEd states, no one can dispute that this deferred tax asset exists. *Id.* ComEd states that it is an asset funded by shareholders and it should be included in ComEd's rate base. *Id.* Therefore, the Commission should reject this proposed disallowance. *Id.*

b. AG/City Position

According to AG/City witness Michael Brosch, deferred income taxes are an "accounting provision for the amounts of additional income taxes that are estimated to become receivable or payable in future periods, because of differences between book accounting and income tax accounting with respect to the timing of revenue or expense recognition." AG/City Ex. 1.0 at 12. AG/City show that Mr. Brosch explained that certain GAAP require that book/tax timing differences be recognized by recording deferred tax expense or income, with the other 'side' of this entry creating ADIT assets or liabilities.

Brosch testified that because utilities are such capital-intensive businesses, they generate large tax deductions and credits related to depreciation and tax deductions and credits. Brosch stated that these large deductions and credits must be normalized by creating ADIT assets and liabilities. He opined that because tax law allows utilities to

claim deductions and credits that do not immediately flow through to ratepayers, only shareholders benefit from the deductions and credits, and thus to account for this zero-cost capital, regulators require that ADIT balances be deducted from rate base so that only the net amount of investor-supplied capital to support rate base assets earns a return that is recovered from ratepayers.

Mr. Brosch reviewed the more-than-100 ADIT balances the Company listed in its Exhibit 2.02 and found that while ComEd included ADIT balances that reduce its rate base by approximately \$3.1 billion, the utility did not include all of its ADIT balances as rate base offsets. Brosch took issue with ComEd's proposal to increase rate base by approximately \$18.5 million by including ADIT debit balances associated with bad debts or uncollectible accounts. Brosch explained that companies do not claim the tax deduction associated with an uncollectible account until the amount owed the utility is actually determined to be worthless; however, GAAP require that bad debts be recognized on an accrual basis, well in advance of the time at which companies claim the associated tax deduction.

Mr. Brosch explained that utilities record on their books a "provision for bad debts" (amounts customers ultimately will not pay) on an estimated basis, as a charge to Account 904 "Uncollectible Accounts," with a corresponding credit to Account 144, "Accumulated Provision for Uncollectible Accounts – credit," as prescribed in the FERC Uniform System of Accounts. AG/City state that, according to Brosch, this Accumulated Provision credit account then serves as a valuation offset to the utility's Account 142 "Customer Accounts Receivable" balances, to include in the utility's balance sheet only the estimated realizable net value of Accounts Receivables, after consideration of expected uncollectible portion recorded therein. Brosch stated that the Account 144 provision for uncollectibles thus reduces the utility's reported assets; then, when any specific customer's account balance later becomes worthless and must be written off, the Account 142 value of the customer's account is reduced and the Account 144 Accumulated Provision balance is charged the same amount.

Mr. Brosch proposed removing ComEd's ADIT debit balance related to bad debts from rate base because the Company did not also include the corresponding Accumulated Provision for Uncollectibles credit balance in Account 144 in rate base. Mr. Brosch concluded that it is fundamentally unfair to inflate rate base by including ADIT related to bad debts "when the associated accounting reserve balance arising from accrual-basis accounting for bad debts is not used to reduce Rate Base." AG/City Ex. 1.0 at 22. AG/City cite Brosch's testimony that ADIT balances should follow the rate base treatment of the corresponding assets and liabilities. AG/City note that ComEd witness Brinkman did not respond to Brosch's testimony that ADIT associated with bad debts should be removed from rate base because the Company has not included in rate base "the corresponding credit 'reserve' for uncollectibles, appearing within Account 144." AG/City Ex. 3.0 at 5.

AG/City argue that its position in this case is consistent with the AG's position in Docket No. 11-0721, contrary to allegations of ComEd witness Brinkman. In Docket No.

11-0721, ComEd proposed to include 100% of ADIT related to bad debt in rate base. AG/AARP witness David J. Effron testified that ComEd's proposal was improper because "[l]ess than 100 percent of bad debt expense is allocated to the jurisdictional revenue requirement, and less than 100% of the ADIT on the Accumulated Provision for bad debt should be allocated to the jurisdictional rate base." AG/City Ex. 3.0 at 7 (citing 2011 Rate Case, AG/AARP 2.0R at 4). AG/City note that the Commission agreed with Mr. Effron's proposal, permitting only a portion of ADIT related to bad debts in rate base, and finding that ComEd presented "no facts establishing that 100% of ADIT that is related to bad debt expense should be allocated to distribution services." 2011 Rate Case Order at 62. AG/City state that the prior decision confirmed a relationship between jurisdictional bad debts expense and the related ADIT, without making any determination regarding the need to consistently either include or exclude the offsetting balance sheet (ADIT/asset and Accumulated Provision for bad debts/liability) accounts in rate base determinations. AG/City now propose to remove the remaining portion of the ADIT related to bad debts that was not previously excluded in Docket No. 11-0721.

AG/City note that Mr. Effron's testimony in the prior case focused on whether, as ComEd recommended, 100% of bad debt expense and ADIT balances should be allocated to distribution services. AG/City show that Effron did not present testimony in Docket No. 11-0721 regarding ComEd's Cash Working Capital lead-lag study, nor was he familiar with whether ComEd's Accounts Receivables or the corresponding offset for Accumulated Provision for Uncollectibles were included in rate base. AG/City state that rather, Mr. Brosch testified regarding the accounting treatment of bad debt in that prior case. Mr. Brosch noted, had his position in Docket No. 11-0721 been adopted, ComEd's Accumulated Provision for Uncollectibles would have been considered in determining the utility's rate base, which is exactly the matching of ADIT with the associated asset/liability balances that Mr. Brosch is proposing in this case.

Mr. Brosch explained that in the earlier case, he recommended that ComEd's uncollectibles be accounted for in the Company's lead-lag study, which would have had the same effect as his proposal in this case – ComEd's uncollectibles would be accounted for in determining the Utility's rate base. AG/City argue that the Commission erroneously rejected Mr. Brosch's proposal in Docket No. 11-0721. 2011 Rate Case Order at 41. As a result, the Company's Accumulated Provision for Uncollectibles balance was not accounted for in the rate base established in that proceeding. AG/City further argue that ComEd's proposal in this case would perpetuate the error made in the prior case – ComEd's rate base would not be adjusted to recognize in rate base the Accumulated Provision for Uncollectibles.

As Mr. Brosch stated, the Commission now has an opportunity to correct its mistake from Docket No. 11-0721 by recognizing that its 2011 Rate Case Order did not include in rate base the credit balance Account 144, the Accumulated Provision for Uncollectibles to reduce cash working capital and, therefore, the rate base should not include the related ADIT balance. AG/City note that on cross-examination, Ms. Brinkman admitted that in her testimony in ComEd's last formula rate update case, she supported the accounting principle that Mr. Brosch advocates here. She testified there that if ADIT

related to the reconciliation balance is included in rate base, then the related asset or liability should also be included in rate base. AG/City argue that this “matching” or “following” is precisely what Mr. Brosch recommends in this case. If, as ComEd recommends, ADIT debit balance related to bad debt is included in rate base, then the related asset or liability – in this instance, the Account 144 Accumulated Provision for Uncollectibles credit balance – must also be included in rate base. AG/City state that alternatively, the Commission can reject ComEd’s proposal to include ADIT related to bad debt in rate base; then it becomes unnecessary to include the Account 144 Accumulated Provision for Uncollectibles credit balance in rate base.

AG/City also state that, while ComEd argues that the Company has effectively pre-paid the taxes on collection and that ComEd will not receive the corresponding tax benefit until later, the timing of cash flows that ComEd now relies upon is normally examined and accounted for within cash working capital studies, and ComEd has consistently declined to do so. Moreover, note AG/City, the argument is inconsistent with ComEd’s constant denial of a relationship to cash flow accounting. At ComEd’s urging, the Commission ruled in the 2011 Rate Case Order that the timing of uncollectible collections and the corresponding Account 144 Accumulated Provision for Uncollectibles liability account should not be considered within lead-lag studies. Finally, argue AG/City, this particular cash flow argument is raised outside the context of ComEd’s lead-lag study, which does not account for the alleged effect ComEd relies upon.

ComEd also argues that Mr. Brosch’s theory that considering bad debts within lead lag studies “would lead to a decrease in the collection lag is based on the false assumption that there is no revenue collections lag with uncollectibles.” ComEd Init. Br. at 22. AG/City argue that as with the “pre-paid the taxes” argument, this point may resonate within a lead-lag study discussion of cash flow timing, but has no home in this docket because AG/City’s argument in this case is not premised on the treatment of cash working capital matters that were decided in the 2011 Rate Case.

AG/City conclude that the Commission should adopt their proposal, which would reduce rate base in each of the 2014 Reconciliation Year and the 2016 Initial Rate Year by \$18.5 million.

c. C/I Position

C/I observe the AG/City is proposing the elimination of the ADIT element captioned, “Provision for Bad Debt” from rate base. C/I opine this ADIT amount is associated with the Company’s accrual basis accounting provisions for Bad Debts, also known as “Uncollectible Accounts”, and serves to overstate ComEd’s proposed Rate Base by approximately \$18.5 million. AG/City Ex. 1.0 at 20.

C/I agree with AG/City that bad debts are deductible for income tax purposes at the time an amount owed to the taxpayer actually becomes worthless. AG/City Ex. 1.0 at 20:482-483. However, GAAP requires the recognition of bad debts on an accrual basis of accounting, well in advance of when customer accounts are actually charged off as worthless, creating a book/tax timing difference for which ADIT amounts are recorded.

The bad debt amounts are accrued before they are actually charged off as worthless and recognized for tax purposes, creating a delayed tax deduction which increases rate base. AG/City Ex. 1.0 at 20-21.

C/I agree with the AG/City assessment that, it is fundamentally unfair to increase Rate Base for bad-debt-related ADIT amounts when the associated accounting reserve balance arising from accrual-basis accounting for bad debts is not used to reduce Rate Base. AG/City Ex. 1.0 at 22.

C/I posit that in general, the treatment of ADIT balances that relate to specific asset and liabilities should “follow” the rate base treatment of the corresponding assets and liabilities. For instance, when credit ADIT balances arise from tax depreciation on plant investments that are included in rate base, those ADIT balances should be included in rate base. AG/City Ex. 3.0 at 5. However, although ComEd has increased its rate base by including the debit ADIT related to Bad Debts/Uncollectibles, C/I point out that it has failed to include the corresponding liability, which would be a reduction to its rate base. This liability is the Accumulated Reserve for Uncollectibles. AG/City Ex. 1.0 at 21-22.

C/I observe that ComEd’s uncollectible expenses are fully recoverable through its Rider UF – Uncollectible Factor. AG/City Ex. 1.0 at 22. Therefore, consistency in accounting treatment requires that ADIT related to Bad Debts/Uncollectibles should be removed from rate base. This is because the Company’s Accumulated Provision for Uncollectibles balance is not in rate base and Uncollectible expense, which is recovered separately through Rider UF, is not included in test year expense. According to C/I, ComEd has failed to demonstrate that its Accumulated Provision for Uncollectibles, which should reduce its rate base, has been recognized anywhere in its rate base calculation, either within Rider UF or its asserted delivery services tariff revenue requirement. The associated ADIT related to bad debts balance should also be excluded from rate base. AG/City Ex. 3.0 at 11.

d. Commission Analysis and Conclusion

ComEd has included in its revenue requirement calculation the ADIT balance related to its accrued bad debt. This is consistent with how ComEd’s rates have been calculated in the past and with our prior decisions. AG/City propose an \$18.5 million rate base disallowance of this deferred tax asset, and C/I join that request in their briefs. The Commission has never accepted such a disallowance and, based on the record, also rejects it here.

Whether and how a particular form of ADIT is reflected in rates is not an abstract question, or one dictated by generic book accounting principles. ADIT itself is a means of addressing a necessary difference between book entries and costs for ratemaking purposes. Also, there are many different types of ADIT and ADIT can arise in many ways. As the Illinois Appellate Court recently held in affirming the Commission’s decision concerning another type of ADIT, while general book accounting rules “dictate[] the methodology for recording revenue and expense items for accounting purposes, it does not purport to predict whether the accounting treatment results in a ‘cash benefit’ to the

business” warranting a particular ratemaking treatment. *Madigan* at ¶42. To set rates that are just and reasonable to both customers and utilities, the Commission must look to the specific characteristics of the ADIT in question, including whether it represents an asset funded by the utility. If it does, it should be reflected in a rate base just like any other asset funded by the utility. Here, the evidence is clear that the bad debt balances are “booked” prior to their recognition as the basis for a tax deduction and ComEd must satisfy the resulting tax liability in advance. That tax prepayment is an asset funded by ComEd shareholders and one that ComEd is entitled to include in rate base.

The argument is made that the book entries in Account 144 must be “offset” against that balance, but this is a formalistic argument. Account 144 represents a book allowance, it does not reflect any cash nor does it provide any source of funds that ComEd can use to pay any part of the prepaid tax liability the ADIT measures. The balance in that account does not, therefore, offset the ADIT that ComEd has actually funded.

Finally, the Commission rejects the argument that ComEd will recover the cost of its tax prepayment through its uncollectibles recovery rider. ComEd’s uncollectibles expense rider only recovers the cost of ComEd’s uncollectibles themselves. The additional cost the Company incurs in connection with the prepaid tax, which is measured by the ADIT on bad debt – is not recovered through that rider. Indeed, the fact that this additional and real cost is not recovered through the uncollectibles rider confirms the need, and the justness, of including that ADIT balance in rate base.

4. Materials & Supplies

a. ComEd Position

ComEd describes its Materials & Supplies (“M&S”) balance as “an inventory of distribution equipment to support its capital projects and to replace necessary equipment, including an emergency reserve.” ComEd Init. Br. at 23. ComEd states its M&S balance of \$52.7 million represents its inventory at year-end 2014 as reflected in its FERC Form 1. *Id.* ComEd requests that the Commission approve this amount and reject C/I witness Mr. Gorman’s proposed \$20.7 million rate base disallowance to ComEd’s M&S inventory balance, which would reduce ComEd’s revenue requirement by approximately \$4.3 million. *Id.*; C/I Ex. 1.0C at 11.

ComEd states that Mr. Gorman incorrectly argues that the actual final historical year-end balance of \$52.7 million is too large because the percentage increase in ComEd’s level of M&S balance since 2010 is too “significant.” ComEd Init. Br. at 23; C/I Ex. 1.0C at 10. According to ComEd, he therefore unlawfully substitutes a hypothetical balance of \$31.977 million based on an average (or normalized) rate of increase in distribution plant and distribution maintenance expense, year over year from 2010 to 2014, of 10%. ComEd Init. Br. at 23; C/I Ex. 1.0C at 10-11.

ComEd further states that as “participating utility” under EIMA, ComEd has elected to recover costs through a performance-based formula rate “which shall specify the cost components that form the basis of the rate charged to customers with sufficient specificity

to operate in a standardized manner and be updated annually with transparent information that reflects the utility's *actual costs* to be recovered during the applicable rate year ..." ComEd Init. Br. at 24; 220 ILCS 5/16-108.5(c) (emphasis added). According to ComEd, EIMA therefore requires that ComEd use actual cost information, more specifically: "final historical data reflected in the utility's most recently filed annual FERC Form 1 ..." ComEd Init. Br. at 24; 220 ILCS 5/16-108.5(d)(1).

ComEd points out that EIMA further states that the formula rate shall:

Provide 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. *The sole fact that a cost differs from that incurred in a prior calendar year or that an investment is different from that made in a prior calendar year shall not imply the imprudence or unreasonableness of that cost or investment.*

220 ILCS 5/16-108.5(c)(1) (emphasis added). ComEd states that EIMA goes on to specifically state: "Normalization adjustments shall not be required." ComEd Init. Br. at 24; 220 ILCS 5/16-108.5(d)(3).

ComEd asserts that per EIMA it used its actual costs: the final historical data reflected in its FERC form 1. ComEd Init. Br. at 24. ComEd states that it submitted ample evidence of the prudence and reasonableness of these costs. *Id.* Specifically, ComEd states that its witness Mr. Moy testified that ComEd considers both "historical usage" and "current demand" in setting inventory levels. *Id.*; ComEd Ex. 6.0 at 19.

In addition, ComEd states that it is careful to avoid delays in completing work due to difficulty in obtaining supplies. ComEd Init. Br. at 25. ComEd explains that in maintaining an appropriate M&S balance, ComEd must therefore consider that certain items such as transformers and cable can require up to 16 weeks lead time. *Id.* ComEd points out that Mr. Gorman admits that he does not dispute the prudence and reasonableness of any specific transactions by which ComEd acquired assets which increased the materials and supplies balance as he looked only at the levels of growth. *Id.*; See ComEd Cross Ex. 3.

ComEd states that Mr. Moy provided additional evidence that the levels of growth in distribution plant and maintenance on the one hand, and M&S inventory on the other hand, are not generally comparable and that while "increases in distribution plant and maintenance are factors that can lead to increases in M&S levels, they are by no means the only factors." ComEd Init. Br. at 25; ComEd Ex. 10.0R at 3. ComEd explains that specifically, since 2010 other factors that have increased ComEd's M&S inventory include the sheer volume of work to implement EIMA infrastructure and reliability investments, as well as the installation of new equipment not previously installed on ComEd's system. ComEd Init. Br. at 25. These factors, ComEd asserts, require it to stock increased volumes of items historically used as well as items not in use prior to 2010, such as AMI meters and their accompanying Network Interface Cards ("NIC"), resilient overhead wire

and cable, and distribution automation switches. *Id.* ComEd states that these three inventory groupings account for \$30.5 million of the \$40.5 million increase in ComEd's M&S inventory since 2010. *Id.*; C/I Ex. 2.0 at 5, 7. ComEd also states it provided further detail for the items comprising the remaining \$10 million increase in its M&S inventory balance. ComEd Init. Br. at 25.

Finally, ComEd describes how Mr. Gorman's averaging or normalization methodology is a sharp departure from Commission practice in ComEd's prior formula rate cases. *Id.* at 26. ComEd states that in every one of those cases, the Commission used ComEd's actual year-end M&S balances. *Id.* According to ComEd, Mr. Gorman's methodology here impliedly rejects those findings and substitutes the normalized amounts in his calculation for the actual yearly figures that the Commission used. *Id.* ComEd further states that the Commission rejected a similar C/I proposal in Ameren's 2014 FRU. *Id.*; *Ameren Illinois*, ICC Docket No. 14-0317, Final Order (Dec. 10, 2014) at 34. In doing so, ComEd notes that the Commission stated: "The Commission comes to this conclusion because CUB and IIEC have not convinced it that such an adjustment is permissible under the EIMA. The averaging of past years' M&S balances would seem to conflict with the bar against normalization of expenses and investments in the EIMA." *Id.*

In its Reply Brief, ComEd states that C/I's proposed disallowance is based on what ComEd asserts is the incorrect and unsupported belief that "the level and growth of the M&S balance should match the level and growth of the distribution plant and maintenance." ComEd Reply Br. at 8; C/I Init. Br. at 8. In response to C/I's position, ComEd details evidence, discussed above, that it asserts shows that the levels of growth in distribution plant and maintenance on the one hand, and M&S inventory on the other hand, are not generally comparable. *Id.* at 8.

ComEd also disagrees with several other arguments made by C/I in their Initial Brief. ComEd states that C/I's claim that no ComEd witness alluded to any delay or problems in obtaining necessary materials and supplies to perform increased construction is in error because, as evidenced by witness testimony, it is because ComEd has maintained an appropriate M&S balance that it has not faced such difficulties. *Id.* at 9. Also incorrect, states ComEd, is C/I's claim that "No ComEd witness testified as to a need for significant lead times between ordering of materials and supplies and placing them into service. *Id.*; C/I Init. Br. at 11. ComEd asserts that it specifically provided evidence that in maintaining an appropriate M&S balance, ComEd must consider that certain items such as transformers and cable can require up to 16 weeks lead time. ComEd Reply Br. at 9-10.

ComEd also takes issue with C/I's argument that the M&S balance includes potential double counting. *Id.* at 10; C/I Init. Br. at 9-10. ComEd explains that the M&S balance reflects the inventory level resulting from the acquisition and installation of facilities and equipment consistent with prudent operational and acquisition practices. *Id.* at 10. Thus, according to ComEd, while facilities and equipment are added to the M&S balance when acquired and ultimately moved to and reflected in plant in service when placed into service, the M&S inventory balance at a given point in time is distinct and

separate from plant in service and does not reflect double counting. *Id.* ComEd further states that the fact that EIMA calls for the inclusion of projected plant additions for the filing year in the Initial Rate Year Revenue Requirement does not double count M&S and is fully consistent with EIMA. Specifically, ComEd states that Section 16-108.5(d)(1) of the PUA refers to using actual data from the most recently available FERC Form 1 and adding “projected plant additions and correspondingly updated depreciation reserve and expense” for the filing year with no reference to a further adjustment for M&S as proposed by C/I. *Id.*; 220 ILCS 16-108.5(d)(1).

In sum, ComEd states that it has shown that the actual final historical cost data from ComEd’s FERC Form 1 reflecting its M&S balance is \$52.7 million and that the M&S making up this \$52.7 million “are both used and useful in meeting ComEd’s obligation to offer and provide delivery services and were prudently acquired at a reasonable cost.” ComEd Init. Br. at 26; ComEd Ex. 6.0 at 19. In contrast, ComEd asserts that Mr. Gorman’s proposal is contrary to the plain language of EIMA, the evidence offered in this case, and Commission practice. ComEd Init. Br. at 26. For these reasons ComEd requests that the Commission accept its M&S inventory balance and reject Mr. Gorman’s proposed disallowance.

b. C/I Position

C/I reason that as a rate base item, ComEd’s M&S balance earns a return and is thus a source of profit for the Company. ComEd describes its M&S as “an inventory of distribution equipment to support its capital projects and to replace necessary equipment, including an emergency reserve.” ComEd Ex. 6.0 at 18. That being the case, C/I argue the level and growth of the M&S balance should match the level and growth of the distribution plant and maintenance. C/I Ex. 1.0C at 10. According to C/I, from 2010 to 2014, ComEd’s distribution plant has increased an average of less than 5% each year, for a total increase of 18.46%. *Id.* at 10. Distribution maintenance expense has increased an average of less than 10% each year, for a total increase of 42.26%. *Id.* at 10-11. These increases do not justify the 141% increase in M&S recorded by the Company since 2010, in C/I’s opinion. *Id.* at 11.

C/I argue that ComEd’s M&S balance had not only significantly increased since 2010, but has exhibited a year-over-year escalation of at least 20%. The M&S balance increases have significantly out-paced increases in maintenance expense and plant additions. C/I Ex. 2.0 at 7. To better match the level and growth of the M&S balance with the level and growth of the distribution plant and maintenance, C/I recommend that the M&S balance be adjusted to reflect an average 10% year-over-year increase. C/I Ex. 1.0C at 11. According to C/I, this adjustment is more representative of the actual growth that ComEd has experienced in distribution plant and maintenance expense, and protects ratepayers from the risk of paying an inflated M&S balance, including a return on that balance.

C/I also demonstrate that the M&S balance includes potential double-counting. ComEd witness Mr. Moy implies that ComEd may have built up its 2014 M&S inventory to address projected 2015 plant additions. See ComEd Ex. 10.0R at 5. C/I reason that

rates set in this proceeding will recover both 2014 actual, year-end M&S balance as well as 2015 projected plant additions. C/I Ex. 2.0 at 6. C/I argue that since a portion of the 2014 year-end M&S balance is intended for use as 2015 projected plant additions, that portion will be double-recovered – once in the 2014 M&S balance and again in the 2015 projected plant additions. *Id.* C/I state ComEd has acknowledged the potential for an item to be included in both the M&S and projected plant additions balance, but ComEd claims it would be “immensely difficult, if not impossible, to determine what specific inventoried items” may be affected. ComEd Ex. 11.0R at 12. ComEd therefore argues that any attempt at adjusting either balance to eliminate double-counting would simply be “another estimate – an estimate that is not necessarily better than the current one used and one that will be reconciled in the following year in any event.” *Id.* C/I observe that while ComEd acknowledges the potential for double-counting, its argument is essentially that it has no better method of accounting and thus its proposed M&S levels are close enough for now.

C/I make clear there is also potential for large and unnecessary M&S build-ups as year-end draws near so that the Company earns a return on that M&S as if it was in inventory for the entire year. This, according to C/I, is exhibited by the transition of the December inventory balance from an average or below average balance in 2010 through 2012 to the largest balance during the year in 2013 and 2014. See C/I Cross Ex. 1 and ComEd Ex. 2.3 at 44. C/I state that when asked, ComEd was unable to provide month-end balances for the specific supplies discussed in their testimony. See C/I Cross Ex. 2 at 1. Instead, the Company objected to providing such data, stating that it does not track specific inventory balances broken down by supply category. *Id.* C/I reason that since the Company has not provided monthly balances for any particular inventory item or even inventory category, the Commission has no way to verify ComEd’s claims about what items are driving the increase in the inventory balance.

C/I state ComEd originally took issue with Mr. Gorman’s recommendation, claiming, in general, that it was too late to make an adjustment because it was contrary to previous original cost determinations and because previous years’ M&S balances had already been approved. ComEd Ex. 8.0R at 29-30. However, on surrebuttal, ComEd witness Ms. Brinkman admitted that Mr. Gorman’s adjustment does not, in fact, retroactively change previously-established rates, nor is it counter to any prior original cost determinations. ComEd Ex. 11.0R at 11.

C/I state no Company witness has alluded to any delays or other problems in obtaining the necessary materials and supplies to perform increased construction. Therefore, C/I conclude that there should be no need for large increases in stores of inventory, or for acquiring inventory well in advance of when it is needed. C/I observe that though the Company cited three specific items that it claimed accounted for the increase in M&S balance, ComEd did not justify maintaining higher inventory balances for those items. C/I opine that while increased usage may require ordering larger quantities of certain supplies, if those supplies are truly needed, then they should be put into service rather than being stored and counted as inventory items. C/I Ex. 2.0 at 6. No ComEd witness testified as to a need for significant lead times between ordering of

materials and supplies and placing them into service. C/I claim that because the Company has an incentive to build up larger-than-needed inventory (so that it can begin earning a return on those items), the Commission must be mindful of that incentive and ensure that the Company's M&S balance is not unnecessarily inflated, leading to inflated rates for customers.

In summary, it is C/I's position that it is the Company's burden to prove that its requested level of recovery is just and reasonable, and ComEd did not provide adequate justification for the significant increase in its M&S levels as compared to its actual maintenance expense increases and distribution plant addition levels. Therefore, recovery for M&S should be limited to no greater than a 10% average year-over-year, for a total of a 46.41% increase since 2010. C/I Ex. 1.0C at 11. That is compared to the Company's proposed 141% increase over that same time. *Id.* at 11. The recoverable balance should thus be no greater than \$31.977 million, resulting in an adjustment to the Company's rate base and revenue requirement of \$20.7 and \$4.3 million, respectively. *Id.* at 11.

c. Commission Analysis and Conclusion

The Commission agrees with ComEd and finds that C/I's proposal to use a year-over-year average amount for ComEd's M&S inventory balance instead of ComEd's actual FERC Form 1 figures is unlawful. The Commission reaches this conclusion because C/I's proposal is contrary to the plain language of EIMA, which states that the formula rate must use the utility's "actual costs." 220 ILCS 5/16-108.5(c). Specifically, the formula rate must use "final historical data reflected in the utility's most recently filed annual FERC Form 1 ..." 220 ILCS 5/16-108.5(d)(1). EIMA further provides that differences in costs from year to year "shall not imply the imprudence or unreasonableness of that cost or investment," and "[n]ormalization adjustments shall not be required." 220 ILCS 5/16-108.5(c)(1); 220 ILCS 5/16-108.5(d)(3).

The Commission rejected a similar C/I proposal in Ameren's 2014 FRU. *Ameren Illinois*, ICC Docket No. 14-0317, Final Order (Dec. 10, 2014) at 34. C/I have offered no new evidence or argument, and the Commission is still unconvinced this adjustment is permissible under EIMA. As the Commission has previously stated: "The averaging of past years' M&S balance conflicts with the bar against normalization of expenses and investments in the EIMA." *Id.* C/I's averaging or normalization methodology is also contrary to Commission practice in every one of ComEd's prior formula rate cases: in every one of those cases, the Commission used ComEd's actual year-end M&S balances.

In addition, the Commission rejects this disallowance because it lacks any evidentiary support. ComEd submitted evidence of the prudence and reasonableness of the costs at issue. C/I argued only that the level and growth of the M&S balance should match the level and growth of the distribution plant and maintenance. ComEd provided evidence to the contrary, that the levels of growth in distribution plant and maintenance and M&S inventory are not generally comparable. ComEd also provided evidence that since 2010, other factors that have increased ComEd's M&S inventory include the sheer volume of work to implement EIMA infrastructure and reliability investments, as well as

the installation of new equipment not previously installed on ComEd's system. These factors require ComEd to stock increased volumes of items historically used as well as items not in use prior to 2010, such as AMI meters and their accompanying NIC, resilient overhead wire and cable, and distribution automation switches. Based on the evidence in the record, the Commission is satisfied that ComEd's M&S balance is a cost of delivery service that is prudently incurred and reasonable in amount.

However, the Commission is cognizant that excessive inventory increases rate base and that the dollar amount of inventories has increased dramatically relative to plant additions in this filing. The Commission directs ComEd to provide specific justification for significant increases in year end inventory balances by supply category in future formula rate filings.

V. OPERATING EXPENSES

A. Overview

ComEd supported its 2014 total operating expenses, adjusted to reflect the depreciation expense associated with the projected 2015 plant additions. ComEd Ex. 12.01, Sch FR A-1, line 11. There are a limited number of contested operating expenses issues, as discussed below.

B. Uncontested Issues

1. Distribution O&M Expenses

ComEd states that its Distribution Operating and Maintenance ("O&M") expenses were \$466,699,000 for 2014. ComEd explains that after reflecting adjustments, a revised total of \$461,417,000 in distribution O&M expenses recorded in FERC Accounts 580-598 is included in the revenue requirement. ComEd Ex. 2.0 at 28; ComEd Ex. 12.01, Sch FR A-1, line 1 and Sch FR C-1, lines 1 and 11. This amount is adjusted later in this Order because of our findings regarding the incentive compensation adjustment.

2. Customer-Related O&M Expenses

ComEd states that its customer-related expenses are expenses recorded in FERC Accounts 901-910, which include the costs of maintaining and servicing customer accounts, *e.g.*, meter reading, customer service, and billing and credit activities. ComEd Ex. 2.0 at 28. ComEd explains that in determining the revenue requirement, ComEd has adjusted the \$496,534,000 of customer related expense for the following:

- (1) \$214,606,000 reduction to remove the costs associated with ComEd's energy efficiency and demand response program recovered under Rider EDA;
- (2) \$45,131,000 reduction to reflect the total amount of uncollectible accounts expense recorded in FERC Account 904, costs recovered through Rider UF;
- (3) \$12,239,000 reduction to remove customer care costs related to supply.

- (4) \$584,000 reduction to remove the non-jurisdictional amount of Outside Agency Collection Fees related to uncollectibles;
- (5) \$171,000 increase to include interest on customer deposits in operating expenses;
- (6) \$1,760,000 reduction to remove costs recovered under Rider PORCB;
- (7) \$936,000 reduction to remove customer assistance costs incurred as part of the \$10,000,000 EIMA customer assistance program;
- (8) \$875,000 reduction to remove certain customer communications costs recorded in FERC Account 908;
- (9) \$199,000 reduction for company credit card costs;
- (10) \$15,000 increase related to Rider MSS;
- (11) \$2,658,000 increase for a donation to the Illinois Science and Technology Foundation; and
- (12) \$27,000 reduction for residential real-time pricing.

ComEd Ex. 2.0 at 28-29; see also ComEd Ex. 12.02, WP 7, line 38f; ComEd Init. Br. at 27-28.

ComEd states that after these adjustments, \$223,021,000 of FERC Accounts 901-910 directly related to and supporting the delivery service function are included in the revenue requirement. ComEd Ex. 2.0 at 29-30; ComEd Ex. 12.01, Sch FR A-1, lines 2 and 3 and Sch FR A-1-REC, lines 2 and 3. No party has objected to the amount of customer-related O&M expenses. The Commission approves this amount.

3. Uncollectibles Expense

ComEd states that it has removed \$45.1 million from FERC Account 904 related to uncollectible expense and therefore has included no uncollectible customer balance in its delivery service revenue requirement. ComEd also states that it has included in the delivery service revenue requirement the costs associated with ComEd's activities to collect past due accounts. ComEd Ex. 4.0 at 11; ComEd Ex. 2.0 at 29. The Commission approves these amounts.

4. Administrative and General Expenses

ComEd states that its Administrative and General ("A&G") expenses were \$345,033,000 for 2014. ComEd explains that A&G costs are recorded in FERC Accounts 920-935 and include corporate support and overhead costs that benefit or derive from more than one business function; costs of employee pension benefits; regulatory expenses; and certain other non-operation costs. ComEd Ex. 2.0 at 30-31; ComEd Ex.

12.01, Sch FR A-1, line 4. ComEd Init. Br. at 29. The Commission approves the adjusted amount discussed later in this Order.

5. Charitable Contributions

ComEd states that in response to Staff's inquiry regarding the classification of certain charitable contributions through rate base instead of through Rider EDA, ComEd adjusted its operating expenses relating to charitable contributions. See Staff Ex. 2.0R, Attachment A (ComEd's Response to Staff Data Request BCJ 2.03). ComEd states that as adjusted on rebuttal, ComEd has included in its operating expenses a jurisdictional amount (based on the W&S allocator) of the total of \$6,456,000 in charitable contributions. ComEd Ex. 2.0 at 43; ComEd Ex. 9.01, App 7, line 5.

Staff proposes an adjustment to disallow recovery of expenses classified as charitable contributions because the costs should be recovered through Rider EDA, Energy Efficiency and Demand Response Adjustment, instead of through base rates. Staff Ex. 2.0R, 10. ComEd agrees that the expenses were misclassified and should be included in ComEd's Rider EDA. Staff Ex. 2.0R, Attachment A.

No party has objected to the adjusted amount of charitable contribution expense. The Commission approves this amount.

6. Merger Expense

a. ComEd Position

ComEd states that on April 14, 2014, Exelon Corporation ("Exelon") and Pepco Holdings, Inc. ("PHI") signed an agreement and plan of merger to combine the two companies (the "Proposed Merger"). ComEd further states that for the year 2014, ComEd incurred a total of approximately \$4.4 million in merger related costs to achieve ("CTA") of which an Illinois jurisdictional amount of approximately \$3.8 million is included in ComEd's total A&G. ComEd Ex. 2.0 at 34-35; ComEd Ex. 12.01, Sch FR A-1, line 4 and FR A-1 REC, line 4. ComEd asserts that it offered undisputed evidence that the CTA were prudently incurred and reasonable in amount. ComEd Ex. 6.0 at 65-66.

According to ComEd, the merger was expected to close in the third quarter of 2015. Tr. at 22-23; ComEd Ex. 15.0. The District of Columbia Public Service Commission ("DC Commission"), however, ruled against the proposed merger on August 25, 2015. AG/City Ex. 4.2. Subsequent to the DC Commission ruling, on August 26, 2015, the AG/City witness Mr. Brosch filed supplemental direct testimony proposing to remove CTA incurred in 2014 related to the Exelon/PHI merger. See *generally*, AG/City Ex. 4.0. ComEd disagrees with the AG/City proposal. However, in order to limit the issues in this case and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd agreed that if the Exelon/PHI merger has not closed by December 1, 2015, ComEd will voluntarily withdraw its request to recover 2014 Exelon / PHI merger related costs. Tr. at 24-25 and 27-28.

In its Reply Brief, ComEd notes that the AG/City has requested in their Initial Brief that ComEd and the Commission meet three additional terms, in addition to ComEd's potential withdrawal of these CTA. ComEd Reply Br. at 11. ComEd states that although it does not agree with the timing, manner, or merits of this request, in order to further limit the issues in this case and without waiving its right to contest other proposals based on similar arguments in this case, or other proposals based on this or similar arguments in any other proceeding, ComEd: (1) is willing to provide alternative revenue requirements for inclusion in the Commission's order; (2) accepts AG/City's definition of "closed" as the occurrence of all the actions and conditions contemplated in Articles I, II, III, IV, and VII of the Agreement and Plan of Merger at issue, dated April 29, 2014; and (3) will submit a certification to the Commission by December 2, 2015 stating that the merger has closed, if the merger has closed by December 1, 2015. *Id.* at 11-12. ComEd states that it cannot, however, commit to filing Exelon's 8K until that document is filed with the United States Securities and Exchange Commission ("SEC"), which may be later than December 2, 2015. *Id.* at 12. ComEd also takes issue with the AG/City's assertion that the undisputed evidence shows that the proposed merger costs are not recoverable and states that the evidence shows only that in the interest of limiting the issues in this case ComEd has not litigated this issue further and it is moot. *Id.* at 11; AG/City Init. Br. at 19, fn 16.

b. AG/City Position

AG/City note that in the year 2014, a total of approximately \$3.84 million in Illinois-jurisdictional Proposed Merger integration costs were either incurred by ComEd or allocated from Exelon to ComEd. AG/City state that in this proceeding, ComEd has included: (a) approximately \$4.42 million of Proposed Merger integration costs in the 2014 Reconciliation Year revenue requirement (including interest on the 2014 reconciliation balance, pursuant to 220 ILCS 5/16-108.5(d)(1)); and (b) approximately \$3.84 million of Proposed Merger integration costs in the 2016 Initial Rate Year revenue requirement. AG/City propose conditionally disallowing recovery of the 2014 merger integration costs from this proceeding, as outlined further below.

AG/City note that Exelon and PHI already obtained required regulatory approval from the FERC and the utility commissions of Virginia, New Jersey, Maryland, and Delaware. However, they note that on August 25, 2015, DC Commission voted 3-0 to deny approval of the Proposed Merger under applicable statutory authority in that jurisdiction.

AG/City observe that in the 2012 Rate Case Order, the Commission found that where costs are incurred for the purpose of realizing post-merger savings, the costs are recoverable where, inter alia, net savings are "reasonably likely to occur" and where ComEd customers are "allocated savings that are reasonably proportional to the risks they face." *Id.* at 79. AG/City note that their witness Michael Brosch observed in his Supplemental Direct Testimony that "if the merger is not consummated, there can be no merger-enabled cost savings benefits to ComEd's ratepayers in Illinois and, therefore, the costs incurred in connection with the merger should not be charged to Illinois ratepayers." AG/City Ex. 4.0 at 2. AG/City further note that ComEd admitted in a

discovery response that obtaining regulatory approval for the Proposed Merger and consummating it is required to secure the associated cost savings.

As AG/City report Mr. Brosch concluded that as of August 26, 2015, consummation of the Proposed Merger is not reasonably likely, because of: (1) the DC Commission's August 25, 2015 decision; (2) press reporting of DC Commission board member Betty Anne Kane's oral comment on August 25th stating that "this decision is forever" and indicating that it was not enough for the companies to prove that the public would not be harmed by the deal and that they had to prove the public would be helped; and (3) the statutory standard (D.C. Code § 34-606) in D.C. that creates a standard of deference to DC Commission factual findings on appellate review in the District of Columbia Court of Appeals. AG/City further note that in direct examination at the evidentiary hearing held August 27, 2015 in this case, ComEd witness Brinkman stated that she had no knowledge of whether the DC Commission would reverse its decision pursuant to a reconsideration request. Because the record was marked heard and taken at the conclusion of the evidentiary hearing, AG/City take the position that the evidentiary record, including Mr. Brosch's testimony and Ms. Brinkman's statements, indicates that approval of the Proposed Merger is not likely.

Notwithstanding that, in the interest of simplifying issues, AG/City agree to a proposal made by ComEd witness Brinkman during supplemental oral direct examination at the evidentiary hearing that if the Proposed Merger has not closed by December 1, 2015, ComEd will voluntarily withdraw its request to recover 2014 Exelon / PHI merger related costs. However, AG/City propose some additional terms to make the proposal actionable by the Commission in a way that assures recovery of only appropriate costs.

First, AG/City urge that the Commission's Order must state expressly the alternative revenue requirement amounts, the determinative conditions that must exist on December 1, 2015, and the process for determining resulting rates pursuant to the Order.

Second, AG/City suggest that the term "closed" should mean that all actions and conditions contemplated in Articles I, II, III, IV, and VII of the Agreement and Plan of Merger among PHI, Exelon, and Purple Acquisition Corp. dated April 29, 2014 as required for the "Closing" (as defined in Section 1.2 of that agreement) shall have occurred.

Third, AG/City propose that the Company should submit a certification by December 2, 2015, in this proceeding stating whether the Proposed Merger closed by 11:59 PM CST on December 1, 2015, and providing supporting documentation (in the form of a Form 8-K filed with the SEC certifying the closing of the merger) if the Proposed Merger did in fact close by 11:59 PM CST on December 1st. AG/City further request that the Commission take administrative notice of such a certification from ComEd, pursuant to Section 200.640(a)(7) of the Commission's Rules.

AG/City propose, as they did in their Initial Brief, that if ComEd does not submit such evidence on or before December 2, 2015, the Commission should, consistent with

Ms. Brinkman's proposal and its appropriate Order, disallow recovery in this proceeding of the 2014 integration costs associated with the Proposed Merger.

c. Commission Analysis and Conclusion

The Commission notes that the AG, the City, and ComEd are all in agreement that the Commission should allow recovery of the 2014 integration costs for the Proposed Merger if – and only if – the merger closes by December 1, 2015. This arrangement can be adopted by the Commission only if consistent with the Commission's prior decisions on merger cost recovery, which required that cost savings from a merger be reasonably likely in order to make the related merger integration costs recoverable, and that customers be allocated savings reasonably proportional to the risks they face. See 2012 Rate Case Order at 79. The Commission cannot approve recovery of the 2014 merger integration costs if consummation of the proposed merger, and thus realization of the related net savings, appears not reasonably likely.

Lack of approval of the merger by December 1, 2015 could mean that either: (1) Exelon and PHI did not apply to the DC Commission within 30 days – by September 8, 2015 – for reconsideration; or (2) Exelon and PHI timely applied to the DC Commission for reconsideration, but the DC Commission denied the request by late October of 2015, within 60 days after the original denial, and Exelon and PHI then appealed to the DC Court of Appeals and the appeal was pending as of December 1, 2015; or (3) the DC Commission denied a timely reconsideration request, and Exelon and PHI then appealed to the DC Court of Appeal, which affirmed the DC Commission's decision by December 1, 2015; or (4) the DC Commission denied a reconsideration request and then Exelon and PHI did not file an appeal in the DC Court of Appeals as of December 1, 2015 (although they would have 60 days from the DC Commission's denial of reconsideration in late October to file an appeal, pursuant to D.C. Code § 34-605). The Commission finds, based on the evidence in the record, that under the first and third scenarios, approval of the merger would be impossible; and under the second and fourth scenarios, approval of the merger would not be reasonably likely because of the statutory standard in D.C. that creates a standard of deference to DC Commission factual findings on appellate review (D.C. Code § 34-606). On the other hand, if the merger closed by December 1, 2015, then, according to evidence in the record, net cost savings are likely to be achieved.

Thus, the Commission finds that the test for cost recovery agreed to by AG/City and ComEd correctly applies the Commission's standard for recovery of merger integration costs.

The Commission will allow recovery of the 2014 Exelon/PHI integration costs, which contribute approximately \$4.4 million (including interest on the reconciliation balance) to the 2014 Reconciliation Year revenue requirement and approximately \$3.8 million to the 2016 Initial Rate Year revenue requirement, if and only if it has received a certification from ComEd on e-Docket by December 2, 2015 stating that the Exelon/PHI merger "closed" by December 1, 2015. The certification must be accompanied by some definitive documentation, such as a Form 8-K filed with the SEC, that is capable of being

administratively noticed pursuant to Section 200.640(a)(7) of the Commission's Rules, 83 Ill. Admin. Code § 200.640(a)(7).

Furthermore, because ComEd (did / did not) file such certification on e-Docket by December 2, 2015, which (filing / omission) the Commission hereby takes administrative notice of under Section 200.640(a)(7) of the Commission's Rules, recovery of the 2014 merger integration costs (are / are not) allowed, because the evidence shows that (approval of the merger makes the realization of net savings reasonably likely / lack of approval of the merger makes the realization of net savings not reasonably likely).

Alternative 1. The Commission finds that the merger closed on or prior to December 1, 2015, and it is undisputed that these costs are prudently incurred and reasonable in amount. The Commission approves this merger expense amount.

Alternative 2. The Commission finds that the merger has not closed on or prior to December 1, 2015. In order to limit the issues in this case, and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd has voluntarily withdrawn these costs.

7. Charges for Services Provided by BSC

ComEd states that BSC is an Exelon affiliate service company that provides services such as information technology, supply, finance, and human relations to ComEd and Exelon's other business units. ComEd Ex. 3.0 at 6. In 2014, ComEd states it incurred \$243,506,627 in costs for services provided by BSC. ComEd Ex. 3.0 at 6; ComEd Ex. 2.10 at 4, column (b). No party contests the BSC charges for the services provided to ComEd. Therefore, the Commission approves the amount of charges.

8. Regulatory Commission Expense (Rock Island Clean Line)

Staff witness Ms. Jones proposed an adjustment to disallow recovery of expenses associated with ICC Docket No. 12-0560 related to Rock Island Clean Line LLC because the costs are not related to delivery service. Staff Ex. 2.0R at 7. ComEd accepted Ms. Jones' proposal and, as adjusted on rebuttal, removed \$320,000 of expense associated with Rock Island Clean Line LLC resulting in a decrease to ComEd's revenue requirement of \$688,000. ComEd Ex. 9.0 at 22; ComEd Ex. 9.02, WP 7 at 8, line 18; ComEd Ex. 9.07, line 3; Staff Ex. 2.0R at 7. No party contests ComEd's regulatory commission expense as adjusted. Therefore, the Commission approves the amount of regulatory expense.

9. Depreciation and Amortization Expense

ComEd states that its revenue requirement, adjusted on surrebuttal, includes \$522,902,000 of depreciation and amortization expense. ComEd Ex. 12.01, Sch FR C-2, line 10. ComEd explains that the level of 2014 depreciation and amortization expense included in the revenue requirement is \$473,085,000, comprised of \$373,571,000 related to Distribution Plant and \$99,514,000 related to G&I Plant. ComEd Ex. 2.0 at 36. ComEd

further explains that the 2016 Initial Rate Year Revenue Requirement and the 2016 Rate Year Net Revenue Requirement include \$49,817,000 of depreciation expense associated with the 2015 projected plant additions. The Commission approves an adjusted amount discussed later in this Order.

10. Taxes

ComEd states that the amount of taxes other than income included in its revenue requirement is \$142,766,000. ComEd explains that these taxes include real estate taxes, the Illinois Electricity Distribution Tax (“IEDT”), payroll taxes, and several other taxes. ComEd Ex. 2.0 at 37; ComEd Ex. 2.01, App. 7 at 2, lines 41 through 62; ComEd Ex. 2.01, Sch FR C-1, line 10. ComEd states that regarding IEDT, ComEd recorded an accrual in 2014 for an estimated IEDT credit of \$14,076,000 related to its actual 2014 IEDT of \$117,299,000, and a credit adjustment of \$1,340,000 to the estimated IEDT credits for the year 2013, reflecting the net amount of \$101,883,000 in operating expense. *Id.* at 37-38. ComEd also states that in compliance with the 2013 Rate Case Order, it excluded \$634,000 of payroll taxes related to previously disallowed incentive compensation. *Id.* at 37; See ComEd Ex. 2.02, WP 7 at 2, lines 41 and 42.

ComEd further states that the amount of income taxes included in the 2014 Reconciliation Revenue Requirement is \$188,559,000 and that the amount of income taxes included in the 2016 Initial Rate Year Revenue Requirement, which includes the impact of the projected 2015 plant additions, is \$225,444,000. ComEd Ex. 12.01, Sch FR A-1- REC, lines 15, 18 and 19; ComEd Ex. 12.01, Sch FR A-1, lines 15, 18, and 19. ComEd explains that income taxes have been calculated based on the expenses and miscellaneous revenues assigned or allocated to the delivery service function. ComEd further explains that it also analyzed differences in book and tax treatment of 2014 revenues and expenses and assigned or allocated those differences to the delivery service function as described in ComEd Ex. 12.01, Sch FR C-4 “Taxes Computation” and App 9 “Permanent Tax Impacts Information.” ComEd Ex. 2.0 at 38.

Although AG/City and C/I initially proposed a disallowance related to State Income Taxes, they have withdrawn that proposal. Staff Ex. 11.0R at 2; AG/City Ex. 3.0 at 2; C/I Ex. 2.0 at 12. The Commission approves an adjusted amount as discussed later in this Order.

11. Rate Case Expenses

a. ComEd Position

ComEd seeks to recover rate case expenses totaling \$2.3 million, comprised of the following:

- (1) ComEd’s rate case expenses of \$8,310 incurred in 2014 for ICC Docket No. 07-0566;

- (2) ComEd's rate case expenses of \$186 incurred in 2014, offset by the return of an overpayment of \$652 recorded in 2014, for ICC Docket No. 10-0467;
- (3) Amortization of \$694,219 of allowed expenses incurred in 2012 for ICC Docket No. 11-0721 and approved in ICC Docket No. 13-0318;
- (4) Amortization of \$65,995 of allowed expenses incurred in 2013 for ICC Docket No. 11-0721 and approved in ICC Docket No. 14-0312;
- (5) Amortization of \$23,758 of expenses incurred in 2014 for ICC Docket No. 11-0721;
- (6) ComEd's rate case expenses of \$9,757 incurred in 2014 for ICC Docket No. 12-0321;
- (7) ComEd's rate case expenses of \$162,351 incurred in 2014 for ICC Docket No. 13-0318; and
- (8) ComEd's rate case expenses of \$1,324,585 incurred in 2014 for ICC Docket No. 14-0312.

ComEd supported these expenses with an affidavit (ComEd Ex. 1.03) and supporting invoices. ComEd Init. Br. at 33.

ComEd submits that this evidence allows the Commission to make a finding pursuant to Section 9-229 of the PUA that the expenses incurred were just and reasonable. ComEd explains that the attachments to the affidavit provide the evidentiary support for each ICC proceeding for which ComEd seeks recovery. See ComEd Ex. 1.03 APO-04 REV., Ex. 1.03 APO-05 REV., Ex. 1.03 APO-06 REV., Ex. 1.03 APO-07 REV., Ex. 1.03 APO-08 REV., Ex. 1.03 APO-09 REV. ComEd further explains that the affidavit also describes the services provided in connection with the fees for which recovery is sought, identifies the individuals working on the matters and their qualifications, and discusses the market rates charged by regulatory lawyers in Chicago to support the reasonableness of the fees charged. ComEd Ex. 1.03 APO-01 (identifying individuals and qualifications); ComEd Init. Br. at 34.

In response to Staff witness Ms. Jones' proposed adjustment to disallow \$24,529 of rate case expense related to the testimony submitted by ComEd witness Mr. Warren in the 2014 Rate Case (Staff Ex. 2.0R at 11-14), in order to limit the issues in this case, and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd agreed not to seek recovery for this expense in this Docket and made the adjustment, thus reducing ComEd's 2016 Rate Year Net Revenue requirement by \$46,000. ComEd Ex. 8.0R at 31-32; Staff Ex. 2.0R, Sched. 2.06 at 2. ComEd states that on surrebuttal it corrected an error in its revenue requirement to reflect Staff's adjustment, further reducing ComEd's 2016 Rate Year Net Revenue requirement by \$6,000. ComEd Ex. 12.0 at 9-10; ComEd Ex. 12.03.

In its Reply Brief, ComEd noted a discrepancy in Staff's and ComEd's calculation of these expenses. ComEd Reply Br. at 12. The figures provided in ComEd's Initial Brief are correct and were adjusted in Staff's Reply Brief. Staff Reply Br. at 5-6.

b. Staff Position

Staff proposed an adjustment to rate case expense to limit the amount of fees recoverable for consultant James Warren. Staff Init. Br. at 9; Staff Ex. 2.0R at 11-12. ComEd disagreed with Staff's adjustment but, to limit the issues in this proceeding, ComEd does not contest the adjustment. Staff Init. Br., 9; ComEd Ex. 8.0 at 31. Though ComEd did not contest the adjustment, there was a discrepancy between the calculations provided by Staff and ComEd in their respective IBs. This discrepancy is due to an inadvertent failure to adjust for ComEd's reclassification of \$1,940 out of rate case expense to rate design and ComEd's removal of \$215 from the revenue requirement. The reasons for this were provided in the Company's Responses to data requests. Staff adopts the figures presented in ComEd's Initial Brief. The correct amounts are \$783,972 associated with Docket No. 11-0721; \$1,324,585 associated with Docket No. 14-0312; and \$179,952 associated with various other dockets, resulting in a total rate case expense of \$2,288,509. ComEd Init. Br. at 33. This discrepancy does not affect Staff's calculation of revenue requirements.

Section 9-229 of the Act (220 ILCS 5/9-229) requires the Commission to specifically assess the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing in the Commission's final order and to expressly address the issue in the Commission's final order. Staff recommends that the Order in this proceeding express a Commission conclusion as follows:

The Commission has considered the costs expended by the Company during 2014 to compensate attorneys and technical experts to prepare and litigate rate case proceedings and assesses that the amount included as rate case expense in the revenue requirements of \$2,288,509 is just and reasonable. This amount includes the following costs: (1) \$783,972 amortized rate case expense associated with the initial formula rate proceeding, Docket No. 11-0721; (2) \$1,324,585 associated with Docket No. 14-0312; and (3) \$179,952 associated with the litigation of Dockets No. 07-0566, 10-0467, 12-0321, and 13-0318.

Staff maintains that if the Commission makes any adjustments to rate case expense beyond Staff's proposed adjustment, those adjustments also should be considered in the Commission's statement that sets forth the amount of rate case expense included in the revenue requirement. Staff Ex. 2.0R at 13-14.

c. Commission Analysis and Conclusion

The Commission has considered the costs expended by the Company during 2014 to compensate attorneys and technical experts to prepare and litigate rate case proceedings and assesses that the amount included as rate case expense in the revenue requirements of \$2,288,509 is just and reasonable. This amount includes the following

costs: (1) \$783,972 amortized rate case expense associated with the initial formula rate proceeding, Docket No. 11-0721; (2) \$1,324,585 associated with Docket No. 14-0312; and (3) \$179,952 associated with the litigation of Dockets No. 07-0566, 10-0467, 12-0321, and 13-0318.

12. Corporate Credit Cards (Employee Recognition)

Staff witness, Ms. Jones, proposed an adjustment to disallow ComEd credit card expenditures related to ComEd employee recognition. Staff Ex. 2.0R at 7-9; Staff Ex. 6.0R at 6-8. Staff argues that these expenditures have not been shown by ComEd to be just and reasonable or prudent and reasonable costs necessary for the provision of delivery services, nor have the expenditures been shown to enhance in some way a customer's experience. Rather, Staff states that benefits accrue to employees in the form of perquisites that are in addition to the compensation the employees receive for performing their work. If ComEd chooses to recognize employee accomplishments, those employee recognition expenses should be the responsibility of utility shareholders. Staff Ex. 2.0R at 7-8.

ComEd disagrees with Staff's proposal. However, in order to limit the issues in this case and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd accepted Ms. Jones' proposal to remove these specific credit card expenditures and reduced its revenue requirement in the amount of \$1,194,000. ComEd Ex. 12.0 at 9; ComEd Ex. 12.03, line 15.

The Commission adopts Staff's proposed adjustment and finds that these expenditures should be removed from the revenue requirement.

13. Long-Term Incentive Compensation Program Expenses

a. Key Manager Long-Term Performance Plan

ComEd states that the Key Manager Long-Term Performance Plan ("LTPP") was established in 2013 to replace the restricted Stock Award Program and that the program grants a cash award that vests over three years. ComEd Ex. 1.0 CORR. at 29. ComEd further states that in 2014, the program was extended to ComEd executives below Senior Vice President to replace approximately 50% of the incentive compensation that was provided within the long term incentive programs previously offered to executives below Senior Vice President. *Id.*; See ComEd Ex. 1.01 ComEd explains that LTPP goals relate to capital and O&M expenses, frequency and duration of outages, safety, customer satisfaction, and EIMA Reliability metrics and that awards are determined by taking a simple average of performance on unweighted ComEd goals to determine whether there will be a payout. *Id.* at 30. The uncontested costs associated with LTPP are prudent and reasonable and are approved by the Commission.

b. Long-Term Performance Cash Awards Program

ComEd states that the Long-Term Performance Cash Awards Program (“LTPCAP”) was established to replace approximately 50% of the incentive compensation previously provided within the executive long term incentive programs offered to executives below Senior Vice President (the other 50% of the incentive compensation was replaced by adding executives to the LTPP) and that LTPCAP grants a cash award that vests at the end of a three year performance cycle. ComEd Ex. 1.0 CORR. at 31. ComEd explains that LTPCAP goals relate to capital and O&M expenses, frequency and duration of outages, safety, customer satisfaction, and EIMA Reliability metrics and that awards under this program are determined by taking the average performance on ComEd’s goals in each year over a three year performance cycle. At the end of the three-year performance cycle, a payout percentage is determined based on an average of the annual performance results and that the annual performance percentage used in this three year average uses the weighted performance for each metric on the LTPCAP performance scale. *Id.* at 31-32; ComEd Ex. 1.01, Appendix. A. The uncontested costs associated with LTPCAP are reasonable and prudent and are approved by the Commission.

14. Gross Revenue Conversion Factor

ComEd submits that its Gross Revenue Conversion Factor (“GRCF”) is 1.700. ComEd Init. Br. at 36. No party has objected to the GRCF. Therefore, the Commission approves ComEd’s GRCF.

C. Contested Issues

1. Short-Term Incentive Compensation Program Expenses – Annual Incentive Program

a. ComEd Position

ComEd states that the Commission should reject Mr. Bridal’s proposed disallowance of \$10 million of ComEd’s Annual Incentive Program (“AIP”) expense related to ComEd employees’ distinguished level performance in 2014 in its entirety. ComEd Init. Br. at 36-37; Staff Ex. 4.0 at 3. Mr. Bridal’s rationale is that these AIP awards are, by definition, above market levels and are therefore imprudent and unreasonable under any circumstance. ComEd Init. Br. at 36-37; Staff Ex. 4.0 at 3-4. ComEd argues that, in other words, Mr. Bridal categorically objects to potential AIP payouts above market levels, and particularly AIP payouts of 200%, opining that such payouts are imprudent and unreasonable *per se*. ComEd Reply Br. at 13; Staff Ex. 4.0 at 3-5. Mr. Bridal defines above market as AIP payouts more than 150%. *Id.* It is undisputed, however, that ComEd’s 2014 AIP payout was less than 150%. The payout was 126.1%. ComEd Ex. 8.0R at 8; Staff Ex. 4.0 at 4. The 2014 payout is well below both Mr. Bridal’s theoretical limit of 150% and the plan maximum of 200%.

ComEd states that this straightforward approach does not support a disallowance. ComEd contends that Mr. Bridal thus sets forth an argument to disallow the portions of the weighted average of ComEd's AIP calculation attributable to distinguished performance for each of the eight AIP metrics. Staff Ex. 4.0 at 4; Staff Ex. 7.0 at 3. In other words, he dissects the balanced scorecard that culminates in ComEd's total AIP payout – that is undisputedly within market levels – to manufacture a disallowance of \$10 million. ComEd Ex. 1.0 CORR. at 20; Staff Ex. 7.0 at 4-5. ComEd points out that Mr. Bridal's own example in his testimony looks at the *total AIP payout* – not the calculation per metric – to determine whether the total AIP award is prudent and reasonable. Staff Ex. 7.0 at 4-6. ComEd argues that the Commission should do the same. ComEd Reply Br. at 13.

ComEd also states that it has provided evidence that its employees' total compensation is at market levels and that any AIP awards earned through distinguished level performance are commensurate with increased customer benefits. ComEd Init. Br. at 37. ComEd further states that in fact, customers enjoyed greater savings than they would have had ComEd employees not performed so well, net of the cost of the payouts, and that the incentives worked as they were designed. *Id.* ComEd asserts that Mr. Bridal does not dispute any of this. *Id.*

ComEd further states that the fundamental concept of incentive compensation is "pay at risk." *Id.* ComEd explains that instead of paying the entire amount of an employee's compensation through base salaries, ComEd makes a portion of each employee's pay subject to the achievement of operational metrics specified in the incentive compensation plans. *Id.* ComEd further explains that AIP is part of the incentive compensation portion of the total compensation package. *Id.* ComEd asserts that it is undisputed that ComEd sets total compensation, including base salaries, benefits, and incentive compensation, at levels necessary to remain competitive with comparable companies, also referred to as market levels. *Id.*

ComEd states that its 2014 AIP had eight operational metrics, also referred to as goals or Key Performance Indicators ("KPIs"). *Id.* According to ComEd, the AIP, as to each of its metrics, includes three levels: (1) a threshold level that must be met in order for any payment to be made under the metric, and which, if met, results in 50% payment of the target payment level for the metric; (2) a target level, which, if met, results in 100% payment of the target level for the metric; and (3) a more rigorous distinguished level, which, if met, could result in up to 200% payment of the target level for the metric. *Id.*

ComEd states that Mr. Bridal acknowledges that in 2014, ComEd employees achieved distinguished level performance on four metrics: Occupational Safety and Health ("OSHA") Index (200%), Customer Average Interruption Duration ("CAIDI") Index (150%), Customer Operations Index (145%), and EIMA Performance Metrics Index (167%). *Id.* at 38; Staff Ex. 4.0 at 4. However, ComEd notes that Mr. Bridal does not mention that ComEd employees also achieved distinguished level performance on the Total O&M Expenses metric, reducing costs by \$24 million. ComEd Init. Br. at 38. ComEd states that this distinguished performance, combined with ComEd employees'

performance on the remaining KPIs, resulted in an AIP payout of 126.1%. *Id.* According to ComEd, its operational excellence should be commended but instead, Mr. Bridal takes the position that ComEd should not be able to recover the entire cost of this AIP expense and should instead be limited to a 150% payout level for each metric, regardless of the performance level actually achieved. *Id.*; Staff Ex. 4.0 at 3; Staff Ex. 7.0 at 2.

ComEd contends that it is undisputed that ComEd's AIP metrics are consistent with EIMA ratemaking and provide benefits to customers and that distinguished achievement of incentive compensation goals that are properly considered in the revenue requirement provide benefits to ComEd's Customers in excess of achievement of those incentive compensation goals at the target level. ComEd Init. Br. at 38.

For example, ComEd states that in order to meet the 2014 target performance level for the O&M expense metric, ComEd must spend no more than \$947.8 million. *Id.* ComEd further states that to meet the distinguished performance level for the O&M expense metric, ComEd would reduce that O&M expense by another \$95 million (distinguished level O&M = \$853). *Id.* at 38-39. In addition, ComEd states that the incremental AIP expense associated with this distinguished level performance is \$15 million and that the savings to customers associated with that distinguished level performance, through lower O&M expenses, exceeds the resulting incremental AIP expense, generating a total of approximately \$80 million of net benefits to customers (\$95 million in O&M savings less \$15 million in additional incentive compensation expense). *Id.* at 39. ComEd concludes that this results in a net jurisdictional savings of approximately \$76 million. *Id.*

ComEd states that similarly, to meet the 2014 target performance level for the capital metric, ComEd must spend no more than \$1,565.2 million. *Id.* at 39. ComEd further states that to meet the distinguished performance level for the capital metric, ComEd would reduce capital expenditures by another \$157 million (distinguished level capital = \$1,408.7 million), resulting in a jurisdictional reduction to the revenue requirement of approximately \$12 million in the current year, which also provides savings in rate base for future years. *Id.* ComEd asserts that the resulting incremental AIP expense of approximately \$15 million drives a jurisdictional increase to the revenue requirement of approximately \$7 million. *Id.* According to ComEd, this generates approximately \$5 million of net benefits to customers (\$12 million in jurisdictional capital savings less \$7 million in additional jurisdictional incentive compensation expense). *Id.* ComEd states that using its actual 2014 payout, net O&M savings to customers on a jurisdictional basis was approximately \$19 million (\$21 million in O&M savings less \$2 million in additional incentive compensation expense). As ComEd did not meet the target performance level for capital expenditures, there are no incremental savings or incremental AIP expense related to capital expenditures. *Id.* ComEd states it also provided testimony about the tangible benefits of achieving distinguished level performance on other AIP metrics. *Id.* at 39-40.

ComEd states that Mr. Bridal improperly argues to disallow the portions of the weighted average of ComEd's AIP calculation attributable to distinguished performance

for each of the eight AIP metrics in an attempt to manufacture a \$10 million disallowance of ComEd's total payout which ComEd states is undisputedly within market levels. ComEd Reply Br. at 13. ComEd asserts that Mr. Bridal would disallow these costs even though they generate a net benefit to customers and that such a disallowance is arbitrary and capricious and creates a perverse incentive for ComEd and its employees. ComEd Init. Br. at 40. ComEd states that the disallowance sends a message to ComEd employees that they should try to be good but not great; and that they should try to benefit customers some but not too much, otherwise the Commission will penalize ComEd financially. *Id.*

In addition, ComEd asserts that Mr. Bridal's recommendation also evidences a fundamental misunderstanding of the pay at risk and market level compensation concepts. *Id.* ComEd states that market level performance and compensation are not static. *Id.* Specifically, ComEd states that if ComEd employees perform exceptionally, their compensation increases but that does not mean their total compensation is above market, it simply means their compensation matches their performance. *Id.* According to ComEd, total compensation, considering performance levels, is still a balanced scorecard at market level. *Id.*

Alternatively, ComEd states that if the Commission adopts Mr. Bridal's proposal to reduce the AIP distinguished level payout to 150%, it should not adopt his calculation of the disallowance because applying Mr. Bridal's suggested 150% maximum payout would change ComEd's recoverable AIP expense to a 118.7% payout, not 111.7%. *Id.*; Staff Ex. 7.0 at 10 and Attachment D. ComEd explains that this is because the performance and payout scales for each ComEd incentive compensation plan are designed in an integrated and coordinated fashion and thus it is incorrect to change either the performance or payout scale independently. ComEd Init. Br. at 40. According to ComEd, Mr. Bridal has made this error by changing only the payout scale and not the performance scale. Staff Ex. 7.0 at 10-11.

ComEd asserts that Mr. Bridal's proposal to reduce the distinguished payment level to 150%, in part because 150% is the maximum payout under the LTPCAP for distinguished performance (Staff Ex. 4.0 at 3-5), fails to take into account that the performance level that is needed to achieve distinguished performance under the 2014 LTPCAP was designed with the 150% scale in mind. ComEd Init. Br. at 41. ComEd explains that it is not the same performance level needed under the 2014 AIP to achieve distinguished performance under the 200% scale. *Id.* Specifically, ComEd explains that while both the 2014 LTPCAP and AIP programs are composed of the same metrics, the results that are needed to achieve distinguished performance are proportionately higher for each KPI under the AIP (due to the higher maximum payout) than what is needed to achieve distinguished performance under LTPCAP (due to the lower maximum payout). ComEd argues that Mr. Bridal has therefore not only reduced the recoverable level of pay ComEd employees would receive (his intended consequence); he has made it harder to earn that pay (an unintended consequence). *Id.*

More importantly, according to ComEd, Mr. Bridal's proposal is inappropriate because AIP and LTPCAP are two different plans as ComEd's AIP is a short term plan available to all employees and the LTPCAP is a long term plan available to executives. *Id.* ComEd states that it is not suggesting that the Commission completely align the AIP and LTPCAP. *Id.* ComEd asserts that it is inappropriate to change only the payout scale and not the performance scale for the AIP. *Id.* ComEd further asserts that the converse is also true – ComEd would not decrease the AIP performance scale to 150% while leaving the payout scale at 200%, because this would make it easier to earn more compensation. By adjusting both the maximum payout and the equivalent performance level to 150%, according to ComEd, ComEd's AIP would be recovered at a level of 118.7%, not the 111.7% calculated by Mr. Bridal. *Id.* ComEd states that this reduces only the amount of recoverable compensation that can be earned and does not change the difficulty level of achieving that compensation. *Id.* at 42.

ComEd also discounts Mr. Bridal's argument that "changing the already narrow performance improvement required to earn distinguished level payout" would not be reasonable as that would lead to "only slight incremental improvement from the target levels." *Id.*; Staff Ex. 7.0 at 7-8. ComEd observes that Mr. Bridal is a CPA, not an Electrical Engineer and opines that he has no expertise or education on which to base his opinion. ComEd Init. Br. at 42; Staff Ex. 4.0 at 1.

ComEd explains that for many of the operational metrics, the threshold performance level is set at first quartile performance under the Edison Electric Institute ("EEI") peer panel with consideration of ComEd's historical performance. ComEd Init. Br. at 42. Target is set between first quartile and Best in Class, and the distinguished performance level is set at Best in Class. *Id.* ComEd states that in order to receive a 100% payout on these metrics, and receive this portion of at-risk pay, ComEd employees must meet first quartile or better performance. *Id.*

ComEd further explains that while Mr. Bridal describes the movement between target and distinguished as a "slight incremental improvement from the target performance levels" (Staff Ex. 7.0 at 8), when viewed through an operational lens, even slight movement at this level of performance is exceptionally difficult to achieve. ComEd Init. Br. at 42. To support its argument, ComEd states that it provided detailed operational testimony on these issues including ComEd witness and Electrical Engineer Ms. Maletich who testified: "Mr. Bridal fails to recognize how hard it is to move [the System Average Interruption Frequency Index, or] SAIFI and CAIDI reliability performance in an upward fashion while already performing at first quartile." ComEd Ex. 14.0 at 5. And "as performance on SAIFI and CAIDI improve, further improved performance becomes more difficult to achieve." *Id.* ComEd states that as it addresses "the 'low hanging fruit' it becomes harder to maintain the same high amount of SAIFI improvements per dollar invested." *Id.* at 6.

In reply, ComEd states that Mr. Bridal incorrectly believes that incentive compensation plans must have a "lawful limiter to protect ratepayers," and that the absence of a limiter in ComEd's 2015 AIP justifies application of his 150% inter-metric

limit. ComEd Reply Br. at 13; Staff Init. Br. at 12. Regarding this issue, ComEd asserts that neither EIMA nor Commission practice require the use of a limiter and that the customer benefit test codified in EIMA appropriately protects customers. ComEd Reply Br. at 14; see 220 ILCS 5/16-108.5(c)(4)(a). ComEd also states that it has provided evidence in this proceeding that ComEd employees' distinguished achievement has benefited customers in excess of the cost of the commensurate AIP payout and thus no protection is needed. ComEd Reply Br. at 14. ComEd further states that the facts of this case, with a 126.1% payout, do not justify Mr. Bridal's recommendation that is predicated on a hypothetical situation where total AIP compensation could reach 200%. *Id.*

ComEd also opines that Staff's alternative suggestion, offered for the first time in briefing, that the Commission could limit ComEd's AIP expense to 102.9% (Staff Init. Br. at 13) is unlawful. ComEd Reply Br. at 14. ComEd states that although the Commission has limited the recoverable amount of ComEd's AIP payout to 102.9%, that occurred under three unique circumstances. *Id.* ComEd explains that in the first case, the 102.9% was supported by the facts in the record, as 102.9% was what the payout percentage would have been using ComEd's net income limiter. *Id.* In the second case, ComEd states that while the appeal from the 2011 Rate Case was pending, in order to limit the issues and without waiving its rights in future proceedings, ComEd voluntarily excluded payouts in excess of 102.9%. *Id.*; 2013 Rate Case Order at 58-59. In the third case, ComEd states that Staff presented testimonial evidence in support of 102.9% as an alternative compromise position resulting from the AG's proposal that 100% of ComEd's AIP be disallowed due to the Shareholder Protection Feature and ComEd accepted the 102.9% alternative compromise position. ComEd Reply Br. at 14.

ComEd cites *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 405 Ill. App. 3d 389, 398 (2d Dist. 2010) for the proposition that a Commission finding of imprudence and unreasonableness must be based on substantial evidence and states that in this case the proposed alternative is not lawful because there is no evidence that supports disallowing ComEd's AIP expense in excess of 102.9%, and ComEd does not agree to that figure. ComEd Reply Br. at 15. ComEd reiterates that the facts in this case support ComEd's 126.1% payout, there is no appeal pending related to AIP, and ComEd removed the Shareholder Protection Feature that served to limit AIP based on the 2014 Rate Case Order. ComEd requests that the Commission deny Mr. Bridal's proposed disallowance and allow full recovery of ComEd's AIP expense associated with ComEd employees' distinguished performance. ComEd argues that this is the only outcome that is fair and equitable and provides the proper incentive to achieve future customer benefits.

b. Staff Position

Staff argues that the Commission should adopt Staff's adjustment to reduce ComEd's AIP cost to a reasonable amount by lowering the payout percentage associated with "distinguished" achievement from the 200% to 150% consistent with the "distinguished" payout used in the Company's new LTPCAP. In the absence of any lawful limiter to protect ratepayers from higher than market level costs associated with AIP awards determined by utilizing 200% payouts, Staff's adjustment reduces the maximum payout level for each AIP metric from 200% to 150% resulting in an overall AIP payout of

111.7%. Further, Staff's proposed AIP payout percentage retains the opportunity for ComEd to recover market level compensation plus a reasonable bonus. Staff Ex. 7.0 at 2-4; Staff Ex. 4.0, Sch. 4.01.

Staff's AIP Adjustment Proposal

Staff's adjustment is made with regards to the reasonableness of the 200% payout level for distinguished performance towards each of the eight AIP metrics. Staff agrees with ComEd witness Ms. Brinkman that the eight AIP metrics are generally consistent with EIMA ratemaking. Staff further agrees that achievement of appropriately set performance goals within those metrics may provide customer benefits. (Staff Ex. 7.0, 3.) However, neither the metrics themselves nor the perceived customer benefits are at issue here. At issue is whether it is reasonable for ComEd to recover from ratepayers the entirety of AIP costs that ComEd determined using a 200% payout for each individual AIP metric. In the absence of any lawful limiter to protect ratepayers from higher than market level costs associated with AIP awards determined by utilizing 200% payouts, Staff's adjustment reduces the maximum payout level for each AIP metric from 200% to 150% consistent with the maximum payout level used for distinguished performance under ComEd's new LTPCAP. *Id.* A 150% payout for distinguished performance towards each of the eight metrics is reasonable and in line with the 150% payout for threshold performance and 100% payout for target performance utilized for both the AIP and LTPCAP metrics. A 150% payout also retains the opportunity for ComEd to recover market level compensation plus a reasonable bonus from ratepayers. The current use of 200% unreasonably inflates the total AIP costs beyond what is reasonable to provide market level compensation funded by ratepayers. *Id.*

ComEd's Analyses of Customer Savings Are Incomplete

ComEd argues that customers have benefited from the distinguished level of achievement towards the eight AIP metrics in excess of the incremental expense associated with this achievement. ComEd goes so far as to claim Staff's adjustment is arbitrary and capricious and creates a perverse incentive for ComEd and its employees. ComEd Init. Br. at 2. Staff agrees that the achievement of appropriately set performance goals within the ComEd AIP metrics may provide customer benefits. Staff Ex. 7.0 at 3. However, ComEd's IB arguments regarding customer savings are short sighted and fail to recognize that Staff's adjustment to reduce AIP payout percentages to a reasonable level: (1) actually increases the benefit provided to ratepayers through lower costs for the same high level of employee achievement; and (2) is clearly based on the Company's own long term incentive compensation payout percentages. Thus, any implication that Staff's adjustment somehow reduces the benefit to ratepayers or is based on anything other than record evidence is wrong.

ComEd's analysis of ratepayer benefits was limited to an individual examination of two specific metrics: Total O&M Expense and Capital Expenditures. ComEd Ex. 11.0R at 3-4. In each instance, ComEd concludes that the savings to customers associated with the distinguished level of performance exceeds the resulting incremental AIP

expense. *Id.* However, ComEd's argument misses three important points. First and foremost, ComEd fails to acknowledge that Staff's adjustment to reduce the payout percentage for distinguished performance for each AIP metric from 200% to 150% – the same distinguished payout percentage used by ComEd in its LTPCAP incentive compensation plan – would reduce the above market AIP costs associated with distinguished achievement and thereby increase the customer savings in the ComEd examples. Second, the ComEd analyses examine the impacts of significantly reduced O&M Expense and Capital Expenditures in a vacuum. ComEd provided no analysis of the impacts that such reduced costs may have on other areas such as reliability, employee safety, and customer satisfaction. Third, ComEd provided no analysis that its payout percentage results in the greatest net benefits to ratepayers. Since a public utility has the burden of proving that the costs for which it seeks reimbursement “directly benefits the ratepayers or the services which the utility renders,” (*Candlewick Lake Utilities v. Illinois Commerce Comm'n*, 122 Ill.App.3d 219, 227) ComEd should have provided such an analysis.

ComEd's faulty claims that Staff's adjustment is arbitrary and capricious and somehow creates a perverse incentive for ComEd and its employees to not perform to their best abilities are both confusing and unsettling. ComEd Init. Br. at 40. First, Staff's adjustment cannot be arbitrary and capricious. Arbitrary and capricious is by definition “action taken by an administrative agency or inferior court meaning willful and unreasonable action without consideration or in disregard of facts or without determining principle.” Black's Law Dictionary, 96 (5th ed. 1979). Contrary to the Company's claims, Staff's adjustment is based on the record evidence and long established Commission principle. Given that ComEd sets its target compensation (including incentive compensation) at market levels, AIP awards paid at 200% of target could cause actual compensation to significantly exceed market values. Staff Ex. 7.0 at 4-6. Pursuant to Section 5/16-108.5(c)(1), ComEd through its formula rate is only allowed to recover costs which are prudently incurred and reasonable in amount. 220 ILCS 5/16-108.5(c)(1). Compensation that exceeds market rates is not a reasonable or prudent cost to be recovered from captive ratepayers of a regulated monopoly such as ComEd. Staff Ex. 4.0 at 4. In its 2014 Rate Case Order, the Commission expressed its concern regarding this specific issue, observing that the design of the AIP could result in above market salaries if the performance on the operational metrics are high enough. 2014 Rate Case Order at 51. In the absence of any lawful limiter that might protect ratepayers from higher than market level costs associated with AIP awards determined by utilizing 200% payouts, Staff's adjustment reduces the maximum payout level for each AIP metric from 200% to 150%, consistent with the maximum payout level proposed by the Company for distinguished performance under ComEd's LTPCAP. Staff Ex. 7.0 at 3. Given the fact that the Commission expressed concern about the potential for AIP to result in above market salaries and the fact that Staff's adjustment is based on record evidence in this case, Staff's AIP adjustment is not arbitrary or capricious. With regards to ComEd's unsettling suggestion that Staff's AIP adjustment would cause ComEd or its employees to strive for good rather than great, Staff simply notes that the 150% payout for distinguished performance proposed by Staff still provides for a 50% bonus for performance above a target level which ComEd has testified is already challenging in

itself. ComEd Ex. 11.0R at 6; ComEd Ex. 14.0 at 5-6. The record contains no evidence that ComEd employees would discontinue the high levels of service that are suggested by their 2014 AIP performance if the Commission determines a 150% payout towards distinguished achievement is more reasonable than the 200% currently provided for in ComEd's AIP plan. Moreover, the Company can choose to continue to reward employees at the 200% level if ComEd so desires, but ComEd should not expect ratepayers to provide an overly generous bonus. The 50% differential between ComEd and Staff's position must be shouldered by shareholders.

Finally, with regards to ComEd's comments regarding Staff's understanding of the pay at risk and market level compensation concepts, ComEd's argument also misses its mark. ComEd Init. Br. at 40. As recently as the 2014 Rate Case, Staff witness Mr. Bridal analyzed and filed testimony favorable to the pay at risk and market level compensation concepts, stating "I have no policy objection to incentive compensation plans per se. I understand that such programs can provide useful incentives to employees and, depending on the structure of such programs, can provide value to ratepayers." 2014 Rate Case, Staff Ex. 8.0 at 15. Further, ComEd's argument that market level performance and compensation are not static assumes facts not in evidence and is factually inaccurate. No party provided evidence that market level performance or compensation is variable throughout the test year. To the contrary, ComEd's own testimony sets forth specific and static amounts of market level target performance and also states that ComEd sets compensation at levels necessary to remain competitive with comparable companies. ComEd Ex. 1.0 CORR at 20-21; ComEd Ex. 1.01 at 4. That ComEd employees may be compensated above market level rates for distinguished performance (or below market level rates for threshold performance) is not evidence that market levels are variable; rather, this is evidence that ComEd performance and compensation levels are variable as compared to the static market level used to set those target amounts. ComEd's arguments should be dismissed.

For the reasons set forth above, Staff's adjustment to reduce the payout level for distinguished performance towards each of the eight AIP metrics from 200% to 150% should be adopted. Staff's adjustment reduces the AIP payout recovered from ratepayers from 126.1% to 111.7%, which still allows ComEd to recover market level compensation plus a reasonable bonus.

Staff states that if the Commission agrees that an adjustment to AIP is warranted but does not agree with Staff's proposed adjustment, the record in this proceeding and the Commission's Orders in recent ComEd formula rate proceedings provide various alternative adjustments for the Commission's consideration. Staff Init. Br. at 13.

c. C/I Position

C/I recommend the Commission adopt the adjustment of Staff witness Bridal, which reduces ComEd's AIP cost to a reasonable amount by lowering the payout percentage associated with "distinguished" achievement from 200% to 150%. This adjustment would make incentive payments for the AIP consistent with the "distinguished" benchmark used in the Company's new LTPCAP, and represents a reasonable level of

payout to incent the achievement of operational metrics. The 200% payout level employed by ComEd, however, would result in an unreasonable amount of incentive compensation being collected from its captive ratepayers, according to C/I.

ComEd seeks to recover from ratepayers the entirety of AIP costs, which includes a 200% payout for each individual AIP metric. Staff Ex. 7.0 at 3. Mr. Bridal's adjustment reduces the maximum payout level for each AIP metric from 200% to 150% to protect ratepayers from higher-than-market level costs associated with AIP awards. *Id.* C/I agree. C/I state Mr. Bridal's 150% payout for distinguished performance towards each of the eight metrics is more reasonable and in line with the 50% payout for threshold performance and 100% payout for target performance utilized for both the AIP and LTPCAP metrics. According to C/I, Mr. Bridal's proposal to limit "distinguished" achievement payouts to 150% represents a prudent and reasonable progressive award for higher levels of achievement of operational metrics.

C/I observe the current use of 200% payout unreasonably inflates the total AIP costs beyond what is necessary to provide market level compensation plus a reasonable bonus. Staff Ex. 4.0 at 4. As Mr. Bridal testified, use of an unconstrained 200% payout for distinguished achievement levels in 2014 resulted in a 126.1% AIP award influenced by 200% payout for the OSHA metric, 150% payout for the CAIDI metric, 145% payout of the Customer Operations metric, and 167% payout of the EIMA reliability metric. Staff Ex. 4.0 at 3-4. C/I aver that both Ms. Brinkman's direct testimony and rebuttal testimony focus on whether the AIP metrics are consistent with EIMA ratemaking and whether the AIP metrics benefit customers. However, C/I point out that ComEd's rebuttal testimony does not address the reasonableness of using a 200% payout for each individual AIP metric in the determination of AIP costs recovered from ratepayers. Staff Ex. 7.0 at 4. While Ms. Brinkman testified that "even slight movement at this level of performance is exceptionally difficult to achieve," (ComEd Ex. 11.0R at 6), she did not recognize that a bonus of 150% of market-based salary is similarly exceptional. C/I conclude that moving that reward to the 200% level is not reasonable and will result in inflated rates.

C/I state that ComEd attempted to justify the different performance scales between the LTPCAP distinguished award of 150% and the AIP distinguished award of 200% based on the payout schedule of the plan. ComEd witness Brinkman testified that the LTPCAP is a long-term incentive plan offered only to executives, scored and awarded on an average of three consecutive years of performance, and paid out after three years. ComEd Ex. 11.0R at 7. The AIP, in contrast, is a one year short term plan, available to all ComEd employees, and is paid out each year. *Id.* ComEd claims the use of the same metrics, but ". . . it is not possible to score them exactly the same (i.e. the AIP cannot be averaged over three years), and "it is reasonable to score the executive plan a bit harder than the plan applicable to all employees." *Id.* ComEd then claimed that Staff's calculation of the proposed disallowance for AIP "distinguished" achievement is flawed, and suggested an alternative AIP payout determination that would reduce the performance level associated with the payout if Staff witness Bridal's adjustment to payout percentages is adopted. ComEd Ex. 8.0 at 8. Mr. Bridal disagreed with Ms. Brinkman's alternative AIP payout determination for three reasons: (1) changing the

already narrow performance improvement required to earn distinguished level payout for many of the AIP metrics is not reasonable; (2) the alternative AIP payout determination does not change the performance or payouts for the EIMA Reliability Metrics Index sub-metrics commensurate with the other seven AIP metrics; and (3) in order to completely align AIP to the scale used within the LTPCAP as suggested by Ms. Brinkman, interpolation of payout percentages between AIP performance levels should be eliminated and replaced with specific payout percentages assigned to defined ranges of performance within the LTPCAP. Staff Ex. 7.0 at 7. According to C/I, ComEd's suggested alternative is, therefore, just as problematic as the 200% "distinguished" achievement award because it does not accurately align AIP performance levels with award levels.

C/I conclude that under the circumstances of this case, Staff's proposed adjustment to the ComEd AIP should be adopted by the Commission.

d. Commission Analysis and Conclusion

The Commission agrees with Staff's adjustment to reduce the payout percentage associated with distinguished achievement performance from 200% to 150%. No party is contesting the AIP metrics or that the metrics provide customer benefits. At issue is the reasonableness of a 200% payout for the distinguished performance level.

The Commission agrees that Staff's adjustment will allow ComEd to recover market level compensation plus a reasonable bonus. ComEd argues that it provided evidence indicating ComEd employees' distinguished achievement has benefited customers in excess of the cost of the commensurate AIP payout. However, there is no evidence in the record showing that lowering the bonus would provide any disincentive for employees to produce the maximum available benefits for ratepayers, especially considering that a 150% payout level is consistent with the maximum payout level for distinguished performance under LTCAP, and consistent with the incremental payout percentages for lower performance thresholds in the AIP. ComEd's argument that Staff's disallowance sends a message to ComEd employees that they should try to be good but not great is pure speculation. The Commission raised prior concerns regarding the potential for AIP to result in above market salaries, and finds that the use of the 200% payout inflates the AIP costs beyond what is necessary to provide market level compensation plus a reasonable bonus. ComEd provides no evidence showing that reducing the payout to 150% would result in a compensation level that would be below market levels. Staff's proposal to limit the payout to 150% is reasonable and equitable, supported by record evidence, and not inconsistent with EIMA.

The Commission agrees with ComEd that Staff's alternative to limit AIP expense in excess of 102.9% is not supported by the evidence in this proceeding. The 102.9% AIP expense adopted in prior formula rate proceedings is based on facts and compromises that are distinguishable from the current proceeding.

The Commission agrees with Staff and C/I that ComEd's alternative AIP payout determination, which would reduce the performance level associated with the payout, is problematic because it does not more accurately align AIP performance levels with award

levels as ComEd suggests. Furthermore, ComEd's argument that Staff's adjustment not only reduces the recoverable level of pay but also makes it harder for employees to earn that pay is not persuasive. As ComEd notes, the AIP and LTPCAP are two different plans. ComEd provides no rationale why a short term incentive compensation program should not require higher results in order to achieve performance levels. Additionally, Staff provided evidence demonstrating that the performance level differentials between target performance and distinguished performance are already narrow, and reducing this margin further would be unreasonable. Because the Commission finds that it is not necessary under these circumstances to reduce the performance level associated with the payout, the Commission rejects the alternative AIP adjustments related to such a reduction.

The Commission adopts Staff's adjustment to reduce the payout percentage associated with distinguished achievement performance from 200% to 150%, resulting in an overall AIP payout of 111.7%.

2. Derivative Adjustments

a. ComEd Position

ComEd states that because the Commission should deny Mr. Bridal's proposed AIP disallowance, it believes that there is no need to make any derivative adjustments to payroll tax, pension cost, depreciation expense, accumulated depreciation, or ADIT. If, however, the Commission does make a disallowance, ComEd will include the requisite derivative adjustments in its compliance filing. ComEd. Init. Br. at 43.

b. Staff Position

Staff recommends that the Commission adopt Staff's adjustment to remove payroll tax, pension cost, depreciation expense, accumulated depreciation, and ADIT associated with AIP incentive compensation disallowed in Staff's AIP adjustment. Staff's adjustment removes the derivative costs associated with disallowed AIP incentive compensation because those costs would not have been included in the Company's proposed revenue requirement if not for the inclusion of the AIP incentive compensation costs disallowed in Staff's adjustment to reduce the payout percentage for individual AIP metrics from 200% to 150%. Staff Ex. 7.0 at 12; Staff Ex. 4.0, Sch. 4.02. No party directly addressed Staff's adjustment to derivative costs associated with disallowed AIP.

ComEd witness Ms. Brinkman in rebuttal testimony suggested an alternative AIP adjustment which amended the metric performance requirements used in Staff's proposed AIP adjustment. If the Commission accepts the AIP adjustment suggested in Ms. Brinkman's rebuttal testimony (119.9% AIP Payout), the Commission should adopt the derivative adjustments to payroll tax, depreciation expense, accumulated depreciation, and ADIT set forth in Staff Ex. 7.0, Attachment B. If the Commission accepts Staff's corrected version of the AIP adjustment suggested by Ms. Brinkman (corrected for EIMA Reliability Metrics Index, see Staff Ex. 7.0, 9-10) (118.7% AIP payout), the Commission should adopt the derivative adjustments to payroll tax, depreciation expense, accumulated depreciation, and ADIT set forth in Staff Ex. 7.0, Attachment D. If the

Commission determines it is appropriate to completely align the AIP to the scales used within the LTPCAP (105.0% AIP Payout), the Commission should adopt the derivative adjustments to payroll tax, depreciation expense, accumulated depreciation, and ADIT set forth in Staff Ex. 7.0, Attachment E. Staff Ex. 7.0 at 12-13.

c. Commission Analysis and Conclusion

In light of the Commission Analysis and Conclusion in Section V.C.1., above, derivative adjustments to payroll tax, depreciation expense, accumulated depreciation, and ADIT are required.

3. Employee Savings Plan

a. ComEd Position

ComEd states that although Mr. Bridal proposes a disallowance of \$1,755,000 (\$990,000 expense plus \$756,000 capitalized) to remove costs associated with the profit sharing match contributed to the Employee Savings Plan (“ESP”) in 2014 (Staff Ex. 4.0 at 7-8), he has not asserted that these costs are unreasonable or imprudent. ComEd Init. Br. at 43. ComEd states that Mr. Bridal’s argument, that the costs should be disallowed because the Commission has held that the cost of compensation associated with the achievement of earnings per share or other financial metrics are not recoverable from rate payers, is incorrect and contrary to the plain language of EIMA and Commission practice. *Id.*

ComEd states that it is undisputed, and that they have evidenced, that ComEd’s ESP is not incentive compensation and that Mr. Bridal has acknowledged that the ESP is not an incentive compensation program. *Id.* at 44. All parties agree that the ESP is a benefit plan: a qualified retirement plan under Sections 401(a) and 401(k) of the Internal Revenue Code. *Id.*

ComEd asserts that although the Commission has often found that the cost of incentive compensation based on the achievement of earnings per share is not recoverable from customers, it is unaware of any instance where the Commission has disallowed employee savings plan costs in a ComEd rate case. *Id.* ComEd further asserts that the cases Mr. Bridal cite stand only for the narrow proposition that incentive compensation based on the achievement of earnings per share is not recoverable and that it is only this Commission practice that is codified in EIMA. Specifically, ComEd notes that EIMA provides for the recovery of incentive compensation based on the achievement of operational metrics but prohibiting incentive compensation based on earnings per share. *Id.*; 220 ILCS 5/16-108.5(c)(4)(A). ComEd quotes EIMA where it states: “Incentive compensation expense that is based on net income or an affiliate’s earnings per share shall not be recoverable under the performance-based formula rate.” *Id.*; 220 ILCS 5/16-108.5(c)(4)(A).

ComEd argues that the rules of statutory construction require that in interpreting a statute, the Commission “cannot find an additional statutory exclusion where one was not

provided for by the legislature” and that neither EIMA nor Commission practice and precedent prohibit recovery of all compensation based on earnings per share. ComEd Init. Br. at 44-45; *State ex rel. Beeler Schad and Diamond, P.C. v. Ritz Camera Ctrs., Inc.*, 377 Ill. App. 3d 990, 1168 (1st Dist. 2007). Moreover, ComEd states that Mr. Bridal acknowledges “that the Commission precedent and case law address only specifically incentive compensation based on earnings per share.” ComEd Init. Br. at 45; Staff Ex. 7.0 at 15.

ComEd asserts that Mr. Bridal’s claim that the costs are not just and reasonable, because they are tied to earnings per share is without factual basis. *Id.* at 45; see also Staff Ex. 7.0 at 16. ComEd rebuts Mr. Bridal’s statement that he is “not aware of any prior instance where the Commission determined it is appropriate for a utility to recover through rates the costs of *any* type of compensation that is based on the achievement of a defined amount of earnings per share.” ComEd Init. Br. at 45; Staff Ex. 7.0 at 16. ComEd states that prudence and reasonableness is the legal standard of recovery and not whether the Commission has specifically approved a type of expense before as Mr. Bridal argues. See, e.g., 220 ILCS 5/16-108.5(c)(1). ComEd further asserts that ComEd’s employee savings plan has had a profit sharing match feature since 2010 and the costs have been included in the Commission-approved revenue requirement multiple times without dispute. ComEd Init. Br. at 45.

In addition, ComEd states that it has demonstrated that the profit sharing match contributed to the ESP is a prudent and reasonable method of cost control and should be approved by the Commission. ComEd Init. Br. at 45, 46. ComEd explains that starting in 2010, it moved from a fixed match of 5% to a 3% fixed match combined with a 3% profit-sharing match. *Id.* Since moving to a combined fixed/profit-sharing match ComEd asserts that it has incurred lower benefit plan costs attributed to the ESP. *Id.* ComEd states that specifically, since 2010, the average ESP expense has been 4.2% and that this represents a 0.8% reduction in overall ESP expense. *Id.* at 46. ComEd further asserts that in 2014, only 0.5% was attributed to the profit-sharing match, providing customers with a 1.5% savings from the fixed match ESP. *Id.*

In its Reply Brief, ComEd states that Staff recognizes that Mr. Bridal’s proposed disallowance of \$1,755,000 to remove costs associated with the profit sharing match contributed to the ESP in 2014 is not supported by EIMA or Commission precedent, which prohibit recovery of incentive compensation costs based on earnings per share. ComEd Reply Br. at 15; Staff Init. Br. at 16. Instead, ComEd asserts that Staff argues that its disallowance is appropriate based on Mr. Bridal’s belief that the logical conclusion of ComEd’s interpretation of the law would result in the hypothetical possibility of a base salary based entirely on earning share being recoverable while incentive compensation based entirely on earnings per share would not. *Id.* ComEd states that none of ComEd’s 6,000 employees has a base salary based in any part on earnings per share, let alone based entirely on earning per share. *Id.* ComEd also asserts that the Commission must decide this issue on the facts of this case and the applicable law and that Mr. Bridal’s hypothetical is not a basis to disallow prudent and reasonable actual costs of delivery

service. *Id.* at 16; see also *Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 405 Ill. App. 3d 389, 420 (2d Dist. 2010).

ComEd also states that although Staff has twice alluded to the existence of some “fundamental reason” why the statutory prohibition on incentive compensation based on earnings per share must also apply to benefit plans, Staff has been unable to articulate that reason. ComEd Reply Br. at 16. ComEd states that this is because no such reason exists. ComEd concludes that the evidence and the law show that ComEd’s ESP expense is a prudent and reasonable cost of delivery service that is not prohibited by Commission practice or EIMA and that the Commission should reject Mr. Bridal’s proposed disallowance and permit recovery of this expense in its entirety.

b. Staff Position

Staff maintains that the Commission should adopt Staff’s adjustment to disallow ComEd’s ESP profit-sharing matching contribution. The ESP profit-sharing match included in ComEd’s revenue requirement resulted from the achievement of earnings per share goals established by the Compensation Committee of Exelon’s Board of Directors. Therefore, the costs associated with the profit sharing match should be excluded from the revenue requirement. Staff Ex. 4.0 at 7-9; Staff Ex. 7.0 at 13-17.

Staff argues that Commission practice and law is that the cost of compensation associated with the achievement of earnings per share or other financial metrics is not recoverable from rate payers and should be the responsibility of shareholders. See, e.g., *Commonwealth Edison Co.*, ICC Docket No. 07-0566, Order at 61 (Sep. 10, 2008); *Peoples Gas and Light Co.*, ICC Docket No. 09-0166/0167 (Cons.), Order at 58-59 (Jan. 21, 2010). ComEd witness Mr. Newhouse in rebuttal testimony correctly observes that Commission precedent and case law address only specifically incentive compensation based on earnings per share. ComEd Ex. 9.0 at 12. However, Mr. Newhouse implies a limited and illogical interpretation of Commission practice and case law. Taken to its logical conclusion, that interpretation would have the Commission allow the entirety of a hypothetical employee’s salary if that salary was based on the achievement of a certain level of earnings per share, but disallow only incentive compensation that was similarly based on earnings per share. Such a result would be unreasonable. Staff Ex. 7.0 at 15. Expenses recovered in rates must be just and reasonable. 220 ILCS 5/16-108.5(c)(1).

Mr. Newhouse further argues that the ESP is an employee benefit rather than incentive compensation, and as such, is not prohibited from recovery. ComEd Ex. 9.0 at 12. That the ESP is an employee benefit rather than incentive compensation cannot overcome the fact that the ESP includes a component that is based on earnings per share. Staff’s adjustment does not seek to remove the entire cost of the ESP; rather, it removes only the costs associated with the profit-sharing matching contribution that would not exist if not for the achievement of a defined earnings per share amount. Staff Ex. 7.0 at 16. For the same fundamental reason that it is not just or reasonable to recover incentive compensation costs tied to earnings per share it is neither just nor reasonable to recover profit sharing costs tied to earnings per share.

Staff's adjustment does not seek to remove the entire cost of the ESP; rather, Staff's adjustment removes only the costs associated with the non-allowable profit-sharing matching contribution that would not exist but for the achievement of a defined earnings per share amount. The Company's attempts to distract the Commission from the applicable precedents and case law should be disregarded.

ComEd argues that Staff has not asserted that the costs associated with the earnings per share-based profit sharing match are unreasonable or imprudent. ComEd Init. Br. at 43. ComEd is wrong. Among Staff's testimony on this topic is this discussion:

Taken to its logical conclusion, Mr. Newhouse's implication would have the Commission allow the entirety of a hypothetical employee's salary if that salary was based on the achievement of a certain level of earnings per share, but disallow only incentive compensation that was similarly based on earnings per share. Such a result would be unreasonable . . . it is not just or reasonable to recover incentive compensation costs tied to earnings per share[.] [I]t is neither just nor reasonable to recover profit sharing costs tied to earnings per share.

Staff Ex. 7.0 at 15. The record demonstrates that Staff asserted the costs associated with the earnings per share-based profit sharing match are not just or reasonable and shows Staff provided sound reasoning for its position.

The Company continues, perpetuating its argument that the ESP is not incentive compensation but rather more akin to health and welfare benefits than traditional salaried compensation. ComEd Init. Br. at 44. Staff does not claim that the ESP is incentive compensation. Staff Ex. 7.0 at 14. Rather, Staff's argument is that the earnings per share-based matching contributions made by the Company into its employee's ESP accounts are other compensation (pay-related benefits) that would not have been provided but for the Company's achievement of a specific level of earnings per share. Staff Ex. 7.0 at 13-14; Staff Ex. 4.0, Attach C at 38.

ComEd also errs in its argument that Staff's recommended disallowance of costs associated with the earnings per share-based profit sharing match is incorrect and contrary to the plain language of EIMA. ComEd Init. Br. at 43. To be clear, Staff did not claim that the section of EIMA cited by ComEd, 220 ILCS 5/16-108.5(c)(4)(A), applies to Staff's proposed adjustment. To the contrary, Section 16-108.5(c)(4)(A) of the Act applies specifically and solely to incentive compensation expense. The statutory basis for Staff's adjustment to the ESP rests within Section 16-108.5(c)(1) of the Act, which states, in relevant part, that the formula rate approved by the Commission shall:

[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).

As stated in both Staff's direct and rebuttal testimony, the Commission has long held that the cost of compensation associated with the achievement of earnings per share or other financial metrics is not recoverable from rate payers and should be the responsibility of shareholders. Staff Ex. 4.0 at 7-9; Staff Ex. 7.0 at 14-15. Staff's testimony cited ComEd's 2007 general rate case, where the Commission found:

Regarding ComEd's AIP's Net Income Metric, the Commission agrees with Staff's proposed adjustment disallowing 100% of AIP costs related to the financial net income goal which primarily benefits shareholders. ComEd's net income goals are financially based and primarily result in shareholder benefits. The Commission has repeatedly held that the cost of financial goals should not be paid by ratepayers.

Docket No. 07-0566, Order at 61.

In adopting Staff's adjustment in Docket No. 07-0566, the Commission agreed with Staff's concern that a financial based metric introduces an inappropriate circular relationship between rates and the expenses such rates are designed to recover: the larger the rate increase granted the more success ComEd will have in achieving its earnings, i.e., income or earnings per share, goal. *Id.* Therefore, allowing recovery of costs tied to earnings per share benefits shareholders, not ratepayers. In order for costs to be recoverable, a public utility has the burden of proving that the costs for which it seeks reimbursement "directly benefits the ratepayers or the services which the utility renders." *Candlewick*, 122 Ill.App.3d 219, 227. Also, while it is true that the Docket No. 07-0566 and the many other prior Commission orders and Appellate Court decisions address specifically only incentive compensation, to interpret these decisions to exclude application to all other compensation would be, to borrow ComEd's term, perverse. Certainly an outcome which allows recovery of employee salaries that are based on earnings per share but disallows only incentive compensation that is similarly based on earnings per share would be arbitrary and capricious and contrary to those orders and Appellate Court decisions. As cited above, Section 16-108.5(c)(1) of the Act provides in part for recovery of actual costs that are consistent with Commission practice and law. Contrary to ComEd's claims, to allow recovery of any type of compensation that is based on the achievement of earnings per share or any other financial goal – regardless of whether that compensation is base pay, incentive pay, or employer contributions to a retirement plan – is not consistent with the Commission's practice to disallow recovery of incentive compensation based on earnings per share.

ComEd also argues in favor of the earnings per share-based profit sharing match by stating that its ESP has included this feature since 2010 and the associated costs have been included in Commission-approved revenue requirements multiple times without

dispute. ComEd Init. Br. at 45. However, ComEd does not point to any Order where the Commission has specifically addressed the earnings per share-based profit sharing match. The fact that the Commission has not addressed this issue previously is not evidence that the associated costs should be allowed; rather, it shows that this is a new issue for the Commission to decide.

Finally, ComEd argues in favor of the earnings per share-based profit sharing match stating that it is a prudent and reasonable method of cost control. ComEd Init. Br. at 45. Given that a similar argument was made and rejected in ComEd's prior formula rate case, with regards to the earnings per share-based Shareholder Protection Feature, the Commission should likewise reject that claim here. First, the information provided by ComEd shows that in the five years since its adoption, the earnings per share-based profit sharing match has actually increased the cost of the ESP in two of those years. *Id.* at 46. Further, although the profit sharing match has been less than the fixed match would have been for three of the five years, that match is trending up. This information shows that the profit sharing match is inconsistent and does not guarantee savings to ratepayers. *Id.* However, this is not the main flaw with ComEd's cost control argument. The bigger issue is that the purported cost control is provided by an earnings per share-based component which benefits shareholders not ratepayers. Staff reasserts that Commission practice does not allow recovery of costs based on the achievement of financial goals such as earnings per share which benefit shareholders. Further, in ComEd's most recent formula rate proceeding, the Commission rejected a similar earnings per share-based cost control mechanism for precisely the same reason – the mechanism was contrary to Commission practice and law. 2014 Rate Case Order at 48-51. As such, the claim that the unlawful profit sharing match led to savings should be dismissed.

Staff concludes that the Commission should adopt Staff's adjustment to remove ComEd's ESP profit sharing matching contribution as it is based on earnings per share goals and not allowable under the Act.

c. Commission Analysis and Conclusion

The Commission adopts Staff's adjustment to remove ComEd's ESP profit sharing matching contribution. The Commission finds that the costs associated with the profit sharing matching contribution are not reasonable.

ComEd argues that its ESP expense is not prohibited by Commission practice or EIMA. Staff maintains that the profit sharing match is inconsistent with Commission practice and the law. ComEd is correct that the profit sharing matching contribution based on earnings per share is not specifically prohibited by the EIMA. However, the Commission must still determine that the costs are prudent and reasonable. 220 ILCS 5/16-108.5(c)(1). Whether such an expense is consistent with Commission practice is not clear. This issue is new and has not been addressed in prior proceedings. Also, while this expense has been in existence since 2010, the fact that Staff did not object to it prior to the current proceeding is irrelevant.

These costs are not incentive compensation, where there is a statutory prohibition of compensation based on earnings per share. Nevertheless, the profit sharing match results from the achievement of earnings per share goals established by the Compensation Committee of Exelon's Board of Directors and primarily benefits shareholders. Moreover, as Staff notes, the profit sharing matching contribution increased the cost of the ESP in two of the five years, is variable, and does not guarantee savings to ratepayers. Accordingly, the Commission finds that Staff's adjustment is reasonable and is approved.

4. Outside Services

a. ComEd Position

ComEd explains that #SmartMeetsSweet ("SMS") is a program used for distributing information and educating customers on automated metering infrastructure ("AMI") meters. ComEd Init. Br. at 46. ComEd therefore believes that Ms. Jones' proposed disallowance of \$518,000 associated with SMS (Staff Ex. 2.0R at 9-10) should be rejected by the Commission because Ms. Jones incorrectly views the program as a giveaway of ice cream cones and cookies and therefore as unrecoverable goodwill or institutional advertising. ComEd Init. Br. at 46; Staff Ex. 2.0R at 9-10. ComEd asserts that to the contrary, the SMS program was an innovative and successful approach to customer outreach and education and these expenses should be recoverable in full. ComEd Init. Br. at 46-47. In support of its argument, ComEd first relies on testimony from ComEd witness Mr. Newhouse who stated:

One of ComEd's goals in association with the deployment of AMI meters is to provide customers with information to build awareness and education around energy management, smart meters and associated smart meter benefits. Channels for such information and education include attending or creating community events in order to abide by the AMI outreach guiding principle of "Meet People Where They Are." This principle focuses on taking AMI deployment information directly to customers in order to facilitate engagement and advocacy. ComEd's AMI community event and outreach program takes a three-pronged approach: ... Community Events ... Street Teams ... [and to] provide outreach in deployment areas where community events were not typically scheduled in correlation with the timing of AMI deployment, ComEd created and launched the #SmartMeetsSweet truck to provide customers with an engaging way to learn about smart meter installations and their associated benefits.

ComEd Ex. 9.0 at 14-15.

Second, ComEd asserts that while Ms. Jones incorrectly premises her disallowance on the fact that ComEd provided ice cream and cookies to customers at

these events, “the vast majority of the costs are not related to the treats. ComEd Init. Br. at 47. ComEd states that approximately \$478,000 of the \$518,000 (jurisdictional), that Ms. Jones recommends for disallowance relate to the event planning, staffing, transportation and educational material costs. *Id.* ComEd states that it provided evidentiary examples of materials provided during the SMS customer engagement and pictures of customers interacting with the team. *Id.*; ComEd Ex. 9.08.

Third, ComEd states that the fact that Ms. Jones disagreed with the amount spent on written materials versus the “event” concept (Staff Ex. 6.0R at 9-10) and the fact that Ms. Jones may have pursued a different method of customer education and outreach does not make ComEd’s choice imprudent. ComEd Init. Br. at 47. ComEd states that the “prudence standard recognizes that reasonable persons can have honest differences of opinion without one or the other necessarily being ‘imprudent.’” *Illinois Power Co. v. Illinois Commerce Comm’n*, 339 Ill. App. 3d 425, 435 (5th Dist. 2003) (citation omitted).

ComEd further opines that it would have incurred customer education and outreach expense no matter which method it chose to disseminate valuable and important information about AMI meters. ComEd Init. Br. at 48. ComEd explains that the expenses of the “event” concept of the SMS truck – the use of cookies and ice cream, friendly staff, and a wrapped vehicle – were prudently incurred and reasonable in amount to engage customers. *Id.* ComEd states that this is part of the premier customer experience that ComEd strives to provide and is a method that brings education directly to customers. *Id.* ComEd also states that there is no evidence that efforts to reach out to customers that focused more on print material and less on staffing or mobility would have been less expensive or targeted a broader audience and there is no evidence that those methods would have been more effective in communicating the AMI message to customers. *Id.*

Fourth, ComEd states Ms. Jones’ argument that because the initiative only reached 6.66% of customers who had smart meters installed in 2014 the expenses related to the SMS program are not prudent and reasonable is in error. ComEd Init. Br. at 48; Staff Ex. 6.0R at 9, 10. The Commission is not permitted to engage in this type of hindsight review. ComEd Init. Br. at 48. ComEd quotes *Illinois Power Co. v. Illinois Commerce Comm’n*, 339 Ill. App. 3d 425, 428 (5th Dist. 2003), for the proposition that: “When a court considers whether a judgment was prudently made, only those facts available at the time judgment was exercised can be considered. Hindsight review is impermissible.” *Id.* ComEd states that the number of customers that would actually be reached is not a fact that was available to ComEd at the time it made the decision to engage in the SMS program. ComEd Init. Br. at 48. ComEd also notes that Ms. Jones does not indicate what percentage of customers reached would have been acceptable. *Id.*

ComEd also asserts that the 6.66% figure obscures the fact that ComEd directly contacted over 36,000 customers as a result of the initiative. *Id.* ComEd contends that the prudence of actions regarding education and outreach efforts cannot be assessed only by quantitative factors but must also include consideration of qualitative factors such as direct personal interactions resulting in an improved customer learning experience. *Id.*

at 49. ComEd states that without the SMS truck to initially engage customers, many of those direct customer interactions would not have otherwise happened. *Id.* Further, ComEd asserts that the program is not finished. ComEd Reply Br. at 16. ComEd states that it will continue to reach customers on an even larger scale as AMI deployment continues and therefore the figure of 36,000 customers reached is not static and will continue to grow. *Id.* ComEd contends that these assets are now in place to continue providing ongoing benefits and customer outreach throughout the AMI deployment and that the program is a success, not a failure. ComEd Init. Br. at 49.

According to ComEd, the SMS concept combines transportation, communication, and educational materials into one mobile package to maximize exposure to customers in order to draw them in for engagement and educate them on the unique features of AMI meters. *Id.* For these reasons ComEd believes that the expenses associated with this program were prudently incurred and reasonable in amount and that the Commission should allow them in full.

b. Staff Position

Staff states that the Commission should accept Staff's proposed adjustment to disallow ComEd expenditures to an event-management company that gave away ice cream cones and cookies in communities where smart meters were being installed as part of the SMS initiative. Staff Ex. 2.0R at 9, Sch. 2.04. The initiative was primarily designed to enhance the image of the company rather than to educate and inform customers: i.e., goodwill advertising, which is not a recoverable expense. Staff Ex. 2.0R at 9; Staff Ex. 6.0R at 10. Further, few customers were contacted and little was spent on educational materials relative to the cost of the initiative. Accordingly, the expenses for the initiative were neither prudently incurred nor reasonable in amount. Staff Ex. 6.0R at 10.

ComEd describes the primary purpose of the SMS initiative as designed to bring AMI educational material to where people live in a manner intended to engage customers, not to improve ComEd's image. ComEd Ex. 12 at 4. ComEd further asserts that the number of customers contacted was a success, not a failure, and that most of the costs were related to the development and implementation of the event. *Id.* at 5.

ComEd's arguments ignore the evidence and should be rejected. While Staff does not dispute that some dissemination of information occurred as a result of the initiative, the strategy of the initiative was primarily designed to enhance the Company's image in the communities ComEd serves. Staff Ex. 6.0R at 8. ComEd spent over \$500,000 for the initiative to achieve only 36,000 direct customer interactions. ComEd Ex. 9.0 at 16. Staff argues that even assuming that each of these "customer interactions" represents one distinct meter installation, only 6.66% of the customers who had meters installed in 2014 were contacted via the SMS initiative. Staff Ex. 6.0R at 9. Moreover, of the \$500,000 that ComEd spent, less than 5% was for documentation and educational materials provided to customers. *Id.* at 9; Staff Cross Ex. 1. In contrast, 84% went to management fees, vehicles and staffing, while the remaining 11% went to insurance costs, site fees and permits, time and labor for creating the social media campaign, and

time and labor for designing the truck wrap. Staff Ex. 6.0R at 9; Staff Cross Ex. 1. Given the small number of customers contacted and how little was spent on educational materials relative to the cost of the initiative, the expenditures for the initiative were neither prudently incurred nor reasonable in amount.

ComEd's arguments primarily attempt to portray the issue as merely an honest difference of opinion over methods. ComEd Init. Br. at 47. These arguments miss the point. Staff states that it has never disputed that some dissemination of information occurred as a result of the initiative. Staff Ex. 6.0R at 8. The evidence demonstrates, however, that the primary purpose of the SMS initiative was to enhance the Company's image in the communities it serves; *i.e.*, goodwill advertising. *Id.* ComEd recorded the expense for the SMS initiative in its financial records – correctly -- as marketing expense. *Id.* at 10. Such expenses are not recoverable under Section 9-225 of the Act. 220 ILCS 5/9-225. Only after Staff proposed an adjustment to disallow recovery of the expense did ComEd decide the expense was misclassified and should be considered customer service and informational expense. Staff Ex. 2.0R at 10.

Staff states even assuming *arguendo* that the SMS initiative should be considered customer service and informational expenses, recovering these expenses from customers would still be unreasonable. ComEd asserts that its actions may only be judged by the facts available at the time it exercised its judgment, and that Staff's adjustment amounts to impermissible hindsight review. ComEd Init. Br. at 48. The available evidence makes clear, however, that ComEd's actions were imprudent and the costs involved unreasonable. ComEd admits that it did not know how many customers would be reached at the time it made the decision to engage in the SMS program. ComEd Init. Br. at 48. Yet ComEd chose to spend over half a million dollars of ratepayers' money to pass out free ice cream and cookies in order to draw in some unknown number of customers. ComEd Ex. 9.0 at 16.

Finally, ComEd claims for the first time in its IB that this SMS event concept is part of the premier customer experience that ComEd strives to provide. ComEd Init. Br. at 48. As Staff has already pointed out, *e.g.*, with respect to credit card expenditures for employee recognition expenses, customers should not be required to pay for ComEd to provide customers with a "premier experience." Staff Ex. 6.0R at 7-8. Customers are not required under the law to receive a premier experience; rather, customers need to receive adequate, efficient, reliable, environmentally safe, and least-cost service based on prudent and reasonable costs necessary to provide such service. *Id.* at 7.

c. Commission Analysis and Conclusion

The Commission agrees with Staff's recommendation to disallow outside services expenses associated with ComEd's SMS program. ComEd spent in excess of \$500,000 distributing free ice cream and cookies to contact at most 36,000 customers about smart meters.

The evidence demonstrates that the primary purpose of the SMS initiative was to enhance the Company's image in the communities it serves through goodwill advertising. As Staff notes, ComEd recorded the expense for the SMS initiative in its financial records as marketing expense. Such expenses are not recoverable under Section 9-225 of the Act. Only after Staff proposed an adjustment to disallow recovery of the expense did ComEd decide the expense was misclassified and should be considered customer service and informational expense.

The record indicates that only 5% of the SMS funds were spent on educational materials. Management fees, vehicles and staffing comprised 84% of the expenditure. Another 11% was spent on insurance, site fees and other miscellaneous costs. Thus, few customers were contacted and little was spent on educational materials relative to the cost of the initiative. The Commission agrees that this was unrecoverable goodwill or institutional advertising that was neither prudently occurred nor reasonable in amount. The Commission finds that it would be unreasonable to impose the costs of the SMS initiative on ComEd's customers.

5. Industry Association Dues

a. ComEd Position

Ms. Jones proposed an adjustment to disallow certain industry association dues. Staff Ex. 2.0R at 3-4. Although ComEd disagreed with parts of Staff's proposal, in order to limit the issues in this case and without waiving its right to contest other proposed disallowances based on similar arguments in this case, or disallowances based on this or similar arguments in any other proceeding, ComEd accepted Ms. Jones' proposal to remove the specific industry association dues listed on her Schedule 2.01 as well as the dues for the Executives' Club of Chicago and 10% of the dues for the Will County Center for Economic Development. These adjustments total approximately \$14,000.

However, ComEd recommends that the Commission reject Ms. Jones' proposed disallowance of 100% of the dues for both the Illinois Environmental Regulatory Group ("IERG"), in the amount of \$16,000, and the Utility Solid Waste Activities Group ("USWAG"), in the amount of \$33,000 (Staff Ex. 2.0R at 4-6; Staff Ex. 2.0R, Sched. 2.01, lines 12 and 13) because ComEd believes that the proposed disallowance is based on Ms. Jones' factually incorrect belief that "the purpose of each organization is regulatory advocacy." ComEd Init. Br. at 49-50; Staff Ex. 2.0R at 4. More specifically, she states: "Regulatory advocacy is not an ancillary function for these two organizations as it is for organizations such as the Edison Electric Institute or the Illinois Chamber of Commerce, which identify the percent of their dues attributable to influencing legislation." ComEd Init. Br. at 50; Staff Ex. 6.0R at 3-4.

ComEd agrees that these entities do engage in regulatory activity or lobbying but asserts that such activity is not the organizations' sole purpose and therefore complete disallowance is not warranted. ComEd Init. Br. at 50. ComEd states that in response to Ms. Jones' claim that IERG and USWAG do not "identify the percent of their dues attributable to legislation," (Staff Ex. 6.0R at 4), ComEd requested and received from the

organizations documents indicating the specific portion of their dues that are attributable to regulatory activity. ComEd Init. Br. at 50. ComEd explains that for IERG, less than 1% of dues are related to lobbying activities, which amounts to less than \$1000 for ComEd in 2014 and thus had no impact on ComEd's revenue requirement. ComEd Init. Br. at 50; ComEd Ex. 12.04 (IERG Lobbying Statement reporting less than 1% of IERG dues). For USWAG, ComEd states that 6.2% of dues are related to lobbying activities which amounts to a \$4,000 reduction to ComEd's revenue requirement. *Id.* at 50; ComEd Ex. 12.04 (Edison Electric Institute ("EEI") letter reporting 6.2% of USWAG dues).

ComEd further asserts that its approach to dues for these organizations is the same approach Ms. Jones used to calculate her proposed disallowances for ComEd's other industry dues and that the evidence ComEd presented in support of the dues is the type of evidence that companies routinely rely on in preparing their books and tax filings. ComEd Init. Br. at 50. In further support of its position, ComEd states that it provided evidence of the services these organizations provide to ComEd beyond regulatory advocacy and that Ms. Jones proposed 100% disallowance does not recognize the functions and benefits reflected in the services the organizations provide. *Id.* at 50-51.

ComEd states that rather than addressing the substance of the statement and letter – the uncontroverted evidence at issue – Staff claims this evidence is "flawed" and should be given zero weight because it believes ComEd should have provided this evidence sooner. ComEd Reply Br. at 17. ComEd argues that Staff's claim that zero weight should be given to the documents evidencing the exact percentage of IERG and USWAG activities attributable to lobbying activities is in essence an objection to the admissibility of the documents. *Id.*; *See Anderson v. United Conveyor Supply Co.*, 461 F. Supp. 2d 699 (N.D. Ill. 2006) (inadmissible hearsay given no weight); *Lindsey v. RadioShack Corp.*, 452 F. Supp. 2d 848, 851-852 (2006) (same).

Therefore, ComEd asserts, Staff should have raised the objection in a pre-trial motion related to surrebuttal testimony or by contemporaneous objection when offered into the record and that by failing to raise this issue at either of those times Staff has waived this objection. ComEd Reply Br. at 17-18. ComEd cites *People v. Trefonas*, 9 Ill. 2d 92, 98 (1956), for the proposition that an "objection to the admission of evidence, to be available, must be made in apt time, or it will be regarded as waived. The general rule is that the admission of incompetent evidence must be objected to, if at all, at the time of its admission." ComEd states that had a timely objection been made, ComEd witness(es) could have explained why they were not previously aware of this information. ComEd Reply Br. at 18.

ComEd further states that the argument lacks merit. *Id.* ComEd asserts that it explained that it did not have this information available when Ms. Jones first proposed a disallowance and the fact that ComEd may or may not have received one of the documents on a previous date is immaterial. *Id.* ComEd also asserts that it should not be penalized for attempting to compromise (to its financial detriment, as a 50% disallowance would have been higher than the 6% actually attributable to non-recoverable activities) before expending resources to track down detailed evidentiary support for

\$49,000 in costs. *Id.* Last, ComEd contends that the statement and letter rebut Ms. Jones' summary of the IERG and USWAG websites. *Id.* ComEd also notes that websites are not the type of evidence that companies routinely rely on in preparing their books and tax filings. *Id.*

For these reasons ComEd recommends that the Commission reject Ms. Jones' proposed 100% disallowance and instead adopt ComEd's proposed \$4,000 disallowance as reflected in ComEd Ex. 12.03.

b. Staff Position

Staff states that the Commission should accept Staff's proposed adjustment to disallow 100% of the dues for the IERG and the USWAG. Staff Ex. 2.0R at 4, Sch. 2.01. The purpose of these organizations is regulatory advocacy. Staff Ex. 2.0R at 4. As such, recovery of such costs is prohibited under Section 9-224 of the Act. 220 ILCS 5/9-224; Staff Ex. 2.0R at 4-6.

Section 9-224 of the Act provides that: "The Commission shall not consider as an expense of any public utility company, for the purpose of determining any rate or charge, any amount expended for political activity or lobbying as defined in the 'Lobbyist Registration Act.'" 220 ILCS 5/9-224. According to the IERG website, the IERG is an affiliate of the Illinois Chamber of Commerce and works cooperatively with the Chamber on legislative matters in the General Assembly. Staff Ex. 2.0R at 5. The IERG's self-described primary mission is to:

Advocate members' interests before governmental agencies, primarily the Illinois Environmental Protection Agency and the Illinois Pollution Control Board;

Negotiate environmental policies, laws and regulations as they are promulgated, administrated and implemented by the State of Illinois; and

Provide accurate and technically sound input early in the regulatory development and legislative processes to promote favorable outcomes for Illinois' business community.

Id. at 5.

Similarly, according to the USWAG website, the USWAG is responsible for addressing solid and hazardous waste issues on behalf of the utility industry and engages in regulatory advocacy pertaining to the Resource Conservation and Recovery Act, the Toxic Substances Control Act, and the Hazardous Material Transportation Act. *Id.* at 6. The USWAG indicated its mission is to address the regulation of utility wastes, byproducts and materials in a manner that protects human health and the environment and is consistent with the business needs of its members. *Id.* at 6.

In rebuttal testimony, ComEd proposed a 50% adjustment for IERG and USWAG membership fees. ComEd Ex. 9.0 at 19. In surrebuttal testimony, ComEd withdrew this proposal having purportedly “. . . asked for and obtained specific information from USWAG and IERG to exactly quantify the portion of their activities that are related to regulatory advocacy . . .” ComEd Ex. 12.0 at 7. ComEd asserts that, based on this information, which consists of two form statements, 6.2% of the payment to USWAG and 1% of that to IERG is related to regulatory advocacy. *Id.* at 7; ComEd Ex. 12.04.

Staff argues that ComEd’s information is flawed and should be given no weight. ComEd provides no explanation why ComEd did not provide this information prior to surrebuttal testimony, yet the USWAG statement is dated March 12, 2015 and references a prior dues invoice and letter from March 2014. The March 12, 2015 date also contradicts ComEd’s claim that, in apparent response to Staff’s rebuttal testimony, ComEd “asked for and obtained specific information from USWAG . . .” ComEd Ex. 12.0 at 7. Staff asserts that the IERG form in turn is even more problematic – the form is undated, unsigned and without contact information. Thus, the IERG form provides no support for ComEd’s assertions regarding IERG’s 2014 membership fees. Further, contrary to ComEd’s claim, the Company provided no evidence of the services it says it receives from IERG and USWAG. ComEd Init. Br. at 51. ComEd did provide descriptions of certain services and information (ComEd Ex. 9.0, 1920), which are simply by-products of the organizations’ primary function of regulatory advocacy. Staff Ex. 6.0R at 4. Most problematic, however, is that ComEd fails to rebut both organizations’ self-described primary missions, which is to engage in regulatory advocacy.

Accordingly, the Commission should accept Staff’s proposed adjustment to disallow 100% of the dues for IERG and USWAG. Staff Ex. 2.0R at 4, Sch. 2.01. The self-described purpose of these organizations is regulatory advocacy and recovery of such costs is prohibited by Section 9-224 of the Act. Therefore, Staff concludes that ComEd should be denied recovery for these costs.

c. Commission Analysis and Conclusion

The Commission agrees with Staff’s recommendation to disallow 100% of the industry association dues for IERG, but adopts ComEd’s proposed 6.2% disallowance of dues paid to USWAG. Section 9-224 of the Act clearly prohibits utilities from listing as an expense for the purpose of determining any rate or charge any amount expended for political activity or lobbying. In that regard, any industry association dues that are used for political activity and lobbying should be disallowed.

When a utility lists as an expense industry association dues for an association that engages in some regulatory advocacy or lobbying, the utility should provide sufficient evidence in this type of proceeding to determine what portion of those dues are attributable to regulatory advocacy or lobbying and what portion is related to other activities. Both ComEd and Staff agree that USWAG and IERG engage, at least to some extent, in regulatory advocacy.

ComEd provides two documents in support of its proposed disallowance: (1) a letter to EEI members stating that 6.2% of dues assessed to USWAG are related to non-deductible activities; and (2) a general IERG Lobbying Statement. As Staff notes, EEI identifies the percent of their dues attributable to influencing legislation. Therefore, a letter from EEI to its members stating that 6.2% of the assessment for USWAG was for expenditures relating to influencing legislation is credible evidence indicating that 6.2% of dues given to USWAG relate to such activity. The Commission declines to discount the EEI letter, as Staff suggests, and will adopt ComEd's proposal to disallow only 6.2% of the dues. However, ComEd shall provide more substantive evidence in future formula rate proceedings for industry dues expenditures related to USWAG, such as a letter from USWAG indicating the amount of association dues it spends on lobbying activities for the relevant year.

Regarding the IERG Lobbying Statement, this is an undated document that states members should report that 1% of dues are spent on lobbying activities as a general provision. The Lobbying Statement further provides that any changes in this amount will be reported to members. ComEd provides no further proof that only 1% of IERG dues are related to lobbying activities for 2014. ComEd would have the Commission assume that this Lobbying Statement was in effect in 2014 and that there were no further reports by IERG to its membership indicating any changes to this amount for 2014. The Commission declines to make any such assumption. Absent further evidence indicating the amount of IERG dues related to lobbying activity, the Commission adopts Staff's proposed 100% disallowance of industry association dues for IERG.

VI. RATE OF RETURN

ComEd provided its capital structure and cost for the purpose of determining both the 2014 Reconciliation Year and the 2016 Initial Rate Year. Staff did not recommend any adjustments to ComEd's proposed capital structure. ComEd and Staff agree and mutually recommend a 7.02% rate of return on rate base for the 2014 Reconciliation Year and a 7.05% rate of return on rate base for the 2016 Initial Rate Year. Staff Ex. 3.0 at 3; ComEd Ex. 2.0 at 45; ComEd Ex. 2.01, Sch FR D-1, line 21; ComEd Ex. 2.01, Sch FR D-2. ComEd has updated its rate of return through agreement with Staff. No other party objected to the proposed capital structure. Therefore, the Commission approves ComEd's rate of return for the 2014 Reconciliation Year and the components for the 2016 Initial Rate Year as indicated in the following chart:

2014 Reconciliation Year

<i>Capital Structure Component</i>	<i>Weighting</i>	<i>Cost</i>	<i>Weighted Cost</i>
<i>Common Equity</i>	46.25%	9.09% ⁽¹⁾	4.20%
<i>Long Term Debt</i>	53.18%	5.24%	2.79%
<i>Short Term Debt</i>	0.57%	0.33%	0.00%
<i>Credit Facility Cost</i>			0.03%
<i>Total Weighted Average</i>	100.00%		7.02%

2016 Initial Filing Year

<i>Capital Structure Component</i>	<i>Weighting</i>	<i>Cost</i>	<i>Weighted Cost</i>
<i>Common Equity</i>	46.25%	9.14%	4.23%
<i>Long Term Debt</i>	53.18%	5.24%	2.79%
<i>Short Term Debt</i>	0.57%	0.33%	0.00%
<i>Credit Facility Cost</i>			0.03%
<i>Total Weighted Average</i>	100.00%		7.05%

(1) Incorporates 5 basis points penalty for missing EIMA reliability metric in 2014

VII. RECONCILIATION**A. Overview**

ComEd supported its reconciliation adjustments for the 2014 Reconciliation Year through the testimony of multiple witnesses. C/I and AG/City initially proposed a contested adjustment, but have withdrawn their proposal, as discussed below.

B. Calculation of Interest on Reconciliation Balance (ADIT Related to Reconciliation)**1. ComEd Position**

ComEd states that AG/City and C/I initially proposed an adjustment to reduce the reconciliation balance upon which interest is calculated by the amount of ADIT purportedly related to that balance. In light of the Illinois Appellate Court decision in *Madigan*, however, AG/City and C/I withdrew their proposal. ComEd Reply Br. at 1; AG/City Init. Br. at 22; C/I Init. Br. at 3-4. ComEd therefore requests that the Commission accept ComEd's calculation of interest on the reconciliation balance. ComEd Ex. 1.0 CORR. at 15-16; see also ComEd Ex. 2.01, Sch FR A-4.

2. Staff Position

Applying interest to the reconciliation balance net of related ADIT has been raised by Intervenors and rejected by the Commission in prior proceedings. Furthermore, the First District recently upheld the Commission's determination on this issue, on July 29, 2015. *Madigan* at ¶48. Accordingly, Intervenors' proposal to apply interest to the reconciliation balance net of related ADIT should once again be rejected.

3. C/I Position

C/I opine that they were aware that when this case was initiated and testimony filed, there was pending before the Appellate Court of Illinois, First District, an appeal of the Commission November 26, 2013 Order in Commonwealth Edison Company tariff investigation in Docket 13-0553. Subsequent to the filing of rebuttal testimony in this matter, the Appellate Court issued its decision affirming the Commission's Order in Docket 13-0553. See *Madigan*. In order to narrow the issues in this case, C/I determined that it would not pursue its proposal to make an accumulated deferred income tax adjustment to the reconciliation balance in this case.

4. Commission Analysis and Conclusion

The Commission finds that ComEd's position is supported by the record.

VIII. REVENUES

The record shows that ComEd deducted a total of \$130,999,000, after adjustments, of miscellaneous revenues from its revenue requirement. ComEd Ex. 2.0 at 40. None of the individual revenue amounts reflected in this total have been contested and this amount is fully supported in the record. The Commission approves ComEd's revenue amount.

IX. COST OF SERVICE AND RATE DESIGN

Cost of service issues in formula rate proceedings are traditionally uncontested. ComEd has supported all of the cost of service issues in this docket, and neither Staff nor any Intervenor has disagreed. Basic rate design issues are not at issue in this formula rate update case – instead, they were addressed in the rate design tariff filing that was filed on April 30, 2013 in Docket No. 13-0387, the 2013 Rate Design Investigation. The Commission entered a final Order in that docket on December 18, 2013 and the Order was affirmed by the Appellate Court of Illinois for the Second District on March 6, 2015. See *Coalition to Request Equitable Allocation of Costs Together (REACT) v. Illinois Commerce Comm'n*, 2015 IL App (2d) 140202 (Ill. App. Ct. March 6, 2015). The Commission finds that cost of service and rate design issues are uncontested and are approved.

X. OTHER

A. Wages and Salaries Allocator Utilized in Rider PE and Rate BESH

1. Staff Position

Rider PE, the tariff under which ComEd recovers the costs of purchased power and the costs of procuring the purchased power, utilizes a wages and salaries (“W&S”) allocator applicable to supply, the value of which is to be approved in each formula rate update proceeding. Staff does not object to ComEd’s calculation of the W&S allocator applicable to supply. Therefore, Staff recommends the language below be included in the Order entered by the Commission in this proceeding:

The Commission finds that the wages and salaries allocator applicable to supply of 0.43%, as calculated in this proceeding, should be used to develop charges determined and filed with the Commission under Rider PE and Rate BESH to be effective with the January 2016 monthly billing period. Subsequent calculations of the wages and salaries allocator applicable to supply made in subsequent ComEd Formula Rate Update proceedings must be applied in the corresponding subsequent determination and filing of charges under Rider PE and Rate BESH.

Staff Ex. 2.0R at 14-15.

ComEd did not address this subject in either its rebuttal or surrebuttal testimony. Therefore, Staff assumes that the Company does not object to the inclusion of this language in the Order.

2. Commission Analysis and Conclusion

Staff and ComEd agreed that the W&S allocator applicable to supply is 0.43%. No other party has contested the calculation or objected to the proposed language. The Commission therefore accepts the use of ComEd’s wages and salaries allocator applicable to supply.

B. Reporting Requirements

1. EIMA Investments

a. ComEd Position

ComEd presented evidence in its case in chief identifying separately its EIMA-related expenditures included in the Rate Year 2014 Reconciliation Revenue Requirement and in the projected plant additions included only in the Initial Rate Year 2016 Revenue Requirement. ComEd Init. Br. at 56. This data meets the Commission’s

requirements as set forth in ICC Docket No. 12-0321. 2012 Rate Case Order at 98; ComEd Ex. 3.0 at 15. Furthermore, in ICC Docket No. 13-0318, the Commission noted that ComEd had agreed to Staff's recommendation that it identify by category cumulative actual EIMA investments in addition to annual actual investments for each year. 2013 Rate Case Order at 85; ComEd Ex. 3.0 at 15. To these ends, and in compliance with these orders, ComEd provided this information as ComEd Ex. 3.01. ComEd Init. Br. at 56.

b. Staff Position

The Company provided direct testimony identifying incremental plant additions of \$463,229,227 placed in service in 2014 pursuant to Section 16-108.5(b) of the Act. ComEd Ex. 3.0 at 17-18. This data meets the Commission's requirements as set forth in Docket No. 12-0321. 2012 Rate Case Order at 98.

The Commission is setting a revenue requirement in this proceeding for the recovery of \$463.2 million in actual 2014 plant additions and \$654.8 million of projected 2015 plant additions in compliance with Section 16-108.5(b) of the Act. Actual 2014 plant additions and projected 2015 plant additions, combined with actual 2012 and 2013 plant additions of \$431.6, total \$1,549.6 million of actual and projected 2015 plant additions.

c. Commission Analysis and Conclusion

No party contests that ComEd has satisfied its obligation to provide the required information. Accordingly, the Commission finds that ComEd has satisfied its investment obligation.

2. Reconciliation Year Plant Additions

In the Commission's final Order in Docket No. 13-0318, Findings paragraph 13 set forth a table with details for the plant additions placed in service in 2012. 2013 Rate Case Order at 90-91. In this proceeding, ComEd provided a similar summary of the \$463,229,227 investment amount by category placed in service in 2014 by ComEd under Section 16-108.5(b) of the Act. ComEd Ex. 3.0 at 17-18. ComEd also provided a similar table for the \$654,813,654 of plant additions projected to be placed in service in 2015. *Id.* at 18-19. No party contests that ComEd has satisfied its obligation to provide the required information. Accordingly, the Commission finds that ComEd has satisfied its obligation to provide the required plant addition information.

3. Contributions to Low-Income Assistance and Support Programs

ComEd presented sufficient evidence demonstrating that it met its commitment to make certain contributions to low-income and other energy assistance programs, as required by EIMA. See 220 ILCS 5/16-108.5(b-10). This evidence was presented both in testimony and in the Annual Customer Assistance Report for 2014 as filed by ComEd on February 20, 2015. ComEd Ex. 4.0 at 27-29. No party contests that ComEd has met

its obligations to low-income and other energy assistance programs as required by EIMA. Therefore, the Commission approves ComEd's reporting of Contributions to Energy Low-Income and Support Programs.

XI. CONCLUSION

For the reasons stated herein, the Commission approves ComEd's 2016 Rate Year Net Revenue Requirement as set forth in the attached appendices, approves the original costs of ComEd's electric plant in service as of December 31, 2014, makes the required factual findings in support thereof, and authorizes and directs ComEd to make a compliance filing implementing the resulting rates and charges. These updates are applicable to delivery services provided by ComEd beginning on the first day of its January 2016 billing period, subject to ComEd's final compliance filing and the rulings in this Order.

XII. FINDINGS AND ORDERING PARAGRAPHS

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

- (1) Commonwealth Edison Company is an Illinois corporation engaged in the transmission, distribution, and sale of electricity to the public in Illinois and is a public utility as defined in Section 3-105 of the Public Utilities Act;
- (2) the Commission has jurisdiction over the parties and the subject matter herein;
- (3) the recitals of fact and conclusions of law reached in the prefatory portion of this Order are supported by the evidence of record and are hereby adopted as findings of fact and conclusions of law; the Appendices attached hereto provide supporting calculations;
- (4) for purposes of this proceeding, as adjusted, Commonwealth Edison Company's rate base is \$7,078,304,000 for the 2014 Reconciliation Year Revenue Requirement and \$8,273,855,000 for the Initial 2016 Rate Year Revenue Requirement;
- (5) the rate of return which Commonwealth Edison Company should be allowed to earn on its net original cost rate base is 7.02% for the 2014 Reconciliation Year and 7.05% for the 2016 Rate Year Initial Revenue Requirement, these rates of return incorporating a return on common equity of 9.09% and 9.14%, respectively, on long-term debt of 5.24%, and on short term debt of 0.33%;
- (6) the rates of return set forth in Finding (5) result in tariffed operating revenues of \$2,513,619,000 (reflecting the reconciliation and ROE Collar adjustments) and net annual operating income of \$583,307,000;

- (7) the Commission, based on Commonwealth Edison Company's proposed original cost of plant in service as of December 31, 2014, before adjustments, of \$17,199,997,000, and reflecting the Commission's determination adjusting that figure, unconditionally approves \$17,198,474,000 as the composite original cost of jurisdictional distribution services plant in service as of December 31, 2014;
- (8) Commonwealth Edison Company is authorized to place into effect tariff sheets and associated informational sheets designed to produce annual tariffed revenues of \$2,513,619,000. Such revenues in addition to other revenues will provide ComEd with an opportunity to earn the rates of return set forth in Finding (5);
- (9) the wages and salaries allocator applicable to supply of 0.43%, as calculated in this proceeding, should be used to develop charges determined and filed with the Commission under Rider PE and Rate BESH to be effective with the January 2016 monthly billing period. Subsequent calculations of the wages and salaries allocator applicable to supply made in subsequent Commonwealth Edison Company Formula Rate Update proceedings must be applied in the corresponding subsequent determination and filing of charges under Rider PE and Rate BESH.
- (10) the determinations regarding other subjects contained in the prefatory portion of this Order are reasonable for purposes of this proceeding; the compliance filing to be filed by Commonwealth Edison Company shall incorporate such determinations to the extent applicable;
- (11) new charges authorized by this Order shall become effective beginning with the first day of the January 2016 monthly billing period consistent with the requirements set forth in Section 16-108.5 of the Act; Commonwealth Edison Company shall be allowed four business days after the issuance of this Order to submit its compliance filing for informational purposes; the new tariff sheets and associated informational sheets authorized to be filed by this Order shall take effect the next business day after the date of filing, with updated charges listed on said tariff sheets, and associated informational sheets to be effective with the first day of the January 2016 monthly billing period; Commonwealth Edison Company shall provide supporting work papers to the Staff of the Commission concurrently with such informational compliance filing;
- (12) that the approved 2016 Rate Year Initial Revenue Requirement includes \$654,813,654 of projected plant additions expected to be placed in service in 2015 by Commonwealth Edison Company in compliance with, or in meeting, the infrastructure investment requirements of Section 16-108.5(b) of the Act. These are projected costs and will be reconciled to actual costs in a future formula rate update and reconciliation filing. The detail of these

projected plant additions in the categories as required by Section 16-108.5(b)(1) are as follows:

Distribution infrastructure improvements (URD program, mainline cable system refurbishment and replacement program, Ridgeland 69kV cable replacement program)	\$258,389,216
Training facility construction or upgrade programs (construction of training facilities program)	\$0
Wood pole inspection, treatment, and replacement	\$22,442,127
Reducing the susceptibility of storm-related damage (storm hardening program)	\$69,341,373
Total electric system upgrades, modernization programs, and training facilities	\$350,172,716
Additional smart meters	\$223,448,659
Distribution automation and associated cyber secure data communication network	\$62,008,683
Substation micro-processor relay upgrades	\$19,183,596
Total upgrade and modernization of transmission and distribution infrastructure and Smart Grid electric system upgrades	\$304,640,938
Total projected incremental 2015 plant additions in compliance with Section 16-108.5(b)(1) of the PUA	\$654,813,654

- (13) that the approved Reconciliation Revenue Requirement for 2014 includes \$463,229,227 of plant additions placed in service in 2014 by Commonwealth Edison Company in compliance with, or in meeting, the infrastructure investment requirements of Section 16-108.5(b) of the Act. The detail of these actual plant additions in the categories as required by Section 16-108.5(b)(1) are as follows:

Distribution infrastructure improvements (URD program, mainline cable system refurbishment and replacement program, Ridgeland 69kV cable replacement program)	\$169,862,795
Training facility construction or upgrade programs (construction of training facilities program)	\$0
Wood pole inspection, treatment, and replacement	\$21,635,390

Reducing the susceptibility of storm-related damage (storm hardening program)	\$29,850,560
Total electric system upgrades, modernization programs, and training facilities	\$221,348,744
Additional smart meters	\$145,187,566
Distribution automation and associated cyber secure data communication network	\$64,918,165
Substation micro-processor relay upgrades	\$31,774,751
Total upgrade and modernization of transmission and distribution infrastructure and Smart Grid electric system upgrades	\$241,880,483
Total actual incremental 2014 plant additions in compliance with Section 16-108.5(b)(1) of the PUA	\$463,229,227

IT IS THEREFORE ORDERED that the updated charges in Commonwealth Edison Company's initial filing shall not go into effect.

IT IS FURTHER ORDERED that Commonwealth Edison Company is authorized to file a compliance filing in accordance with Findings (8), (9), (10) and (11) and the prefatory part of this Order, applicable to service furnished on and after the effective date of said compliance filing, with updated charges to be effective with the first day of the January 2016 monthly billing period; work papers supporting the compliance filing shall be provided to the Staff of the Commission concurrently with the filing of said compliance filing.

IT IS FURTHER ORDERED that the approved revenue requirement set forth in Finding (8) above reflects \$463,229,227 of plant additions placed in service in 2014 by Commonwealth Edison Company, and \$654,813,654 of projected plant additions expected to be placed in service in 2015 by Commonwealth Edison Company, in compliance with or in meeting the infrastructure investment requirements of Subsection 16-108.5(b) of the Act.

IT IS FURTHER ORDERED that Commonwealth Edison Company's updated Embedded Cost of Service Study is accepted as a basis for setting rates in this proceeding.

IT IS FURTHER ORDERED that any motions, petitions, objections, and other matters in this proceeding which remain outstanding are hereby disposed of consistent with the conclusions herein.

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

DATED:
BRIEFS ON EXCEPTIONS DUE:
REPLY BRIEFS ON EXCEPTIONS DUE:

October 19, 2015
October 27, 2015
November 3, 2015

Terrance Hilliard
Heather Jorgenson
Administrative Law Judges