PECO ENERGY COMPANY
STATEMENT NO. 2

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION
v.
PECO ENERGY COMPANY – ELECTRIC DIVISION

DOCKET NO. R-2021-3024601

DIRECT TESTIMONY

WITNESS: ROBERT J. STEFANI

SUBJECT: EXPLAINING PECO'S NEED FOR RATE RELIEF; DISCUSSING PECO'S EFFORTS TO CONTROL OPERATING AND MAINTENANCE COSTS; PROVIDING AN OVERVIEW OF PECO'S PRINCIPAL ACCOUNTING EXHIBITS AND BUDGETING PROCESS; DESCRIBING PECO'S SALES FORECAST; DESCRIBING THE NATURE AND LOCATION OF THE COST OF SERVICES THAT PECO RECEIVES FROM THE EXELON BUSINESS SERVICES COMPANY; AND DESCRIBING PECO'S INCREMENTAL COSTS AND LOST REVENUES RELATED TO THE COVID-19 PANDEMIC

DATED: MARCH 30, 2021

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DIRECT TESTIMONY
OF
ROBERT J. STEFANI

I. INTRODUCTION AND PURPOSE OF TESTIMONY

1. Q. Please state your name and business address.

A. My name is Robert J. Stefani. My business address is 2301 Market Street, Philadelphia, PA 19103.

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

A. I am employed by PECO Energy Company ("PECO" or the "Company") as Senior Vice President, Chief Financial Officer and Treasurer. In that capacity, I am responsible for PECO's financial function, including budgeting, long range financial planning, financial analysis and reporting, project evaluation, and financings. In addition, I have oversight and coordination responsibilities for PECO's accounting, tax, treasury, investor relations, and risk management activities, and I monitor the Company's financial performance to ensure that PECO complies with its financial internal controls and management discipline.

3. Q. Please briefly describe your educational background and professional experience.

A. I received a bachelor's degree in accounting from the University of Notre Dame and an MBA from the University of Texas at Austin. Prior to joining PECO, I was Vice President of Corporate Development at Exelon, responsible for identification and execution of merger, acquisition, and divestiture opportunities.

Before joining Exelon, I led strategic investments in North America, Europe, and South Africa for Caterpillar's Corporate Development Group. Prior to my work at Caterpillar, I was an investment banker at Citigroup and then Marathon Capital where I provided strategic and capital markets advisory services to major corporations. I also previously served as an Officer in the United States Navy and was on active duty from 1996 to 2003.

4. Q. What is the purpose of your direct testimony?

A. The purpose of my direct testimony is to: (1) briefly explain PECO's need for rate relief; (2) to summarize PECO's efforts to control operating and maintenance ("O&M") costs since its last approved base rate increase in 2018; (3) provide an overview of PECO's principal accounting exhibits, as well as its budgeting process; (4) describe the Company's electric sales forecast; (5) describe the nature and allocation of costs for services that PECO receives from the Exelon Business Services Company ("EBSC"); and (6) provide an overview of the incremental costs incurred by the Company, its uncollectible accounts expense, and lost revenues related to the COVID-19 pandemic.

II. PECO'S NEED FOR RATE RELIEF

5. Q. Why is PECO seeking a rate increase at this time?

A. As explained by Mr. John E. McDonald in his testimony (PECO Statement No. 1), PECO last requested a base rate increase for its electric operations approximately three years ago. Since the Company's current base rates became effective on January 1, 2019, PECO has invested approximately $1.5 billion in new and replacement electric distribution plant and is planning to invest an additional $1.6 billion in new and replacement electric distribution plant in between January 1, 2021 and December 31, 2022. During 2019, deliveries of electricity to the Company's customers were comprised of approximately 36% to residential customers, approximately 21% to commercial customers, approximately 40% to industrial customers, and approximately 2% to street lighting, railroads, and sales for resale. As explained by Mr. McDonald, the projected expenditures are designed to maintain and/or enhance the safety and reliability of our backbone electric delivery system to these customers, strengthen system resiliency, and maintain and/or enhance physical security and cybersecurity. During the same period, PECO has granted its employees annual wage and salary adjustments and has experienced the effects of inflation on material and contracting costs.

Despite the need to incur these increased costs to maintain reliable service for its customers, the Company experienced decreasing sales. Sales declined annually by -0.5% between January 1, 2016 and December 31, 2019. Sales also declined by -3.5% in 2020 due to the impact of the COVID-19 pandemic.[1]

Notwithstanding this decline in sales, the Company's number of customers increased by an average of 0.9% annually from 2016 through 2020. The Company expects to see load recovery from COVID-19 impacts in 2021 and 2022, leading to a slight decline in overall load growth between 2019 and 2022. This forecast

[1] The Company's load growth data is weather normalized.

mitigates the anomalous usage impacts related to COVID-19, as described in Section V of my testimony.

Between 2019 and 2022, sales are forecasted to have a compound annual growth rate ("CAGR") of -0.1% notwithstanding customer growth of 0.8%. This is a smaller decline in customer sales than the -0.5% CAGR that the Company experienced during the 2016 to 2019 period.

The decline in usage per customer is due, in significant part, to PECO's successful implementation of energy efficiency and conservation ("EE&C") mandates under Act 129 of 2008 ("Act 129"). PECO is a strong supporter of energy efficiency, and since the inception of its EE&C program in 2009, the Company's residential and commercial customers have reduced their collective energy consumption by 4,230,075 megawatt hours ("MWh"). The net effect to PECO is a continuing reduction in revenue (with potentially significant additional penalties for any failure to meet required reductions in usage by designated milestone dates). As reflected in the Company's projected load growth, PECO's current Phase III EE&C program is designed to reduce customer consumption by 1,962,659 MWh between June 1, 2016 and May 31, 2021. The Phase III program will be followed by Phase IV, which is designed to reduce customer consumption by an additional 1,380,837 MWh between June 2021 and May 2026.

Despite efforts to attract new customers and to contain expenses, the factors I described above have compromised the Company's ability to earn a fair return on its investment.

6. Q. Please elaborate.

A. Absent an increase in revenues, PECO's electric distribution operations are projected to produce an overall return on invested capital of 5.12% and an indicated return on common equity of only 6.15%, during the twelve months ending December 31, 2022. As explained by Mr. Paul R. Moul (PECO Statement No. 5), such return levels are inadequate under any reasonable standard. These return levels would deteriorate even further in 2022 and thereafter, jeopardizing PECO's ability to make investments necessary to maintain and enhance the provision of safe, reliable, and resilient service to customers. Inadequate returns would also adversely impact PECO's credit coverage ratios and its ability to maintain or improve its investment-grade credit ratings, which, in turn, would increase the Company's financing costs.

7. Q. Why is it important that PECO maintain or possibly improve its credit ratings?

A. PECO projects that it will need to invest $4.6 billion in new and replacement electric distribution plant over the next five years (2021-2025). A significant portion of these planned investments (approximately 47%) will be financed with debt and other forms of capital. PECO's capital costs are dependent, in part, on the Company's favorable credit ratings. Capital costs ultimately are borne by customers and, therefore, maintaining strong credit metrics helps to reduce customer costs.

8. Q. What steps, if any, has PECO taken to minimize its costs of borrowing?

A. PECO has taken various steps to obtain debt financing at favorable terms to the Company and its customers. The Company has utilized the public debt market, which is efficient and typically provides the best pricing for index-eligible bonds. The Company has also issued longer term debt under its mortgage, enabling the Company to obtain lower coupons compared to unsecured debt. In addition, PECO has leveraged the low interest rate environment and its strong credit rating to reduce its weighted average long-term debt rate of 4.43% in 2017 to approximately 3.93% as projected for 2022.

The Company, since its last electric rate case in 2018, successfully priced over $1 billion in bond offerings over three separate issuances. Each of the issuances lowered the Company's average cost of debt since the rate for each issuance was below the Company's weighted average cost of debt prior to the issuance.

In September 2019, PECO priced a $325,000,0000, 30-year first mortgage bond offering at a coupon rate of 3%. In June 2020, PECO successfully priced a $350,000,000, 30-year first mortgage bond offering at a spread of 135 basis points over the 30-year U.S. Treasury for an all-in coupon rate of 2.80%. The 2.80% coupon rate is 20 basis points lower than PECO's previous all-time lowest coupon rate and, at the time of issuance, was one of the lowest coupon rates ever issued in connection with a 30-year U.S. utility corporate bond. In March 2021, PECO successfully priced a $375,000,000, 30-year first mortgage bond offering at a spread of 82 basis points over the 30-year U.S. Treasury for an all-in coupon rate of 3.05%.

III. PECO'S EFFORTS TO CONTROL OPERATING AND MAINTENANCE COSTS

9. Q. Please describe PECO's efforts to control O&M expenses since its current base rates became effective on January 1, 2019.

A. The Company has taken reasonable and prudent steps to minimize its O&M expenses. When adjusted for major storms, PECO projects that the CAGR in O&M expense from 2019 through the end of the fully projected future test year ("FPFTY") ending December 31, 2022 will be 2.5%. In addition to several minor storms, PECO experienced two top-ten major storms in a single year with a Derecho storm in June 2020 and Tropical Storm Isaias in August 2020. The Company incurred total storm-related O&M expense of $115 million in 2020.

Furthermore, when the Company's projected 2019-2022 CAGR is adjusted for O&M increases related to customer reliability improvements under its Long Term Infrastructure Improvement Plan (LTIIP),[2] additional make ready work for the deployment of new technologies, and COVID related uncollectible accounts

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[2] In November 2020, the Commission approved PECO's LTIIP II plan which proposed additional capital investments totaling $1.36 billion over the period 2021 through 2025 to accelerate infrastructure improvements in order to enhance system resiliency and reliability. *See* Opinion and Order, *Petition of PECO Energy Company for Approval of its Second Long-Term Infrastructure Improvement Plan for its Electric Operations*, Docket No. P-2020-3020974 (Order entered Nov. 19, 2020).

expense, the projected CAGR in O&M decreases further to 1.4%, which is well below the expected inflation CAGR for the same period.

10. Q. What steps has the Company taken to manage its pension contribution and OPEB costs?

A. PECO actively manages its employee benefit costs by evaluating trends in benefits and identifying and implementing cost reduction measures while maintaining a competitive compensation package for its employees. As part of this effort, in 2021, the Company modified its OPEB plans for non-represented, non-craft participants. The amendments (i) eliminate eligibility for such employees who have not reached age 40 by January 1, 2021; (ii) eliminated retiree medical savings account interest credits and health reimbursement account cost of living increases for such employees who did not retire prior to February 1, 2021; and (iii) eliminated retiree life insurance benefits for such employees who have not retired prior to January 1, 2022. These plan amendments will result in a reduction to the Company's benefit obligation, which is being amortized through a prior service credit. Amortization of the prior service credit, in turn, lowers the Company's OPEB expense.[3] The Company's FPFTY OPEB expense of $1.6 million reflects the amortization of this prior service credit and associated reduction in OPEB expense.

[3] Amortization of prior service credit is a component to OPEB expense, and since the amortization is a credit (i.e., a negative expense), it lowers the Company's total OPEB expense. Conversely, when the prior service credit and associated amortization expires, the Company's OPEB expense will increase.

The Company's FPFTY OPEB expense is also impacted by the expiration in 2021 of a similar prior service credit related to retirement plan amendments that the Company adopted in 2014, which will result in an increase in the Company's FPFTY OPEB expense. In 2014, the Company modified its retirement plan design to limit the Company's exposure to increases in healthcare cost. Following the change, participants were eligible for the lesser of (i) 80% of the premium cost of a Medicare Advantage and Prescription Drug plan, or (ii) a stipend of $3,200 per year, increasing at an annual rate of 3%, that the participant could use to purchase insurance on an exchange (i.e., in the public market). The 2014 plan design change resulted in a reduction in the Company's OPEB obligation, which was being amortized through a prior service credit (similar to the 2021 plan change) over the remaining service life of the active plan participants (approximately seven years). The prior service credit resulting from the 2014 plan change is expiring in June 2021, and the expiration of the associated amortization is the primary driver behind the Company's increase in OPEB expense.[4] PECO is continuously seeking ways to implement additional cost reduction measures, such as the 2021 plan amendments discussed above, which will mitigate the financial impact from the expiration of the prior service credit resulting from the 2014 plan changes.

With respect to pension costs, the Company makes contributions to its pension trust fund, consistent with its obligations, to ensure funds will be available when

[4] The accounting report attached as PECO Exhibit RJS-1 (Confidential), prepared by the Company's independent third-party actuary, Willis Towers Watson, shows that as of January 1, 2020 the remaining amortization period associated with 2014 amendments is 1.54703 years (i.e., the amortization of the prior service credit will expire in June 2021). *See* PECO Exhibit RJS-1 (Confidential), p. 9 of 9.

needed to pay pension benefits to active and former employees. Since 2010, the Company has implemented an investment strategy that reduces volatility and supports a higher return on assets. PECO's projected pension cash contribution in 2022 is $12.2 million, which is $14.1 million lower than the Company's 2019 contribution of $26.3 million. The decrease in the Company's pension contribution and pension cost is being driven primarily by the Company's sound investment strategy and the higher investment returns earned by the Company's pension plan assets.

IV. OVERVIEW OF PECO'S PRINCIPAL ACCOUNTING EXHIBITS AND BUDGETING PROCESS

11. Q. Please provide an overview of PECO's principal accounting exhibits.

A. PECO's principal accounting exhibits are PECO Exhibits MJT-1, MJT-2, and MJT-3, which represent PECO's revenue requirement for the FPFTY, future test year ("FTY"), and historical test year ("HTY"), respectively, and which are sponsored by Mr. Michael J. Trzaska (PECO Statement No. 3). As explained by Mr. Trzaska, these exhibits are based, in part, upon data provided by other PECO witnesses. PECO Exhibit MJT-1, which presents PECO's revenue requirement for the FPFTY ending December 31, 2022, is comprised of four sections, as follows:

Section A consists of a summary schedule setting forth PECO's claimed measures of value (i.e., rate base) and the derivation of the Company's requested rate increase.

Section B contains basic accounting data from the Company's books and records, including a FPFTY-end balance sheet; statements of net utility operating income and FPFTY revenues, with the separation of Pennsylvania jurisdictional and non-jurisdictional amounts; a schedule of O&M expense items; and a calculation of PECO's taxes other than income. Also included are schedules developing PECO's embedded cost of debt, its FPFTY capital structure, and its overall claimed rate of return.

Section C provides a detailed development of the major components of the Company's rate base claim. Included therein are summaries of the original cost and accrued depreciation at the end of the FPFTY of the various categories of utility plant, including allocated common plant; and calculations of PECO's working capital, materials and supplies, accumulated deferred income taxes, customer deposits and advances, the unamortized balance of AMI reading investment related to legacy meters that are being retired and replaced with AMI and a pension-related asset.

Section D contains the detailed adjustments to place FPFTY revenues and expenses on a ratemaking basis. These adjustments are summarized on Schedules D-3 to D-17, and, together with certain tax adjustments, are carried forward to Schedule D-1 to derive PECO's pro forma operating income at present and proposed rates.

As explained by Mr. Trzaska, adjustments were made to budgeted data, where necessary, to ensure that PECO's claimed revenue, expenses and taxes are representative of the levels that the Company expects to experience on a normalized, ongoing basis, and in accordance with established Pennsylvania Public Utility Commission ("Commission") ratemaking precedent. Because PECO is basing its requested rate increase on FPFTY data, PECO Exhibit MJT-1 is key to understanding and evaluating the derivation of the Company's claimed revenue requirement. For that reason, Mr. Trzaska devotes most of his testimony to a discussion of PECO Exhibit MJT-1.

12. Q. What is contained in PECO Exhibit MJT-2?

A. PECO Exhibit MJT-2 mirrors PECO Exhibit MJT-1 in format, but presents information for the FTY ending December 31, 2021.

13. Q. What is contained in PECO Exhibit MJT-3?

A. PECO Exhibit MJT-3 mirrors PECO Exhibit MJT-1 and MJT-2 in format but presents information for the HTY ended December 31, 2020. This information is being furnished in accordance with the Commission's filing requirements and provides a basis for comparing PECO's FPFTY claims to actual historic results of operations, adjusted for rate making purposes for the HTY.

14. Q. What are the sources of the data contained in PECO Exhibits MJT-1, MJT-2, and MJT-3?

A. The base data set forth in PECO Exhibits MJT-1 and MJT-2 were derived, for the most part, from PECO's 2021 and 2022 capital and operating budgets, respectively, while the corresponding base data in PECO Exhibit MJT-3 were taken from PECO's 2020 books and records.

15. Q. Please briefly describe PECO's budgeting process.

A. One of the key goals of the annual planning process is to integrate and align PECO's operational, regulatory, and financial plans. The operational plan includes goals focused on achieving best in class safety performance at top decile and first quartile performance for both reliability and customer satisfaction, as explained in Mr. McDonald's testimony. The operational plan is also consistent with statutory and Commission-imposed regulatory requirements. The Company sets spending targets in its financial plan to achieve its operational goals and comply with such regulatory requirements. As I explained earlier, the Company attempts to minimize its O&M expenses to the extent possible, and has generally been successful in controlling these expenses at a lower CAGR than the rate of inflation.

The planning process starts with a review and update of PECO's operational and regulatory goals and initiatives to determine if changes are required for the future. Any significant changes in such goals and initiatives are taken into consideration when updating the Company's financial Long Range Plan ("LRP"). The LRP consists of a five-year outlook and is updated with key assumptions (e.g., inflation rates, interest rates) and with detailed input provided by "responsibility areas" (e.g., Electric Operations and Customer Operations). Each responsibility area reviews its historic expense levels, current and anticipated employee staffing levels, performance assessments, regulatory requirements, operational goals, specific projects, and other factors and develops a responsibility area-specific LRP. The individual "responsibility area" LRPs are typically submitted to finance in June of each year and are carefully analyzed for consistency, completeness, and appropriateness. The responsibility area LRPs are then consolidated into a single LRP and delivered to PECO's senior management (i.e., the Chief Executive Officer, Chief Operating Officer, and Chief Financial Officer) for review and approval in September.

Once that LRP has been updated and approved, its data is thoroughly scrutinized to formulate a detailed two-year budget. The two-year budget is "built up" by "responsibility area," similar to the LRP process described above. The Company then develops its financing plan to ensure PECO can maintain investment grade credit ratings. Based on that plan, PECO determines the amount it can borrow to fund its spending plans and the dividend levels that will achieve its targeted capital structure. The consolidated budget is then submitted to PECO senior management for review and approval. The Board reviews and approves the Company's capital, O&M, and financing plan annually.

16. Q. Is that the end of the process?

A. No. Although the budget, as approved, remains in place throughout the year and is not formally amended, it is reviewed and updated on a monthly basis to reflect estimates derived from the Company's latest data. Actual results are then compared to both the original budget and the latest estimates. Any significant variances are thoroughly investigated to determine why the Company's actuals have departed from its estimated budget, and actions are taken as appropriate.

17. Q. Has PECO's budgeting process been reviewed by the Commission?

A. Yes. PECO's budgeting process was reviewed by the Commission during its Focused Management and Operations Audit of PECO in 2014 ("2014 Audit").[5] The Commission's auditors found no deficiencies or weaknesses in the way PECO prepares its budgets.

18. Q. Do the personnel in each of the responsibility areas develop their budget*s* by FERC account?

A. No, they do not. Instead, the responsibility area budgets are prepared on the basis of business activities (i.e., GAAP basis) and related cost elements, such as payroll, employee benefits, outside services, etc.

19. Q. Schedules B-2, B-3, and B-4 of PECO Exhibit MJT-1 present the 2022 budgeted data on a FERC account basis. How were those figures derived?

A. As Mr. Trzaska describes more fully in his testimony, he analyzed the recorded 2020 FERC account balances to determine their composition (e.g., payroll, benefits, rent) and then distributed the 2022 budgeted cost elements based on his findings. The results of Mr. Trzaska's proposed distribution of costs were then reviewed and confirmed with members of my staff.

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[5] *See* Focused Management and Operations Audit of PECO Energy Company, Docket No. D-2013-2370921 (issued September 2014).

20. Q. Do PECO Exhibits MJT-1, MJT-2, and MJT-3 contain all of the data needed to evaluate PECO's claimed revenue requirement?

A. No. While PECO Exhibits MJT-1, MJT-2, and MJT-3 present, in considerable detail, PECO's rate base, revenue, expense, and tax claims, much of the supporting data are provided in the separately-bound volumes comprising the Company's responses to the Commission's standard rate case filing requirements at 52 Pa. Code §§ 53.53, 53.62, and 53.64 and supplemental data requests issued by the Commission's staff. I note that, consistent with the approach to develop responsibility area budgets on the basis of business activities (GAAP basis) as described above, many of the Company's responses to the standard filing requirements and supplemental data request that accompany this rate filing were prepared on the basis of business activities (GAAP basis). As a result, there may be differences between those responses and figures in MJT-1, MJT-2, and MJT-3, which were prepared on a FERC account basis.

In addition, other PECO witnesses are sponsoring testimony and specific exhibits in the areas of depreciation (Ms. Caroline Fulginiti, PECO Statement No. 4), and rate of return (Mr. Paul R. Moul, PECO Statement No. 5).

21. Q. Are there any differences between the Company's capital budgeting process and its procedures for determining plant additions for purposes of determining rate base?

A. Yes. With respect to capital budgeting, the Company accounts for capital expenditures in the period when such expenditures are made. The Company determines plant additions based upon when plant will be placed into service – this can differ from the period in which capital spending occurs. PECO only included in its claimed rate base the plant that will actually be in service during the FPFTY. The larger projects with which that plant is associated for PECO's budgeting purposes may, however, show an overall project completion date that is beyond the end of the FPFTY. That does not change the fact that the plant actually claimed in rate base by PECO in this case will be completed and used and useful during the FPFTY.

22. Q. In Paragraph 19 of the Joint Petition for Partial Settlement of PECO's 2018 electric base rate case, PECO agreed that it would provide comparisons of its actual expenditures, expenses, and rate base additions for the twelve months ended December 31, 2019 to the projections made in its 2018 base rate case. Has PECO provided these comparisons?

A. Yes. First, on March 26, 2020, PECO provided the Commission's Bureau of Technical Utility Services ("TUS"), the Commission's Bureau of Investigation and Enforcement ("I&E"), the Office of Consumer Advocate ("OCA"), and the Office of Small Business Advocate ("OSBA") with an update on its electric division's actual capital expenditures, plant additions, and plant retirements by month for the twelve months ending December 31, 2019. A copy of the filing is attached as Exhibit RJS-2.

As described therein, the Company's actual capital expenditures, capital additions, and retirements were greater than its projections in the 2018 electric base rate proceeding.

With respect to O&M expense, PECO spent $588.8 million in 2019 in comparison to the 2019 budget of $573.6 million in the 2018 base rate case. The variance is primarily due to the impact of minor storms in 2019 compared to the five-year historical average of storm costs in 2018. The Company also experienced higher than anticipated costs related to distribution corrective maintenance and make safe work, which also contributed to the variance. Please see the Company's response to SDR-OM-1 for more detailed information.

V. ELECTRIC SALES FORECAST

23. Q. How does PECO develop its electric sales forecast, generally?

A. The electric sales forecasting process uses multiple regression-analysis models that determine the relationship between monthly electric sales and predictive variables, such as weather, economic indicators, energy efficiency, and calendar. The modeled results are evaluated using standard statistical criteria (e.g., the Adjusted R-Squared Score, Mean Absolute Percentage Error (MAPE), t-statistics, and coefficients) to ensure that there are statistically significant relationships between the dependent and independent variables.

24. Q. How does PECO utilize historical weather data in developing its electric sales forecasts?

A. PECO's electric forecasts utilize "weather normal" assumptions based on weather averages from the prior 30 years. PECO's weather normal assumptions are re-calculated annually using the latest 30-year period. The Company also utilizes weather normals to normalize historical sales results, which are leveraged to analyze usage trends over time. Out-of-Model adjustments are then made to the modeled forecasts to reflect these trends along with additional impacts of solar, electric vehicles and large customer projects. The results of the forecast are then compared to prior forecasts for consistency and reviewed with the Exelon Utilities Manager of Load Forecasting, the PECO Director of Financial Planning and Business Analysis, and other Exelon Utilities and PECO senior management for their approval.

25. Q. Has PECO accounted for the impact of COVID-19 on electric sales in the forecast?

A. Yes. The impact of COVID-19 on sales has been noticeable. 2020 weather normalized electric sales were approximately 3% lower than budget forecast primarily due to COVID-19 impacts. However, the impacts on individual customer classes varied. Residential sales were approximately 5% higher than expected due to stay-at-home orders while commercial and industrial sales (which represent a majority of the Company's overall sales), were approximately 7% lower than expected due to business closure mandates. While the partial reopening of businesses and lifting of state mandates in the early summer of 2020 produced some recovery in sales, the sharp rise in COVID-19 infections in late 2020 (and the attendant re-imposition of certain restrictions and slowdown in resumption of normal activities) is expected to stall load recovery through 2021. A full recovery is not expected until the economy is able to fully re-open and recover from lingering recessionary impacts. The Company currently anticipates this occurring sometime in the second quarter of 2022. This projection aligns with the economic forecast provided by the Company's economics vendor, IHS Markit, which advised the Company it anticipates a return to pre-recession economic levels in the second quarter of 2022. The Company forecasts that the COVID-19 impact on sales will be reduced from approximately -3% in 2020 to only -0.2% in the FPFTY. In other words, the Company expects that the COVID-19 impact to sales will taper off almost completely by the FPFTY. As I explained in my response to Question No. 5, load growth from 2019-2022 is forecasted to be relatively flat, with a CAGR of -0.1%, which represents a smaller decline in sales than the -0.5% CAGR the Company experienced bet-ween 2016 and 2019.

VI. EXELON BUSINESS SERVICES COMPANY

26. Q. Does PECO procure certain shared services from an affiliated service company?

A. Yes. Like many other energy holding company enterprises, Exelon created a service company, the EBSC, following the merger of PECO and the former Unicom Corporation, to house specific support functions that it believed could be staffed more efficiently and economically on a centralized basis.

27. Q. What types of services does the EBSC make available and to whom?

A. The EBSC is designed to provide a range of what would typically be regarded as in-house services in the case of a stand-alone utility. In broad terms, those services fall into the following categories: information technology ("IT"); supply; commercial operations; finance; human resources; government, external affairs, and public policy; legal; corporate governance; strategy; and communications. The EBSC offers its services to PECO and other affiliated members of the Exelon family of companies, including Atlantic City Electric Company, Baltimore Gas and Electric Company, Commonwealth Edison Company, Delmarva Power & Light Company, and Potomac Electric Power Company.

28. Q. Is PECO required to utilize the EBSC's services?

A. No, it is not. Under the terms of the General Services Agreement ("GSA") between PECO and the EBSC, which was approved in the PECO/Unicom merger proceeding at Docket No. A-110550F0147, PECO has the discretion to determine whether and to what extent to utilize the EBSC's services in all areas except corporate governance.

29. Q. What role does the EBSC play in PECO's electric distribution operations?

A. PECO's overall approach is to use its own personnel or independent contractors to staff the day-to-day operations of its electric delivery system, as well as its customer-service functions (e.g., call taking, billing). Other services, such as employee-benefits administration, mass purchasing, insurance, and treasury, to name a few, are provided by the EBSC.

30. Q. What is the principal advantage of the service company structure?

A. The EBSC enables PECO to realize economies of scale and scope that, in my judgment, could be very difficult to achieve on an individual company basis. Indeed, if PECO were to try to maintain comparably qualified personnel on its own payroll, the total cost PECO would incur to obtain the same level and quality of service it receives from the EBSC likely would be considerably higher.

31. Q. How does the EBSC price the services it provides to PECO?

A. The GSA provides that the services furnished by the EBSC to PECO are to be billed at the EBSC's cost. Prior to enactment of the Energy Policy Act of 2005, the Exelon utility companies were subject to the affiliate-transaction and cost-allocation rules prescribed by the Securities and Exchange Commission ("SEC") under the Public Utility Holding Company Act of 1935 ("PUHCA"), which generally mandated that service companies, such as the EBSC, offer their services to affiliates at fully distributed cost. The "at cost" rules were incorporated into the GSA, and their continued use in the provision of non-power goods and services has been approved by the FERC, which assumed some of the SEC's oversight responsibilities when PUHCA was repealed, in part, several years ago.

32. Q. How is the cost of those services determined?

A. Direct charges are made for services where possible. Otherwise, costs are allocated on the basis of the allocation factors/methodologies identified in the attachment to the GSA, which were previously reviewed and approved by the SEC. These allocations and methodologies were also reviewed as part of the Commission's 2014 Audit and the Commission's auditors found no issues with respect to PECO's allocations and methodologies.

33. Q. How does PECO satisfy itself that the services it procures from the EBSC are provided at a competitive price?

A. PECO takes several steps to ensure that the services it procures from the EBSC are provided at a competitive price. First, PECO and the management of EBSC work together to identify PECO's needs and to define service priorities and major new initiatives. As a consequence, PECO has meaningful input into the development of the EBSC's budget for the upcoming year, and PECO's Chief Financial Officer ultimately approves the service level arrangements ("SLAs"). SLAs are annual agreements between the EBSC and Exelon's operating companies (including PECO) entered into under the express authority of the Commission-approved GSA that detail the specific services that the EBSC will provide during the following year, including the scope of services, unit cost expectations and performance measures. Services are grouped by function so that budgeted and actual costs can be tracked.

Second, the EBSC's monthly billings are carefully scrutinized by PECO personnel. Variances between actual and budgeted charges are reviewed by PECO personnel with their EBSC counterparts to ensure that all costs are properly justified.

In addition, for functions that are not already outsourced, PECO obtains extensive information regarding the composition of the EBSC's costs, which PECO can then review for reasonableness. This "Market Testing Analysis," developed in conjunction with the Commission's management auditors, is a formal approach for evaluating the cost-effectiveness of using the EBSC's shared services. This analysis is performed on an annual basis, which, along with allocation factors and methodologies used for EBSC costs, was reviewed as part of the 2014 Audit. In 2017, the Commission conducted a Management Efficiency Investigation to evaluate PECO's implementation of recommendations from the 2014 Audit.[6] The Commission again examined PECO's affiliated interest and cost allocations processes and concluded that PECO (and EBSC) had taken steps to verify that "shared services are being provided in an efficient and cost-effective manner and/or improvement opportunities are identified to ensure service offerings are fair and reasonable." PECO has also worked to implement recommendations made by the Commission, including those related to its payroll and accounts

[6] *See PECO Energy Company Management Efficiency Investigation Evaluating the Implementation of Selected Management Audit Recommendations from the 2014 Focused Management and Operations Audit*, Docket No. D-2016-2562303 (August 2017).

payable systems and the sharing of benchmarking reviews between EBSC, PECO, and other Exelon companies.

34. Q. What is PECO's claim in this proceeding for EBSC services?

A. PECO has included $114.1 million in its FPFTY expense claim for charges from EBSC. A breakdown of those costs is attached as PECO Exhibit RJS-3.

35. Q. On February 24, 2021, Exelon announced that it intends to transfer 100% ownership of its subsidiary, Exelon Generation Company, LLC ("Exelon Generation"), to a newly-created subsidiary of Exelon Corporation, that will then be spun-off, becoming Exelon Generation's new ultimate publicly-traded parent company. Will this transaction impact the Company's FPFTY EBSC costs?

A. The transaction is not expected to increase the Company's FPFTY EBSC costs. The Company's claims for the FPFTY do not include any EBSC costs related to the separation announcement.

VII. COVID-19 INCREMENTAL COSTS AND LOST REVENUE

36. Q. Can you please address the Secretarial letter at Docket No. M-2020-3019775 titled *COVID-19 Cost Tracking and Creation of Regulatory Asset* that the Commission issued on May 13, 2020?

A. The Secretarial letter acknowledged that utilities would incur additional costs and experience other financial impacts because of the COVID-19 emergency, including increased uncollectible accounts expense resulting from the service-termination moratorium established by the Commission's Order in *Public Utility Service Termination Moratorium Proclamation of Disaster Emergency-COVID-19*, issued at Docket No. M-2020-3019244 and ratified on March 26, 2020 ("Emergency Order"). The Secretarial letter authorized utilities "to create a regulatory asset for any incremental uncollectible expenses incurred above those embedded in rates since the issuance of the Emergency Order;" directed utilities to notify the Commission upon establishing such a regulatory asset; and stated that it will consider requests for recovery of the regulatory asset in future proceedings if claimed "at [a utility's] first available opportunity." Additionally, the Secretarial letter directed jurisdictional utilities "to track extraordinary, nonrecurring incremental COVID-19 related expenses" and to maintain detailed accounting records of "the incremental expenses incurred for the provisioning of utility services used to maintain the health, safety and welfare of Pennsylvania customers during the COVID-19 pandemic." The Secretarial letter did not authorize utilities to establish a regulatory asset or otherwise defer the expenses that it directed them to "track."

37. Q. Has PECO incurred incremental uncollectible accounts expense as a result of the COVID-19 pandemic?

A. Yes, PECO recorded $74.4 million of uncollectible accounts expense related to the electric business in 2020 (an increase of approximately $45 million over 2019). On October 13, 2020, PECO filed a notice for its electric distribution business in accordance with the Secretarial letter, notifying the Commission that it would be creating a regulatory asset for these incremental expenses for its electric business. In 2020, PECO established a regulatory asset for incremental uncollectible expense totaling $37.9 million. PECO is currently projecting $47 million of uncollectible accounts expense in 2021. $36.7 million of this amount is being recorded as regular O&M expense, and $10.3 million is being tracked and recorded pursuant to the Emergency Order as incremental uncollectible accounts expense to be recovered in this rate case. The Company is projecting $35.6 million of uncollectible accounts expense in 2022. These figures take into account the Commission's recent determination in Docket No. M-2020-3019244 to end the emergency service-termination moratorium on March 31, 2021. The Company's claim is detailed further in the direct testimony of Mr. Trzaska regarding Schedule D-11.

38. Q. Has PECO incurred incremental COVID-19 related expenses or lost revenues?

A. Yes. PECO incurred incremental costs related to COVID-19 in 2020. These incremental costs include additional personal protective equipment ("PPE") purchases, cleaning and sanitizing costs, health screening costs, and other expenses that would not have been incurred but for the pandemic. PECO has not collected late payment charges or reconnection fees since the moratorium was instituted. However, the Company is not seeking recovery for the incremental COVID-19 related expenses or lost revenues at this time.

VIII. CONCLUSION

39. Q. Does this complete your direct testimony at this time?

A. Yes, it does.