

**STATE OF ILLINOIS**  
**BEFORE THE ILLINOIS COMMERCE COMMISSION**

<b>COMMONWEALTH EDISON COMPANY</b>	)	
	)	
<b>Petition for Approval of Tariffs</b>	)	<b>Docket No. 06-0411</b>
<b>Implementing ComEd's Proposed</b>	)	
<b>Residential Rate Stabilization Program</b>	)	

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**REPLY TESTIMONY OF**  
**JONATHAN WALLACH**  
**ON BEHALF OF**  
**THE CITIZENS UTILITY BOARD, THE COOK COUNTY STATE'S ATTORNEY'S**  
**OFFICE, AND THE CITY OF CHICAGO**

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**CUB-CCSAO-CITY Ex. 2.0**

**AUGUST 21, 2006**

1 | **Q: Please state your name, occupation, and business address.**

2 | A: I am Jonathan F. Wallach. I am Vice President of Resource Insight, Inc., 5  
3 | Water Street, Arlington, Massachusetts.

4 | **Q: Are you the same Jonathan F. Wallach who submitted direct testimony in**  
5 | **this docket?**

6 | A: Yes.

7 | **Q: What is the purpose of your reply testimony?**

8 | A: The purpose of this testimony is to respond to ~~the these~~ portions of the  
9 | rebuttal testimony of Commonwealth Edison Company (“ComEd” or “the  
10 | Company”) witnesses J. Barry Mitchell, Robert K. McDonald, Paul R.  
11 | Crumrine, and Michael J. Meehan that pertain to the findings and  
12 | recommendations of my direct testimony. In addition, this testimony  
13 | addresses the Company’s proposal to offer the Residential Rate Stabilization  
14 | Program (RRSP) on an opt-in basis, per the recommendation of Staff witness  
15 | Peter Lazare.

16 | **Q: Please summarize the findings and recommendations of your direct**  
17 | **testimony.**

18 | A: My direct testimony addresses ComEd’s proposal to accrue interest on  
19 | deferred amounts at its authorized rate of return, and discusses why deferrals  
20 | under the RRSP are less risky than other regulated investments and are thus  
21 | likely to require a lower return than other regulated investments. My direct  
22 | testimony also suggests that carrying costs should be based on the actual  
23 | costs to finance deferrals. In this regard, I note in my direct testimony that  
24 | ~~the finding by Ameren, in its~~ initial filing in Docket No. 06-0448, ~~where~~  
25 | Ameren stated found that short-term debt would be a likely source of funds

26 | for financing the deferral asset. Moreover, , along with Ameren’s and Ameren  
27 | recommended that the Commission investigate the feasibility of  
28 | reducing interest costs through securitized financing of deferrals.

29 | In addition, my direct testimony discusses the fact that the Company’s  
30 | filing lacks specific detail on the treatment of new customer accounts and other  
31 | essential information for evaluating the reasonableness of its proposal.

32 | In light of these findings, I recommend in my direct testimony that the  
33 | Commission not approve the Company’s proposal. Instead, I recommend  
34 | that the Commission undertake an investigation of the feasibility of  
35 | securitized financing of power-cost deferrals. Neither the Company’s  
36 | rebuttal testimony or the testimony of the Staff has persuaded me to change  
37 | any of my recommendations.

38 | **Q: Are there elements of the proposed RRSP that reduce cost-recovery risk?**

39 | A: As I noted in my direct testimony, there are a number of elements of the  
40 | Company’s proposal that reduces recovery risk. For example, the Company’s  
41 | proposal includes a true-up mechanism to ensure recovery of the deferral  
42 | balance. This provision should significantly dramatically reduce the risk of less-  
43 | than-full return of and on deferred amounts.

44 | **Q: Have other state commissions found that power-cost deferrals are less risky**  
45 | **than other ratebase assets?**

46 | A: Yes. In an order approving a deferral mechanism for Baltimore Gas and  
47 | Electric, the Maryland Public Service Commission found that “the risk  
48 | associated with the deferred generation balance is much less than for normal  
49 | utility assets.”<sup>1</sup>

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1 Maryland Public Service Commission, Order No. 80638, Case No. 9052, March 6, 2006, p.  
38.

50 **Q: What is ComEd’s position with regard to the risk and appropriate return**  
51 **on RRSP deferrals?**

52 A: While acknowledging that aspects of the RRSP reduce recovery risk relative to  
53 other ratebase assets, Mr. McDonald asserts that this reduced risk has no bearing  
54 on required return on deferrals. Instead, Mr. McDonald claims that: “Absent an  
55 absolute guarantee of recovery, actual carrying costs will not be lower than  
56 ComEd’s weighted average cost of capital.”<sup>2</sup>

57 **Q: Does this position appear reasonable?**

58 A: No. Mr. McDonald’s argument appears counter-intuitive in its assertion that  
59 any reduction in recovery risk short of an “absolute guarantee” of full recovery  
60 will not reduce carrying costs. The implication of Mr. McDonald’s assertion  
61 would appear to be that the deferral asset would have to be equivalent to a risk-  
62 free investment in order to reduce carrying costs below the Company’s cost of  
63 capital.

64 Mr. McDonald’s argument in this regard also appears inconsistent with his  
65 claims regarding the benefits of securitization. Specifically, Mr. McDonald  
66 believes that securitized financing would lower carrying costs on the deferral  
67 balance, even though securitization does not offer the “absolute guarantee” of  
68 recovery that Mr. McDonald posits as required to reduce carrying costs.

69 **Q: Does the Company dispute your suggestion that carrying costs should be**  
70 **based on the actual costs to finance deferrals?**

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<sup>2</sup> *Rebuttal Testimony of Robert K. McDonald*, ComEd Ex. 5.0, ICC Docket No. 06-0411, August 1, 2006, p. 8.

71 | A: No.<sup>3</sup> \_However, Mr. McDonald does take issue with the findings by both  
72 | Ameren and Staff witness Michael McNally that short-term debt is a likely  
73 | source of funds for financing the deferral asset.

74 | **Q: What rates of return will Maryland utilities apply to the regulatory assets**  
75 | **established for deferral of residential power-supply costs?**

76 | A: Both Baltimore Gas and Electric and the PHI Companies (Potomac Electric  
77 | Power and Delmarva Power and Light) intend to accrue interest on power-cost  
78 | deferrals at their actual short-term borrowing rates.<sup>4</sup>

79 | **Q: What is the Company’s response to your recommendation for an**  
80 | **investigation of securitized financing?**

81 | A: The Company appears to be of two minds with regard to my recommendation.  
82 | Mr. McDonald states that, under the right conditions, ComEd would be  
83 | interested in securitized financing of the deferral balance. \_Mr. Mitchell, on the  
84 | other hand, states that “an investigation of the type suggested by Mr. Wallach is  
85 | neither timely nor useful.”<sup>5</sup>

86 | **Q: What is the basis for Mr. Mitchell’s concerns regarding the timeliness of**  
87 | **such an investigation?**

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[In fact, in its application for rehearing in Docket No. 05-0597, the Company proposes to derive the interest cost on its pension contribution at the actual cost of debt that would have been used to fund the contribution. See \*Verified Application for Rehearing of Commonwealth Edison Company\*, ICC Docket No. 05-0597, August 15, 2006, p.22.](#)

<sup>4</sup> BGE will accrue interest at short-term rates until and unless it issues securitized debt.

<sup>5</sup> *Rebuttal Testimony of J. Barry Mitchell*, ComEd Ex. 4.0, ICC Docket No. 06-0411, August 1, 2006, p. 9.

88 A: Mr. Mitchell misreads my direct testimony as proposing that the investigation be  
89 conducted in a proceeding separate from the instant docket. As such, he is  
90 concerned that such an investigation would delay implementation of the RRSP.

91 In fact, I suggested that the investigation could be part of the instant docket  
92 or carried out in a separate docket. If the Company is concerned about the  
93 timeliness of a separate docket, then I see no reason why the investigation could  
94 not be pursued as part of this proceeding. However, such an investigation  
95 would require an additional phase to collect testimony on the issues surrounding  
96 securitized financing.

97 **Q: Did the Company respond to the concerns raised in your direct testimony**  
98 **regarding treatment of new customer accounts?**

99 A: Yes. As part of its proposal to implement the RRSP on an opt-in basis, the  
100 Company proposes to limit eligibility to accounts existing as of December 31,  
101 2006. This proposal to limit eligibility reasonably addresses my concerns  
102 regarding new accounts. I address the Company's opt-in proposal below.

103 **Q: How did the Company respond to your finding that the filing lacked the**  
104 **information needed to evaluate the reasonable~~ness~~ of the proposed RRSP?**

105 A: The Company provided a number of *pro forma* financial analyses in response to  
106 discovery, and suggests in its rebuttal filing that additional information  
107 regarding the likely magnitude of rate increases and deferrals will be entered  
108 into the record once auction results are known and distribution rates are finally  
109 approved in Docket No. 05-0597.

110 The Company's proposal to supplement the record is reasonable, so long  
111 as other parties have ~~retain~~ the right to provide evidence in response to the  
112 Company's supplemental filings.

113 **Q: Please describe the Company's opt-in proposal.**

114 A: Based on the recommendation by Staff witness Lazare, the Company proposes  
115 to implement the RRSP on an opt-in basis. According to Mr. Crumrine, the opt-  
116 in version of the RRSP would have the following features:

- 117 • The enrollment period will extend from January to March of 2007.
- 118 • Starting with the April, 2007 billing period, participant bills will be credited  
119 with an amount that ensures that total rates increase by no more than 10%,  
120 as proposed by Mr. Lazare.
- 121 • In addition, participants will receive a one-time credit to cover deferrals for  
122 the January through March billing periods.
- 123 • Deferral balances will be tracked by customer account. Any customer that  
124 terminates service will be rendered a final bill for recovery of the  
125 outstanding deferral balance.
- 126 • Program eligibility will be limited to existing accounts as of December 31,  
127 2006.

128 **Q: What are the potential benefits of implementing the RRSP on an opt-in**  
129 **basis?**

130 A: The opt-in approach offers two major advantages over the mandatory version of  
131 the RRSP. First, it provides consumers the opportunity to decide whether to  
132 finance their power-supply costs (at the interest rate ultimately approved by the  
133 Commission) or to simply pay the full market price of power upfront.

134 Second, participation, and thus deferred amounts, are likely to be  
135 substantially less than under the mandatory version of the RRSP. As a result,  
136 the opt-in approach (in conjunction with the 10% rate increase proposed by Mr.  
137 Lazare) should alleviate the Company's concerns regarding the financial risk  
138 and capital constraints associated with deferral balances.

139 **Q: How should the Company proceed with the development of the opt-in**  
140 **proposal?**

141 A: The Company should develop detailed specifications for the design and  
142 implementation of the opt-in mechanism, including detailed budgets for  
143 implementation and operations. According to Mr. Meehan, the Company’s  
144 current estimates of program costs are “high level estimates.”<sup>6</sup> As part of the  
145 detailed design process, the Company should develop more precise budgets for  
146 fixed and variable program expenditures.<sup>7</sup>

147 As part of this development effort, the Company should undertake  
148 additional financial analyses that incorporate estimates of likely program  
149 participation rates and that evaluate financial metrics under a range of scenarios  
150 for financing deferral balances. Once available, these analyses should also  
151 incorporate the results of the auctions and final resolution of Docket No. 05-  
152 0597.

153 **Q: Please summarize your conclusions. Does incorporation of an opt-in**  
154 **provision eliminate your concerns with the RRSP?**

155 A: I support tNo. The incorporation of an opt-in provision, because it provides  
156 customers with a choice regarding their participation in the plan. However, the  
157 opt-in provision, but it does not eliminate my concerns regarding the carrying  
158 charges that apply to deferred balances.- The Commission should not approve  
159 any RRSP plan that includes carrying charges above the actual cost of the funds

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<sup>6</sup> *Rebuttal Testimony of Michael J. Meehan*, ComEd Ex. 8.0, ICC Docket No. 06-0411, August 1, 2006, p. 9. Mr. Meehan also provides an estimate of the impact of the program on uncollectible expenses. Presumably, this is also a “high level” estimate.

<sup>7</sup> However, as suggested in Mr. Mitchell’s rebuttal testimony (p. 3), recovery and allocation of program costs and incremental uncollectible costs is subject to approval by the Commission in future rate cases.



160 | used to finance deferral amounts. The Commission should also investigate the  
161 | benefits of securitized financing as a way to reduce the carrying charges  
162 | associated with deferred balances, as Ameren has recommended in its initial  
163 | filing in Docket No. 06-0448. **The Commission should not approve any plan**  
164 | **without fully investigating the options for minimizing the cost of financing**  
165 | **power-cost deferrals.**

166 | **Q: Does this conclude your reply testimony?**

167 | A: Yes.