STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

ILLINOIS COMMERCE COMMISSION On its Own Motion vs. MidAmerican Energy Company Reconciliation of revenues collected under gas adjustment charges with actual costs prudently incurred.	)	ICC Docket No. 01-0703

REPLY BRIEF ON REOPENING
OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

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Table of Contents

The Staff of the Illinois Commerce Commission ("Staff") hereby submits its reply brief on reopening in this matter.

I. INTRODUCTION

Staff in its initial brief on reopening set forth its position that Section 7--210 of the Public Utilities Act ("PUA")(220 ILCS 5/7--210) must be applied prospectively not retroactively as MidAmerican Energy Company ("MEC") argues in its initial brief. Staff's initial brief set forth the relevant case law, Caveny v. Bower, 207 Ill.2d 82, 797 N.E.2d 596 (2003) for determining whether Section 7--210 should be applied prospectively or retroactively. Caveny provides the Illinois Supreme Court's approach for determining when new or amended statutes apply retroactively or prospectively. MEC's initial brief fails to consider this relevant case.

Staff's initial brief set forth its position that the Commission's PGA rules, specifically Section 525.40, applied to MEC's "competitive sales." MEC's arguments regarding Part 525 and Section 9--220 of the PUA are based upon the faulty premise that MEC's "competitive sales" during the reconciliation period are not public utility business. That premise is contrary to the Commission's Order on Rehearing in ICC Docket No. 03-0659 (Order at 9) and MEC's arguments are in effect improper collateral attacks on the Commission's prior order. MEC makes other arguments regarding Section 525.40 which Staff addresses in this reply brief and those MEC arguments should also be rejected.

Finally, MEC's initial brief insinuates that Staff must have known about MEC's "unregulated" sales (MEC IB, p. 4) and that MEC did not hide its unregulated sales from the Commission. (Id. at 7) While MEC does not tie these false accusations to any substantive arguments made in its brief, Staff will address these points and other arguments in Staff's reply brief which follows.

II. ARGUMENT

A. Section 7--210 must be applied prospectively not retroactively

Staff's initial brief set forth the relevant case law, Caveny v. Bower, 207 Ill. 2d 82, 797 N.E.2d 596 (2003), for the Commission to follow when determining whether Section 7--210 of the PUA should be applied prospectively or retroactively. When Caveny is considered, it is clear that Section 7--210 must be applied prospectively. In Caveny, the Illinois Supreme Court modified its approach for determining when new or amended statutes apply retroactively. Caveny adopted a test that focuses on legislative intent, and the court concluded that the necessary intent may be found, in virtually every case, either in the language of the statute at issue or, if the particular statute is silent on the matter, in section 4 of the Statute on Statutes (5 ILCS 70/4). Section 4 provides, as a general matter, that procedural changes in the law, but not substantive changes, are to be given retroactive effect. In the Court's view, Section 4 serves as a default standard, supplying the necessary statement of legislative intent when the statute at issue fails to articulate the legislature's choice with regard to retroactivity. (Caveny, at 95)

As Staff discussed in its initial brief, under Caveny, the first step in resolving a question about the retroactive effect of a statute is determining whether the statute itself contains a statement of legislative intent about its intended temporal reach. The relevant provision here is found in section 7--210(b), which states:

> After the effective date of this amendatory Act of the 93rd General Assembly, unregulated sales of natural gas by a gas utility within or outside its service area shall be subject to the provisions of this Section. This Section shall not be interpreted to invalidate any contract for unregulated sales of natural gas executed by a gas utility prior to the effective date of this amendatory Act of the 93rd General Assembly, but unregulated sales of natural gas pursuant to such contract after the effective date of this amendatory Act of the 93rd General Assembly shall be subject to the provisions of this Section.

(220 ILCS 5/7--210(b)) This provision does not, on its face, validate existing contracts against all challenges. The provisions scope is limited, for the operative language in the provision states only that "[t]his section shall not be interpreted to invalidate any contract for unregulated sales of natural gas" executed prior to the statute's effective date. The provision says nothing about the then-pending proceeding (i.e., ICC Docket No. 03-0659) in which the validity of those contracts was being addressed nor the then pending PGA dockets (i.e., ICC Docket Nos. 01-0703, 02-0723, and 03-0701) and it contains no indication that the legislature intended to express a view on any other grounds on which those contracts might be subject to challenge. Again, the language found in section 7--210 is limited, saying only that the prior contracts are not invalid for failing to comply with the new section.

MEC argues that the same language "demonstrates that the General Assembly was being careful <u>not</u> to change the effect of what had occurred <u>before</u> enactment of Section 7--210, such as the competitive sales of natural gas made during the 2001 reconciliation period that are at issue in this proceeding." (MEC IB, p. 10) MEC's argument begs the question. Its argument assumes that the new statute retroactively validates everything that occurred before it took effect. The second sentence in the quoted section above simply provides that pre-existing competitive contracts are not invalid for failing to comply with the new section. Neither the second sentence of Section 7--210(b) nor any other provision in Section 7--210 says that pre-existing contracts are valid against all other challenges. The earlier bar to MEC's unregulated sales was not contained in Section 7--210, a new provision. Thus excusing noncompliance with "this section," Section 7--210, does not mean that past noncompliance with other provisions must also be excused.

MEC argues that Section 7--210 clarifies the intent of the PUA given the content of Section 7--210 and the timing of the General Assembly's enactment to the Commission proceeding. (MEC IB, pp. 11-13) However, generally a statutory amendment gives rise to the presumption that the legislature intended to change the law. (Valeris v. Northwestern Memorial Hospital, 167 Ill.2d 449, 461 (1995)) If the legislature had meant for the new provisions simply to be "clarifying," the House sponsor would not have said, in response to a question, that the legislation would have no effect on the Commission's authority to fine the Company for its past competitive sales.

May: And so this legislation is neutral on the position whether they were right or wrong. Is that correct?

Verschoore: They… they took a 'no' position on, I'm assuming that's true. I …

May: So… so…okay. Just… I want to clarify that. That its neutral on that and that at some time we can expect MidAmerican to pay some sort of fines if the ICC should so decide?

Verschoore: If they would decide, yeah, I'm cer… yeah, they would. (House Transcript, May 24, 2004, p. 38)

MEC also argues that the legislative history itself confirms the clarifying effect of Section 7--210. (MEC IB, pp. 13-14) This argument should also be rejected. As Staff's initial brief pointed out the legislative history is contradictory and inconsistent. There are comments contrary to what MEC quotes in its initial brief and as the above comments indicate, those comments suggest that the drafters were adopting a “hands off” approach toward pending Commission proceedings and the drafters only intended that the new provisions by themselves would be not be grounds for invalidating existing contracts. (Staff IB, p. 17)

As Staff’s initial brief set forth, if the Commission finds Section 7--210 to not contain an expression of legislative intent, then the default provision in section 4 of the Statute on Statutes (5 ILCS 70/4) would apply. In this case, since Section 7--210 is substantive rather than procedural in effect, Section 7--210 applies prospectively not retroactively as MEC argues. (Staff IB, pp. 17-18)

B. The revenues from MEC’s competitive sales must be included in the PGA

1. Part 525 does apply to MEC’s competitive sales

MEC argues that the PGA Rules do not apply because the applicability provision limits the use of the gas charge to the recovery of costs and revenues associated with regulated sales. (MEC IB, p. 17) MEC’s argument should be rejected for a number of reasons. First, the Commission should reject this argument since it amounts to a collateral attack on the Commission’s order in ICC Docket No. 03-0659. The Commission’s order on rehearing in ICC Docket No. 03-0659 was very clear that “[t]he act does not permit MEC to decide which of its gas sales are subject to regulation and which are not. Accordingly, one of the premises upon which this rehearing is conducted is that any sale of gas by either MEC’s “competitive divisions’ or regulated noncompetitive division is public utility business." (ICC Docket No. 03-0659, Order on Rehearing at 9) MEC disregards the Commission's order in ICC Docket No. 03-0659 and assumes the opposite of what the Commission found. Because as MEC acknowledges in its brief, "'[t]he PGA allows utilities to adjust their rates to recover gas costs without the need for frequent rate proceedings'" (citations omitted)(MEC IB, p. 18) and MEC has a PGA in place, the gas sales made by MEC, both regulated and competitive, are subject to the PGA Rules. In particular, MEC's competitive sales are subject to Section 525.40(d)'s requirements for purposes of determining whether associated gas revenues offset recoverable PGA costs. That section provides no exemption whatsoever for MEC's revenues from competitive gas sales or sales from "separate gas portfolios" to be excluded from the PGA.

Second, in addition to MEC's argument regarding the applicability section of Part 525 being a collateral attack on the Commission's prior order, MEC misinterprets Section 525.10. In fact, MEC interprets Section 525.10 in such a way that it is even contradictory to its own stated position. MEC argues that the gas transactions subject to Part 525 are those which are associated with "service classifications" identified in MEC's filed rate schedules. MEC's argument is inconsistent with its own brief. (MEC IB, p. 18) Later in its brief, MEC argues that the only revenues which should flow through the PGA are those associated with wholesale transactions. (MEC IB, pp. 21-22) However, the same revenues associated with wholesale transactions which MEC itself admits flow through the PGA do not necessarily involve entities that are identified in the service classifications in MEC's filed rate schedules. For example, marketers, brokers, other utilities, transporters (i.e. large industrial companies) and natural gas producers all may enter into capacity release transactions with a utility like MEC but all are not necessarily identified in MEC's service classifications.

Section 525.10(a) identifies which customers pay the PGA. It simply provides that once the cost of gas under the PGA is determined, "[that] gas charge is applied to all therms associated with the service classifications so identified in the filed rate schedules of all gas public utilities in the State of Illinois." The applicability section does not define which revenues that are under Section 525.40(d) are offset against the recoverable gas costs. Section 525.40(d) provides that definition.

2. Section 9--220 of the PUA does apply to MEC's competitive sales.

MEC makes the same argument regarding Section 9--220 of the PUA that it makes with respect to Part 525. (MEC IB, pp. 16-17) MEC's argument should be rejected for the same reasons as set forth above given that it is a collateral attack on the Commission's prior order. In its brief, MEC also argues that because Subsection 7--210(c) does not list Section 9--220 as one of the sections of the PUA which unregulated sales are subject to, the gas costs and revenues from MEC's competitive sales should be reflected below the line and not flow through the PGA. (MEC IB, p. 15) MEC again begs the question. MEC assumes that Section 7--210(c) is retroactive. However, as set forth above, Section 7--210 applies prospectively not retroactively. Given the fact that Section 7--210 applies prospectively, it is not relevant for purposes of this docket that Section 9--220 is not enumerated in Section 7--210(c).

3. The competitive sales revenues do fall under the PGA definition.

MEC's argues that gas costs and revenues from competitive sales were never intended to be included in the PGA. (MEC IB, p. 20) In making this argument, MEC first sets forth "its" definition of "transactions at rates that are not subject to the Gas Charge(s) …" (MEC IB, p. 21) MEC argues that the Commission in ICC Docket No. 94-0403 defined that phrase to mean "wholesale transactions." (MEC IB, p. 21) MEC next argues that Staff defined the transactions that would produce revenues to include "'… capacity releases, sales for resale, buy/sell transactions and exchanges.'" (MEC IB, p. 22) MEC then argues that since Staff did not "list retail sales of unregulated gas as one of the types of transactions that could be made using PGA costs," (MEC IB, p. 22) it would be improper for the Commission in this docket to apply the PGA rules to MEC's competitive sales. (MEC IB, p. 20-22) MEC's argument should be rejected for a number of reasons. First, as explained in part D of this reply brief, Staff did not know that MEC was conducting competitive sales when it started reviewing MEC's 2001 PGA filing and most certainly did not know about those transactions more than eleven years ago when the PGA rulemaking was initiated. (Initiating Order ICC Docket No. 94-0403)(Attached to this brief as Attachment 1, p. 13)[1] Therefore, for MEC to argue that Staff should have listed "retail sales of unregulated gas" is vexing. Second, a careful review of the Commission's order in the PGA rulemaking shows that the transactions included within the phrase "transactions at rates that are not subject to the Gas Charge(s) …" is more encompassing than wholesale transactions as MEC suggests and therefore gas costs and revenues from competitive sales do fall within the scope of the PGA.

[1] Part 525 rulemaking was initiated on October 5, 1994.

A review of the Commission's order in ICC Docket No. 94-0403[2] shows that MEC itself was concerned about transactions other than those listed by Staff. The Commission's order in the PGA rulemaking indicates as much when it states the position of MEC's predecessor Iowa-Illinois "For other transactions involving costs included in the Gas Charge, Iowa-Illinois recommended that the revenue credit should equal the costs included in the gas charge." (ICC Docket No. 94-0403, Order at 6) Iowa-Illinois was not only concerned with wholesale transactions, but also other transactions. The fact that Iowa-Illinois, MEC's predecessor, made such an argument at the rulemaking is evidence that "MEC" knew its competitive sales (i.e. other transactions) would be covered by the new PGA rule and for that reason Iowa-Illinois argued more than eleven years ago that the revenue credit to the PGA should be limited to the gas cost charges. However, the Commission rejected Iowa-Illinois's proposal when it rejected all of the utilities' various revenue sharing proposals. (ICC Docket No. 94-0403, Order dated August 23, 1995, Order at 8)

Even though the Commission rejected Iowa-Illinois/MEC's revenue sharing proposal more than ten years ago, that did not stop MEC from making the same proposal in this docket, in Mr. Miltenberger's rebuttal testimony on reopening which states:

> Q. Do you have any additional comments concerning the proposed adjustment from Staff?
>
> A. Yes, I do. If the Commission does determine that the gas costs related to the competitive sales need to be included in the PGA reconciliation, then I would propose that the <u>revenues included only recover the competitive sales gas costs</u>. In other words, only a

2 The Commission's order in docket 94-0403 issued on August 23, 1995 is attached to this brief as Attachment 2. A subsequent amendatory order dated October 3, 1995 is attached to the brief as Attachment 3. The amendatory order corrected a scrivener's error in one of the ordering paragraphs.

> direct matching of the cost of gas and gas cost recoveries related to competitive gas sales should be included.

(MEC Exhibit 11, p. 3)(emphasis added) The Commission should reject this proposal again. As the Commission pointed out, it had a concern "that revenue sharing would create incentives for utilities to subsidize off-system transactions with on-system transactions and could therefore result in PGA gas charge increases." (ICC Docket No. 94-0403, Order at 8) That concern was a valid one as evidenced by the actions of Iowa-Illinois and MEC. Despite the fact that the Commission rejected the revenue sharing proposal, MEC still could not resist the incentive to subsidize off-system transactions with on-system transactions as evidenced by the fact that MEC admits that PGA assets are used for competitive sales. This point is discussed in further detail in part E of this brief.

In addition, the plain language of Section 525.40(d) does not support MEC's argument. Despite MEC's claim, the plain language of Section 525.40(d) is clear that revenues being credited against gas costs are much broader then those revenues associated with "wholesale transactions." Section 525.40(d) states as follows:

> Recoverable gas costs shall be offset by the revenues derived from transactions at rates that are not subject to the Gas Charge(s) if any of the associated costs are recoverable gas costs as prescribed by subsection (a) of this Section. This Subsection shall not apply to transactions subject to rates contained in tariffs on file with the Commission, or in contracts entered into pursuant to such tariffs, unless otherwise specifically provided for in the tariff. Taking into account the level of additional recoverable gas costs that must be incurred to engage in a given transaction, the utility shall refrain from entering into any such transaction that would raise the Gas Charge(s).

The first sentence defines in the negative what revenues offset gas charges. In particular, the language provides that if the revenues are derived from transactions that are not subject to the Gas Charges then the revenues are used to offset the gas charge provide that "any of the associated costs are recoverable gas costs." Under Part 525, the transactions which are subject to the Gas Charge (i.e., customers charged the PGA) are those set forth in the applicability section, Section 525.10(a). Section 525.10(a) provides that:

> The Gas Charge(s) shall be applied to all therms associated with the service classifications so identified in the filed rate schedules of all gas public utilities operating in the State of Illinois. If a utility elects to establish separate Gas Charge(s) for recovery of costs of a seasonal nature, such Gas Charge(s) shall be applied to therms associated with the appropriate seasonal period. The Gas Charge(s) shall be applied either to each therm billed during the effective month or to each therm delivered during the effective month. The utility shall elect whether a billed or a delivered method shall be used, and such election shall remain in effect until a utility request to effect a change is approved by the Commission. Each Gas Charge shall be determined in accordance with Section 525.60.

Therefore,"transactions at rates that are not subject to the Gas Charge(s)" are <u>any transactions that are not identified in the filed rate schedules of the utility</u>. MEC admits that its competitive sales are not identified in its filed rate schedules (MEC IB, p. 18), therefore, MEC's competitive sales revenues must offset the gas costs in the PGA.

The second sentence in Section 525.40(d) further supports this reading. Staff's proposed rule (See Attachment 1 to this brief, Appendix B to the Initiating Order in ICC Docket No. 94-0403) did not contain the second sentence "[t]his Subsection shall not apply to transactions subject to rates contained in tariffs on file with the Commission, or in contracts entered into pursuant to such tariffs, unless otherwise specifically provided for in the tariff." Central Illinois Public Service Company ("CIPS") proposed that language to clarify that Section 525.40(d) was not intended to flow through the PGA "revenues which are 'subject to Illinois Commerce Commission tariffs' and contracts entered into with customers pursuant to tariff provisions …" (ICC Docket No. 94-0403, Order at 8) The Commission agreed and therefore, included that sentence in the rule. There is no doubt that MEC's competitive sales outside of its service territory are not pursuant to Commission tariffs and the competitive sales within its service territory also are not pursuant to tariffs since MEC never had them approved by the Commission. (ICC Docket No. 03-0659, Order on Rehearing at 11) Therefore, given that none of MEC's competitive sales during 2001 are pursuant to filed rate schedules all the revenues from those sales must offset the gas charges in the PGA.

4. The Commission should disregard MEC's cross-subsidization and confiscation of assets arguments.

MEC argues that if the PGA rules are applied to its competitive sales with gas costs and revenues being treated as recoverable gas costs there is a possibility that "unregulated sales could be subsidized by regulated sales." (MEC IB, p.24) MEC's argument should be rejected for a number of reasons. First, it's a redherring. MEC's argument assumes a hypothetical that is not supported by the facts in this record. A review of MEC's Exhibit 10, Schedule 1, page 1 of 1 (formerly a proprietary schedule) shows that for 2001 the revenues from non-regulated trading were $7,963,723 with a cost of gas equal to $7,196,089 and the Non-regulated Marketing and Sales' revenues were $32,125,457 with a cost of gas equal to $31,869,294. These figures result in a $1,023,797 profit for 2001. (MEC Exhibit 10, Schedule 1) That is the same profit which Staff witness Ebrey recommends flows through the PGA. The only subsidization going on in 2001 was a subsidization going the opposite way which was due to "MEC's diversion of money and resources into its competitive divisions..” (ICC Docket No. 03-0659, Order on Rehearing, p. 10)

In addition, MEC’s argument should be rejected given that the PGA Rule contains language which guards against that which MEC suggests may happen (i.e., MEC having to sell gas for less than it paid for it). MEC in its brief, when quoting from 525.40(d), fails to set forth all of the language from 525.40(d). Section 525.40(d) in its entirety states as follows:

> Recoverable gas costs shall be offset by the revenues derived from transactions at rates that are not subject to the Gas Charge(s) if any of the associated costs are recoverable gas costs as prescribed by subsection (a) of this Section. This Subsection shall not apply to transactions subject to rates contained in tariffs on file with the Commission, or in contracts entered into pursuant to such tariffs, unless otherwise specifically provided for in the tariff. Taking into account the level of additional recoverable gas costs that must be incurred to engage in a given transaction, <u>the utility shall refrain from entering into any such transaction that would raise the Gas Charge(s).</u>

(83 Ill. Adm. Code Part 525.40(d))(emphasis added) Contrary to MEC’s argument, it is not “guaranteed dollar-for-dollar recovery under th[e] rule.” (MEC IB, p. 24) The last sentence in Section 525.40(d) clearly provides that MEC cannot enter into transactions that will increase the gas charge which MEC suggests by its hypothetical. For all of these reasons the Commission should disregard MEC’s cross-subsidization argument.

MEC after arguing that there could be a cross subsidization if Staff’s proposal were adopted, next argues that Staff’s proposal is confiscatory. MEC argues that because Staff will not allow MEC’s nongas costs in the PGA and the same nongas costs are not includable in base rates, that is a confiscation. (MEC IB, pp. 26-27) MEC’s argument should be disregarded. MEC ignores the fact that “the competitive divisions’ employees, equipment, inventory, and contracts are utility assets that have been diverted from service to regulated customers without prior Commission approval in violation of subsection 7-102(A)(g).” (ICC Docket No. 03-0659, Order on Rehearing at 9-10) Given that MEC diverted employees, equipment, etc. from ratepayers it would be absurd to charge ratepayers for those nongas costs as MEC suggests.

C. MEC’s “nongas costs” should not flow through the PGA but rather only the cost of the actual gas and revenues from MEC’s competitive sales are allowed to flow through the PGA.

MEC cites to Mr. Miltenberger’s testimony to support its claim that the PGA should include “all expenses” (i.e. including “nongas cost” (MEC IB, p. 23)) of making competitive sales not just gas costs and revenues. (MEC IB, p. 22) MEC states that Staff did not object to the accuracy of Mr. Miltenberger’s Schedule 1 which allegedly shows the nongas costs of “unregulated sales.” (MEC IB, pp. 22-23) Whether Mr. Miltenberger’s nongas cost figures are accurate or not is irrelevant. The nongas costs do not meet the PGA definition of gas costs and for that reason Staff did not challenge Mr. Miltenberger’s numbers. Mr. Miltenberger’s nongas costs do not flow through the PGA.

As Staff set forth in its initial brief and contrary to MEC’s claim in its initial brief (MEC IB, p. 20) the PGA rules specifically define recoverable gas costs. (Staff IB, pp. 7-8) The nongas costs that MEC proposes to recover through the PGA clearly do not fall within any of the “four categories of costs” (ICC Docket No. 94-0403, Order at 2) set forth in Section 525.40, in particular Section 525.40(a)(1)-(4). MEC’s nongas costs are not: 1) costs of natural gas etc.; 2) costs for storage services purchased; 3) transportation costs or 4) out-of-pocket direct non-commodity costs related to hydrocarbon procurement, transportation, supply management, or price management. In addition, the Commission's order when adopting Part 525 in response to a Nicor Gas argument to include "other costs" specifically found that "…the Gas Charge determined under Part 525 should be used exclusively for gas costs and associated revenues. We find that cost and revenues not directly associated with the purchase of gas should not be included in the Purchased Gas Charge(s). The Commission, therefore, rejects NIGas proposed language revision." (ICC Docket No. 94-0403, Order at 4) (Staff IB, p. 8) Despite MEC's claim, the fact that the Commission rejected NIGas's attempt to redefine recoverable gas costs is relevant. It is relevant because MEC itself is trying to accomplish the same thing in this docket. In ICC Docket No. 94-0403, Staff argued and the Commission agreed that costs and revenues not directly associated with purchased gas should not be recovered through the PGA. (ICC Docket No. 94-0403, Order at 3-4) NIGas sought to alter the definition of 525.40(d) but the Commission rejected NIGas's attempt to change the definition. The Commission likewise in this docket should reject MEC's attempt to include within the definition of gas cost, MEC's nongas costs. Those costs do not meet the definition.

D. MEC's insistence that Staff must have known about its competitive sales should be rejected.

In its statement of the case, MEC insists that Staff must have known about its competitive sales. (MEC IB, pp. 1-4) While Staff will respond to these statements, the argument is another red herring. The Commission has already determined that (1) with respect to competitive sales outside of its service territory, the PUA prohibits those transactions and (2) with respect to MEC's competitive sales within its service territory MEC had an obligation to comply with 9--102.1. (ICC Docket No. 03-0659, Order on Rehearing at 1 and 12, respectively). Because the Commission has found that the PUA prohibits certain transactions made by MEC in their entirety (i.e. those outside of its service territory) and also requires that other transactions receive prior Commission approval (i.e. those within the service territory) whether Staff knew about the transactions, which is not the case, is irrelevant. Never the less, Staff will respond to MEC's statements.

First, the issue of when Staff learned of MEC's competitive sales was resolved a long time ago. Staff's Motion For Additional Discovery and Hearings clearly sets forth that when the record was marked heard and taken back on November 21, 2002, Staff did not know MEC was engaging in competitive sales (Motion For Additional Discovery and Hearings, p. 2) As is stated in that motion, it was not until Staff received data request responses relating to MEC's 2002 PGA that Staff had reason to believe the competitive sales transactions occurred in 2001.

In its brief, when MEC first insinuates that Staff knew about its competitive sales, MEC first refers to MEC witness Kremer's Supplemental Rebuttal testimony which was filed on October 16, 2002. Mr. Kremer stated that with respect to maintaining certain documentation it would "only apply to transactions that are part of the costs attributed to MidAmerican's PGA customers." (MEC IB, p. 2) MEC's argument that this testimony somehow put Staff on notice that MEC was conducting competitive sales should be rejected for a number of reasons. First, Staff had no reason to believe that MEC was conducting competitive sales and therefore Mr. Kremer's testimony would not raise a red flag with Staff. Second, MEC's argument assumes that if a customer is not a PGA customers then it's a "competitive sales" customer, however MEC has many customers known to Staff generally who are not PGA customers but appropriately take service from MEC such as transportation customers. (TR 22) Therefore, the fact that MEC referred to "PGA customers" would not lead Staff to question MEC's statement. What would have raised a red flag with Staff would have been testimony from Mr. Kremer that MEC would not maintain documentation for its competitive sales. But Mr. Kremer did not disclose that in his testimony. What also would have raised a red flag with Staff was if MEC had complied with 9--102.1, but that did not happen either as the Order on Rehearing found. (ICC Docket No. 03-0659, Order on Rehearing at 11)

MEC next argues that Staff witness Bowers should have realized that the total cost of gas on invoices with the notations of "SC" and "DM"[3] would have exceeded the amount reflected on MEC's PGA reconciliation schedules. (MEC IB, p. 4) MEC completely disregards the fact that when it described "Mid American's Natural Gas Business" in its direct testimony, MEC did not refer to its unregulated business and its regulated business. Rather, MEC's testimony provided detail on the number of customers in Illinois, where those customers were located, the location of customers in other states, and what pipelines provided MEC with gas. The testimony failed to give the significant detail that "MidAmerican's Natural Gas Business" also included competitive sales. (MEC Ex. 2, Direct Testimony of Todd J. Kremer, pp. 2-3) Mr. Kremer did not testify that excess supply is sold to MEC's competitive division. MEC's criticism of Staff is an attempt to shift responsibility from itself to Staff and the

[3] "SC" represents purchases for regulated sales. "DM" represents purchases for competitive sales. (TR. 188-189)

Commission should not allow that. The PUA is clear that the burden of proof rests with MEC and not Staff "to establish the prudence of [MEC's] cost of … gas." (220 ILCS 5/9--220(a))

E. MEC's separate portfolio statements are misleading.

In its brief, MEC discusses the separateness of its "unregulated business," ("…[unregulated, unbundled natural gas] sales are, and have always been, made out of a separate portfolio of natural gas resources." (MEC IB, p. 5, 7)), and because of that separateness, the sales (i.e., gas costs and revenues) are not part of the PGA. (MEC IB, pp. 16-17) MEC's brief on the point of separate portfolios is misleading. Staff addressed this same issue in its initial brief. Staff cross Exhibits 1 and 2 provide evidence that gas purchases were not segregated into separate portfolios. Gas from the same contract is being used to satisfy the needs of both the regulated operations and the unregulated operations. (Staff Cross Exhibit 2) (Staff IB, p. 6) In addition, MEC itself has admitted that such "separateness'' does not in fact exist. In its Brief on Exceptions in ICC Docket 03-0659 MEC states the following: "… no PGA resources are used to make competitive sales, <u>with the single exception that *excess* PGA assets such as excess supply</u> (i.e., those assets *not* needed by PGA customers) <u>may be sold</u> via arms-length transactions either to <u>MidAmerican's competitive gas division</u> or to third parties." (Verified Brief on Exceptions of MidAmerican Energy Company, Dated March 31, 2004, p. 11) (emphasis added) By MEC's own admission and the evidence in this case, it is clear that there was no separate portfolio back in 2001. Furthermore, even if a "separate portfolio exists" which is not the case, that other portfolio of gas is a "cost[]

of natural gas" under Section 525.40(a)(1) and pursuant to Section 525.40(d), the revenues associated with those gas costs must offset the "[r]ecoverable gas costs."

III. CONCLUSION

WHEREFORE, for the foregoing reasons and those previously stated in Staff's briefs, Staff respectfully requests that the Commission approve the Company PGA reconciliation as presented by Staff on ICC Staff Ex. 8.00, Schedule 1, which results in an Ordered Reconciliation Factor (Factor O) in the amount of $1,467,936[4] for Commodity Gas Charge.

Respectfully submitted,

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4 Factor O in the amount of $1,467,936, which is to be refunded to PGA customers, consists of Ms. Ebrey's adjustment of $1,023,797 and Mr. Luth's adjustment of $444,139.