

**PECO ENERGY COMPANY  
STATEMENT NO. 2-R**

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PECO ENERGY COMPANY – ELECTRIC DIVISION

DOCKET NO. R-2010-2161575

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REBUTTAL TESTIMONY

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WITNESS: PHILLIP S. BARNETT

SUBJECTS: FUTURE TEST YEAR CAPITAL  
ADDITIONS, FUTURE TEST YEAR  
SALES LEVELS, AMORTIZATION  
OF 2010 LOST REVENUES, RATE  
EFFECTIVE PERIOD SALES  
LEVELS, SALARIES AND WAGES,  
INCENTIVE COMPENSATION,  
OTHER OPERATING EXPENSES  
AND RING-FENCING

DATED: AUGUST 3, 2010

## TABLE OF CONTENTS

	<b>Page</b>
I. INTRODUCTION AND PURPOSE OF TESTIMONY.....	1
II. FUTURE TEST YEAR CAPITAL ADDITIONS.....	2
III. FUTURE TEST YEAR SALES LEVELS .....	5
IV. AMORTIZATION OF 2010 LOST REVENUES.....	8
V. ACT 129 LOST REVENUE PRO FORMA ADJUSTMENT FOR 2011 AND 2012.....	9
VI. SALARIES AND WAGES.....	13
VII. INCENTIVE COMPENSATION.....	14
VIII. OTHER OPERATING EXPENSES.....	16
IX. RING-FENCING .....	17
X. CONCLUSION.....	21

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**REBUTTAL TESTIMONY  
OF  
PHILLIP S. BARNETT**

**I. INTRODUCTION AND PURPOSE OF TESTIMONY**

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5  
6 **1. Q. Please state your name and business address.**

7 A. My name is Phillip S. Barnett. My business address is PECO Energy Company, 2301  
8 Market Street, Philadelphia, Pennsylvania 19103.

9 **2. Q. By whom are you employed and in what capacity?**

10 A. I am employed by PECO Energy Company (“PECO” or the “Company”) as Senior  
11 Vice President and Chief Financial Officer.

12 **3. Q. Have you previously testified in this proceeding?**

13 A. Yes. I submitted direct testimony, pre-marked as PECO Statement No. 2, which (1)  
14 explained PECO’s need for rate relief; (2) provided an overview of PECO’s principal  
15 accounting exhibits, as well as its planning process; and (3) described the nature and  
16 allocation of costs for services that PECO receives from the Exelon Business Services  
17 Company. My background and qualifications are set forth in that statement. In  
18 addition, I submitted supplemental testimony, pre-marked as PECO Statement No. 2-  
19 S, in which I addressed certain issues raised by the Commission.

20 **4. Q. What is the purpose of your rebuttal testimony?**

21 A. I will respond to various rate base, revenue and operating expense adjustments  
22 proposed by Office of Consumer Advocate (“OCA”) witness David J. Effron (OCA  
23 Statement No. 1) and Office of Trial Staff (“OTS”) witnesses Dorothy Morrissey

1 (OTS Statement No. 2) and Gary L. Yocca (OTS Statement No. 3). In addition, I will  
2 reply to certain statements made by OCA witness David C. Parcell (OCA Statement  
3 No. 2) regarding PECO's ring-fencing efforts.

## 4 II. FUTURE TEST YEAR CAPITAL ADDITIONS

5 **5. Q. Mr. Efron contends that PECO has overstated its claim for future test year**  
6 **(FTY) plant additions and has proposed a \$53.5 million rate base adjustment**  
7 **(and corresponding adjustments to the Company's depreciation reserve and**  
8 **annual depreciation accrual) based on a three-year (2007-2009) historic average**  
9 **of actual plant additions. Please comment.**

10 A. Mr. Efron offers two reasons for his recommendation: (1) that PECO's estimated  
11 2010 distribution plant additions (Accounts 360-374) of \$260.9 million exceed the  
12 level of additions in recent years; and (2) that the amount of plant placed in service  
13 during the first five months of the FTY lagged behind budgeted levels.

14 **6. Q. Is Mr. Efron correct that estimated FTY plant additions exceed prior year**  
15 **levels?**

16 A. Yes, but that alone certainly doesn't justify Mr. Efron's proposed disallowance.  
17 Initially, I would note that the \$260.9 million figure that Mr. Efron uses to calculate  
18 his adjustment (see OCA St. No. 1, Schedule B-1) does not represent PECO's FTY  
19 distribution plant additions claim. As shown on Schedule C-2, pages 4 and 6, of  
20 Exhibit RLO-1, that figure was adjusted downwards by approximately \$2.7 million to  
21 reflect the removal from base rates of certain Act 129 investments.

22 In addition, and as noted above, Mr. Efron focuses solely on the distribution plant

1 accounts (Nos. 360-374). However, in any given year, PECO must allocate capital  
2 dollars between its distribution and transmission functions. Thus, in 2009, the  
3 Company added nearly \$67 million of transmission plant; in 2010, as proportionately  
4 more dollars are being dedicated to the distribution function, transmission plant  
5 additions are expected to decline to about \$40 million (see Exhibit RLO-1, Schedule  
6 C-2, page 4 and Exhibit RLO-2, Schedule C-2, page 4).

7 **7. Q. Is PECO's 2010 capital budget out of line with projected capital expenditure**  
8 **levels over the next several years?**

9 A. No, it is not. In fact, PECO expects to spend, on average, approximately \$353 million  
10 on its distribution operations over the next three years (2011-2013).

11 **8. Q. What about Mr. Effron's observation that less plant was placed in service**  
12 **during the first five months of 2010 than anticipated?**

13 A. Mr. Effron asserts that actual capital additions were \$25.1 million "below budget"  
14 through May 2010. However, as the Company explained in response to discovery  
15 (Interrogatories OCA-III-3 and OCA-IX-5), that apparent shortfall, which occurred  
16 during the January-March period, was only about \$6.4 million when the budgeted  
17 additions are properly stated on a seasonally adjusted basis.

18 **9. Q. What accounts for the \$6.4 million seasonally adjusted shortfall?**

19 A. As the Commission is aware, PECO experienced an unusually high level of storm  
20 activity during the first part of 2010, requiring the reassignment of workforce and the  
21 shifting of some capital projects to the second half of the year. Nonetheless, and as  
22 we indicated in response to Interrogatory OCA-IX-5, actual expenditures were on

1 track with budgeted amounts as of May 31, 2010.

2 **10. Q. In his rebuttal testimony (PECO Statement No. 3-R), Mr. O'Brien notes that the**  
3 **Company is reducing its FTY plant additions claim by approximately \$40.0**  
4 **million. If PECO disagrees with Mr. Effron's proposal, why is it making this**  
5 **adjustment?**

6 A. The Company has concluded that although this \$40 million in capital expenditures  
7 will be made in 2010, work on two new large substations -- the Peltz and Penrose  
8 projects -- will not be completed until 2011. Even though these projects will be used  
9 and useful in providing service within months after the rates in this case go into  
10 effect, I am advised by counsel that they do not qualify as rate base-eligible  
11 construction work in progress (CWIP).

12 **11. Q. Why did PECO undertake these projects?**

13 A. The new Peltz and Penrose substations are needed to improve reliability and support  
14 future growth in South Philadelphia and the University of Pennsylvania area. In short,  
15 they are part of PECO's broader efforts to address replacement of infrastructure in  
16 center city that is obsolete and to support capacity growth.

17



1 OTS-RS-29 is attached to this rebuttal testimony as Schedule A.

2 **15. Q. Mr. Effron’s proposed adjustment would increase PECO’s present rate revenues**  
3 **by \$15.442 million, or approximately \$2.5 million more than the revision PECO**  
4 **has made in Exhibit RLO-5. Please comment.**

5 A. Mr. Effron would utilize 2009 weather normalized distribution revenue, adjusted to  
6 capture an estimated negative (0.203%) impact on 2010 sales attributable to PECO’s  
7 implementation of energy efficiency and demand reduction programs in compliance  
8 with Act 129.

9 **16. Q. Do you agree with Mr. Effron’s recommendation?**

10 A. No, I do not. I believe that PECO’s updated sales forecast, as embodied in its  
11 response to Interrogatory OTS-RS-29 (Schedule A hereto) provides a more current  
12 and more accurate estimate of the Company’s 2010 present rate revenues than  
13 defaulting to historic test year (2009) data as Mr. Effron proposes. In addition, I do  
14 not agree with his conclusion that sales will decline by only (0.203%) in 2010 as the  
15 result of Act 129.

16 **17. Q. Why?**

17 A. Because Mr. Effron’s derivation of the negative (0.203%) factor, as set forth on his  
18 Schedule C-1.1, is flawed in a number of critical respects:

- 19 ■ Mr. Effron assumes a usage reduction target of 1,182 GWh, which  
20 represents the 3.0% legislatively imposed minimum savings  
21 requirement. However, PECO’s Energy Efficiency and  
22 Conservation (“EE&C”) Plan, as approved by the Commission,  
23 calls for energy savings of 1,296 GWh, or approximately 3.3%.

- 1                   ▪ Mr. Efron assumes that customer usage will decline linearly  
2                   through equal 0.087% monthly decrements. Such reductions in  
3                   usage would not enable PECO to satisfy the 1.0% and 3.0%  
4                   minimum savings requirements established by Act 129.
- 5                   ▪ Mr. Efron assumes that savings began in June 2010 when the  
6                   EE&C program was actually launched in October 2009.

7 **18. Q. Why would Mr. Efron’s assumed 0.087% monthly sales reductions not satisfy**  
8 **the Act 129 mandates?**

9 A. Mr. Efron apparently believes that the Act 129 savings targets are met as long as  
10 PECO achieves usage reductions of 1.0% and 3.0% during the months of May 2011  
11 and May 2013, respectively. PECO, in contrast, interprets Act 129 to require it to  
12 achieve savings of 1.0% and 3.0% for the full twelve months ending May 2011 and  
13 May 2013 (i.e., not on an end-of-program-year, annualized-May basis).

14 **19. Q. Are there any other problems with Mr. Efron’s proposed adjustment?**

15 A. Yes. On his Schedule C-1, Mr. Efron applies his (0.203%) sales decline factor  
16 across-the-board. In other words, he assumes that each customer class will  
17 experience the same (0.203%) average usage reduction in 2010. However, under  
18 PECO’s Commission-approved EE&C Plan, roughly 60% of the projected 2010  
19 energy savings are projected to come from the residential class. And, because  
20 residential customers pay the highest variable distribution rate, Mr. Efron’s approach  
21 seriously understates the impact of PECO’s EE&C programs on distribution revenue.

22 **20. Q. Have you determined the extent to which Mr. Efron has understated the effect**  
23 **of Act 129 on PECO’s 2010 sales levels?**

24 A. Yes. If the various flaws in Mr. Efron’s analysis that I previously identified are

1 corrected, his proposed Act 129 sales reduction factor of 0.203% would increase to  
2 0.612% and his proposed \$15.442 million adjustment drops to \$9.406 million.

3 **21. Q. What do you recommend?**

4 A. I recommend that the Commission accept the \$12.963 million revenue adjustment  
5 included in Exhibit RLO-5 because it more accurately reflects the anticipated impacts  
6 of improved economic conditions and PECO's EE&C Plan on 2010 sales levels.

7 **IV. AMORTIZATION OF 2010 LOST REVENUES**

8 **22. Q. Messrs. Effron and Kalcic would disallow the Company's proposed two-year**  
9 **amortization of the revenues that PECO will not realize in 2010 as a**  
10 **consequence of its implementation of Act 129 energy efficiency programs. Please**  
11 **comment.**

12 A. Mr. Effron asserts that to allow PECO to recover its 2010 lost revenues would  
13 constitute impermissible "retroactive ratemaking," while Mr. Kalcic contends, based  
14 on "advice of counsel," that Act 129 does not permit such lost-revenue recovery. The  
15 legality of PECO's proposal will be addressed in full in the Company's Main Brief to  
16 be filed in September. That said, I need to point out that PECO is simply seeking to  
17 be made whole for the revenues it will lose in 2010 as a result of its compliance with  
18 a Commission-approved EE&C Plan. In fact, because it has not asked for recovery of  
19 the revenues it lost in the fourth quarter of 2009 following its accelerated  
20 implementation of a compact fluorescent lamp (CFL) program, PECO will not be  
21 made entirely whole even if its proposed amortization is approved. In any event, I  
22 believe it would be inequitable and would unquestionably send the wrong message

1 for the Commonwealth to direct and encourage utilities to take steps to help  
2 customers reduce their consumption and then penalize those same companies for their  
3 successful compliance with – and aggressive implementation of – that legislative  
4 mandate.

5  
6 **V. ACT 129 LOST REVENUE PRO FORMA ADJUSTMENT FOR 2011 AND 2012**

7 **23. Q. Messrs. Kalcic, Yocca and Effron each challenges, in whole or in part, PECO’s**  
8 **proposal to set rates based on sales levels that take into account the anticipated**  
9 **revenues to be lost, on average, during 2011 and 2012 as the result of PECO’s**  
10 **compliance with Act 129. Please address their recommendations.**

11 A. Mr. Kalcic rejects the Company’s proposal on the same basis that he would disallow  
12 the amortization of 2010 revenue losses, namely that his counsel has advised him that  
13 Act 129 only permits a utility “to adjust its test period billing determinants  
14 downwards” (OSBA Statement No. 1, p. 13). As noted previously, PECO strongly  
15 disagrees with this interpretation of the applicable statutory language. Unlike Mr.  
16 Kalcic, Messrs. Yocca and Effron seemingly agree with PECO that Act 129 permits  
17 the recognition of prospective revenue losses but disagree with the Company’s  
18 quantification of the appropriate adjustment.

19 **24. Q. What changes would Mr. Yocca make and what reasons does he give in support**  
20 **of his recommendation?**

21 A. Mr. Yocca would impute additional present rate revenues of \$13.974 million and  
22 thereby reduce the Company’s claimed revenue requirement by a like amount.

23 Notably, Mr. Yocca does not take issue with the recognition of 2011 lost revenues:

1 I am not contesting the 2011 projected lost revenues claimed by the  
2 Company since they are built into rates on an average basis over the  
3 first year that the rates will be in effect. (p. 20)

4 Rather, Mr. Yocca explains that “[t]he basis for my recommendation is the removal  
5 of the impact of lost revenues for 2012” (p. 18).

6 **25. Q. Does Mr. Yocca’s proposed \$13.964 million adjustment achieve its intended  
7 purpose?**

8 A. No, it does not. In fact, Mr. Yocca has removed from PECO’s lost revenue  
9 calculation not only the 2012 lost revenues, but also one-half of the 2011 lost  
10 revenues. Consequently, even if there were any basis for disregarding the 2012 lost  
11 revenues, and in my opinion there is not, Mr. Yocca’s recommended adjustment is  
12 overstated by \$7.839 million.

13 **26. Q. Please explain.**

14 A. As he discusses at page 18 of his testimony, and as shown in his Schedule 8, Mr.  
15 Yocca stripped out of his calculation the incremental revenue impact for 2012 of  
16 \$27.298 million, as depicted on line 25 of Schedule D-5E of Exhibit RLO-1, but  
17 deliberately left in the \$15.678 million revenue impact for 2011 at line 15, which, as  
18 indicated previously, he does not contest. However, at line 35 of his Schedule 8, Mr.  
19 Yocca divides the \$15.678 million 2011 lost revenue impact by two and ends up  
20 imputing an additional \$7.359 million of revenue that he agrees PECO will not  
21 recover.

22 **27. Q. Is there any justification for halving the 2011 lost revenue impact?**

23 A. No. On its Schedule D-5E, PECO averaged the lost revenue impacts for 2011 and

1 2012 for purposes of developing its proposed adjustment. Once Mr. Yocca stripped  
2 out the 2012 data, the need for the column 5 averaging (column E on Mr. Yocca's  
3 Schedule 8) went away.

4 **28. Q. Have you recalculated Mr. Yocca's recommended adjustment to correct this**  
5 **oversight?**

6 A. Yes. Schedule B to this testimony replicates Mr. Yocca's Schedule 8 but recognizes  
7 the full impact of the 2011 lost revenues. As corrected, Mr. Yocca's composite lost  
8 revenue adjustment increases from \$17.574 million to \$25.413 million.

9 **29. Q. Please turn now to Mr. Effron's proposed adjustment.**

10 A. Mr. Effron would impute additional present rate revenues of \$7.21 million (Schedule  
11 C-1) based on his determination that reductions in consumption attributable to  
12 PECO's Act 129 programs will average 1.69% during 2011 and 2012 (Schedule C-  
13 1.1). In support of this adjustment, Mr. Effron contends that (1) reductions in  
14 consumption are less than projected and (2) the rates per kWh used by PECO in  
15 quantifying its adjustment were too high, thus overstating the lost revenue effect.

16 **30. Q. Do you agree with Mr. Effron's proposed adjustment?**

17 A. No, I do not. First, and as shown on my Schedule C, actual EE&C savings were at  
18 target of forecasted levels during the first five months of 2010. Second, and more  
19 importantly, Mr. Effron's calculations of the likely impact of Act 129 on 2011 and  
20 2012 sales levels are plagued by the same flaws and erroneous assumptions  
21 previously discussed in connection with his recommended adjustment to PECO's  
22 FTY sales levels (Section III of this testimony). In summary, those errors included:

1 (1) a later than actual assumed program start date; (2) a lower than actual assumed  
2 usage reduction target; (3) an assumption that usage reductions would be achieved in  
3 equal 0.087% monthly decrements; and (4) an assumption that each customer class  
4 would experience the same percentage usage reduction.

5 **31. Q. Have you attempted to replicate Mr. Effron's proposed \$7.21 million adjustment**  
6 **but correcting these errors?**

7 A. Yes. On Schedule D, I show the usage reductions set forth in PECO's approved  
8 EE&C Plan broken down between residential customers and commercial and  
9 industrial ("C&I") customers. As indicated, residential customers are expected to  
10 generate 58% and 55% of the Act 129 savings in 2011 and 2012 respectively.  
11 Utilizing those data and PECO's projected monthly usage reductions, I reconstructed  
12 Mr. Effron's Schedule C-1.1. As can be seen on my Schedule E, residential  
13 customers are expected to experience average 2011-2012 Act 129 usage reductions of  
14 4.714% while C&I customers are expected to achieve average annual savings of  
15 1.953%. Finally, on Schedule F, I have replicated Mr. Effron's Schedule C-1,  
16 substituting the customer class specific savings projections.

17 **32. Q. What conclusion do you draw from your analysis?**

18 A. That there is no basis for Mr. Effron's proposed adjustment and that it should be  
19 rejected. As shown on Schedule F on the line captioned "Modify Prospective Effect  
20 of Act 129," Mr. Effron's methodology, once corrected, suggests that PECO's  
21 estimated average 2011-2012 revenue loss of \$21.803 million may understate the  
22 potential revenue loss by \$11.160 million.

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**VI. SALARIES AND WAGES**

**33. Q. Mr. Effron has recommended that PECO’s allowance for wages and salaries be reduced by \$3.24 million to reflect the fact that the Company’s employee complement has not yet increased to the level forecast. Please comment.**

A. Mr. Effron is correct that PECO has not yet reached its projected year-end headcount of 1,918 employees. However, the Company fully expects to do so by December 31, 2010.

**34. Q. What was PECO’s headcount at June 30, 2010?**

A. Our headcount at June 30, 2010 was 1,868 employees.

**35. Q. Why do you expect PECO to add 50 employees during the second half of the year?**

A. For two reasons. First, the Company is in the process of staffing twenty-eight vacant positions. As detailed on Schedule G to this testimony, PECO has extended offers of employment comprising the equivalent of thirteen electric positions (of which four have already been accepted); has interviewed or is in the process of interviewing for an additional ten positions; and has posted the remaining four positions. Second, the Company has scheduled an Electric Line School session for September, which, when completed, will add another twenty employees to our ranks.

**36. Q. What is the Electric Line School and what positions will its graduates fill?**

A. The Electric Line School is a ten-week training program where, upon graduation,

1 employees are qualified to work safely and effectively on PECO's electric system.

2 The graduates will fill open positions and, over time, will become 1st Class Linemen.

3 **VII. INCENTIVE COMPENSATION**

4 **37. Q. Please describe the Company's Annual Incentive Program.**

5 A. The Company's Annual Incentive Program (AIP) places a portion of salaried  
6 employees' total annual compensation at risk based on Exelon Corporation,  
7 Operating Company and individual-employee performance against a variety of Key  
8 Performance Indicators (KPIs) or similar metrics. The portion of the total annual  
9 compensation placed at risk varies depending on the employee's salary grade, with  
10 employees in higher grades having a larger portion of their compensation dependant  
11 on performance. Specifically, under the terms of the program, there are four main  
12 performance metrics used to determine an employee's annual incentive. One  
13 performance metric relates to Exelon Earnings Per Share (EPS), while the other three  
14 components are attributable to the Operating Company's performance, a PECO  
15 Operating Cost measure, and a Composite PECO reliability, customer satisfaction and  
16 employee-safety measure. In addition to the four metrics, for salaried, non-  
17 represented employees, an employee's individual performance is a measure used to  
18 determine the amount of the employee's payout under the AIP.

19 **38. Q. Please explain the Company's compensation philosophy.**

20 A. PECO's compensation targets the total salaries and wages component of its  
21 employees (including performance-based incentive compensation) at the 50<sup>th</sup>  
22 percentile of a comparison group's total compensation for like job titles. We believe

1 that, by using these parameters to determine total compensation, the Company offers  
2 a fair and reasonable compensation package that is necessary to attract and retain  
3 talented employees. By tying a portion of an employee's annual compensation to the  
4 achievement of practical Exelon, Operating Company and individual performance  
5 goals, we believe that the employee is given the appropriate incentive to excel.

6 **39. Q. Do you agree with either Ms. Morrissey's recommendation that incentive**  
7 **compensation expense be "shared" equally by customers and shareholders or**  
8 **Mr. Effron's proposal to disallow the 20% of PECO's incentive compensation**  
9 **claim that is triggered by its parent company, Exelon, achieving certain earnings**  
10 **per share (EPS) targets?**

11 A. No, I do not. Even though a portion of the Company's AIP cost is based on Exelon  
12 achieving certain EPS goals, inclusion of the full amount of the budgeted AIP  
13 compensation in our rates is reasonable for several reasons. First, we believe that the  
14 Commission should look at the reasonableness of the Company's total compensation  
15 philosophy, and not whether certain features of that compensation are based on  
16 financial performance. By having a 50<sup>th</sup> percentile target, total compensation  
17 (including incentive compensation) is still lower than 50% of the comparable group  
18 companies, but sufficient to attract and retain a talented workforce. Second, the AIP  
19 formula is driven primarily by Company targets that focus on customer service,  
20 service reliability, safety, cost management, and other operational metrics. Third,  
21 achieving financial performance goals benefits customers in a variety of ways. A  
22 financially healthy public utility typically can borrow at better interest rates and



1 still fully engaged, albeit on other matters.

2 **IX. RING-FENCING**

3 **42. Q. Have you reviewed OCA witness Parcell’s testimony regarding PECO’s ring-**  
4 **fencing efforts?**

5 A. Yes, I have. Mr. Parcell quotes from a February 24, 2010 Ratings Direct from  
6 Standard and Poor’s to the effect that PECO’s ring-fencing measures may not be  
7 “effective in insulating the Company from Exelon and its unregulated operations.”

8 **43. Q. Do you agree with Mr. Parcell’s apparent conclusion that PECO’s ring-fencing**  
9 **efforts have been insufficient?**

10 A. No. On the contrary, PECO conducts its businesses and operates under a governance  
11 model and other arrangements and procedures (commonly referred to as “ring-  
12 fencing” measures) intended to assure that PECO is treated as a separate, independent  
13 company, distinct from Exelon subsidiaries in the event of financial difficulty at  
14 Exelon or another Exelon subsidiary. PECO has implemented numerous robust ring-  
15 fencing protections over the past decade. Ring-fencing is designed to insulate one  
16 member of a corporate family from credit and other risks of other members of the  
17 same corporate family. PECO implemented significant ring-fencing commitments in  
18 2000, in the PECO/Unicom merger proceeding at Docket No. A-110550F0147 –  
19 which was the first time that PECO was a member of a larger corporate family, and  
20 therefore for the first time in a situation in which ring-fencing was warranted. Those  
21 early commitments were extensive and were voluntarily entered into by PECO in  
22 settlement with other parties, including the OCA.

1 Moreover, as I discussed in my supplemental testimony (PECO Statement No. 2-S),  
2 PECO has continued its commitment to, and indeed an expansion of, its ring-fencing  
3 measures over time. When PECO proposed to merge with NRG in 2008, it again  
4 recommitted to and proposed to expand its ring-fencing measures. Even though this  
5 transaction did not occur, PECO largely implemented, on a voluntary basis, the ring-  
6 fencing measures that it had proposed.

7 This commitment to enacting effective ring-fencing measures continues today. For  
8 example, PECO's outside counsel has prepared and issued a non-consolidation  
9 opinion – that is, an opinion of legal counsel that, based on PECO's existing ring-  
10 fencing measures, regulatory structure and other factors, in the event of a bankruptcy  
11 by Exelon, a bankruptcy court would not order that PECO's assets and liabilities be  
12 “substantially consolidated” into Exelon's bankruptcy proceeding. Such a legal  
13 opinion is an important step toward demonstrating to the investment community that  
14 effective separation is in place.

15 **44. Q. Please address the Standard & Poor's statement.**

16 A. First, I need to point out that PECO cannot speak for the credit rating agencies. We  
17 do not believe S&P's credit rating to be the sole driver of PECO's cost of capital.  
18 PECO's first mortgage bonds are also rated by Fitch and Moody's who, unlike S&P,  
19 rate PECO's first mortgage bonds using a bottom's-up approach that does not place as  
20 much weight on the creditworthiness of Exelon's other subsidiaries. Moody's has  
21 rated PECO's first mortgage bonds at A2, and Fitch at A, while S&P has rated  
22 PECO's first mortgage bonds at A-. Fixed-income investors will review all three

1 credit ratings associated with PECO's first mortgage bonds, among other factors,  
2 when considering the price at which to purchase the bonds. Similarly, PECO's  
3 unsecured credit facility is priced using the average of PECO's unsecured credit  
4 ratings from S&P, Fitch and Moody's. In addition to these credit ratings, PECO's cost  
5 of capital is also impacted by the type of debt issued and prevailing market conditions  
6 at the time of issuance. PECO issues first mortgage bonds, which are secured by  
7 PECO's assets, allowing for cheaper cost of capital as compared to unsecured debt.  
8 PECO has various sources of liquidity including the ability to issue  
9 commercial paper, draw on its credit facility and issue long-term bonds. PECO  
10 leverages each of those sources of liquidity to ensure a cost-effective capital structure.

11 Ultimately, the question of whether PECO's management has been effective in  
12 managing this portion of its business should be determined in part by looking at the  
13 analysis of the full array of rating agency outcomes, but perhaps more importantly by  
14 looking at the bond market's reaction to PECO's overall financial management and  
15 risk profile. Generally, the market's view of a company's creditworthiness is implied  
16 in the price which investors are willing to pay for the bonds of that company, and on  
17 that basis it appears that the market views PECO's risk profile favorably. Indeed, as  
18 demonstrated in the attached Schedule H, PECO's first mortgage bonds have priced  
19 comparably with those of A rated utility companies. Schedule H shows the yields  
20 and spreads (i.e., the amount by which a corporate bond's yield exceeds a U.S.  
21 Treasury yield of comparable maturity) on PECO first mortgage bonds, as traded in  
22 the secondary market, as compared to the yields and spreads of first mortgage bonds  
23 for A-rated utility companies. The trading performance of bond yields and spreads in

1 the secondary market is a strong indicator of investor sentiment analogous to a  
2 company's stock price performance. As such, the data suggest that when fixed-  
3 income investors consider all of the factors relevant to PECO's risk profile, including  
4 S&P's assessment, they tend to conclude that PECO's creditworthiness is in line with  
5 that of A rated utilities – and they are willing to pay accordingly to own PECO's first  
6 mortgage bonds.

7 **45. Q. Are there any other factors that should be considered with respect to the**  
8 **sufficiency of PECO's ring-fencing efforts?**

9 Yes. It's well-known that, for the past several years, there has been a financial crisis  
10 triggered by a liquidity shortfall in the United States banking system. Throughout  
11 this period, PECO has maintained strong credit metrics. These metrics, coupled with  
12 PECO's ongoing ability to issue commercial paper and draw on its corporate credit  
13 facility, have enabled PECO access to liquidity throughout this period and allowed  
14 PECO to continue operations without any significant additional "crisis-driven" costs.  
15 Another recent accomplishment involves its recently-negotiated \$200 million "Smart  
16 Meter Smart Grid" stimulus grant from the Department of Energy (DOE). When the  
17 grant was originally awarded to PECO, it was unclear whether the funds to be  
18 received from the DOE would be subject to federal income tax. In addition, DOE  
19 regulations do not allow any lien or encumbrance to be put on equipment or real  
20 property purchased with grant money without the prior consent of the DOE. Since  
21 PECO's Mortgage, under which PECO has \$2.25 billion of outstanding first  
22 mortgage bonds, constitutes a first lien in favor of PECO's bondholders on

1 substantially all of PECO's assets, including after-acquired property, the lien consent  
2 requirement was a significant issue for PECO. Absent DOE authorization for an  
3 encumbrance of the applicable property, a consent solicitation of all of PECO's first  
4 mortgage bondholders would have been required to accept the DOE agreement  
5 without modification. Both of these factors would have decreased the long-term  
6 value of the \$200 million stimulus grant to PECO's customers. To avoid those  
7 adverse effects, PECO management collaborated with other stakeholders in seeking  
8 and obtaining confirmation from the IRS and DOE that the stimulus grant money  
9 would not be subject to federal income tax. PECO also successfully obtained consent  
10 from DOE for the encumbrance under the PECO Mortgage of equipment or real  
11 property purchased with grant money. Non-taxable status means that approximately  
12 \$80 million in federal income taxes will not have to be paid upon receipt of the  
13 stimulus grant funds. Obtaining DOE's consent for the encumbrance of property  
14 purchased with grant funds allowed PECO to avoid approximately \$14-17 million of  
15 costs that would otherwise have been incurred to obtain such consents through the  
16 more formal and costly First Mortgage Bond consent solicitation process. Overall,  
17 these accomplishments reflect the fact that PECO management is successfully taking  
18 steps to make sure that the \$200 million stimulus grant has the greatest available  
19 value for our customers.

## 20 X. CONCLUSION

21 **46. Q. Does that conclude your rebuttal testimony?**

22 A. Yes, it does.



## Schedule A

Pennsylvania Public Utility Commission  
v.  
PECO Energy Company –Electric Division  
Docket No. R-2010-2161575

Responses of PECO Energy Company  
To the Interrogatories of the Office of Trial Staff

### **OTS-RS-29-D:**

Explain why changing the 2010 projected Gross Metropolitan Product from negative 0.3% to positive 0.6% caused Other Operating Revenue to decrease by 58%, from \$16,431,000 in the original filing to \$6,866,000 as shown on the Company's response to OTS-RS-28 (b), Schedule A-1, line 14.

### **Response:**

The Other Operating Revenue in the Company's response to OTS-RE-28 (b), Schedule A-1, line 14 should be the same as the Company's original filing of \$16,431,000. The Act 129 Energy Efficiency programs related costs and revenues were not treated consistently in the Company's response to OTS-RS-28.

Refer to Attachment OTS-RS-29(a) for the updated Exhibit ABC-13 – revenue at present and proposed rates after applying the positive Gross Metro Product and increase in Large C&I sales.

Refer to Attachment OTS-RS-29(b) for the updated Exhibit RLO-1 after applying the positive Gross Metro Product and increase in Large C&I sales.

**Responsible Witness:** Phillip S. Barnett



## Schedule B

OTS Exhibit NO. 3  
Schedule 8PECO Energy Company  
R-2010-2161575Revised OTS Act 129 Adjustment  
(Reference PECO Ex. RLO-1, Sch. D-5E)

Description	2010 Revenue Loss	2010-2011 Revenue Loss	2010-2011 Revenue Loss Over Budget	Recovery of 10-11 Revenue Loss	Total Revenue Loss Adjustment
(A)	(B)	(C)	(D)	(E)	(F)
<b>Revenue Impact in 2010 -- Included in Test Year Budget</b>					
1 ---Residential	\$ (14,359)				
2 ---Residential Heating	(2,370)				
3 ---Small C & I	(1,148)				
4 --- Large C & I	(1,592)				
5 Total	\$ (19,469)	\$ -	\$ -	\$ -	
<b>Target Revenue Impact in 2011</b>					
6 ---Residential		\$ (23,789)			
7 ---Residential Heating		(4,272)			
8 ---Small C & I		(2,652)			
9 --- Large C & I		(4,434)			
10 Total	\$ -	\$ (35,147)	\$ -	\$ -	
<b>Incremental Revenue Impact over 2010 Budget</b>					
11 ---Residential			\$ (9,430)		
12 ---Residential Heating			(1,902)		
13 ---Small C & I			(1,504)		
14 --- Large C & I			(2,842)		
15 Total	\$ -	\$ -	\$ (15,678)	\$ -	
<b>Target Revenue Impact in 2012</b>					
16 ---Residential		\$ (31,492)			
17 ---Residential Heating		(5,835)			
18 ---Small C & I		(3,393)			
19 --- Large C & I		(6,677)			
20 Total	\$ -	\$ (47,397)	\$ -	\$ -	
<b>Incremental Revenue Impact over 2010 Budget per OTS</b>					
21 ---Residential					
22 ---Residential Heating					
23 ---Small C & I					
24 --- Large C & I					
25 Total	\$ -	\$ -	\$ -	\$ -	
<b>Recovery of 2010 Revenue Loss</b>					
26 ---Residential	\$ (7,180)				
27 ---Residential Heating	(1,185)				
28 ---Small C & I	(574)				
29 --- Large C & I	(796)				
30 Total	\$ (9,735)	\$ -	\$ -	\$ -	
<b>Recovery of 2011 Revenue Loss</b>					
31 ---Residential				\$ (9,430)	
32 ---Residential Heating				(1,902)	
33 ---Small C & I				(1,504)	
34 --- Large C & I				(2,842)	
35 Total	\$ -	\$ -	\$ -	\$ (15,678)	
<b>Recovery of 2010 and 2011 Revenue Loss</b>					
36 ---Residential					\$ (16,610)
37 ---Residential Heating					(3,087)
38 ---Small C & I					(2,076)
39 --- Large C & I					(3,636)
40 Total	\$ -	\$ -	\$ -	\$ -	\$ (25,413)



## Schedule C

(in GWh)

**Actual Act 129 Reduction to Sales by Month \***

	Jan-10	Feb-10	Mar-10	Apr-10	May-10	YTD-May
Residential	(22)	(19)	(16)	(5)	(26)	(90)
C&I	-	-	-	-	(27)	(27)
<b>Total</b>	<b>(22)</b>	<b>(19)</b>	<b>(16)</b>	<b>(5)</b>	<b>(53)</b>	<b>(116)</b>
Percentage Reduction vs. 2009 Actual 37,755	0.059%	0.051%	0.043%	0.014%	0.140%	0.308%

**Act 129 Reduction to Sales by Month in 2010 Budget**

	Jan-10	Feb-10	Mar-10	Apr-10	May-10	YTD-May
Residential	(8)	(8)	(24)	(24)	(24)	(89)
C&I	(2)	(2)	(7)	(7)	(7)	(24)
<b>Total</b>	<b>(10)</b>	<b>(10)</b>	<b>(31)</b>	<b>(31)</b>	<b>(31)</b>	<b>(113)</b>
Percentage Reduction vs. 2009 Actual 37,755	0.027%	0.027%	0.082%	0.082%	0.082%	0.300%

\* Actual savings calculated based on approved Act 129 plan.



# Schedule D

PECO ENERGY COMPANY - ELECTRIC OPERATIONS  
Act 129 Reduction to Sales Split Between Residential and C&I  
(in GWh, except %)

Based on the Approved Act 129 Plan		PY 2010		PY 2011		PY 2012	
		Jun 10-May 11	Jun 11-May 12	Jun 11-May 12	Jun 12-May 13		
1	CFL Initiative	162	252	290			
2	Residential lower-income energy	22	49	80			
3	Residential whole home performance	1	2	6			
4	Residential home energy incentives	45	85	126			
5	Residential new construction	0	1	1			
6	Residential appliance pickup	30	52	75			
7	Commercial/industrial equipment incentives	115	199	283			
8	Commercial/industrial new construction	-	9	25			
9	Government/public facility energy savings	69	128	187			
10	Residential direct load control	3	4	6			
11	Residential super peak TOU	-	0	1			
12	Commercial/industrial direct load control	1	2	3			
13	Commercial/industrial super peak TOU	-	1	1			
14	DR Aggregator Contracts	5	10	15			
15	Distributed Energy Resources	16	27	39			
16	Permanent load reduction	6	18	29			
17	Conservation Voltage Reduction	110	110	110			
<b>Total Reduction to Sales</b>		<b>584</b>	<b>949</b>	<b>1,275</b>			

	Actual *	PY 2010		PY 2011		PY 2012	
		Jan-May 10	Jun 10-May 11	Jun 11-May 12	Jun 12-May 13		
Residential	90	263	447	584			
C&I	27	184	338	498			
COMB	-	137	165	193			
<b>Total</b>	<b>116</b>	<b>584</b>	<b>949</b>	<b>1,275</b>			
Residential	77%	59%	57%	54%			
C&I	23%	41%	43%	46%			
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>			

Estimated Calendar Year Split Between Residential and C&I		2010	2011	2012
Residential		68%	58%	55%
C&I		32%	42%	45%
<b>Total</b>		<b>100%</b>	<b>100%</b>	<b>100%</b>

\* Actual savings calculated based on approved Act 129 plan.



Schedule E

PECO ENERGY COMPANY - ELECTRIC OPERATIONS  
ACT 129 REDUCTIONS TO SALES

2009 Weather Normalized Sales - R, RH, SCI and LCI OCA-IX-2 37,755 GWh  
 Monthly Incremental reduction June 2010 - May 2011 (PY 2010) 0.2184%  
 Monthly Incremental reduction June 2011 - May 2013 (PY 2011 and 2012) 0.0346%

	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]	
	<b>Calendar Year</b>				<b>Program Year</b>				
	<b>Month</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>Month</b>	<b>2010 (Jun 10 - May 11)</b>	<b>2011 (Jun 11 - May 12)</b>	<b>2012 (Jun 12 - May 13)</b>
1									
2	<b>January</b>	0.059%	1.871%	3.014%	3.429%	<b>1</b>	0.357%	2.771%	3.187%
3	<b>February</b>	0.051%	2.088%	3.048%	3.464%	<b>2</b>	0.573%	2.806%	3.221%
4	<b>March</b>	0.043%	2.304%	3.083%	3.498%	<b>3</b>	0.790%	2.841%	3.256%
5	<b>April</b>	0.014%	2.520%	3.117%	3.533%	<b>4</b>	1.006%	2.875%	3.291%
6	<b>May</b>	0.140%	2.737%	3.152%	3.567%	<b>5</b>	1.222%	2.910%	3.325%
7	<b>June</b>	0.357%	2.771%	3.187%		<b>6</b>	1.439%	2.944%	3.360%
8	<b>July</b>	0.573%	2.806%	3.221%		<b>7</b>	1.655%	2.979%	3.394%
9	<b>August</b>	0.790%	2.841%	3.256%		<b>8</b>	1.871%	3.014%	3.429%
10	<b>September</b>	1.006%	2.875%	3.291%		<b>9</b>	2.088%	3.048%	3.464%
11	<b>October</b>	1.222%	2.910%	3.325%		<b>10</b>	2.304%	3.083%	3.498%
12	<b>November</b>	1.439%	2.944%	3.360%		<b>11</b>	2.520%	3.117%	3.533%
13	<b>December</b>	1.655%	2.979%	3.394%		<b>12</b>	2.737%	3.152%	3.567%
14									
15	<b>Average</b>	0.612%	2.637%	3.204%		<b>Average</b>	1.547%	2.962%	3.377%
16	<b>Consumption Reduction (GWh)</b>	<b>231</b>	<b>996</b>	<b>1,210</b>			<b>584</b>	<b>1,118</b>	<b>1,275</b>
17	<b>Total Act 129 Reduction Allocation Percentage</b>						<b>2011</b>	<b>2012</b>	
18	Residential						58%	55%	
19	C&I						42%	45%	
20	<b>Total Act 129 Reduction (GWh)</b>						<b>2011</b>	<b>2012</b>	<b>Average 2011-2012</b>
21	Residential						576	671	624
22	C&I						419	539	479
23	Total						<b>996</b>	<b>1,210</b>	<b>1,103</b>
24	<b>2009 Weather Normalized Sales for Residential and C&amp;I (GWh)</b>						<b>2009</b>		
25	Residential						13,230		
26	C&I						24,526		
27	Total						37,756		
28	<b>Act 129 Sales Reduction Percentage from 2009</b>						<b>2011</b>	<b>2012</b>	<b>Average 2011-2012</b>
29	Residential						4.356%	5.073%	4.714%
30	C&I						1.710%	2.196%	1.953%



Schedule F

PECO ENERGY COMPANY - ELECTRIC OPERATIONS  
OPERATING REVENUE  
(\$000)

		Revised Effron's Schedule C-1 with actual Jan-May 2010 and Approved Act 129 Plan with PaPUC				Total	Effron's Schedule C-1
		RES	RES-H	C&I Small	C&I Large		
2009 Actual Revenues	(1)	563,026	97,739	161,199	144,658	966,622	966,622
Weather Normalization	(2)	15,874	2,293	2,251	1,156	21,574	21,574
2009 Weather Normalized Revenues		578,900	100,032	163,450	145,814	988,196	988,196
Customer Charge Revenue	(3)	83,705	10,149	22,626	11,154	127,634	127,634
Normalized Distrib. Charge Revenues		495,195	89,883	140,824	134,660	860,562	860,562
2010 Forecasted Revenues	(4)	628,254	111,034	187,316	164,857	1,091,461	1,091,461
Energy Efficiency	(5)	34,654	8,495	22,668	26,946	92,763	92,763
Smart Meter	(6)	22,113	2,709	2,814	54	27,690	27,690
2010 Net Distribution Revenues		571,487	99,830	161,834	137,857	971,008	971,008
Eliminate Recovery of PECO Estimated 2010 129 Load Reduction					(7)	\$ 9,735	\$ 9,735
Adjust 2010 FTY Revenues to 2009 Weather Normalized Revenues					(8)	\$ 17,188	\$ 17,188
Recognize Effect of Act 129 on 2010 FTY Distribution Revenue					(9)	(1,746)	(1,746)
Net Adjustment to Forecasted 2010 Revenues						\$ 15,442	\$ 15,442
Modify Prospective Effect of Act 129					(10)	(11,160)	7,210
Total Revenue Adjustment						\$ 14,017	\$ 32,386

Sources:

- (1) Exhibit RLO-2, Schedule D-5B
- (2) Exhibit RLO-2, Schedule D-5
- (3) Exhibit ABC-13
- (4) Exhibit RLO-1, Schedule D-5B
- (5) Exhibit RLO-1, Schedule D-5F
- (6) Exhibit RLO-1, Schedule D-5G
- (7) Exhibit RLO-1, Schedule D-5E
- (8) 2009 Weather Normalized Revenues - 2010 2010 Net Distribution Revenues
- (9) Normalized Distribution Charge Revenues \* (2010 Avg. Act 129 Effect, Sch C.1.)

	RES	RES-H	C&I Small	C&I Large	Total	
Normalized Distribution Charge Revenues	495,195	89,883	140,824	134,660	860,562	860,562
2011/2012 Avg. Act 129 Effect, Sch C.1.1	4.714%	4.714%	1.953%	1.953%		1.696%
Act 129 Effect - Average 2011-2012	23,345	4,237	2,750	2,630	32,963	14,593
PECO Estimated 2011 - 2012 Estimated load Reduction					21,803	21,803
Adjustment to Company Position					(11,160)	7,210



**Schedule G**

<b>Count of Open Positions as of June 30, 2010 (Electric Portion)*:</b>		Exempt	Craft	Total
<b>Status</b>	<b>Job Title:</b>	<b>Electric Total</b>	<b>Electric Total</b>	<b>Electric Total</b>
Interviewing	Business Analyst	0.8	0.0	0.8
	Dist Sys Dispatcher I - PECO	1.7	0.0	1.7
	Engineer	1.0	0.0	1.0
	Mgr Customer Care	0.8	0.0	0.8
	Principal Analyst	0.7	0.0	0.7
	Sr Business Analyst	0.8	0.0	0.8
	Sr Business Project Manager	0.8	0.0	0.8
	Sr Dist Sys Dispatcher - PECO	0.9	0.0	0.9
	Sr Emerg Prep Administrator	0.9	0.0	0.9
	Revenue Protection Technician	0.0	0.8	0.8
<b>Interviewing Total</b>		<b>8.4</b>	<b>0.8</b>	<b>9.2</b>
<b>Interviews Complete</b>	<b>Prin Reg &amp; Rates Specialist</b>	<b>1.5</b>	<b>0.0</b>	<b>1.5</b>
<b>Interviews Complete Total</b>		<b>1.5</b>	<b>0.0</b>	<b>1.5</b>
Offer Extended	Engineer	1.8	0.0	1.8
	Real Estate Specialist	0.8	0.0	0.8
	Sr Business Analyst	0.8	0.0	0.8
<b>Offer Extended Total</b>		<b>3.5</b>	<b>0.0</b>	<b>3.5</b>
Offer Pending	Senior Project Eval Analyst	0.8	0.0	0.8
	Customer Consultant	0.0	3.9	3.9
<b>Offer Pending Total</b>		<b>0.8</b>	<b>3.9</b>	<b>4.7</b>
Offered & Accepted	Mgr Work Management	1.0	0.0	1.0
	Work Planner	3.1	0.0	3.1
<b>Offered &amp; Accepted Total</b>		<b>4.1</b>	<b>0.0</b>	<b>4.1</b>
Offered as E04	Sr Communications Specialist	0.7	0.0	0.7
<b>Offered as E04 Total</b>		<b>0.7</b>	<b>0.0</b>	<b>0.7</b>
Posted	Assistant General Counsel	0.7	0.0	0.7
	Financial Analyst	0.7	0.0	0.7
	Mgr Const & Maint	1.0	0.0	1.0
	Mgr Fleet Ops	0.8	0.0	0.8
	Sr Engineer	1.0	0.0	1.0
<b>Posted Total</b>		<b>4.3</b>	<b>0.0</b>	<b>4.3</b>
<b>Grand Total</b>		<b>23.3</b>	<b>4.7</b>	<b>28.0</b>

\* The Electric portion is determine by multiplying the percentage of electric base payroll dollars (electric/total) to the headcount.

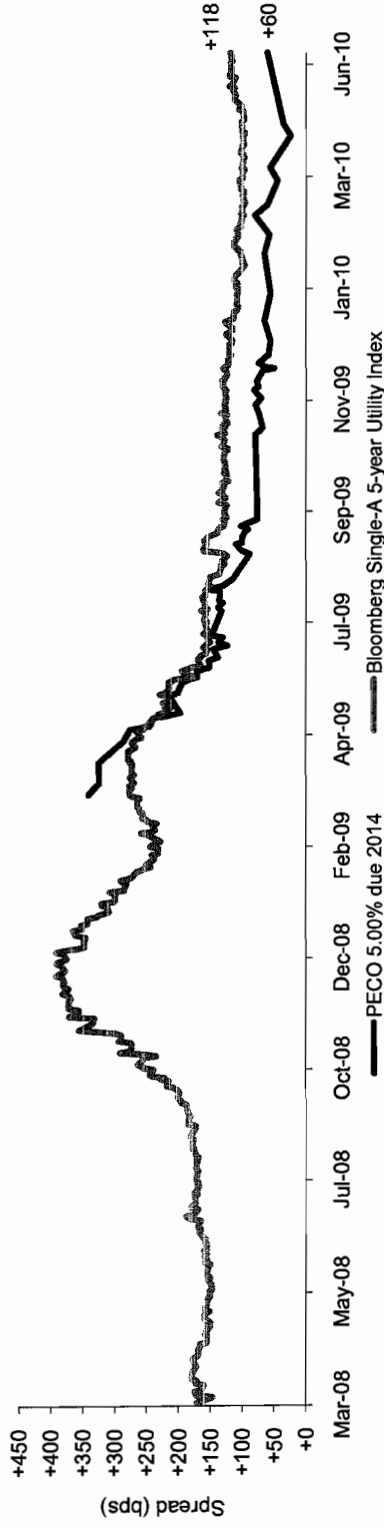


# PECO Energy Company

## Historical spreads and yields for Notes due 2014

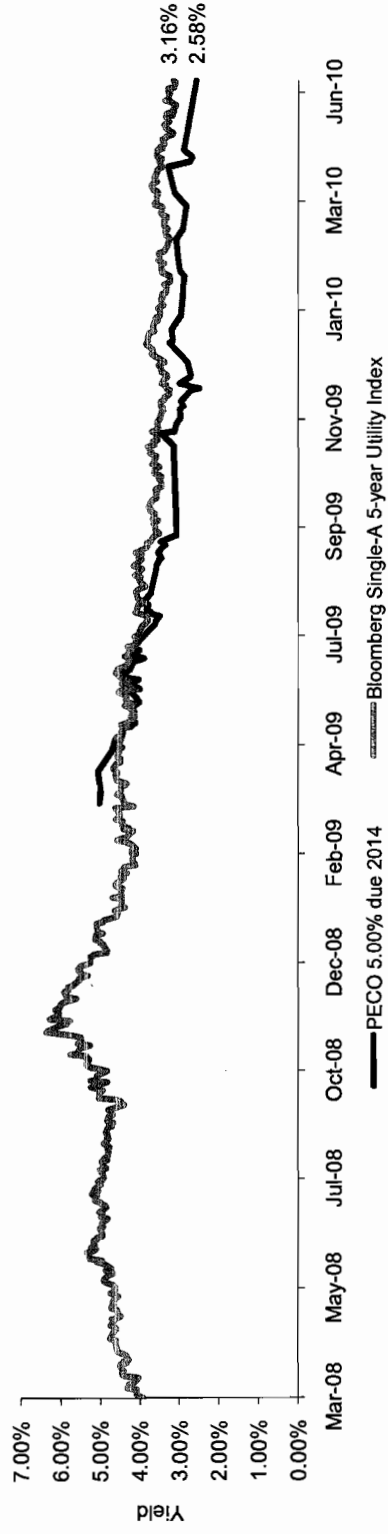
PECO's bonds have largely moved in line with the Bloomberg single-A utility index

PECO spread performance: 5.00% Notes due 2014



Source: MarketAxess, Bloomberg, Deutsche Bank

PECO yield performance: 5.00% Notes due 2014



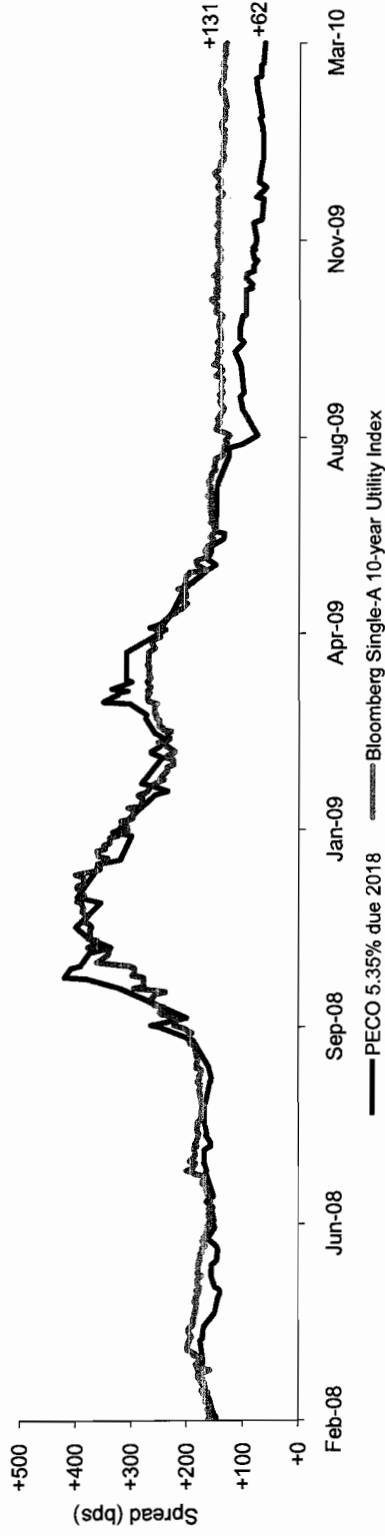
Source: MarketAxess, Bloomberg, Deutsche Bank

# PECO Energy Company

## Historical spreads for Notes due 2018 and 2036

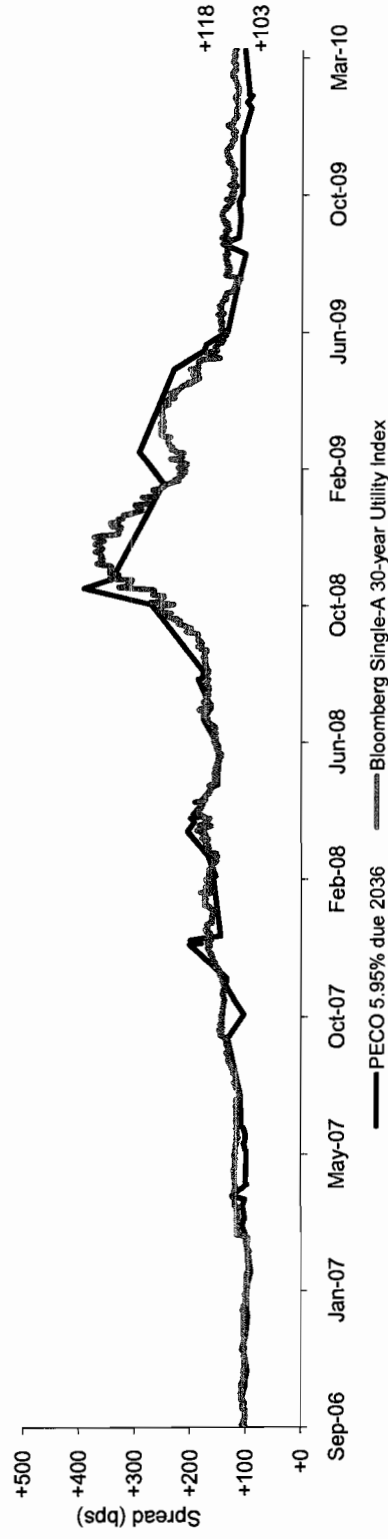
PECO's bonds have largely moved in line with the Bloomberg single-A utility index

PECO spread performance: 5.35% Notes due 2018



Source: MarketAxess, Bloomberg, Deutsche Bank

PECO spread performance: 5.95% Notes due 2036



Source: MarketAxess, Bloomberg, Deutsche Bank