PECO ENERGY COMPANY
STATEMENT NO. 2

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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

DOCKET NO. R-2022-3031113

DIRECT TESTIMONY

WITNESS: ROBERT J. STEFANI

SUBJECT: PECO'S NEED FOR RATE RELIEF; OPERATIONS AND MAINTENANCE COSTS; OVERVIEW OF PECO'S ACCOUNTING EXHIBITS AND BUDGETING PROCESS; GAS SALES FORECAST; AFFILIATED SERVICES; AND INCREMENTAL COVID-19 COSTS

DATED: MARCH 31, 2022

TABLE OF CONTENTS

Page

DIRECT TESTIMONY
OF
ROBERT J. STEFANI

I. INTRODUCTION AND PURPOSE OF TESTIMONY

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

A. My name is Robert J. Stefani. My business address is 2301 Market Street, Philadelphia, Pennsylvania 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. I am responsible for PECO's financial function, including budgeting, long-range financial planning, financial analysis and reporting, project evaluation and financings. I also conduct oversight and coordination of PECO's accounting, tax, treasury, investor relations and risk management activities.

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?

The purpose of my direct testimony is to: (1) briefly explain PECO's need for rate relief; (2) summarize PECO's efforts to control operating and maintenance ("O&M") costs since its last approved base rate increase in 2021; (3) provide an overview of PECO's accounting exhibits and its budgeting process; (4) explain the derivation of PECO's gas sales forecast; (5) describe the nature and allocation of costs for services that PECO receives from Exelon Business Service Company ("EBSC"); and (6) provide an overview of the incremental costs incurred by the Company related to the COVID-19 pandemic.

II. NEED FOR RATE RELIEF

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

A. PECO last requested a base rate increase in 2020, which was the Company's first proposed increase for its gas division in over ten years. Since the Company's current base rates became effective on July 1, 2021, PECO has continued to invest in new and replacement gas utility plant. At the same time, materials and contracting costs have escalated as a result of general inflationary trends and rising labor and material costs in the utility industry. These cost increases have been particularly acute in the past year. Usage per residential customer is also expected to decline further due to an increase in gas commodity prices and more customers returning to the workplace after an extended period of time working remotely.

PECO has also continued to responsibly grow its operating and maintenance ("O&M") budget to address system and customer needs. For example, the Company allocated significant funding to its gas mapping and locate programs in response to an increased number of customer requests, the maintenance of gas mains, addressing leaks and odor investigations, low-income customer programs, and needed improvements to its information technology ("IT") infrastructure.

6. Q. Does the Company anticipate these trends will continue?

A. Yes. The Company anticipates that many of the factors that have led to the Company filing this base rate case will continue in the coming years. Inflation is on the rise, labor and materials costs continue to increase, and residential usage per customer is expected to decline. Meanwhile, the Company must continue to make significant capital investments in its system and maintain a strong O&M program in order to provide customers exemplary service and maintain system reliability and safety.

Notably, the Company's actual O&M spending necessary to maintain the Company's distribution system and high levels of customer service in 2021 was entirely consistent with the Company's projections in its last base rate case. The Company's actual O&M expenditures in 2021 were $136.0 million, which is in line with the amount originally budgeted for 2021 in PECO's prior base rate case

($136.4 million) and well above the amount approved for O&M recovery in the Company's current Commission-approved rates ($119 million). The Company's actual 2022 expenditures are also on track to be consistent with our prior projections.

7. Q. Can you provide further detail on the Company's projected growth in its contracting expense?

A. Yes. As I noted earlier, the Company's overall O&M budget and the work necessary to maintain a high level of system reliability, safety, and customer service will grow in the coming years. To accomplish its workplan, the Company relies upon a combination of PECO employees (compensated through payroll and overtime) and contractors (compensated through contracting expense). The Company will need to increase its overall employee and contracting expenditures in order to execute its capital plans and maintenance programs.

8. Q. You stated that the Company's need for rate relief is also being driven by its capital investments in its distribution system. Can you please describe the Company's currently-planned investments?

A. PECO is planning significant investments in new and replacement gas utility plant designed to maintain and enhance the safety and reliability of the Company's distribution system. PECO recognizes that it is imperative, for the continued provision of safe and reliable service to its customers, to continually invest in its distribution infrastructure. To that end, PECO projects that it will need to invest approximately $1.8 billion in new and replacement gas utility plant between January 2022 – December 2026 as follows:

	Capital Expenditures (in $ millions)
Jan. 2022 – Dec. 2022	$317
Jan. 2023 – Dec. 2023	$328
Jan. 2024 – Dec. 2024	$384
Jan. 2025 – Dec. 2025	$364
Jan. 2026 – Dec. 2026	$363

These amounts include both Accelerated Gas Infrastructure Modernization Plan ("AGIMP") and non-AGIMP related capital expenditures. While some portion of the AGIMP costs is eligible property and the associated fixed costs are recoverable through the Pennsylvania Public Utility Commission ("Commission") authorized Distribution System Improvement Charge ("DSIC"), the Company anticipates that it will need to obtain external financing for the remainder of these costs. As it has in the past, PECO will endeavor to obtain such financing at the most favorable terms possible.

Increases in the capital plan relate to increasing the number of miles of main replacement through 2026 to meet existing Company commitments to the Commission, gate station security enhancements, relocating indoor meters outdoors, investment in the Company's low pressure system elimination program, concrete restoration, the development of a new gas training facility, and residential high pressure regulator replacement.

9. Q. Are there any other costs you would like to highlight that are driving the Company's need for rate relief?

A. Yes. The Company's payroll and benefits cost continues to increase. As I mentioned, the Company needs to increase the size of its workforce to execute its capital plans and maintenance programs. PECO has also continued to provide its employees with reasonable increases in wages and salaries and incur increasing employee health care costs. The need to make such investments in the Company's labor force has not dissipated since the Company's last base rate case.

10. Q. Please elaborate as to why PECO's current base rates are insufficient to support its current and planned operations.

A. As a result of the Company's increased expenditures incurred in providing customers with exemplary service and a distribution system that is reliable and safe, PECO has been unable to achieve a fair return on its investment in its Gas Division. Without an increase in revenues, PECO's gas operations are projected to produce an overall return on investment capital of 5.67%, and a return on common equity of 7.18%, during the twelve months ending December 31, 2023.

As explained by Mr. Paul R. Moul (PECO Statement No. 5), such levels of return are inadequate under any reasonable standard and below the rates of return generally afforded to public utilities. Absent a rate increase, the erosion to PECO's projected returns would impair the Company's ability to make all of the reasonable and prudent investments in gas infrastructure that are necessary to maintain and enhance the provision of safe, reliable, and resilient natural gas service to its customers. Inadequate returns would also negatively impact PECO's credit coverage ratios and its ability to maintain or improve its investment grade credit ratings, thereby increasing the Company's financing costs.

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

A. Maintaining or improving PECO's credit ratings is important to reducing customer costs. As previously stated, the Company needs to make significant investments in its system to ensure the continued provision of safe and reliable service. PECO projects that it will need to invest approximately $1.8 billion in new and replacement gas distribution plant by December 31, 2026. A meaningful portion of these planned investments will be financed with debt and other forms of capital. The Company's credit ratings will impact the cost it will need to pay to attract such capital, and ultimately, such costs will be borne by PECO's gas customers. Therefore, it is important that the Company maintain its favorable credit metrics in order to minimize customer costs.

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

A. PECO has leveraged the recent low interest rate environment and its strong credit ratings to reduce its weighted average long-term debt rate of 3.97% in 2021 to approximately 3.92% as projected for 2023, which remains below its 2019 long-term debt rate of 4.1%. PECO has also taken steps to obtain debt financing at favorable terms to the Company and its customers. In 2021, PECO had two successful debt offerings. In March 2021, PECO successfully priced a $375,000,000, 30-year first mortgage bond ("FMB") offering at a spread of 82 basis points over the 30-year U.S. Treasury for an all-in coupon rate of 3.05%. In September 2021, PECO successfully priced a $375,000,000, 30-year mortgage bond offering at a spread of 88 basis points over the 30-year U.S. Treasury for an all-in coupon rate of 2.85%. These issuances are the third and fifth lowest interest rates for a FMB in the Company's current portfolio.

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

13. Q. Please describe PECO's efforts to control its O&M expenses since its current base rates became effective on July 1, 2021.

PECO projects that the compound annual growth rate ("CAGR") in O&M expense from 2021 through the end of the fully projected future test year ("FPFTY") will be 2.8%. This continues PECO's long-term favorable CAGR and is well below recent inflationary trends. When the Company's projected December 2010 to December 2023 CAGR is adjusted for increases in gas mapping and locate expenses, which are prudently incurred but largely beyond the Company's control, the projected CAGR in O&M expense decreases further to 1.7%. That rate is well below the expected inflation CAGR for the same period. Notwithstanding the overall increase in the Company's O&M expense that I described earlier, which is necessary to maintain exemplary service and maintain system reliability and safety, PECO has taken concrete action to control its O&M expenditures, including controlling bad debt expense and effectively managing pension and other post-employment benefits ("OPEB").

14. Q. Are there any specific infrastructure programs you would like to highlight, which exemplify this cost-control strategy?

A. PECO strives to make smart investments that will minimize costs in the long-term. Accordingly, it is PECO's practice to prioritize the replacement of infrastructure partly on the basis of leak performance. This minimizes long-term O&M expenditures related to main repairs and surveying. The Company has strategically identified 1.6 miles of leak-prone main for which O&M repairs are particularly costly. As an additional effort to control O&M costs, PECO has established a capital project to address this main, which is expected to contain the elevated costs of main repair in future years.

15. Q. What steps has PECO taken to reduce its bad debt expense?

A. PECO has seen a significant long-term reduction in its bad debt expense, which the Company reduced from $7 million in 2010 to $5 million in 2020 and $2 million in 2021, respectively. The Company expects comparable reduced levels in bad debt expense with estimated expenses of $3 million in the future test year ("FTY") and $3 million in the FPFTY. PECO achieved these reductions through a variety of initiatives, which included increasing oversight of high balance accounts and providing customer assistance programs such as the Customer

Assistance Program ("CAP"), Low Income Usage Reduction Programs ("LIURP") and the Matching Energy Assistance Fund ("MEAF").

16. Q. What steps has PECO taken to manage its employee benefit costs?

A. There are three main categories I would like to address: health care costs, the Company's OPEB expense, and pension costs. National health care costs have been trending above the rate of inflation. PECO, however, actively manages its employee benefits cost to achieve savings to the maximum extent practicable. The Company does this by evaluating trends in benefits and identifying and implementing cost reduction measures while maintaining competitive compensation and benefit packages to successfully attract and retain employees.

The Company has a self-insured health care program. Therefore, the Company's projected cost increases are based on increased employee participation, actual claims experience, and administrative costs trended to the next year based on participant utilization and projected medical price inflation. The Company engages Willis Towers Watson, a national health plan consulting firm, to complete the actuarial underwriting for its health plans in order to set premiums and determine the cost projections.

As PECO's medical rates are calculated based on its actual claims experience, the Company has undertaken several initiatives to manage its costs. This strategy includes collaborating with our vendor partners to offer population health management programs, such as a diabetes program for high-risk members, promoting lower cost care options including behavioral telehealth visits and virtual physical therapy sessions, implementing utilization management guidelines for our prescription drug formulary, conducting plan audits to ensure contract compliance, and obtaining competitive contract renewals. As a result of these initiatives, the Company's health care cost trend is below the national average based on the *2021 Segal Health Plan Cost Trend Survey*[1] for the period 2018-2021. The Company expects its 2022 health care cost trend to remain below the national average based on projections by Willis Towers Watson.

17. Q. Please address the Company's OPEB expense.

A. As part of our benefit cost containment strategy, PECO recently modified its OPEB plans for non-represented, non-craft participants. The amendments (i) eliminated 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 modifications followed prior PECO amendments to its OPEB plan in 2014 and 2018, which were also instituted to reduce the Company's future benefit obligation and cost. PECO is continuously seeking ways to implement additional cost reduction measures, as discussed above.

[1] *Available at* https://www.segalco.com/media/1913/segal-trend-survey-2021.pdf.

18. Q. What steps is the Company taking to control pension costs?

A. 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 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 2023 is $1.1 million, which is $16.2 million lower than the Company's 2021 contribution of $17.3 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.

Additionally, as part of the Company's strategy to reduce benefit costs, (i) non-represented, non-craft new hires and rehired employees and (ii) represented craft new hires and rehired employees are no longer eligible for pension effective January 1, 2021 and April 15, 2021, respectively; and instead, are eligible to participate in a 401(k) defined contribution plan.

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

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

A. PECO's principal accounting exhibits are MJT-1, MJT-2, and MJT-3, which represent PECO's revenue requirement for the FPFTY, 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. Exhibit MJT-1, which represents PECO's revenue requirement for the FPFTY ending December 31, 2023, is comprised of five sections, as follows:

Section I 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 II contains basic accounting data, primarily extracted from the Company's financial records, including a FPFTY-end balance sheet; statements of net operating income and FPFTY revenues; a schedule of expense items by primary account; and a calculation of PECO's tax expenses. Also included are schedules developing PECO's embedded costs of debt and stock, its FPFTY capital structure, and the Company's overall claimed rate of return.

Section III provides a detailed development of the major components of the Company's rate base claim. This section includes summaries of the original cost and accumulated depreciation at FPFTY-end of the various categories of utility plant, including allocated common plant, and calculations of PECO's working capital, gas inventories, materials and supplies, accumulated deferred income taxes ("ADIT"), regulatory liability for excess ADIT, and customer deposits and advances.

Section IV contains detailed adjustments required 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.

Section V briefly describes the FTY and HTY data.

Exhibits MJT-2 and MJT-3 are essentially identical in format. As explained by Mr. Trzaska, adjustments were made to budgeted data, where necessary, to ensure that the Company'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 the Commission's established ratemaking precedent.

Because PECO is basing its requested rate increase on FPFTY data, 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.

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

A. PECO Exhibit MJT-2 follows the same format as PECO Exhibit MJT-1, but presents information for the FTY ending on December 31, 2022.

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

A. PECO Exhibit MJT-3 follows the same format as PECO Exhibits MJT-1 and MJT-2, but presents information for the HTY, which ended on December 31, 2021. This information is being furnished in accordance with the Commission's filing requirements and provides a basis for comparing PECO's FPFTY claims to the actual results of historic operations, adjusted for rate making purposes, for the HTY.

22. Q. Please 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. Bradley'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 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., Gas 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 for review by other departments 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, dividend, and financing plan annually.

23. 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.

24. 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").[2] The Commission's auditors found no deficiencies or weaknesses in the way PECO prepares its budgets. The Commission's 2021 audit report of the Company is currently pending.

25. Q. Do the personnel in each of the responsibility areas develop their budgets by FERC account?

A. No, the responsibility areas do not budget by FERC account. Rather, the responsibility areas 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.

26. Q. Mr. Trzaska, in Schedules B-2 and B-4 of PECO Exhibit MJT-1, presents the budgeted data for the twelve months ending December 31, 2023 on a FERC account basis. How were those figures derived?

A. As Mr. Trzaska explains more fully in his testimony, he analyzed PECO's

---

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

recorded FERC account balances for the twelve months ending December 31, 2021 to determine their composition (e.g., payroll, benefits, rent) and then distributed the FPFTY budgeted costs to the appropriate FERC account based on his findings. The results of Mr. Trzaska's proposed distribution of costs were then reviewed and confirmed with members of my staff.

27. 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 MJT-1, MJT-2, and MJT-3 present, in considerable detail, the Company's rate base, revenue, expense and tax claims, much of the supporting data is provided in the separately-bound volumes comprising the Company's responses to the Commission's standard rate case filing requirements at 52 Pa. Code §§ 53.52, 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 requests 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 also sponsoring testimony and specific exhibits in the areas of depreciation, rate of return, energy-efficiency programs, and unbundling of certain costs.

28. 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 the plant that will actually be in service during the FPFTY in its claimed rate base. 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 by the end of the FPFTY.

V. GAS SALES FORECAST

29. Q. How does PECO develop its gas sales forecast, generally?

A. The natural gas forecasting process uses multiple regression-analysis models that determine the relationship between monthly gas sales and predictive variables, such as weather, usage trends, and time of year. The modeled results are evaluated using standard statistical criteria (like 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. Further detail is provided in the Company's responses to Commission filing requirements SDR-RR-9 and SDR-RR-10.

30. Q. How does PECO utilize historical weather data in developing its gas sales forecasts?

A. PECO's gas 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. The Company then analyzes that temperature-normalized historical usage to discern customer usage trends that result from factors other than weather. Out-of-Model adjustments are then made to the modeled forecasts to remain consistent with these trends and address any new growth drivers expected to impact future sales. The results of the forecast are then compared to prior forecasts for consistency and reviewed with the Exelon Senior Manager of Load Forecasting, the PECO Director of Financial Planning and Business Analysis, and other Exelon and PECO senior management for their approval.

31. Q. You previously observed that PECO had witnessed a general decrease in use per residential customer. Has the COVID-19 pandemic impacted that trend since the Company's last rate case?

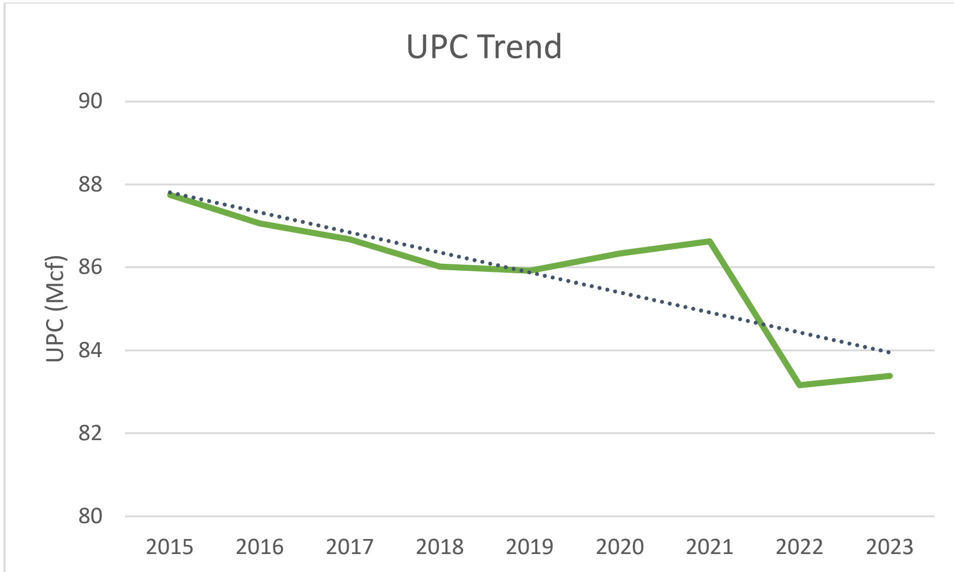
A. The average residential use per customer ("UPC") has generally declined year-over-year, primarily due to increases in energy efficiency and declining Heating

Degree Day ("HDD") trends in weather normal calculations over time. 30-year moving averages of HDD since 2015 are displayed in the following table:

Year	HDD (30 Yr Avg)
2015	4,529
2016	4,513
2017	4,487
2018	4,458
2019	4,437
2020	4,409
2021	4,408
2022	4,409
2023	4,409

Moving averages between 2015 and 2021 are based on 30-year periods that end one year prior. Averages provided for years 2022 and 2023 are based on the 1990 to 2019 range because that was the 30-year period used by PECO at the time of forecasting.

Despite declining HDDs used to weather normalize sales, UPC increased year-over-year in 2020 and 2021 due to work-from-home measures in response to COVID-19. 2020 weather normalized residential UPC grew as pandemic-related restrictions led to more customers working from their homes driving an estimated impact of approximately 1% on residential sales. As state closure mandates were lifted in 2021, businesses reopened, and more customers returned to their offices, the impact of COVID-19 on residential sales decreased to approximately 0.5%. Weather normalized UPC for residential customers, including projections for the FTY and FPFTY, is displayed in the following graph:



Green line represents UPC; blue line represents trended UPC data

32. Q. What is the expected impact of COVID in the FTY and FPFTY?

A. The Company expects COVID impacts to continue to decrease over time. When combined with the historical trend and increasing commodity costs, as I will discuss below, the Company anticipates additional year-over-year declines in UPC in 2022 and 2023.

33. Q. Has PECO taken the historical trend into account in calculating its gas sales forecast for this case?

A. Yes. As mentioned above, the forecasting process includes an evaluation of historical weather normalized UPC trends. These historical observations are impacted by the change in the Company's weather normal calculations over time. While PECO does not forecast future weather changes, the Company does adjust its forecasts so that they are consistent with UPC trends, net of any changes in gas usage drivers expected to impact future sales (e.g. COVID-19 impacts, gas prices).

34. Q. How has PECO accounted for the rise in gas prices in its gas sales forecasts? Please explain.

A. Average gas commodity prices almost doubled in 2021 compared to the prior year (source: Henry Hub Gas Spot Prices) with the commodity price increase driving higher customer bills in 2022. Studies have shown that higher gas prices cause customers to moderate their gas consumption. *See Price Elasticity for Energy Use in Buildings in the United States* (January 2021), U.S. Energy Information Administration.[3] This results in reduced Company sales. The Company projects that higher gas prices will have a negative impact on sales. The most significant impact is anticipated to be during the FTY, with higher gas prices resulting in an approximately (2%) reduction and (2.4%) reduction in residential and commercial sales, respectively. Some moderation in gas commodity prices is expected by the FPFTY, with the impact to residential and commercial sales decreasing to a (1.1%) and (1.3%) reduction in sales, respectively. These impacts, when taken together with the anticipated decrease in COVID impacts and the Company's

[3] *Available at* https://www.eia.gov/analysis/studies/buildings/energyuse/pdf/price_elasticities.pdf.

historical trend, result in the marked decrease in UPC from 2021 to 2022 and 2023 that is depicted in the graph above.

VI. AFFILIATED SERVICES

35. 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.

36. 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: IT, supply, finance, human resources, government and external affairs and public policy, legal, corporate governance, strategy, communications, compliance and audit, and corporate and information security services. The EBSC offers its services to PECO and other affiliated members of the Exelon family of companies, including the other Exelon utilities (Atlantic City Electric Company, Baltimore Gas and Electric Company, Commonwealth Edison Company, Delmarva Power & Light Company, and Potomac Electric Power Company).

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

A. No, PECO is not required to use the EBSC's services. Under the terms of the General Services Agreement ("GSA") between PECO and the EBSC, as 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.

38. Q. What role does the EBSC play in PECO's natural gas 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 natural gas 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, and certain highly specialized services, for which it would not be cost-effective to maintain the required expertise at either PECO or the EBSC, are obtained through contracting with outside firms (e.g. Human Resources).

39. 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 a full complement of 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.

40. 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 the 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 United States 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.

41. 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.

42. 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 Commission's audits of the Company in 2014 and 2021. In 2017, the Commission conducted a Management Efficiency Investigation to evaluate PECO's implementation of recommendations from the 2014 Audit.[4] 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 payable systems and the sharing of benchmarking reviews between EBSC, PECO, and other Exelon companies.

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

A. PECO has included $24.4 million in its FPFTY expense claim for charges from EBSC. A breakdown of those costs is attached as PECO Exhibit RJS-1.

44. Q. On February 1, 2022, Exelon Corporation closed a transaction resulting in the transfer of 100% ownership of its subsidiary, Exelon Generation Company, LLC ("Exelon Generation"), to a newly-created subsidiary of Exelon Corporation that was spun-off, becoming Constellation Energy

[4] *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).

Group. Will Exelon Corporation's separation of its distribution utility companies from its generation companies 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.

VII. COVID-19 COSTS

45. Q. Are you familiar with 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. Yes.

46. Q. Has PECO complied with the Secretarial Letter?

A. Yes. PECO is tracking its extraordinary, nonrecurring incremental COVID-19 related expenses as directed by the Secretarial Letter.

47. Q. Is PECO making a claim in this case to recover incremental COVID-19 related expenses and lost revenues?

A. No. The full impact of COVID-19 is not known at this time and the Company is continuing to evaluate its effects.

VIII. CONCLUSION

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

A. Yes, it does.

DB1/ 128622131.1