

Nicor Gas Company
Weighted Average Cost of Capital

	Nicor Gas Co. Capital Structure (Percent) ¹	Average Cost (Percent) ¹	Weighted Cost (Percent)
Debt	43.11 %	6.80 %	2.93 %
Preferred Stock	0.12	4.77	0.01
Equity	56.77	11.36	6.45
WACC	100.00		9.39 %

Cost of Equity Summary

	With Issuance Costs	Without Issuance Costs
DCF Cost of Capital ²	10.54%	10.37%
CAPM ³		
Method 1	13.71%	13.61%
Method 2	10.25%	10.25%
Average CAPM	11.98%	11.93%
Average of DCF and CAPM	11.26%	11.15%

[1] See: NICOR Gas Exhibit D-1.

[2] See: Exhibit 10.8.

[3] See: Exhibit 10.9.

Nicor Gas Company
Comparable Group
Spot - Date Adjusted Stock Prices

Company	Ticker Symbol	Ex-Dividend Date ¹		Stock Price Date	Days to Ex-Div Date	Percent Days Expired	Last Dividend	Adjusted Dividend	Closing Stock Price	Adjusted Stock Price
		Last [a]	Next [b]							
1 Avista Corp.	AVA	28-May-08	26-Aug-08	22-Jul-08	35	61.11	0.17	0.10	20.95	20.85
2 MGE Energy	MGEE	29-May-08	27-Aug-08	22-Jul-08	36	60.00	0.36	0.21	34.65	34.44
3 Nicor	GAS	28-Jun-08	26-Sep-08	22-Jul-08	66	26.67	0.47	0.12	39.74	39.62
4 Northwest Nat. Gas	NWN	30-Apr-08	29-Jul-08	22-Jul-08	7	92.22	0.38	0.35	45.23	44.88
5 Piedmont Natural Gas	PNY	24-Apr-08	23-Jul-08	22-Jul-08	1	98.89	0.26	0.26	26.07	25.81
6 Southwest Gas	SWX	15-May-08	13-Aug-08	22-Jul-08	22	75.56	0.23	0.17	28.25	28.08
7 Vectren Corp.	VVC	15-May-08	13-Aug-08	22-Jul-08	22	75.56	0.33	0.25	29.33	29.08
8 Wisconsin Energy	WEC	14-May-08	12-Aug-08	22-Jul-08	21	76.67	0.27	0.21	43.74	43.53

Notes:

[1] $((90 - \text{Days to Ex-Div Date}) / 90) * 100$ [2] Yahoo! Finance Research, <http://finance.yahoo.com>. Closing prices on July 22, 2008.

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Nicor Gas Company
Comparable Group
Dividends

Company	Recent Quarterly Dividends Paid Per Share (D ₀) ¹				Growth ² Rate, g (Percent)	Expected Quarterly Dividend Growth Rate Per Share (D ₁)			
	Q ₁ (\$/Share)	Q ₂ (\$/Share)	Q ₃ (\$/Share)	Q ₄ (\$/Share)		Q ₁ (\$/Share)	Q ₂ (\$/Share)	Q ₃ (\$/Share)	Q ₄ (\$/Share)
1 Avista Corp.	0.150	0.150	0.165	0.165	9.27	0.164	0.164	0.180	0.180
2 MGE Energy	0.355	0.355	0.355	0.355	5.65	0.375	0.375	0.375	0.375
3 Nicor	0.465	0.465	0.465	0.465	5.62	0.491	0.491	0.491	0.491
4 Northwest Nat. Gas	0.355	0.375	0.375	0.375	4.94	0.373	0.394	0.394	0.394
5 Piedmont Natural Gas	0.250	0.250	0.250	0.260	5.67	0.264	0.264	0.264	0.275
6 Southwest Gas	0.215	0.215	0.215	0.225	7.04	0.230	0.230	0.230	0.241
7 Vectren Corp.	0.315	0.325	0.325	0.325	4.20	0.328	0.339	0.339	0.339
8 Wisconsin Energy	0.250	0.250	0.270	0.270	8.68	0.272	0.272	0.293	0.293
Average					6.38				

Notes:

[1] *The Value Line Investment Survey*, June 13, June 27, and August 13, 2008.

[2] Simple Average of Value Line, Zacks earnings and BR+SV growth rates.

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**Nicor Gas Company
Comparable Group
Sustainable Growth Method**

Company	R	D _e	V _e	V		R _{av}	B ³	B*R ⁴	S*V	B*R+S*V
	Estimated Return on Common Equity ¹ (Percent)	Estimated Dividend Per Share ¹ (\$)	Estimated Book Value Per Share ¹ (\$)	Book Value Per Share	2007 2006 (\$) (\$)	Return on Average Equity ² (Percent)			Average ⁵ (Percent)	
1 Avista Corp.	8.50	1.15	21.25	17.27	17.46	8.45	35.98	3.04	0.34	3.38
2 MGE Energy	12.00	1.50	21.05	19.49	17.89	12.51	43.06	5.39	2.00	7.39
3 Nicor	14.00	1.86	25.70	20.58	19.43	14.40	49.75	7.17	0.41	7.57
4 Northwest Nat. Gas	11.00	1.88	26.50	22.52	22.01	11.13	36.24	4.03	0.34	4.37
5 Piedmont Natural Gas	12.50	1.19	14.70	11.99	11.83	12.58	35.67	4.49	1.19	5.68
6 Southwest Gas	10.00	1.06	26.05	22.98	21.58	10.31	60.55	6.25	0.94	7.19
7 Vectren Corp.	10.50	1.47	19.30	16.16	15.43	10.74	29.10	3.13	1.08	4.21
8 Wisconsin Energy	12.00	1.60	36.00	26.50	24.70	12.42	64.22	7.98	0.06	8.04
Average:										5.98 %

The Value Line Investment Survey, June 13, June 27, and August 13, 2008.

Notes:

[1] 2011-2013 estimated return on common equity, dividends per share, and book value per share as reported in Value Line.

[2] $R_{av} = (2 * R * V_{01}) / (V_{01} + V_{00})$.

[3] $B = 1 - (D_e / (R_{av} * V_e))$.

[4] $B * R = B * R_{av} = (R_{av} - D_e / V_e)$.

[5] S*V equals five year average of S, multiplied by current V, where S = annual growth rate of common shares outstanding and V = fraction of new funds provided that accrues to original shareholders.

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**Nicor Gas Company
Comparable Group
S and V Estimation**

Company	Growth Rate of Common Shares Outstanding (S)					Average S ¹	V ²	S*V (h)=[(f)*(g)]
	2003 (a)	2004 (b)	2005 (c)	2006 (d)	2007 (e)			
1 Avista Corp.	0.0062	0.0027	0.0025	0.0807	0.0076	0.0199	0.1717	0.0034
2 MGE Energy	0.0438	0.1118	0.0029	0.0259	0.0462	0.0461	0.4340	0.0200
3 Nicor	0.0007	0.0014	0.0018	0.0163	0.0223	0.0085	0.4805	0.0041
4 Northwest Nat. Gas	0.0137	0.0621	0.0011	(0.0123)	(0.0305)	0.0068	0.4983	0.0034
5 Piedmont Natural Gas	0.0171	0.1391	0.0004	(0.0272)	(0.0185)	0.0222	0.5355	0.0119
6 Southwest Gas	0.0282	0.0748	0.0690	0.0620	0.0249	0.0518	0.1816	0.0094
7 Vectren Corp.	0.1116	0.0040	0.0038	(0.0012)	0.0034	0.0243	0.4444	0.0108
8 Wisconsin Energy	0.0207	(0.0122)	(0.0001)	(0.0001)	(0.0003)	0.0016	0.3913	0.0006

Source: *The Value Line Investment Survey*, June 13, June 27, and August 13, 2008.

Notes:

[1] Average common shares outstanding growth rate for 2003-2007.

[2] V = (1-(2007 Book Value per Share/Average Stock Price))

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**Nicor Gas Company
Comparable Group
Growth Rate Estimates**

Company	Value Line EPS ¹		Estimated	Zacks	B*R+S*V	Average
	2007 (\$)	2011-2013 (\$)	VL Growth ² (Percent)	Growth ³ (Percent)	Growth (Percent)	Growth ⁴ (Percent)
1 Avista Corp.	0.72	1.75	19.44	5.00	3.38	9.27
2 MGE Energy	2.27	2.75	3.91	N/A	7.39	5.65
3 Nicor	2.99	3.55	3.49	5.80	7.57	5.62
4 Northwest Nat. Gas	2.76	3.35	3.95	6.50	4.37	4.94
5 Piedmont Natural Gas	1.40	1.85	5.73	5.60	5.68	5.67
6 Southwest Gas	1.95	2.60	5.92	8.00	7.19	7.04
7 Vectren Corp.	1.83	2.05	2.30	6.10	4.21	4.20
8 Wisconsin Energy	2.84	4.25	8.40	9.60	8.04	8.68
Average:			6.64 %	6.66 %	5.98 %	6.38 %

Notes:

[1] *The Value Line Investment Survey*, June 13, June 27, and August 13, 2008.

[2] $(\text{[2011-2013 EPS Estimate]} / \text{[2007 EPS]}^{0.20} - 1) * 100$.

[3] Estimated Long Term EPS Growth Rate for the next five years as reported by Zacks in its Full Company Reports at <http://www.zacks.com>.

[4] Simple average of Estimated Value Line growth, Zacks growth, and B*R+S*V growth.

NA = Not Available

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Nicor Gas Company
Equity Issuance Expense ⁴

SEC Filing Date	Number of Shares Issued (No.)	Price/Share (\$)	Proceeds (\$)	Per Share Underwriting Discounts & Commissions (\$)	Total Underwriting Discounts & Commissions (\$)	Net Proceeds ¹ (\$)	Estimated Company's Expenses (\$)	Selling & Issuance Costs ² (Percent)	
7/25/1979	1,500,000	31.50	47,250,000	0.83	1,245,000	46,005,000	80,000	2.80	%
8/26/1980	1,500,000	32.50	48,750,000	0.89	1,335,000	47,415,000	90,000	2.92	
Average				0.86	1,290,000	46,710,000	85,000	2.86	%
Borun and Malley ³								5.50	
Average Expense								4.18	
Issuance Expense Adjustment								95.82	%

Notes:

[1] Net Proceeds = Proceeds - Total Underwriting Discounts & Commissions.

[2] Selling & Issuance Costs = (Total Underwriting Discounts & Commissions + Estimated Company's Expenses)/Proceeds.

[3] Victor M. Borun and Susan L. Malley, "Total Flotation Costs for Electric Company Equity Issues."

[4] Issuance data is derived from NICOR Gas Exhibit D-5.

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Nicor Gas Company
Comparable Group
DCF Cost of Equity

Company	Dividend ¹ Yield (Percent)	Growth ² Rate, g (Percent)	Adjusted ³ Stock Price, P ₀ (\$)	Stock Price ⁴ S&I Adjusted (\$)	Unadjusted ^{5,6} ROE, k _e Before S&I (Percent)	Change (Percent)	S&I ⁷ Adjusted ROE (Percent)
1 Avista Corp.	3.45	9.27	20.85	19.98	12.73	0.11	12.84
2 MGE Energy	4.52	5.65	34.44	33.00	10.17	0.18	10.35
3 Nicor	5.16	5.62	39.62	37.96	10.78	0.22	11.00
4 Northwest Nat. Gas	3.57	4.94	44.88	43.01	8.51	0.17	8.68
5 Piedmont Natural Gas	4.29	5.67	25.81	24.73	9.96	0.20	10.15
6 Southwest Gas	3.44	7.04	28.08	26.91	10.48	0.11	10.59
7 Vectren Corp.	4.78	4.20	29.08	27.87	8.98	0.25	9.23
8 Wisconsin Energy	2.70	8.68	43.53	41.71	11.38	0.11	11.49
Average	3.99	6.38			10.37	0.17	10.54

Notes:

[1] Forward Quarterly Dividend per Share (Q_t) = $\{[Q_f^*(1+ke)^{0.75}+Q_f^*(1+ke)^{0.5}+Q_f^*(1+ke)^{0.25}+Q_f]/P_0\} * (1+\text{Growth Rate})$

[2] Simple Average of Value Line, Zacks earnings and BR+SV growth rates.

[3] Spot-Date Adjusted Stock Price. See Exhibit 10.6.

[4] Adjusted Price=0.9582*Ex-Div Price. Adjustment based on flotation cost of 4.18 percent.

[5] Calculated using Quarterly DCF Formula: Cost of Equity (k_e) = $\{[Q_t^*(1+ke)^{0.75}+Q_t^*(1+ke)^{0.5}+Q_t^*(1+ke)^{0.25}+Q_t]/P_0\}$

[6] Not adjusted for selling and issuance expenses.

[7] ROE adjusted by selling and issuance expenses.

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Nicor Gas Company
Comparable Group
Capital Asset Pricing Model (CAPM)

<u>No. Company</u>	<u>30-Year T-Bond Return (Rf)¹</u>	<u>Beta Value Line²</u>	<u>Market Risk Premium</u>	<u>CAPM Cost of Equity⁵</u>
			<u>Top-Down DCF - 30 Yr T- Bond Return^{3,4}</u>	<u>Top-Down DCF - 30 Yr T-Bond Return</u>
	%			%
1 Avista Corp.	4.59	0.90	10.35	13.90
2 MGE Energy	4.59	0.95	10.35	14.42
3 Nicor	4.59	0.95	10.35	14.42
4 Northwest Nat. Gas	4.59	0.80	10.35	12.87
5 Piedmont Natural Gas	4.59	0.85	10.35	13.39
6 Southwest Gas	4.59	0.90	10.35	13.90
7 Vectren Corp.	4.59	0.90	10.35	13.90
8 Wisconsin Energy	4.59	0.80	10.35	12.87
Average		0.88		13.71

Notes:

[1] From *The Value Line Selection and Opinion*, July 25, 2008.

[2] *The Value Line Investment Survey*, June 13, June 27, and August 13, 2008.

[3] The formula used is Risk Premium = $[(Do * (1+g)) + g] - Rf$

[4] Dividend yield for S&P 500 is from Standard & Poors Online, Indices, S&P 500, Month End Data. See Exhibit 10.15. Five-year earnings growth rate is from Reuters

[5] Cost of Equity = $Rf + Beta (RM - Rf)$, where Rf is the return on the 30-year Treasury Bond, and (RM - Rf) is the market premium computed as described in footnote [3] and [4].

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Nicor Gas Company
Comparable Group
Capital Asset Pricing Model (CAPM)

No.	Company	30-Year T- Bond Return (Rf) ¹ %	Beta Value Line ²	Market Risk Premium	CAPM Cost of Equity ⁴
				(I/S) ³ 1926-2007	Value Line, (I/S) 1926-2007 %
1	Avista Corp.	4.59	0.90	6.42	10.37
2	MGE Energy	4.59	0.95	6.42	10.69
3	Nicor	4.59	0.95	6.42	10.69
4	Northwest Nat. Gas	4.59	0.80	6.42	9.73
5	Piedmont Natural Gas	4.59	0.85	6.42	10.05
6	Southwest Gas	4.59	0.90	6.42	10.37
7	Vectren Corp.	4.59	0.90	6.42	10.37
8	Wisconsin Energy	4.59	0.80	6.42	9.73
	Average		0.88		10.25

Notes:

[1] From *The Value Line Selection and Opinion*, July 25, 2008.

[2] *The Value Line Investment Survey*, June 13, June 27, and August 13, 2008.

[3] Computed as the difference between the arithmetic averages of annual returns over the periods 1926-2007 from [a] large company stocks, and [b] long-term government bonds, from Ibbotson Associates, 2007 Yearbook.

[4] Cost of Equity = Rf + Beta (RM - Rf), where Rf is the return on the 30-year Treasury Bond, and (RM - Rf) is the market premium computed as described in footnote [3].

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Nicor Gas Company
DCF of the S&P 500

Dividend Yield S&P 500 ¹	2.27 %
Growth Rate S&P 500 ²	12.28 %
DCF S&P 500 ³	14.83 %
Issuance Expense ⁵	0.11 %
Total DCF S&P 500⁴	14.94 %

Notes:

[1] From Standard & Poor's S&P 500 Earnings and Estimate Report at http://www2.standardandpoors.com/portal/site/sp/en/us/page.topic/indices_500/2,3,2,2,0,0,0,0,5,11,0,0,0,0.html

[2] Reuters, August 29, 2008.

[3] $DCF = (Div\ Yield * (1 + Growth)) + Growth$

[4] $Total\ DCF = ((Div\ Yield\ S\&P\ 500) * (1 + Growth\ Rate\ S\&P\ 500)) / (1 - Average\ Issuance\ Expense) + Growth\ Rate\ S\&P\ 500$

[5] Average Issuance Expense: Calculated in Exhibit 10.12

"X" Marks the Spot

How to calculate price caps for the distribution function.

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Exhibit No. 25.11

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WHEN THE CALIFORNIA PUBLIC UTILITIES COMMISSION approved a price-cap plan for Southern California Edison's distribution operations, it lamented the lack of a "distribution-only" study on productivity. So we prepared one. Unlike electricity generation, electricity distribution will remain a regulated business. But the form of regulation likely will change to price caps, mirroring events in telecommunications regulation here and energy regulation abroad.

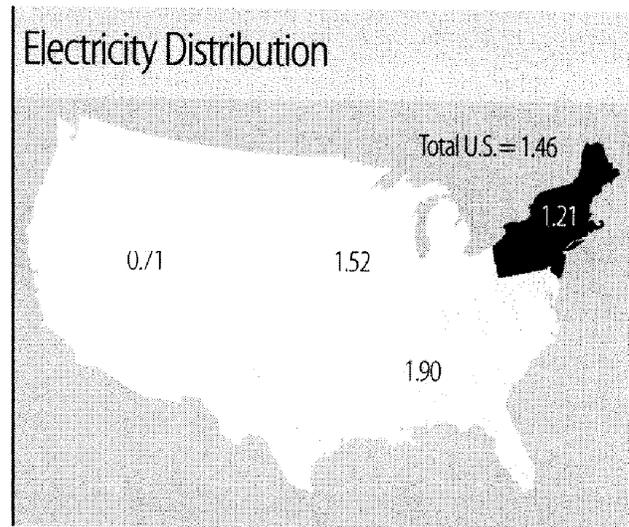
With price caps, rates are reviewed formally only at set intervals. In the meantime, rates move via a pre-set formula which looks at inflation and productivity (i.e., Retail Price Index minus "X"). Price caps break the link between costs and prices by providing more competition-style efficiency incentives for regulated companies.

Key to the price cap formula is "X," which reflects productivity growth. The best and most objective basis for such an index is "Total Factor Productivity." That is, the TFP for an industry, minus the corresponding TFP for the economy, reveals the best measure of X to calculate a price cap.

Electricity distribution presents a challenge for measuring productivity since, as a rule, the industry is vertically integrated. Only a few electric utilities operate separate distribution businesses.

Using Federal Energy Regulatory Commission Form 1 data, we created a cost-of-service study to compare the distribution component of each integrated electric utility (for 87 companies over 23 years). For the entire country, we found an average TFP-based X of 1.46 percent (after subtracting a 0.40 percent economy-wide TFP). More importantly, we found significant differences among companies based on region and use per customer. The regional differences are shown in the figure.

In recommending a value for productivity in the price-cap formula, Edison had put forward values of 0.9 percent



Source: Jeff D. Makholm, Michael J. Quinn, "Price Cap Plans for electricity Distribution Companies Using TFP Analysis," NERA Working Paper (July 23, 1997)

for nongeneration functions and 1.4 percent for the total system, including generation. It then added a so-called "stretch" factor, to boost the two figures to 1.4 (nongeneration) and 1.8 (total system).

The PUC ended up approving a productivity factor for transmission and distribution of 1.2 percent for 1997, 1.4 percent for 1998 and 1.6 percent for the years 1999 through 2001. These values will apply to both the nongeneration performance-based rate and its ultimate successor, the distribution PBR. See, *Decision 96-09-092, Sept. 20, 1996, 172 PUR4th 393 (Cal.P.U.C.)*

Price caps are the new kid on the block in regulation. Targeting distribution activities may make price caps easier to apply in electricity. **F**

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