Docket No. 08-0363
ICC Staff Exhibit 15.0

REBUTTAL TESTIMONY

of

Dianna Hathhorn
Accountant

Accounting Department
Financial Analysis Division
Illinois Commerce Commission

Northern Illinois Gas Company
d/b/a Nicor Gas Company

Proposed General Increase in Gas Rates

Docket No. 08-0363

October 23, 2008

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Witness Dianna Hathhorn
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SCHEDULES

Schedule 15.01 Pension Asset Adjustment
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ATTACHMENTS

Attachment A Exhibit 2 to Company response to Staff Data Request DLH-15.01
Attachment B Company response to Staff Data Request ENG-1.08
Attachment C Excerpt from Company 2004 ILCC Form 21
Attachment D Company response to Staff Data Request DLH-27.12
Attachment E Company responses to Staff Data Requests PL 1.09, DLH-25.02, and DLH-27.09
Attachment F Nicor Gas Operating Agreement

Witness Identification

Q. Please state your name and business address.

A. My name is Dianna Hathhorn. My business address is 527 East Capitol Avenue, Springfield, Illinois 62701.

Q. Have you previously filed testimony in this proceeding?

A. Yes, my direct testimony is ICC Staff Exhibit 2.0.

Purpose of Testimony

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is as follows:

1. to update my uncontested Invested Capital Taxes Adjustment for Staff's rebuttal position;
2. to respond to Northern Illinois Gas Company's ("Nicor Gas" or "Company") opposition to my adjustments regarding the pension asset, uncollectibles expense, and incentive compensation expense;
3. to respond to Mr. David Effron, the witness for the People of the State of Illinois represented by the Attorney General and the Citizens Utility Board ("AG/CUB") regarding his payroll adjustment that Nicor Gas opposes;

23 4. to propose an adjustment for Nicor Services billing rates due to
24 information discovered after the filing of my direct testimony;
25 5. to respond to Nicor Gas' proposed revisions to Riders QIP,
26 UEA, CUA, and FCA;
27 6. to respond to the Company concerning its accounting for gas
28 storage losses;
29 7. to respond to the Company concerning my recommendation for
30 affiliated interest transaction reporting; and
31 8. to discuss affiliated interest transaction issues resulting from
32 information discovered after the filing of my direct testimony.
33

34 **Schedule Identification**

35 Q. Are you sponsoring any schedules with your rebuttal testimony?

36 A. Yes. I prepared the following schedules that show data as of, or for the
37 test year ending December 31, 2009:

38 Schedule 15.01 Pension Asset Adjustment
39 Schedule 15.02 Uncollectibles Expense Adjustment
40 Schedule 15.03 Incentive Compensation Adjustment
41 Schedule 15.04 Invested Capital Taxes Adjustment
42 Schedule 15.05 Nicor Energy Services Billing Adjustment
43

44 Q. Have you included any attachments as part of your rebuttal testimony?

A. Yes, I have included the following Company responses to Staff data requests ("DR"):

Attachment A	Exhibit 2 to Company response to Staff Data Request DLH-15.01
Attachment B	Company response to Staff Data Request ENG-1.08
Attachment C	Excerpt from Company 2004 ILCC Form 21
Attachment D	Company response to Staff Data Request DLH-27.12
Attachment E	Company responses to Staff Data Requests PL 1.09, DLH-25.02, and DLH-27.09
Attachment F	Nicor Gas Operating Agreement

Uncontested Adjustment

Q. Did the Company accept in its rebuttal testimony any adjustments proposed in your direct testimony?

A. Yes. Nicor Gas agreed with my proposal to calculate the incremental increase in State invested capital taxes based upon the final Commission approved rate of return and rate base. (Co. Ex. 26.0, p. 47) Therefore, I have updated my calculation for Staff's rebuttal positions and reflected the adjustment on Schedule 15.04, Invested Capital Taxes Adjustment.

Contested Adjustments

Pension Asset Adjustment

Q. Please describe Schedule 15.01 Pension Asset Adjustment.

A. Schedule 15.01 revises my Schedule 2.01 to present a net $141.524 million adjustment to exclude the Company's pension asset from rate base

since it is not provided by shareholder supplied funds. The revision reflects the update proposed in Co. Ex. 26.0.

Q. The Company states it continues to believe that inclusion of the pension asset in rate base is warranted. (Co. Ex. 26.0, p. 21) Do you agree?

A. No. The Company has presented no new evidence to reverse the prior two Nicor Gas rate orders[1] which exclude the pension asset from rate base. The Company's position that a court decision in the pending Commonwealth Edison Company ("ComEd") appeal will most likely resolve the pension asset issue is unconvincing since the facts[2] of the two companies are so dissimilar.

Q. Nicor Gas disagrees that the ComEd pension asset facts are different than those of Nicor Gas. (Co. Ex. 26.0, pp. 21-22) What material facts do you believe distinguish the two cases from each other?

A. The test year $803 million cash contribution[3] from Exelon, ComEd's parent company, to ComEd caused the pension asset issue in Docket No. 05-0597. The facts in the Nicor proceeding can be distinguished on 2 bases. First, the test year cash contribution from Nicor Gas' parent company or Nicor Gas itself in the instant proceeding is zero.[4] Additionally, it is necessary to review the source of the funds that gave rise to the pension

[1] Staff Ex. 2.0 at 4
[2] Id., p.9
[3] Docket No. 05-0597 Order on Rehearing, Dec. 20, 2006

92 asset. In the case of ComEd, the cash contribution that created the
93 pension asset was made with shareholder monies. In the instant case, no
94 cash contributions were necessary due to the existing pension asset that
95 was created with ratepayer supplied funds in prior years. This refutes Mr.
96 Gorenz's assertion that "in both cases, Nicor Gas and ComEd have
97 pension assets which were created by cash outflows (i.e., contributions to
98 the pension trust) made by the Company." (Co. Ex. 26.0, p. 22) The
99 relevant question is not whether the Company made its required pension
100 contributions, but rather what the source of those contributions was. In
101 the case of ComEd, it was shareholder monies and in the case of Nicor
102 Gas, it was revenues collected from ratepayers.
103
104 Q. The Company states, in addition to preserving its rights, it is responding to
105 "new arguments" presented by you relating to the inclusion of the pension
106 asset in rate base. (Co. Ex. 26.0, p. 21) Do you believe you have made
107 new arguments?
108 A. No, I believe this statement mischaracterizes my testimony. Rather, my
109 testimony elaborates on the pension accounting and ratemaking policies
110 that support the Commission's conclusions in the prior two rate orders.
111
112 Q. The Company states concerns and general comments regarding your
113 testimony that the Commission does not have to follow Generally

[4] No cash contributions have been made since 1995, and prior to that, 1987. Staff Ex. 2.0 at 5 and Attach. A, p. 2 of Staff Ex. 2.0

Accepted Accounting Principles ("GAAP") for rate recovery. (Co. Ex. 26.0, p. 22) Please respond.

A. My intention was not to advocate against GAAP in this case but to point out that the Commission has that option, and that any discussion of GAAP and rate recovery should recognize such possibility exists.

Q. Mr. Gorenz states that it is my position that in order to determine the actual cumulative pension credit, Commission rates and orders back to 1954 would need to be analyzed, and suggests such analysis is retroactive ratemaking. (Co. Ex. 26.0, p. 23) Please respond.

A. Mr. Gorenz's testimony incorrectly implies that I propose to determine the actual cumulative pension credit by analyzing rates and Commission orders back to 1954. The Company conducted an analysis of cumulative pension obligations (which resulted in $108 million) that it claims reduced operating expense from 1954-2009. My testimony simply is that such analysis is flawed because the Company would have had to file a rate case each and every year since 1954 to arrive at a $108 million result. (Staff Ex. 2.0, lns. 160-168) It is uncontested that such annual rate cases did not occur; therefore, the result of the Company's analysis should be some other number than $108 million. While I do not endorse the Company's analysis, I simply pointed out that an analysis of past Commission orders and rates would be necessary to determine a result that would be more accurate than the Company's $108 million figure.

Interestingly, Mr. Gorenz's point of retroactive ratemaking would apply to the Company's position that it should get $108 million because it is based upon its claim that it reduced operating expense by that much from 1954-2009.

Nevertheless, it appears further clarification of my statement with which Mr. Gorenz takes issue is necessary at this point. The pension credit to operating and maintenance expenses in Nicor Gas' last rate case was set based on a future test year 2005, roughly $6 million according to Co. Ex. 26.0, p. 23. In 2006 and 2007, the Company's pension credit rose to $9.8 and $11.3 million, respectively. However, base rates did not change. Therefore, it is inaccurate to state that, for example, in 2007 ratepayers received an $11.3 million credit for pension expense, since the amount recovered in base rates did not change. My testimony simply recognizes this fact; I do not suggest nor recommend any retroactive ratemaking actions, as the Company contends.

Q. The Company disagrees with your testimony that it is not out any money due to the credits charged to ratepayers since there is no offsetting cash inflow realized by the Company. (Co. Ex. 26.0, pp. 23-24) Why is there no cash inflow when the Company experiences a pension credit?

A. A pension credit results when the Company's expected return on its assets exceeds the service and interest costs of the period, as well as

prior period amortizations of gains or losses. Stated differently, this means that the Company has earned more money in its pension trust fund than it has incurred obligations for its pension trust fund. Although the pension credit reduces the current revenue requirement, it does not take money away from the Company or the shareholders because there is no need to fund the pension currently; thus the revenue requirement is lower than if the pension needed to be funded. The shareholders are unaffected; if the pension needed to be funded the revenue requirement would increase, but shareholders would not benefit. Similarly since there is a pension credit, the revenue requirement is lower as it does not include pension expense, but again, the shareholders are not harmed. To suggest that the Company is out money when it experiences a pension credit misrepresents the facts.

Uncollectibles Expense Adjustment

Q. Please describe Schedule 15.02 Uncollectibles Expense Adjustment.

A. Schedule 15.02 presents my adjustment to operating expense to lower the projected test year uncollectibles expense percentage from 2.25% to 2.02%, as discussed in my direct testimony.[5] The Company's rebuttal testimony provides no change in its projection of $68,900,000 of charge offs for 2009.[6] Further breakdown of the Company's proposal is shown on

[5] Staff Ex. 2.0 at 10-11
[6] Co. Ex. 21.1 and Co. Resp to Staff DR DLH-29.06

181 Attach. A-Ex. 2 to Co. Resp. to Staff DR DLH-15.01. The 2009 budgeted
182 charge offs are increased 25% due to the economy and increased cost of
183 gas. This increase is on top of the 33% increase to 2008 charge offs for
184 the same factors. The 2009 25% contingency factor results in an increase
185 of $13,887,500 over the regularly budgeted charge offs that are already
186 $8,225,000 ($72,050,000-$63,825,000) higher than the 2008 projection
187 due to the cost of gas.
188
189 Q. Have you reviewed the AG/CUB Uncollectibles Expense Adjustment
190 sponsored by Mr. Effron (AG/CUB Ex. 1.0, pp. 22-25)?
191 A. Yes. I agree with the AG/CUB that an adjustment is necessary; however, I
192 prefer my methodology since the AG/CUB proposed uncollectibles
193 expense adjustment appears to give no weight to the 2008 actual activity
194 and treats 2007 data as an outlier.
195

196 **Incentive Compensation Adjustment**

197 Q. Did the Company accept in rebuttal testimony your Incentive
198 Compensation Adjustment?
199 A. The Company accepted one subpart of my adjustment related to incentive
200 compensation expense included in Nicor Gas' consolidated pool charges.
201 (Co. Ex. 26.0, p. 30) It also corrected my calculation of payroll taxes
202 related to the consolidated pool charges. (Co. Ex. 26.1, Sch. 1.04) I agree

203 with the Company's correction. The Company contested the other two
204 subparts of my adjustment, which I respond to below.
205
206 Q. Please describe Schedule 15.03 Incentive Compensation Adjustment.
207 A. Schedule 15.03 reflects my proposed adjustment to reduce the
208 Company's operating expenses and rate base for Incentive
209 Compensation Units ("ICU") plan costs related to shareholder-oriented
210 goals and for half the costs related to one performance goal unlikely to
211 be achieved at its 100% target level.
212
213 Q. The Company opposes your adjustment for the ICU Plan because it
214 "fulfills a legitimate purpose, has been approved in previous rate cases
215 and is not excessive." (Co. Ex. 22.0, p. 2) Have the ICU Plan costs rate
216 recovery been a contested issue in the Company's previous rate
217 cases?
218 A. No. (Co. Resp. to Staff DR DLH-29.02)
219
220 Q. Do you agree with the Company that the ICU Plan fulfills a legitimate
221 purpose?
222 A. I disagree with the Company's criteria for rate recovery of incentive
223 compensation expense. My opinion is based on several Commission
224 orders which expressly state that: a) costs paid out solely on
225 achievement of financial goals should be paid by shareholders and b)

226 costs of achievement of non-financial goals must demonstrate tangible
227 benefits to ratepayers.[7] The ICU Plan fails both tests as its payout is
228 100% tied to financial goals, and the plan cannot benefit ratepayers
229 since the employees no longer work for the Company.
230
231 Q. Do you agree with the Company that the ICU Plan cost is not
232 excessive?
233 A. Again, I disagree with the Company's criteria for rate recovery of
234 incentive compensation expense. My adjustment is not based on the
235 amount of the ICU Plan, but rather on the Commission orders
236 discussed above. An expense may not be excessive, but due to
237 Commission orders or law, it is not allowable in rates. Lobbying
238 expenses are an example of this scenario, since they are barred from
239 rate recovery no matter the amount.[8] The Commission orders that I
240 discussed in direct testimony did not appear to base their conclusions
241 on the amount of the adjustment but rather on the facts of the specific
242 incentive compensation plans at issue.
243
244 Q. Have you reviewed the Company rebuttal by Ms. Bacidore (Co. Ex. 22.0,
245 pp. 2-3) regarding your adjustment to disallow recovery for incentive
246 compensation costs related to the at-fault hit ratio per 1,000 locates?

[7] Staff Ex. 2.0 pp. 15-19
[8] Section 9-224 of 220 ILCS 5 Public Utilities Act

A. Yes. Ms. Bacidore points out that while the target ratio for a 100% payout has not been achieved from 2004 through 2007, the Company did achieve average ratios in that time period which resulted in a 50% payout. Therefore, as it appears the Company is likely to achieve the 50% payout level of this goal in the future, I have reduced my adjustment to reflect disallowance of only 50%, rather than all, the costs of this goal. This calculation is reflected on page 3 of Schedule 15.03.

Payroll Expense Adjustment

Q. Have you reviewed the AG/CUB Payroll Expense Adjustment sponsored by Mr. Effron (AG/CUB Ex. 1.0, pp.18-21)?

A. Yes.

Q. Do you agree with the proposed adjustment?

A. No. My review of Co. Ex. 18.0, its supporting workpaper, and additional discovery on that workpaper resulted in a conclusion that corroborates the Company's position that its test year headcount is reasonable.

Nicor Energy Services Billings Adjustment

Q. Do you agree with CEAFUR witness Schramel that a revenue adjustment may be necessary to reflect that Nicor Gas bills Nicor Energy Services ("Nicor Services") a rate that is lower cost than the tariffed charge of $0.25? (CEAFUR Schramel Direct p. 13)

A. Yes.

Q. Please describe Schedule 15.05, Nicor Energy Services Billings Adjustment.

A. Schedule 15.05 presents my adjustment to reduce operating expenses resulting from calculating Nicor Gas' billing services charges to Nicor Services at prevailing price rather than fully distributed costs. The Company's testimony at Co. Ex. 32.0, p. 4 and the Company's response to Staff DR PL 1.09 (Staff Ex. 15.0-Attach. E) describe how Nicor Gas provides billing services to both Nicor Solutions and Nicor Services. Nicor Gas simply states that it charges Nicor Services fully distributed costs rather than prevailing price because there is no prevailing price for such services. (Co. Ex. 32.0 lns. 86-89) The only difference explained by the Company is that Nicor Solutions uses a different billing system than Nicor Services. (Attach. E-Co. Resp. to Staff DR DLH-27.09) Use of a different billing system is not sufficient to justify why Nicor Gas charges Nicor Services only fully distributed costs rather than a prevailing price for what appears to be the same billing services to Nicor Services:

> "The billing services that Nicor Gas provides for each non-utility affiliate are as follows:
>
> - Nicor Energy Services and Nicor Solutions – printing, mailing, cash remittance processing and customer inquiry services for the affiliates' customers who are billed via Nicor Gas' utility bill."[9]

Nicor Gas bills the following rates for these services:

294

Billing Services Charged to Nicor Solutions' Customer Select Suppliers	Prevailing Price	$0.25 per bill
Billing Services Charged to Nicor Services for HVAC and GLCG business[10]	Fully Distributed Cost	$0.112 per bill

295

296 Q. How did you calculate your adjustment in Schedule 15.05?

297 A. Since Nicor Solutions' prevailing price is approximately double the fully
298 distributed cost rate, I doubled the test year charges to Nicor Services to
299 reflect the prevailing price. The adjustment reduces the test year revenue
300 requirement, consistent with the Company's treatment of such revenues.[11]

301

302 **Recommendations Regarding Nicor Gas' Proposed Riders QIP, UEA, and**
303 **CUA and Existing Rider FCA**

304 Q. Has the Company accepted your recommendations concerning Nicor Gas'
305 proposed Riders QIP, UEA, and CUA and existing Rider FCA?

306 A. Yes. (Co. Ex. 29.0, pp. 58, 50, 51, and 48, respectively)

307 **Recommendations Regarding Nicor Gas' Accounting for Storage Gas**
308 **Losses**

309 Q. Please summarize your recommendations from direct testimony.

---

[9] Co. Resp. to Staff DR PL 1.09 (Staff Ex. 15.0, Attachment E).
[10] Co. Ex. 32.0 at 4; HVAC stands for heating, ventilation and air conditioning and GLAC for gas line comfort guard.
[11] Co. Ex. 32.0, p. 5 lines 90-94

310 A. I recommended that, in the future, Nicor Gas be required to record gas
311 losses in compliance with the Uniform System of Accounts for Gas
312 Utilities Operating in Illinois, 83 Ill. Adm. Code 505 ("USOA") according
313 to the nature of the loss, with physical losses expensed in the period
314 incurred in Account 823 Gas Losses, and adjustments for underground
315 storage field performance variations recorded in rate base Account
316 352.3 Non-recoverable natural gas and subject to depreciation.[12] I also
317 concurred with Staff witness Anderson's recommendation for a written
318 policy to be formulated regarding underground storage adjustments or
319 corrections and that the written policy specify the proper accounting
320 treatment based on the type of gas losses.[13]
321

322 Q. Has the Company accepted your recommendations concerning Nicor Gas'
323 accounting for storage gas losses?
324 A. I do not believe so. Nicor witness Gorenz states he agrees, subject to
325 any accounting changes to be applied prospectively. (Co. Ex. 26.0, p. 53)
326 Staff agrees that any changes in Nicor Gas' accounting for gas storage
327 losses should be applied prospectively. However, Mr. Gorenz also states
328 his agreement is "subject to a study being conducted after the conclusion
329 of this proceeding." Id. Nicor Gas witness Bartlett seems to oppose the
330 accounting change and would so implement it only if ordered by the
331 Commission:

[12] Staff Ex. 2.0 at 34

> "While Nicor Gas does not believe that a split is necessary, in the event that the Commission finds that a split of the losses should be determined, the Company would agree to conduct a study directed toward developing a reasonable estimate of the surface losses by field based on typical operations." Co. Ex. 19.0 at 11 (Emphasis added)

Since the Company's position appears to be that it will only change its accounting if ordered by the Commission to conduct a study, the Company has not agreed with my position.

Q. The Company describes how it has consistently charged operating expense for gas storage losses since the 1960s, and that the only change has been from recovering gas losses through its purchased gas adjustment ("PGA") clause to Account 823 in base rates. (Co. Ex. 26.0 at 52) Has the Company made past adjustments to Account 352.3 for performance variations?

A. Yes. According to Staff witness Anderson[14], the inventory correction included in Attach. B-Co. Resp. to Staff DR ENG-1.08 represents a performance variation, and the Company recorded an adjustment from recoverable to non-recoverable base gas. (See Attach. C-Excerpt from the Company's 2004 ILCC Form 21) Since the Company has made this type of adjustment to non-recoverable base gas in the past, I do not understand why it objects to doing so again unless ordered by the Commission.

---

[13] Id. at 35
[14] Staff Ex. 22.0

Q. Has the Commission recently recognized the fact that there are two types of storage losses and that they should be recorded separately as the USOA requires?

A. Yes. The Ameren rate case order conclusion states:

> "The record supports the accounting perspective that a portion of the gas losses should, in all likelihood, be recorded as a rate base item with the remainder recorded as an operating item." (Order, Docket Nos. 07-0585 et al. (Cons.), September 24, 2008, p.73)

Q. Has the Company accepted your recommendation for Nicor Gas to develop a written policy specifying the proper accounting treatment based on the type of gas losses?

A. Again, I do not believe so. While Company witness Gorenz agrees with my recommendation (Co. Ex. 26.0, p. 54), his agreement is contingent upon a study of storage gas losses being completed, which Company witness Bartlett opposes.

Q. At Co. Ex. 27 p. 17, the Company criticizes AG/CUB witness Rubin's suggestion that Nicor Gas has available an alternative accounting method for Account 823 rather than its proposed Company Use Adjustment ("CUA") Rider. Does the USOA provide that the Company can amortize a substantial adjustment to Account 823 with Commission approval?

380 A. Yes. Amortization does not provide the Company instant recovery of its
381 costs, as it seeks with Rider CUA, but it does provide an opportunity to
382 recover the amortized amount should that amount be reflected in a test
383 year. The Company criticizes this option as not allowing recovery of the
384 higher costs and merely postponing recognition of costs over an
385 amortization period. (Co. Ex. 27.0 at 17) While the Company is correct
386 that amortization of Account 823 does not provide for the dollar for dollar
387 protection it seeks with Rider CUA, it is an option available to the
388 Company should it experience a large adjustment due to the cost of gas.
389

390 **Recommendation for Reporting of Affiliated Interest Transactions**

391 Q. Has the Company accepted your recommendations concerning Nicor Gas'
392 reporting of affiliated interest transactions?
393 A. Yes, so long as the form and substance of the report is consistent with Co.
394 Ex. 26.3 and the Part 285 filing requirements for Schedule C-13. (Co. Ex.
395 26.0, p. 55) I agree with these reporting formats.
396

397 **Concerns Regarding Affiliate Interest Transactions**

398 Q. Have you reviewed CEAFUR witness Schramel's testimony and the
399 Company's related supplemental rebuttal testimony, Co. Exs. 32.0, 33.0,
400 and 34.0?

401 A. Yes. These testimonies prompted Staff to issue data requests pertaining
402 to affiliated transaction issues. The Company's responses suggest
403 deficiencies in the Company's affiliate transaction agreement approved in
404 Docket No. 00-0537, known as the Operating Agreement. (Attach. F). The
405 allegations made in Schramel's testimony are serious enough to warrant
406 Commission consideration of that Operating Agreement. I have concerns
407 about the agreement as well, discussed below. My concerns about the
408 agreement now in effect are significant enough to cause me to propose
409 that a proceeding should be initiated within 120 days of an order in this
410 proceeding to investigate whether the Company's Operating Agreement is
411 in the public interest and make to appropriate revisions. The proceeding,
412 at a minimum, should investigate the following issues:

413 1) Criteria for when it is appropriate to apply the prevailing price and
414 when it is appropriate to only charge fully distributed costs;

415 2) Consideration of Nicor Gas employees that are dedicated full-time
416 to Nicor Gas' affiliates;

417 3) Facilitation of affiliate endeavors through utility activities; and

418 4) Annual reporting and auditing requirements to the Commission.

419

420 Q. Do you have adjustments based upon these concerns?

421 A. Yes, my adjustment in Schedule 15.05 concerns my first point above.
422 However, I do not have sufficient information to make further adjustments
423 in this proceeding. Rather than recommending further adjustments, I am

recommending that an investigation be initiated to revise the Operating Agreement where appropriate as necessary to be consistent with the public interest.

Q. Discuss the issue of Nicor Gas employees who solely work for its affiliates.

A. Nicor Gas employed 46 individuals at 12/31/2007 who were employees of Nicor Gas for payroll and benefit plan eligibility purposes but who were fully dedicated to the business of Nicor Enerchange (33 individuals) and Nicor Inc. (13 individuals). (Attach. D-Co. Resp. to Staff DR DLH-27.12) The Company claims that all the costs of these individuals were charged to the affiliates, and that because these work groups are small, it is more efficient to utilize the Nicor Gas payroll system to pay them and also provide them with retirement and welfare benefits. (Id.) There is insufficient time in this proceeding to verify that Nicor Gas appropriately accounts for individuals devoted to its affiliates.

Further, the Operating Agreement provides that Nicor Gas and its affiliates be billed monthly for Consolidated Pool charges, such as accounting, finance, legal, and information systems. The Consolidated Pool charges are billed on a two-factor methodology of gross payroll and total assets. Therefore, even if Nicor Gas is recovering its fully distributed costs of the 46 employees from its affiliates, there is a risk that Nicor Gas' share of the Consolidated Pool charges is overstated unless that calculation reduces

447 Nicor Gas' gross payroll for the affiliate personnel. It is likely that Nicor
448 Gas should also reduce its total assets factor as well, to reflect the
449 computer, telephone, and other assets used by the 46 individuals. In a
450 proceeding to investigate and re-approve Nicor Gas' Operating
451 Agreement, this issue could be fully vetted and any necessary changes to
452 the Operating Agreement approved by the Commission.
453
454 Q. What concerns do you have with respect to facilitation of affiliate
455 endeavors through utility activities?
456 A. As discussed further by Staff witness Sackett (Staff Ex. 24.0), the use of
457 the utility's call center and Web site to facilitate affiliate endeavors while
458 withholding similar functions for non-affiliated companies needs to be
459 investigated.
460
461 Q. Discuss the issue about reporting and auditing requirements.
462 A. The Operating Agreement contains no reporting to the Commission of its
463 activity and charges, nor any internal audit requirements. Reporting and
464 monitoring are keys to ensuring there is no cross-subsidization by the
465 utility to its affiliates.
466
467 Presently in a rate case, Staff must begin with nearly no data at all in
468 reviewing all of the affiliated interest transactions approved in the
469 Operating Agreement. To date, the Operating Agreement involves at least

470 the following affiliate transactions that Nicor Gas provides to its affiliates:
471 (See generally Co. Exs. 32.0 and 33.0)
472 a) Billing to Nicor Solutions;
473 b) Billing to Nicor Services;
474 c) Initial and ongoing programming costs for Nicor Services;
475 d) Software application support and website maintenance services
476 for the Nicor Inc. website;
477 e) Sales and repair services for Nicor Services;
478 f) Data license agreement to Nicor Advanced Energy; and
479 g) Fully devoted personnel as described in Attach. D
480 In addition, Nicor Gas receives services from IBT Solutions LLC ("IBT") for
481 processing of a portion of inbound customer calls. IBT also provides sales
482 services to Nicor Services. Nicor Gas also receives services from Nicor
483 Inc. for Consolidated Pool charges.
484
485 In a the proceeding to review the affiliate agreement, the Operating
486 Agreement should be updated to reflect the monitoring, reporting and
487 auditing necessary so that Staff can ensure compliance. Section 4.0 of
488 the updated affiliated interest agreement approved in Docket No. 07-0361
489 for The Peoples Gas Light and Coke Company and North Shore Gas
490 Company is an example of the monitoring, reporting, and auditing tools
491 which are needed for Staff to assess compliance with the agreement.
492

493 **Conclusion**

494 Q. Does this conclude your prepared rebuttal testimony?

495 A. Yes, it does.

VERIFICATION

I, Dianna Hathhorn, being first duly sworn, depose and state that I am an Accountant in the Accounting Department of the Financial Analysis Division of the Illinois Commerce Commission; that I sponsor the foregoing Rebuttal Testimony of Dianna Hathhorn; that I have personal knowledge of the information stated in the foregoing Rebuttal Testimony; and that such information is true and correct to the best of my knowledge, information and belief.

Dianna Hathhorn
Accountant
Illinois Commerce Commission

Subscribed and sworn to before me
this 23rd day of October, 2008.

Mary Ellen Ruffner
Notary Public

OFFICIAL SEAL
MARY ELLEN RUFFNER
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:02/04/09

Nicor Gas Company
Pension Asset Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description	Amount	Source
	(a)	(b)	(c)
1	Pension Asset per Staff	$ -	
2	Pension Asset per Company	231,625	Co. Ex. 26.0, p. 20, line 443
3	Staff Proposed Adjustment to Rate Base	$ (231,625)	Line 1 - line 2
4	Accumulated Deferred Income Taxes per Staff	$ -	
5	Accumulated Deferred Income Taxes per Company	(90,101)	Co. Ex. 11.0, p. 16 & Sch. B-1.2+ Co. Ex. 26.1, p.4, col. (B)
6	Staff Proposed Adjustment to Rate Base	$ 90,101	Line 4 - line 5
7	Net Rate Base Adjustment per Staff	$ (141,524)	Line 3 + line 6

Nicor Gas Company
Uncollectibles Expense Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description	Amount	Source
	(a)	(b)	(c)
1	Uncollectibles Expense per Staff	$ 61,330	Line 6
2	Uncollectibles Expense per Company	68,311	Schedule C-16, col. (J), line 5
3	Staff Proposed Adjustment to Uncollectibles Expense	$ (6,981)	Line 1 - line 2
4	Revenue Used in Calculation	$ 3,036,130	Schedule C-16, col. (I), line 5
5	Uncollectibles Expense Percent per Staff	2.02%	
6	Uncollectibles Expense per Staff	$ 61,330	Line 4 x line 5

Nicor Gas Company
Incentive Compensation Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description (a)	Amount (b)	Source (c)
	Summary:		
1	Incentive Compensation Expense per Staff	$ -	
2	Incentive Compensation Expense per Company	378	Staff Ex. 15.0, Sum of Sch. 15.03, p. 2 line 3 and Sch. 15.03, p. 3, line 9
3	Staff Proposed Adjustment to Admin. & General Expense	$ (378)	Line 1 - line 2
4	Payroll Taxes on Incentive Compensation Expense per Staff	$ -	
5	Payroll Taxes on Incentive Compensation Expense per Company	29	Line 2 x 7.65%
6	Staff Proposed Adjustment to Taxes Other Than Income	$ (29)	Line 4 - line 5
7	Capitalized Incentive Compensation per Staff	$ -	
8	Capitalized Incentive Compensation per Company	15	Staff Ex. 15.0, Sch. 15.03, p. 3, line 8
9	Staff Proposed Adjustment to Gross Utility Plant in Service	$ (15)	Line 7 - line 8

Nicor Gas Company
Incentive Compensation Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description	Amount	Source
	(a)	(b)	(c)
	Incentive Compensation Units ("ICU") Plan		
1	ICU Expense per Staff	$ -	
2	ICU Expense per Company	325	Company response to Staff data request DLH-13.02
3	Staff Proposed Adjustment to Admin. & General Expense	$ (325)	Line 1 - line 2

Nicor Gas Company
Incentive Compensation Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description	Amount	Source
	(a)	(b)	(c)
	At-fault hit ratio per 1,000 locates goal:		
1	Target Amount for Officer Bonus Plan	$ 15	Company response to Staff data request DLH-9.10, Exhibit 1
2	Target Amount for Manager Incentive Plan	131	Company response to Staff data request DLH-9.10, Exhibit 1
3	Total for Goal	$ 146	Line 1 + line 2
4	Disallow 50%	50%	Co. Ex. 22.0 p 3; Staff Ex. 15.0
5	Sub-Total	$ 73	Line 3 x line 4
6	Amount Charged to Affiliates (Line 5 x 6%)	4	Company response to Staff data request DLH-16.02
7	Sub-Total	$ 69	
8	Amount Capitalized (Line 5 x 21%)	15	Company response to Staff data request DLH-16.02
9	Net Amount Charged to Expense	$ 53	Line 5 - line 6 - line 8

Northern Illinois Gas Company
Invested Capital Tax Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description (a)	Amount (b)	Source (c)
1	Rate Base	$ 1,336,817	Staff Ex. 14.0, Schedule 14.01, col. i, line 24
2	Rate of Return	7.35%	Staff Ex. 14.0, Schedule 14.01, col. i, line 25
3	Operating Income Required	$ 98,195	Line 1 x Line 2
4	Pro forma operating income at present rates adjusted before ICT adjustment	61,522	Staff Ex. 14.0, Schedule 14.01, col. d line 23 - Staff Ex. 14.0, Schedule 14.02, page 1, col. e line 16
5	Operating Income Additional Allowed	$ 36,673	Line 3 - line 4
6	Invested Capital Tax Rate	0.80%	Co. Ex. 11.1, p 6
7	Incremental Invested Capital Tax Impact per Staff	$ 293	Line 5 x line 6
8	Incremental Invested Capital Tax Impact per Company	664	Co. Ex. 26.1, Sch. 1.05, line 7
9	Staff Proposed Adjustment	$ (371)	Line 7 - line 8

Nicor Gas Company
Nicor Energy Services Billings Adjustment
For the Test Year Ending December 31, 2009
(In Thousands)

Line No.	Description	Amount	Source
	(a)	(b)	(c)
1	Adjustment to Customer Accounts Expense for Billings to Nicor Services per Staff	$ (588)	Co. Resp. to Staff DR DLH-25.02
2	Adjustment to Customer Accounts Expense for Billings to Nicor Services per Company	-	
3	Staff Proposed Adjustment	$ (588)	Line 1 - line 2

Nicor Gas Company
Budgeted 2008/2009 Charge Off

	2008		2009
Budgeted Revenue	$2,896,979,000		$3,036,130,000
Budgeted Gross Charge-Off (less bankruptcy)	$ 63,825,000		$ 72,050,000
Budgeted Bankruptcy	$ 4,500,000		$ 5,000,000
Budgeted Gross Charge-Off (before adjustments)	$ 68,325,000	(A)	$ 77,050,000
Budgeted Recoveries	$ 13,700,000	(B)	$ 12,000,000
Collection Programs	$ 7,500,000	(B)	$ 9,500,000
Budgeted Net Charge-Off (before adjustments)	$ 47,125,000		$ 55,550,000
33% (2008) and 25% (2009) increase to gross charge-off due to economy and higher GSC	$ 15,551,250	(A)	$ 13,887,500
	$ 62,676,250		$ 69,437,500
Additional recoveries on higher anticipated charge -off	$ 1,400,000	(B)	$ 500,000
Budgeted Net Charge-Off	$ 61,276,250		$ 68,937,500
Gross Charge-off	$ 83,876,250	(As)	$ 90,937,500
Recoveries	$ 22,600,000	(Bs)	$ 22,000,000

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
ENG First Set of Data Requests

ENG 1.08 Q. For each Company-owned storage field, provide the annual total (volume and dollars) amount of inventory storage corrections for the last ten years (1997-2006) broken down by account charged (e.g., 352.3, 823, etc.).

ENG 1.08 A. See attached Exhibit 1 for the total volume and dollars by storage field for the top to base gas reclassification that was made in 2004. The accounts charged are as follows:

101	Utility Plant	$1,971,180
117	Gas Stored Underground – Noncurrent	$78,666
164.1	Gas Stored Underground – Current	$(2,049,846)

There have been no other top to base gas reclassifications since 2004.

Witness: James M. Gorenz

NICOR GAS COMPANY	AN ORIGINAL	DECEMBER 31, 2004

GAS STORED (Account 117, 164.1, 164.2 and 164.3)

1. If during the year adjustment was made to the stored gas inventory (such as to correct cumulative inaccuracies of gas measurements), furnish in a footnote an explanation of the reason for the adjustment, the Mcf and dollar amount of adjustment, and account charged or credited.
2. Give in a footnote a concise statement of the facts and the accounting performed with respect to any encroachment of withdrawals during the year, or restoration of previous encroachment, upon native gas constituting the "gas cushion" of any storage reservoir.
3. *If the company uses a "base stock" in connection with its inventory accounting, give a concise statement of the basis of establishing such "base stock"* and the inventory basis and the accounting performed with respect to any encroachment of withdrawals upon "base stock," or restoration of previous encroachment, including brief particulars of any such accounting during the year.
4. If the company has provided accumulated provision for stored gas which may not eventually be fully recovered from any storage project, furnish a statement showing: (a) date of Commission authorization of such accumulated provision, (b) explanation of circumstances requiring such provision, (c) basis of provision and factors of calculation, (d) estimated ultimate accumulated provision accumulation, and (e) a summary showing balance of accumulated provision and entries during year.
5. Report pressure base of gas volumes as 14.73 psia at 60 degrees F.

Line No.	Description (a)	Noncurrent (Account 117) (b)	Current (Account 164.1) (c)	LNG (Account 164.2) (d)	LNG (Account 164.3) (e)	Total (f)
1	Balance at Beginning of Year	$ 50,339,797	$ 209,139,861			$ 259,479,658
2	Gas Delivered to Storage (contra account) *		687,648,975			687,648,975
3	Gas Withdrawn from Storage (contra account)		(705,712,797)			(705,712,797)
4	Other Debits or Credits (Net)**	78,666	(2,037,088)			(1,958,422)
5	Balance at End of Year	$ 50,418,463	$ 189,038,951			$ 239,457,414
6	Mcf	73,307,766	86,489,900			159,797,666
7	Amount per Mcf	$0.6878	$2.1857			$1.4985

8 *State basis of segregation of inventory between current and noncurrent portions:*

Current gas is gas in an underground storage field that is available for market.
Noncurrent gas is the portion of base gas that is expected to be economically recovered prior to abandonment of the aquifer.

*Column (c) includes an adjustment of $62,868 relating to a prior period adjustment.

**As a result of a top/base gas study performed in 2004, the company reduced current gas (Acct 164.1) by $2,049,846 and increased noncurrent gas (Acct 117) by $78,666 and non-recoverable gas (Acct 352.3) by $1,971,180. Column (c) also includes an adjustment of $12,758 relating to additional Line Pack.

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
DLH Twenty-Seventh Set of Data Requests

DLH 27.12 Q. In response to Staff Data Request PL 1.08(a), the Company stated as follows:

> Note that at 12/31/07 there were 48 individuals who were employees of Nicor Gas for payroll and benefit plan eligibility purposes but who were fully dedicated to the business of, and the costs of whom were fully charged to, Nicor Enerchange (35 individuals) and Nicor Inc (13 individuals),

Please answer the following concerning this response:

a. Please provide the average annual salary (excluding benefits) for 2007 for these 48 employees.
b. Please provide the total number of Nicor Gas employees as of 12/31/2007.
c. Please provide the average annual salary (excluding benefits) for 2007 for the Nicor Gas employees identified in response to part b. of this question.
d. Please provide the fully distributed costs billed to Nicor Enerchange for 2007 for the 35 individuals identified in response to PL 1.08(a).
e. Please provide the fully distributed costs billed to Nicor Inc. for 2007 for the 13 individuals identified in response to PL 1.08(a).
f. Please explain why these employees were retained by Nicor Gas if all their services are dedicated to affiliates of the Company.
g. Please provide a copy of all workpapers relied on to respond to parts a-f of this question.

DLH 27.12 A.

a. Please note that there was an error in the employee count for Nicor Enerchange reported in the Company's response to PL 1.08(a). The correct number is 33 not 35, for a total of 46 not 48. The average salary (excluding benefits) for the 46 employees for 2007 was $90,689.29
b. 2,163 (includes employees dedicated to Nicor Enerchange – 33 and Nicor Inc – 13)
c. $57,429.19
d. $3,081,175 was billed to Nicor Enerchange for these 33 individuals. An additional $386,436 was allocated to other subsidiaries of Nicor Inc. for these individuals to account for services provided by Nicor Enerchange through these individuals for these other subsidiaries.
e. $1,251,071 was billed to Nicor Inc. for these 13 individuals. An additional $370,337 was allocated to subsidiaries of Nicor Inc. for these individuals to account for services provided by Nicor Inc. through these individuals for these subsidiaries.

f. The employees referred to in response "a" are assigned to Nicor Enerchange and Nicor Inc due to their job responsibilities. They are Nicor Gas employees for payroll and benefit purposes. Because these work groups are small, it is more efficient to utilize the Nicor Gas payroll system to pay them and also provide them with retirement and welfare benefits. These decisions were made to minimize expenses related to technology systems and benefit design and administration.

g. See attached Exhibit 1 for a, b, & c; See attached Exhibit 2 for d & e

Witness: Rebecca C. Bacidore

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
DLH Twenty-Seventh Set of Data Requests

Average Annualized Base Salary effective December 31, 2007
Nicor Enerchange and Nicor Inc employees

Average Salary **$90,689.29**

		Total Annualized Salary	# of Incumbents
Enerchange	$	3,043,304.42	33
Inc	$	1,128,403.12	13
Totals	$	4,171,707.54	46

Average Annualized Base Salary effective December 31, 2007
Nicor Gas employees including employees dedicated to Nicor Enerchange and Nicor Inc

Average Salary **$57,429.19**

Salary Grade		Total Annualized Salary	# of Incumbents
Hourly	$	64,261,891.20	1,396
1	$	634,302.50	16
2	$	1,917,005.74	42
3	$	6,341,883.74	117
4	$	12,162,818.53	187
5	$	11,873,644.12	156
6	$	6,926,061.09	82
7	$	5,879,208.14	63
8	$	4,473,304.94	42
9	$	3,256,003.40	25
61	$	199,000.62	4
62	$	495,800.50	6
63	$	111,000.24	1
64	$	222,900.08	2
65	$	373,000.42	3
66	$	523,700.32	3
67	$	236,800.20	1
Officer	$	4,331,002.52	17
Totals	$	124,219,328.30	2,163

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
DLH Twenty-Seventh Set of Data Requests

Part d:
Fully distributed costs billed for Nicor Enerchange employees by company:

	Company Billed To							
	Nicor Enerchange	Nicor Inc	Nicor Gas (does NOT include additive)	Nicor Services	Nicor Horizon	Nicor Solution	Nicor Advanced Energy	Total
Management Employees	$ 2,226,554	$ 195,933	$ 86,787	$ 7,347	$ 7,382	$ 1,104	$ 29	$ 2,525,135
Clerical Employees	29,601	-	-	-	-	-	-	29,601
Payroll Additive	825,019	78,373	-	5,657	2,953	850	23	912,874
Fully distributed costs	$ 3,081,175	$ 274,306	$ 86,787	$ 13,004	$ 10,334	$ 1,953	$ 52	$ 3,467,611

Part e:
Fully distributed costs billed for Nicor Inc employees by company:

	Company Billed To				
	Nicor Inc	Nicor Energy Solutions Inc	Nicor Gas (does NOT include additive)	Nicor Services	Total
Management Employees	$ 604,069	$ 4,315	$ 328,645	$ 19,240	$ 956,269
Clerical Employees	102,751	-	-	-	102,751
Payroll Additive	544,251	3,323	-	14,815	562,388
Fully distributed costs	$ 1,251,071	$ 7,638	$ 328,645	$ 34,054	$ 1,621,408

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
PL First Set of Data Requests

PL 1.09 Q. Please answer the following concerning the Company's response to DGK 5.03:

a. Please provide a detailed explanation of the billing services Nicor Gas provides for each non-utility affiliate.
b. Please provide the dollar amount of billing services provided by Nicor Gas to each non-utility affiliate for 2007.
c. Please provide a full explanation of how each amount provided in response to PL-1.09(b) above was derived.
d. Please provide a copy of all cost studies and workpapers relied on to derive the dollar amounts provided in response to PL-1.09(b) above.
e. Please separately identify the amount of benefits, computer software maintenance, rent, telephone, meals and entertainment and transportation and lodging expenses identified with these billing services.

PL 1.09 A. Objection. The subject of DGK 5.03 and other questions in that series was Administrative Code section 506, *Accounting for Non-Public Utility Business of Gas Utilities*. In its response, the company referred to filing schedule C-32, which lists the non-public utility business activities the utility conducts on its own behalf. PL 1.09 requests information pertaining to billing services activities Nicor Gas provides to non-utility affiliates. These services are not addressed in the response to DGK 5.03. Without waiving this objection, Nicor Gas states as follows:

a. The billing services that Nicor Gas provides for each non-utility affiliate are as follows:

- Nicor Energy Services and Nicor Solutions – printing, mailing, cash remittance processing and customer inquiry services for the affiliates' customers who are billed via Nicor Gas' utility bill.

b. For 2007, Nicor Gas charged affiliates the following amounts for the services noted in (a), above:

- Nicor Energy Services - $470,910
- Nicor Solutions – $157,812

c. The basis for each charge is as follows:

- Nicor Energy Services – fully distributed cost
- Nicor Solutions – prevailing tariff price

d. See Exhibit 1 for the cost study and workpapers supporting the Nicor Services' charges listed in response to PL-1.09(b). Nicor Solutions is treated similarly as other Customer Select vendors; thus, the affiliate is charged the tariff rate of $0.25 per bill as approved in docket #00-0620/21.

e. For cost-based charges, the amount of benefits, computer software, maintenance, rent, telephone, meals and entertainment, transportation and lodging are embedded within the various additive rates and department costs that form the basis of the cost studies, and they are not separately identifiable.

Witness: James M. Gorenz

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
DLH Twenty-Fifth Set of Data Requests

DLH 25.02 Q. Referring to the Company's response to Staff data request PL-1.09, provide the amount included in the test year Schedules B-1 and C-1, by line and column reference, for services provided by Nicor Gas to a) Nicor Energy Services and b) Nicor Solutions. Include all supporting workpapers, assumptions, and calculations in the response.

DLH 25.02 A. The amounts reflected in the Company's response to PL 1.09 relate to the year 2007 charges for billing services. The test year amounts for these services are $588,000 for Nicor Energy Services and $70,000 for Nicor Solutions. These amounts are included in Schedule C-1 at column H in lines 13 and 5, respectively. See attached Exhibits 1 and 2 for supporting workpapers.

Witness: James M. Gorenz

Northern Illinois Gas Company d/b/a Nicor Gas Company
Response to: Illinois Commerce Commission
Ill.C.C. Docket No. 08-0363
DLH Twenty-Seventh Set of Data Requests

DLH 27.09 Q. Referring to the Company's response to Staff data request DLH-25.02, explain why Exhibit 1 and Exhibit 2 charge different accounts and amounts to Nicor Energy Services and Nicor Solutions, respectively, for similar services provided by Nicor Gas. Explain in detail the basis for the difference in charges.

DLH 27.09 A. The ICC-approved Operating Agreement permits Nicor Gas to provide certain types of services to affiliates. In addition to setting forth in broad terms the types of inter-company services that are allowed (including billing services in Section 2.2(a)), it also specifies what charges are to be assessed for those services. Generally, Nicor Gas must receive at least the prevailing price for which the service is provided for sale to the general public or, if there is no such prevailing price, it must receive at least its fully distributed cost for the service.

Nicor Solutions pays for billing services on the basis of a prevailing price. Nicor Solution's Fixed Bill program is an alternative to Customer Select Supplier programs and the Nicor Solutions' charge is located on the same line as a Customer Select Supplier's charge. Therefore, Nicor Solutions uses the same billing system as Customer Select Suppliers. In its dealings with Nicor Solutions, Nicor Gas follows the standards applicable to transactions with "affiliated interests in competition with alternative retail gas suppliers" under Part 550 of the Commission's rules. Consistent with the Operating Agreement and the provisions of Part 550, the prevailing price applicable to Nicor Solutions is the rate charged to Customer Select Suppliers.

Nicor Energy Services pays for its billing service at the Company's fully distributed cost. To be able to provide this billing service for Nicor Energy Services, the Company initially needed to modify and upgrade its IT system. The billing system utilized for Nicor Energy Services is a different billing program within the Customer Care & Billing ("CC&B") system than the one utilized for Customer Select Suppliers. The affiliate's customer charge is placed on a different line on the Nicor Gas bill. Nicor Gas was reimbursed for these startup costs at its fully distributed cost. Nicor Gas also has directly charged Nicor Energy Services for ongoing maintenance programming expenses at the Company's fully distributed cost. In addition, Nicor Energy Services pays a charge per bill message to Nicor Gas that is computed on a fully distributed cost basis.

Nicor Gas records the credits from providing these services to different accounts based on the nature of the billing mechanism. The Nicor Energy Services charge is a fully-distributed-cost charge so the credit is reflected in the same account as the original costs. The Nicor Solutions charge is based on a prevailing price under Illinois Administrative Code Part 550 and accordingly the credit is reflected in Other Revenues.

Witness: James M. Gorenz

ILLINOIS
COMMERCE COMMISSION
OCT 31 9:03 AM '01
CHIEF CLERK'S OFFICE

OPERATING AGREEMENT

Dated as of October 25, 2001

Among

NICOR Inc.

Northern Illinois Gas Company

d/b/a Nicor Gas Company

and

Each of the Entities Identified on Exhibit A Hereto

ARTICLE I

Definitions and Interpretation 1

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ADDENDUM

Short-term Borrowing and Investing Between Parties

OPERATING AGREEMENT

THIS OPERATING AGREEMENT (this "Agreement") is made and entered into as of the 25th day of October, 2001, among NICOR Inc., an Illinois corporation ("NICOR"), Northern Illinois Gas Company, an Illinois corporation doing business as Nicor Gas Company ("Nicor Gas"), and each of the entities identified on Exhibit A hereto, as such Exhibit A may be amended from time to time in accordance with the provisions of this Agreement.

WITNESSETH:

WHEREAS, the parties are related by virtue of common ownership, directly or indirectly, of their equity securities by NICOR; and

WHEREAS, the parties believe that the central management of certain services, the provision to each other of certain services and facilities, and the transfer of certain property are or may be efficient and cost-effective, and the parties desire to make provision for these and other transactions as between Nicor Gas and a NICOR Entity or Entities;

WHEREAS, the parties are currently signatories to an Operating Agreement approved by the Illinois Commerce Commission in Docket No. 60256;

WHEREAS, this agreement is intended to supercede the Operating Agreement approved in Docket No. 60256.

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants contained herein, the parties hereby agree as follows:

ARTICLE I
Definitions and Interpretation

Section 1.1. *Definitions.* As used in this Agreement, the following terms shall have the respective meanings set forth below unless the context otherwise requires:

"Acquiring Party" means a Party who desires to acquire real property, interests in real property, tangible personal property or Intangible Assets from a Selling Party.

"ICC" means the Illinois Commerce Commission.

"Intangible Assets" means items, other than tangible assets and real property, for which costs have been incurred to create future economic benefits that may or may not be recorded as assets on the Selling Party's financial statements. Intangible Assets include, but are not limited to, operational knowledge, software or intellectual property derived from internal research and development efforts.

"Party" means each, and *"Parties"* means all, of the entities who are from time to time a party to this Agreement.

"Provider" means a Party who has been requested to, and who is able and willing to, furnish facilities, provide services or both to a Requestor under the terms of this Agreement.

"Requestor" means a Party who desires to use facilities, receive services or both, and has requested another Party to furnish such facilities, provide such services or both.

"Selling Party" means a Party who is willing to sell and transfer real property, interests in real property, tangible personal property or Intangible Assets to an Acquiring Party.

"NICOR Entity" means any of NICOR and the entities identified on Exhibit A hereto, as amended from time to time.

Section 1.2. *Purpose and Intent; Interpretation.* (a) The purposes and intent of this Agreement are to set forth procedures and policies to govern (i) transactions between a NICOR Entity and Nicor Gas, whether such transactions occur directly or indirectly as the end result of a series of related transactions and (ii) the allocation of certain joint service costs. It is not intended to govern transactions between NICOR Entities that do not involve Nicor Gas (although such entities may elect to apply the provisions of this Agreement to specific transactions) or to govern transactions between Nicor Gas and its subsidiaries. This Agreement shall be interpreted in accordance with such purposes and intent.

(b) The headings of Articles and Sections contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. References to Articles, Sections and Exhibits refer to articles, sections and exhibits of this Agreement unless otherwise stated. Words such as "herein," "hereinafter," "hereof," "hereto," "hereby" and "hereunder," and words of like import, unless the context requires otherwise, refer to this Agreement (including the Exhibits hereto).

ARTICLE II
Use of Facilities and Services

Section 2.1. *Facilities.* Upon the terms and subject to the conditions of this Agreement, a Requestor may request a Provider or Providers to make available or provide, and, subject to the provisos at the end of this Section, such Provider or Providers may make available or provide to such Requestor, the use of:

(a) facilities, including, without limitation, office space, warehouse and storage space, transportation, repair facilities, manufacturing and production facilities, fixtures and office furniture and equipment;

(b) computer equipment (both stand-alone and mainframe) and networks, peripheral devices, storage media, and software;

(c) communications equipment, including, without limitation, audio and video equipment, radio equipment, telecommunications equipment and networks, and transmission and switching capability;

(d) vehicles, including, without limitation, automobiles, trucks, vans, trailers, railcars, marine vessels, aircraft, transport equipment, material handling equipment and construction equipment; and

(e) machinery, equipment, tools, parts and supplies;

provided, however, that a Provider shall have no obligation to provide any of the foregoing, considering such factors as the extent that such item or items are not available (either because such Provider does not possess the item or the item is otherwise being used); and *provided further,* it is understood that a Provider has sole discretion in scheduling the use by a Requestor of facilities, equipment or capabilities so as to avoid interference with such Provider's operations.

Section 2.2. *Services.* Upon the terms and subject to the conditions of this Agreement, a Requestor may request a Provider or Providers to provide, and, subject to the provisos at the end of this Section, such Provider or Providers may provide to such Requestor:

(a) administrative and management services, including, without limitation, accounting (including, without limitation, bookkeeping, budgeting, forecasting, billing, accounts receivable and accounts payable administration, and financial reporting); audit; executive; finance; cash management (including, without limitation, electronic fund transfers, cash receipts processing, managing short-term borrowings and investments with third parties, and short-term borrowing and investing between Parties to this Agreement subject to the limitations and at the interest rates specified in the Addendum to this Agreement); governmental affairs; insurance; information systems services; investment advisory services; legal; library; record keeping; secretarial and other general office support; real estate management; security holder services; tax; treasury; and other administrative and management services;

(b) personnel services, including, without limitation, recruiting; training and evaluation services; payroll processing; employee benefits administration and processing; labor negotiations and management; and related services;

(c) purchasing services, including, without limitation, preparation and analysis of product specifications, requests for proposals and similar solicitations; vendor and vendor-product evaluations; purchase order processing; receipt, handling, warehousing and disbursement of purchased items; contract negotiation and administration; inventory management and disbursement; and similar services;

(d) operational services, including, without limitation, drafting and technical specification development and evaluation; consulting; engineering; environmental; construction; design; resource planning; economic and strategic analysis; research; testing; training; public and governmental relations; and other operational services; and

(e) customer solicitation, customer support and other marketing-related services, including, without limitation, customer lists and other customer-related information;

provided, however, that a Provider shall have no obligation to provide any of the foregoing, considering such factors as the extent that it is not capable of providing such service (either because such Provider does not have personnel capable of providing the requested service or the service is otherwise being used); and *provided further,* it is understood that a Provider has sole discretion in scheduling the use by a Requestor of services so as to avoid interference with such Provider's operations.

Section 2.3. *Joint Purchasing.* A Party may also request that another Party or Parties enter into arrangements to effect the joint purchase of goods or services from third parties; *provided, however,* that if Nicor Gas is so requested to enter into and agrees to participate in such arrangements, it shall do so only if its fully distributed cost for such goods or services is not thereby increased. In the event that any such arrangements are established, one Party may be designated as, or serve as, agent for the other Parties to the arrangement and may administer the arrangement (including billing and collecting amounts due the vendor(s)) for the other Parties.

Section 2.4. *Agreements, Etc.* A Provider and Requestor may evidence their agreement with respect to the availability, provision or use of the facilities, services and activities described in this Article II by entering into an agreement, lease, license or other written memorandum or evidence; *provided* such agreement, lease, license or other written memorandum or evidence shall not contain terms inconsistent with this Agreement; and *further provided* that this Section 2.4 shall not be deemed to require any such agreement, lease, license or other written memorandum or evidence.

ARTICLE III
Asset Sales

Section 3.1. *Real Property Transfers.* Upon the terms and subject to the conditions of this Agreement, an Acquiring Party may purchase from a Selling Party, and the Selling Party may sell to the Acquiring Party, real property or interests in real property.

Section 3.2. *Tangible Personal Property.* Upon the terms and subject to the conditions of this Agreement, an Acquiring Party may purchase from a Selling Party, and the Selling Party may sell to the Acquiring Party, tangible personal property. This Section 3.2 shall not apply to joint purchasing arrangements (and the transactions thereunder) entered into pursuant to Section 2.3 of this Agreement.

Section 3.3. *Intangible Assets.* An Acquiring Party may enter into an agreement with a Selling Party to purchase, and the Acquiring Party may purchase from the Selling Party and the Selling Party may sell to the Acquiring Party pursuant to such agreement, Intangible Assets.

Section 3.4. *NICOR Stock.* Upon the terms and subject to the conditions of this Agreement, NICOR may issue and sell to Nicor Gas shares of NICOR Common Stock for the sole purpose of enabling Nicor Gas to meet its obligations to its directors and employees in respect of compensation (it being understood that Nicor Gas would cause any shares so purchased and received to be reissued to such directors and employees in payment of such compensation obligations).

Section 3.5. *Agreements, Etc.* An Acquiring Party and a Selling Party may evidence their agreement with respect to the sale of real property and/or tangible personal property described in Sections 3.1 or 3.2 by entering into an agreement or other written memorandum or evidence; *provided* such agreement or other written memorandum or evidence shall not contain terms inconsistent with this Agreement; and *further provided* that this Section 3.5 shall not be deemed to require any such agreement or other written memorandum or evidence.

ARTICLE IV
Charges; Payment

Section 4.1. *Charges.* (a) Charges for assets sold and transferred under Sections 3.1, 3.2 and 3.4 shall be determined in accordance with the provisions of Section 5.1(a); charges for the use of facilities, equipment, capabilities or services under Sections 2.1 and 2.2 shall be determined in accordance with Section 5.1(b); and charges for assets sold and transferred under Section 3.3 shall be determined in accordance with the provisions of Section 5.1(c). By acquiring real property, interests therein, tangible personal property or Intangible Assets in accordance with the provisions of Article III, an Acquiring Party shall be deemed to have agreed to pay, and shall pay, to the Selling Party the charge determined therefor in accordance with Section 5.1(a) or, in the case of Intangible Assets, Section 5.1(c). By requesting the use of facilities, equipment, capabilities and/or services, a Requestor shall be deemed to have agreed to pay, and shall pay, to the Provider or Providers the charge determined therefor in accordance with Section 5.1(b).

(b) Charges related to arrangements under Section 2.3 for the joint purchase of goods or services shall be determined in accordance with Section 5.1(a), in the case of asset transfers, and Section 5.1(b), in the case of services and overhead, administrative and other costs.

Section 4.2. *Accounting.* Each Party shall maintain adequate books and records with respect to the transactions subject to this Agreement and shall establish unique account numbers in its general ledger system which shall be used to record the costs to be apportioned to the other Parties. Each Party shall be responsible for maintaining internal controls to ensure the costs associated with transactions covered by this Agreement are properly and consistently allocated and billed in accordance with the terms and provisions of this Agreement.

Section 4.3. *Invoicing, Payment.* Invoicing and payment for the facilities and services specified in Article II, the asset sales specified in Article III or the joint services costs specified in Section 5.3(a) shall be as follows:

(a) for the use of facilities, equipment or capabilities specified in Section 2.1 or the provision of services specified in Section 2.2, a Provider shall invoice the Requestor on a monthly basis for the charges therefor as provided in Section 4.1(a), and such invoices shall be payable within thirty days of receipt;

(b) for joint purchasing arrangements specified in Section 2.3, a Party participating in any such arrangement shall be invoiced for charges as provided in Section 4.1(b), which invoices will be payable according to the terms set by the vendor(s) providing the purchased goods or services, or if a Party has been selected to administer such arrangement, pursuant to invoices rendered by such Party or the vendor of the goods or services, which invoices will be payable no later than thirty days of receipt;

(c) for the sale of real property or interests in real property specified in Section 3.1, the Acquiring Party shall pay the charges therefor as provided in Section 4.1(a) to the Selling Party upon the closing of the sale and transfer of such real property or interests therein;

(d) for the sale of tangible personal property specified in Section 3.2, or intangible assets specified in Section 3.3, the Selling Party shall invoice the Acquiring Party for the charges therefor as provided in Section 4.1(a), and such invoices shall be payable within thirty days of receipt;

(e) for the transfer of NICOR Common Stock specified in Section 3.4, Nicor Gas shall pay the charges therefor as provided in Section 4.1(a) and such payment shall be made to NICOR concurrently with the issuance and delivery of the shares of such stock; and

(f) for joint service costs under Section 5.3(a), NICOR shall invoice the other Parties for such costs as provided in Section 5.3(c), and such invoices shall be payable within thirty days of receipt.

Late payments shall bear a rate of interest representing NICOR's cost of funds, as determined by contacting NICOR's commercial paper dealers, but shall in no event exceed the then-effective rate of interest announced by Bank of America Illinois in Chicago, Illinois. The interest shall be based on the period of time that the payment is late.

ARTICLE V
Cost Apportionment Methodology

Section 5.1. *General Principles.* The following general principles shall be used in setting charges for transactions between Nicor Gas and NICOR Entities:

(a) Sales of Assets. Asset sales between Nicor Gas and a NICOR Entity shall be charged by the Selling Party to the Acquiring Party at: (i) the fair market value of the transferred asset, as evidenced by (1) the prevailing price for which the same or similar assets are offered for sale to the general public by the Selling Party (e.g., for Nicor Gas, the tariffed charge or other pricing mechanism approved by the ICC) or, if no such prevailing price exists, (2) the price at which nonaffiliated vendors offer the same or similar assets for sale by reference to quoted market prices, independent appraisals or other objectively determinable evidence or, if no such fair market value is objectively or practicably determinable, (ii) the historical cost of the asset to the Selling Party, less all applicable valuation reserves.

(b) Use of Facilities or Services.

(i) Facilities or services provided by Nicor Gas to a NICOR Entity shall be charged by the Provider to the Requestor at: (1) the prevailing price for which the facility or service is provided for sale to the general public by the Provider (i.e., the tariffed rate or other pricing mechanism approved by the ICC) or, if no such prevailing price exists, (2) an amount equal to or greater than the fully distributed cost (determined as provided in Section 5.2) incurred by the Provider in providing such facility or service to the Requestor.

(ii) Facilities or services provided by a NICOR Entity to Nicor Gas shall be charged by the Provider to the Requestor at: (1) the prevailing price for which the facility or service is provided for sale to the general public by the Provider (i.e., the price charged to nonaffiliates if such transactions with nonaffiliates constitute a substantial portion of such NICOR Entity's total revenues from such transactions) or, if no such prevailing price exists, (2) an amount not to exceed the fully distributed cost (determined as provided in Section 5.2) incurred in providing such facility or service.

(c) Sales of Intangible Assets. Intangible Asset sales between Nicor Gas and a NICOR Entity shall be charged by the Selling Party to the Acquiring Party (i) under a mechanism to reflect the fair market value of the asset as determined by an appraisal or other fair market value study or, if no such fair market value is objectively or practicably determinable, (ii) at the fully distributed cost incurred to purchase or develop the asset, adjusted to reflect imputed amortization of, if applicable, any carrying costs on the unrecorded asset.

Costs shall be charged to a Party in accordance with these general principles using either a direct charge or an allocation methodology. Costs of assets or services specifically attributable to a Party should be charged directly to such Party. Joint and common costs not specifically attributable to a Party should be charged to the appropriate Parties based on specific allocation methodologies. The Parties intend to develop and implement a set of guidelines to address applications of the foregoing general principles.

Section 5.2. *Fully Distributed Costs.* Costs charged on a fully distributed cost basis shall reflect the amounts of direct labor, direct materials and direct purchased services associated with the related asset or service as provided in subsections (a) and (b). These amounts shall be increased by a portion of indirect costs to reflect labor, administrative and general and other overhead amounts as provided in subsection (c).

(a) Direct Costs. Costs incurred that are specifically attributable to a Party shall be directly charged to the appropriate account.

(i) Direct Labor: Amounts of direct labor charged to a Party shall be based on actual direct labor, reflecting the effects of overtime and nonproductive time.

For most employees, direct labor shall be charged to a Party pursuant to the following methodology: an employee shall report each month the number of hours incurred in performing activities for such Party. Based on the time reported each month, the regular, predetermined account distribution for the employee shall be adjusted to reflect the distribution of direct labor charges to the appropriate affiliate function.

Some individuals, departments or organizations may provide a recurring, predictable level of services to a Party or Parties. For these individuals, departments or organizations, at a minimum annual reviews shall be performed to determine a normal distribution of time to such Party or Parties. The distribution percentages derived from such reviews shall then be used to allocate time with respect to each month. Significant deviations of actual activity from these predetermined percentages shall be reported and shall result in adjustments to the predetermined distribution of direct labor charges to the affiliate accounts.

Overtime shall be reflected in the direct labor rates charged to a Party. For bargaining unit employees, direct labor shall be charged based on the base and overtime pay amounts under a Party's collective bargaining agreements. Likewise, for non-bargaining employees who are compensated for overtime, direct labor shall be charged based on the base pay amounts incurred for such employees, including overtime. For management employees not compensated for overtime, direct labor charged to affiliates shall be adjusted, on a departmental or organizational basis, to reflect estimated overtime incurred based on an overtime review performed annually.

All direct labor charges shall be increased by a factor to reflect nonproductive time. The nonproductive time factor shall be developed based on a review of actual nonproductive time incurred for the previous year. The nonproductive time factor reflects time incurred for vacations, holidays, disability, jury duty and other paid absences.

(ii) Direct Materials and Purchased Services. Amounts incurred for materials or purchased services directly attributable to a Party shall be charged directly to the appropriate account for that Party.

(b) Allocated Costs. Costs incurred that are not specifically attributable to a Party but that have joint benefit to two or more Parties shall be charged to the appropriate Parties based on specified allocation methodologies. The allocation methodologies used shall be reasonably based on cost causative measures to ensure an equitable allocation among such Parties.

(c) Indirect Costs. The direct and allocated costs apportioned to a Party or Parties shall be increased to reflect indirect labor, administrative and general and other overhead amounts. These indirect costs are not specifically identifiable or attributable to the direct costs incurred on behalf of a Party.

All direct labor charges apportioned to a Party (either apportioned directly or using an allocation methodology) shall be increased by a loading factor to reflect indirect labor-driven costs. For each Party, this loading factor shall be determined annually based on actual indirect labor-driven charges incurred during the prior year as a percentage of total direct labor charges incurred in that year. The labor loading shall include payroll taxes; medical, dental and vision insurance costs; pension and other

ostretirement health care benefits costs; incentive compensation plan costs; employee savings plans costs; training costs; other employee benefits; the employee benefits department costs; communications and computer support and facilities costs.

Facilities costs include buildings and related property, such as equipment, machinery, furniture and fixtures, and related services, such as mail delivery and library services. These indirect charges shall include an amount to reflect the cost of such assets (e.g., depreciation, operations, maintenance, utilities, insurance, real estate taxes, etc.) and, for owned assets or assets leased under capital leases, a return equal to the rate of return on rate base most recently authorized for Nicor Gas by the ICC.

Section 5.3. *Costs Charged to/from NICOR.* NICOR shall maintain unique account numbers in its general ledger system: Consolidated Pool accounts (as described in Section 5.3(a)) and Unallocated Pool accounts (as described in Section 5.3(b)). All costs incurred by NICOR and not directly charged to another Party and all costs apportioned and billed to NICOR by other Parties shall be charged to one of these two types of accounts.

(a) Consolidated Pool Costs. The Consolidated Pool accounts shall be charged with costs related to activities that jointly benefit all of the Parties. Each month, the costs accumulated in the Consolidated Pool shall be apportioned and billed to the Parties (other than NICOR) using a two-factor formula methodology. A representative listing of the types of Nicor services for which costs shall be charged to the Consolidated Pool is as follows:

Accounting	Forecasting
Auditing	Governmental Affairs
Branding and Other Marketing	Information Systems
Budgeting	Investor Relations
Corporate Planning	Legal
Corporate Secretary's Office	Risk Management
Executive Services	Shareholder Services
Financial Reporting	Tax Administration
Finance	

(b) Unallocated Costs. The Unallocated accounts shall be charged with costs that have been determined as not appropriate for apportionment by NICOR to the other Parties. These costs primarily relate to NICOR's diversification and divestiture activities.

(c) Two-Factor Formula Methodology. Monthly, costs charged to the Consolidated Pool shall be apportioned and billed by NICOR to the other Parties based on a two-factor formula methodology. Under this approach, each such Party wholly owned by NICOR (other than non-operating Parties) is allocated and billed for a portion of the total costs in the Consolidated Pool based on an average of such Party's gross payroll and total asset amounts relative to the corresponding averages for the other wholly owned operating Parties. To adjust for seasonality in operations, the gross payroll amounts used in this allocation shall be the twelve-month-ended amounts through the prior quarter-end. The total asset amount shall reflect the month-end balance from the prior quarter ended. Non-operating affiliates are those that exist solely for the purpose of enabling Nicor Inc. to perform its corporate function and which do not engage in the active management or oversight of any

enterprise doing business with third parties. For majority-owned Parties that are not wholly owned, the two-factor formula shall consider only the proportional ownership share of such Party's gross payroll and total assets. Affiliates that are not controlled by Nicor Inc. are precluded from becoming Parties to this Agreement. For purposes of this Agreement, control exists when Nicor Inc. holds, directly or indirectly, more than 50 percent of the voting rights of the entity's common stock or more than 50 percent of the seats on the board of directors or other oversight committee.

Section 5.4. *Allocations Among Parties Other Than Nicor Gas.* Nothing in this article, or any other article, shall limit or restrict the rights of Parties other than Nicor Gas to allocate costs among themselves, so long as it does not adversely impact Nicor Gas, such as by increasing Nicor Gas' costs. If a Nicor Entity charges Nicor Gas based upon its fully distributed costs, and such costs include any intercompany charges from affiliates, such intercompany charges shall be determined in accordance with the cost apportionment methodology described in this Agreement

ARTICLE VI
Limitations of Liability

Section 6.1. *No Warranties For Facilities or Services.* Each Party acknowledges and agrees that any facilities, equipment or capabilities made available, and any services provided, by a Provider to a Requestor hereunder, are so made available or provided WITHOUT ANY WARRANTY (WHETHER EXPRESS, IMPLIED OR STATUTORY AND NOTWITHSTANDING ANY ORAL OR WRITTEN STATEMENT BY A PARTY'S EMPLOYEES, REPRESENTATIVES OR AGENTS TO THE CONTRARY) WHATSOEVER. ALL SUCH WARRANTIES (INCLUDING, WITHOUT LIMITATION, THE WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE) ARE HEREBY DISCLAIMED AND EXCLUDED.

Section 6.2. *Limited Warranties For Asset Sales.* (a) Except as provided in Section 6.2(b), each Party acknowledges and agrees that any real property, interests in real property, tangible personal property or Intangible Assets sold and transferred in accordance with Article III is so sold and transferred WITHOUT ANY WARRANTY (WHETHER EXPRESS, IMPLIED OR STATUTORY AND NOTWITHSTANDING ANY ORAL OR WRITTEN STATEMENT BY A SELLING PARTY'S EMPLOYEES, REPRESENTATIVES OR AGENTS TO THE CONTRARY) WHATSOEVER. ALL SUCH WARRANTIES (INCLUDING, WITHOUT LIMITATION, THE WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE) ARE HEREBY DISCLAIMED AND EXCLUDED.

(b) In connection with a sale and transfer of real property, interests in real property, tangible personal property, Intangible Assets or NICOR stock pursuant to Article III, the Selling Party shall be deemed to have represented and warranted to the Acquiring Party that: (i) title conveyed is good, (ii) conveyance of such title is authorized and rightful, and (iii) the title so conveyed is free and clear of all liens, claims, encumbrances or security interests of persons or entities claiming by or through the Selling Party, except, in the case of this clause (iii), as the Acquiring Party and the Selling Party may otherwise agree.

Section 6.3. *No Partnership.* The Parties acknowledge and agree that this Agreement does not create a partnership between, or a joint venture of, a Party and any other Party. Each Party is an independent contractor and nothing contained in this Agreement shall be construed to constitute any Party as the agent of any other Party except as expressly set forth in Section 2.3.

Section 6.4. *No Third Party Beneficiaries.* This Agreement is intended for the exclusive benefit of the Parties hereto and is not intended, and shall not be deemed or construed, to create any rights in, or responsibilities or obligations to, third parties.

ARTICLE VII
Term

Section 7.1. *Term.* This Agreement will be effective on the date it is approved by the ICC and shall continue, unless terminated as provided in Section 7.2.

Section 7.2. *Termination.* Any Party may terminate this Agreement as to it by providing at least 30 days prior written notice to the other Parties of the effective date of such termination. In addition, this Agreement shall terminate as to a Party upon the date that NICOR determines that such Party shall no longer be a party to this Agreement and shall automatically terminate as to a Party upon the date that NICOR ceases, directly or indirectly, to own equity securities in such Party. Any such termination shall not affect the terminating Party's accrued rights and obligations under this Agreement arising prior to the effective date of termination or its obligations under Section 9.4.

ARTICLE VIII
Confidential Information

Each Party shall treat in confidence all information which it shall have obtained regarding the other Parties and their respective businesses during the course of the performance of this Agreement. Such information shall not be communicated to any person other than the Parties to this Agreement, except to the extent disclosure of such information is required by a governmental authority. If a Party is required to disclose confidential information to a governmental authority, such Party shall take reasonable steps to make such disclosure confidential under the rules of such governmental authority. Information provided hereunder shall remain the sole property of the Party providing such information. The obligation of a Party to treat such information in confidence shall not apply to any information which (i) is or becomes available to such Party from a source other than the Party providing such information, or (ii) is or becomes available to the public other than as a result of disclosure by such Party or its agents.

ARTICLE IX
Miscellaneous

Section 9.1. *Entire Agreement; Amendments.* Upon its effectiveness as provided in Section 7.1, this Agreement shall constitute the sole and entire agreement among the Parties with

respect to the subject matter hereof and shall supersede all previous agreements, proposals, oral or written, negotiations, representations, commitments and all other communications between some or all of the Parties. Except as provided in Section 9.2 with respect to new Parties and except that NICOR may amend Exhibit A to this Agreement to delete any terminated Party, this Agreement shall not be amended, modified or supplemented except by a written instrument signed by an authorized representative of each of the Parties hereto.

Section 9.2. *New Parties.* Any other entity which is or may become an affiliate of NICOR or any of the other Parties to this Agreement may become a party to this Agreement by executing an agreement adopting all of the terms and conditions of this Agreement. Such agreement must be signed by NICOR in order to become effective, but need not be signed by any other Party to this Agreement. Upon such execution, such entity shall be deemed to be a Party and shall be included within the definition of "Party" for all purposes hereof, and Exhibit A shall be amended to add such entity. Nicor Gas shall notify the ICC by means of an informational filing each time a new Party becomes eligible to receive or provide services and facilities under this Agreement. This informational filing should include the name and business purpose of the Party and its relationship to Nicor Gas.

Section 9.3. *Assignment.* This Agreement may not be assigned by any Party without the prior written consent of NICOR.

Section 9.4. *Access to Records.* During the term of this Agreement and for a period of seven years after the expiration or termination of this Agreement as to a Party, such Party shall have reasonable access to and the right to examine any and all books, documents, papers and records which pertain to services and facilities provided by the other Parties under this Agreement to such Party, and such Party shall provide access to, and the opportunity to examine, all such records which pertain to services and facilities provided to the other Parties under this Agreement by such Party. Each Party shall maintain all such records for a period of seven years after expiration or termination of this Agreement as to such Party. In addition, during the term of this Agreement and for a period of seven years after the expiration or termination of this Agreement as to a Nicor Entity, the ICC shall have access to the books and records of such Nicor Entity as they relate to transactions between such Nicor Entity and Nicor Gas to the extent allowed under Section 7-101 of the Illinois Public Utilities Act and subject to Section 5-108 of the Illinois Public Utilities Act.

Section 9.5. *Partial Invalidity.* Wherever possible, each provision hereof shall be interpreted in such manner as to be effective and valid under applicable law, but in case any one or more of the provisions contained herein shall, for any reason, be held to be invalid, illegal or unenforceable in any respect, such provision shall be ineffective to the extent, but only to the extent, of such invalidity, illegality or unenforceability without invalidating the remainder of such invalid, illegal or unenforceable provision or provisions or any other provisions hereof, unless such a construction would be unreasonable. In the event that it is determined that the charges for a particular transaction covered by this Agreement were not determined properly for any reason, such determination and/or finding shall not affect the validity of such transaction; *provided, however,* that if the transaction involved Nicor Gas and a NICOR Entity, NICOR (or, if NICOR so determines, such NICOR Entity) shall pay to or reimburse Nicor Gas, or Nicor Gas shall pay to or reimburse such NICOR Entity, as the case may be, for the difference between the amount that was charged in connection with the transaction and the charge that is determined to be proper under the provisions of Article V.

Section 9.6. *Waiver.* Failure by any Party to insist upon strict performance of any term or condition herein shall not be deemed a waiver of any rights or remedies that such Party may have against any other Party nor in any way affect the validity of this Agreement or any part hereof or the right of such Party thereafter to enforce each and every such provision. No waiver of any breach of this Agreement shall be held to constitute a waiver of any other or subsequent breach.

Section 9.7. *Governing Law.* This Agreement shall be governed by, construed and interpreted pursuant to the laws of the State of Illinois.

IN WITNESS WHEREOF, the Parties have each caused this Agreement to be executed by a duly authorized representative as of the day and year first above written.

NICOR INC.

By: Philip S. Cali
Name: Philip S. Cali
Title: Executive Vice President Operations

NORTHERN ILLINOIS GAS COMPANY

By: Philip S. Cali
Name: Philip S. Cali
Title: Executive Vice President Operations

BIRDSALL, INC.

By: George M. Behrens
Name: George M. Behrens
Title: Director

TROPIC EQUIPMENT LEASING INC.

By: George M. Behrens
Name: George M. Behrens
Title: Director and Vice President

TROPICAL BAHAMAS LTD.

By: George M. Behrens
Name: George M. Behrens
Title: Director

NICOR ENERGY VENTURES COMPANY

By: _____
Name: Daniel R. Dodge
Title: Vice President

NICOR ENERGY MANAGEMENT SERVICES COMPANY

By: _____
Name: Philip S. Cali
Title: Director and President

NICOR ENERGY SERVICES COMPANY

By: _____
Name: Philip S. Cali
Title: Director and President

NICOR ENERGY SOLUTIONS INC.

By: _____
Name: Daniel R. Dodge
Title Vice President

ENERCHANGE L.L.C.

By: _____
Name: Philip S. Cali
Title: Vice President

NICOR NGV CORP.

By: _____
Name: Philip S. Cali
Title: Director and President

NICOR TECHNOLOGIES INC.

By: _____
Name: Daniel R. Dodge
Title: Vice President

NICOR HOME SERVICES, L.L.C.

By: _____
Name: Daniel R. Dodge
Title: Vice President

NICOR HORIZON, INC.

By: _____
Name: Philip S. Cali
Title: Director and President

NICOR POWER HOLDING COMPANY

By: _____
Name: Daniel R. Dodge
Title: Vice President

NICOR ROCKY ROAD COMPANY

By: _____
Name: Daniel R. Dodge
Title: Vice President

NICOR OIL & GAS CORPORATION

By: _____
Name: Kathleen L. Halloran
Title: Vice President, Controller & Treasurer
Director

NICOR NATIONAL INC.

By: _____
Name: Kathleen L. Halloran
Title: Director and Treasurer

NICOR MINING INC.

By: _____
Name: Kathleen L. Halloran
Title: Vice President, Controller & Treasurer
Director

Exhibit A

Parties to the Operating Agreement

NICOR Inc. (Parent)
Northern Illinois Gas Company
Birdsall, Inc.
Tropic Equipment Leasing Inc.
Tropical Bahamas Ltd.
NICOR Energy Ventures Company
NICOR Energy Management Services Company
NICOR Energy Services Company
NICOR Energy Solutions Inc.
Enerchange L.L.C.
NICOR NGV Corp.
NICOR Technologies Inc.
NICOR Home Services, L.L.C.
NICOR Horizon, Inc.
NICOR Power Holding Company
NICOR Rocky Road Company
NICOR Oil & Gas Corporation
NICOR National Inc.
NICOR Mining Inc.

ADDENDUM

Short-term Borrowing and Investment between Parties

Cash advances made by Nicor Gas to a NICOR Entity pursuant to this Agreement shall be in accordance with the following terms:

(a) The balance of cash advances at any time shall not exceed the unused balance of funds actually available to the NICOR Entity under the NICOR Entity's existing bank credit agreement(s) or commercial paper facility(ies) entered into between the NICOR Entity and an unaffiliated third party or parties; and

(b) the interest rate on cash advances from Nicor Gas to a NICOR Entity shall be calculated at the higher of (i) the interest rate at which the NICOR Entity could have borrowed the funds pursuant to an existing bank credit agreement(s) or commercial paper facility(ies) entered into between the NICOR Entity and an unaffiliated third party or parties, or (ii) Nicor Gas' actual interest cost for the funds obtained or used to provide the cash advance to the NICOR Entity.

Cash advances made by a NICOR Entity to Nicor Gas pursuant to this Agreement shall be in accordance with the following terms:

(a) The balance of cash advances shall not at any time exceed the unused balance of funds actually available to Nicor Gas under Nicor Gas' existing bank credit agreement(s) or commercial paper facility(ies) entered into between Nicor Gas and an unaffiliated third party or parties; and

(b) the interest rate on cash advances from NICOR Entity to Nicor Gas shall be calculated at the lower of (i) the interest rate at which Nicor Gas could have borrowed the funds pursuant to an existing bank agreement(s) or commercial paper facility(ies) entered into between Nicor Gas and an unaffiliated third party or parties, or (ii) the NICOR Entity's actual interest cost for the funds obtained or used to provide the cash advance to Nicor Gas.