

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

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| NORTH SHORE GAS COMPANY                             | ) |                |              |
|   | ) |                |              |
| Proposed General Increase in Rates for Gas Service. | ) | No. 09-0166    |              |
|   | ) |                | On Rehearing |
|   | ) | No. 09-0167    |              |
| THE PEOPLES GAS LIGHT & COKE COMPANY                | ) |                |              |
|   | ) |                |              |
|   | ) | (consolidated) |              |
| Proposed General Increase in Rates for Gas Service. | ) |                |              |
|   | ) |                |              |

**THE PEOPLE OF THE STATE OF ILLINOIS'  
BRIEF ON REHEARING**

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The People of the State of Illinois, by and through Lisa Madigan, Attorney General of the State of Illinois (“the People” or “the AG”), respectfully submit their Brief on Rehearing pursuant to parts 200.800 and 200.880 of the Illinois Commerce Commission’s (“the Commission” ) Rules of Practice (83 Ill. Admin. Code 200.800, 880) and the schedule established by the Administrative Law Judges in this case.

### **I. Procedural Background**

In its Order of January 21, 2010 in this docket, the Commission approved, against the recommendations of the People, the Citizens Utility Board, and the Commission Staff, Peoples Gas Light & Coke Company’s (“Peoples Gas”) requested infrastructure cost recovery rider known as Rider ICR, which authorizes the utility to collect from ratepayers, from April through December each year, additional surcharges to recover a return of and on plant investments associated with cast iron/ductile iron (“CI/DI”) main replacement. In addition, the Commission ordered the Company to complete the CI/DI main replacement program by the year 2030. Order of January 21, 2010 at 196. In response to the AG’s argument that approval of the rider along with the requirement that Peoples complete the project by the year 2030 – 27 years faster than the existing main replacement plan -- would set Peoples Gas on a trajectory of regular rate increase requests and unjustified surcharges, the Commission ordered Peoples Gas to meet with the Commission Staff and establish a baseline that excluded from the rider “ongoing legacy costs” from the current main replacement plan and routine operating and maintenance costs. Order of January 21, 2010 at 179.

The People filed an application for rehearing that challenged the legality of Rider ICR, among other issues, as well as the Commission’s decision to illegally delegate its ratemaking authority to Peoples Gas and the Commission Staff in order to establish the Rider ICR baseline and other tariff definitions that would establish the amount Peoples Gas ratepayers will pay each month under the rider. The People argued, at a minimum, that both the Public Utilities Act and the Commission’s own rules require that a rehearing be conducted on the substantive issue of establishing the benchmark that determines the amount Peoples Gas customers will pay under the rider -- especially in light of the Commission’s own acknowledgment that the evidentiary record lacks the information necessary to set the benchmark. Final Order at 179.

The People also argued in the AG Application for Rehearing that the Public Utilities Act (“the Act”) sets forth various findings the Commission must make before the Commission may approve the proposed rates of a utility. Among those findings is the requirement that the Commission determines whether the proposed rates are just and reasonable. 220 ILCS 5/9-101, 9-201. In order to make such decisions, the Commission holds hearings and then issues an order announcing its findings, the basis for its findings and its decision. *See Business and Professional People for the Public Interest v. Illinois Commerce Comm’n*, 136 Ill.2d 192, 209 (1989) (“*BPI I*”).

The People pointed out that the “agreement” reached between the Company and Staff on the baseline figure for Rider ICR amounts to the kind of partial settlement that the Illinois Supreme Court in *BPI I* deemed illegal.<sup>1</sup> When it ordered Peoples Gas in the

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<sup>1</sup> In that decision, the Court reviewed a Commission Order in a ComEd rate case that established rates through a settlement proposal negotiated between the Commission Staff and the utility. While the Commission stated in its Order that it judged the “settlement” as a traditional rate case based on the evidence in the record, the Court ruled that in fact the Commission judged the matter outside the context of

instant case to “meet with Staff to determine the baseline for calculating the costs that can properly be recovered under the rider as modified herein” and then file a statement with the Commission “outlining how the Company will calculate the portion of the accelerated program that is limited to those costs determined to be beyond the agreed upon baseline” (Final Order at 179), the Commission accepted a non-unanimous settlement between the Company and Staff that established Rider ICR tariff rates without any finding that the baseline and tariff terms created were just and reasonable.

On March 10, 2010, the Commission denied in part and granted in part the People’s and CUB’s applications for rehearing, and granted the City of Chicago’s application for rehearing, on the issue of establishing a baseline for Rider ICR based on record evidence. Notice of Corrected Commission Action of March 11, 2010.

On April 8, 2010, the Company filed the direct testimony of Salvatore Marano and PGL employee Christine Gregor. Ms. Gregor testified that routine operations and maintenance costs will not be considered as part of the rider ICR recovery amount. NS-PGL Ex. CMG-5.0 at 2. Mr. Marano testified that, in his opinion, the baseline for Rider ICR should be set at \$45,275,708 for 2011 (rounded to \$45.28 million in the Rider ICR tariff) and that the Handy-Whitman Index January Index (published by Whitman, Requardt and Associates, LLP) should be used as the 2011 base index escalator to capture the effects of inflation on the benchmark amount. NS-PGL Ex. SDM-4.0 at 14. Mr. Marano testified

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a traditional rate case. The Court concluded that “the Commission treated the ...Order as a settlement and failed to base its decision exclusively on the record.” *Id.* at 212. The Court further held that if a settlement proposal has unanimous support, the Commission can adopt it as a settlement. However, if the proposal lacks unanimous support, the agency may adopt it “if the agency makes an independent finding, supported by substantial evidence in the record as a whole, that the proposal would establish just and reasonable rates”. *Id.* at 217.

that that baseline amount represented the construction costs associated with replacing 45 miles of CI/DI main annually. *Id.* at 6, 9.

The Commission Staff filed the testimony of Dianna Hathhorn in response to the Company's testimony, in which she stated that she had no objection to the new baseline established by the Company and that she was satisfied that no routine O&M expenses associated with the main replacement project would be recovered in the rider. ICC Staff Ex. 30.0 on Rehearing at 2, 4, 5. Ms. Hathhorn also testified that the Company had agreed to changes in language to the audit provisions of the Rider ICR tariff that provided (1) a test to verify the rider baseline was calculated and applied correctly to the ICR Charge Percentage; and (2) independent audits conducted every five years include a requirement to review the number of miles completed during the audit period. *Id.* at 3, 4.

The Company's response to AG Rehearing Data Request 2.01 was also admitted into the record. That response, attached to this Brief at Attachment A, asked the Company to provide "the Company's best estimate of revenues to be collected under Rider ICR from 2011 through 2030, assuming the baseline proposed by Mr. Marano in his April 8, 2010 testimony, and assuming the Company satisfies the Commission's directive to complete CI/DI main replacement by the year 2030." The request also sought customer bill impacts associated with these estimated revenue levels, and asked the Company to indicate each instance in which it is assumed that Peoples has filed a rate case in order to reset the 5% of base rate revenue cap provided in the Rider ICR tariff. Attachment A, AG Cross Ex. 1 on Rehearing. The record was marked heard and taken on May 6, 2011.

## **II. The Establishment of a Baseline Revenue Recovery Level for Rider ICR Does Not Alter the Illegality of the Rider.**

As thoroughly discussed in the People's prior briefs in this docket, as well as the AG Application for Rehearing, the Commission's adoption on January 21, 2010 of Rider ICR ignores critical evidence, omits any evaluation of crucial points raised by Staff, the AG and CUB, and misinterprets Illinois law regarding when riders are permissible. In addition, the Commission's decision to require Peoples Gas to complete CI/DI main replacement in the City of Chicago by the year 2030 was not supported by substantial evidence. While the Marano testimony presented by Peoples Gas envisioned a 2030 preferred acceleration completion date for purposes of demonstrating the time value of money, the testimony in no way argued that completion by 2030 was necessary for system safety and reliability. In addition, the terms of Rider ICR will not cure the rate impact effect of the deadline. Under the rider, Peoples is permitted to recover revenues associated with main replacement investment above the baseline established in this rehearing up to an amount that equals 5% of Rider ICR base rate revenues. The ordered 2030 deadline will set the Company on a rate case trajectory that the evidence shows will likely trigger regular rate cases for years to come in order to permit the Company to recover the revenue allegedly needed to finance the main replacement project. *See* AG Initial Brief, pp. 20-27, 28-34, 37-42, 44-46; AG Reply Brief, at 6-12, 17-19; AG Brief on Exceptions at 11-13, 17-22 and 22-30; AG Application for Rehearing at 9-29.

Given the limited scope of this rehearing, which is to establish the appropriate baseline of Rider ICR for purposes of revenue recovery through the rider tariff and reflect necessary changes to the rider tariff, the People will not repeat those arguments here. However, it should be noted that the establishment of a baseline that effectively reduces

the amount of revenue to be collected through the rider, does not change the illegality of the underlying rider. The arguments articulated in the briefs cited above continue to apply to the newly configured Rider ICR, notwithstanding the newly established baseline. The Commission's decision to saddle ratepayers with monthly surcharges, over and above the rate increase approved on January 21, 2010, by approving a rider for recovery of cast iron main replacement expenses – expenses that only two years ago it concluded were “the subject of routine, traditional Commission ratemaking”<sup>2</sup> -- was not supported by substantial evidence, contrary to law, arbitrary and capricious and beyond the jurisdiction of the Commission.

### **III. The Commission's Establishment of a Baseline for Rider ICR Revenue Recovery Does Not Establish Just and Reasonable Rates.**

As the People noted in the AG Application for Rehearing, the Commission cannot fulfill its statutory duty to balance the competing interests of stockholders and ratepayers without taking into account the interests of ratepayers by considering the impact of a proposed rate on ratepayers. *Citizens Utility Board v. Illinois Commerce Comm'n*, 276 Ill.App.3d 730, 737 (1995). In addition, 9-101 and 9-201(c) of the Act requires the Commission to establish only just and reasonable rates. 220 ILCS 5/9-101, 9-201.

AG Cross Exhibit 1 (Appendix A to this Brief), which is the aforementioned Company response to the People's request for revenue and bill impact data associated with the revised Rider ICR through the 2030 deadline prescribed in the Commission's January 2, 2010 Order, indicates that the Company estimates it will collect through the rider an additional \$8.2 million in 2011, \$21.3 million in 2012 and \$25.4 million in 2013.

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<sup>2</sup> ICC Docket Nos. 07-0241, 07-0242, Order of February 5, 2008 at 160-161.

The investment amounts relative to cast iron main replacement for those years are \$180.4 million in 2011, \$101.8 million in 2012 and \$108.8 million in 2013. *See* Appendix A (AG Cross Exhibit 1 on Rehearing, pages 2-4, 5, 8, 11).

In the response, the Company also stated that it “did not calculate revenue estimates beyond 2013 as the estimated revenues in 2013 would meet the capped revenues allowed under Rider ICR.” *Id* at 1. Under the operation of Rider ICR, in order to increase the amount to be collected under the Rider, the Company would have to file a rate case. That is because Rider ICR’s so-called revenue “cap” is calculated by multiplying 5% times the annual ICR base rate revenues. ICC Staff Ex. 30.0 on Rehearing, Attachment A, p. 2 Of 9; PGL Ex. VG-1.14 at 3 of 12. Specifically, under the tariff, the “annual ICR base rate revenue” increases each time plant additions are added to the Company’s rate base. So as Peoples’ rate base and revenue requirement grows, so too does the amount under the 5% “cap” that can be recovered from ratepayers.<sup>3</sup> This phenomenon was confirmed by Staff witness Dianna Hathhorn in the case below. Tr. 709-711. Thus, as acceleration of infrastructure and the filing of rate cases occurs, the amount that can be collected under Rider ICR grows.

The Company’s response to AG RHG 2.01 (Appendix A) indicates that in order to (1) maintain the Commission-ordered 2030 completion date, and (2) continue to pay for accelerated CI/DI main replacement through the rider that keeps pace with the required investment, the Company will have to file regular rate cases. The Commission’s response to this issue in its Final Order of January 21, 2010, when raised in briefs and oral argument below, was to require the establishment of a baseline that would exclude

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<sup>3</sup> As a simple hypothetical, if Peoples’ base rate revenue is 500 million, the cap would allow revenues of \$25 million. If the Company files a rate case and another 50 million is added to the revenue requirement, then the tariff permits \$27.5 million to be collected under the tariff, and so on.

legacy replacement costs from rider recovery. Order of January 21, 2010 at 179.

However, as noted above, the Company's data request response reveals that within three years, the Company would have to file a rate case in order to recover more revenues under the rider.

Mr. Marano himself testified that adoption of a 2030 completion date would require Peoples to step up main replacement from the forecasted 10 miles per year in 2010 to 114 miles per year. Tr. at 831-833. Given the Company's testimony that a \$45.28 million baseline covers the total construction cost of about 45 miles of CI/DI main replacement, the evidence suggests that regular rate cases will be essential to both permit the Company to keep pace with the 114-mile annual replacement rate, increase the amount to be collected through the rider, and recover the increased expenses *not* recovered through the rider that are tied to the rigorous 2030 completion deadline. As noted in the People's application for rehearing, the Commission is obligated to examine the revenue requirement effect of that 2030 requirement, coupled with the approval of Rider ICR, and consider its impact on ratepayers. While the Commission's decision to establish a legacy baseline reduced the amount that can be recovered through the rider, the Commission must assess the true impact of its conclusions on both the approval of the rider and the 2030 timetable. That still has not occurred on rehearing.

In order for the Commission to have confidence that it has established just and reasonable rates, the Commission must specifically examine the impact of requiring Peoples Gas to complete the main replacement program by 2030 and collect rider surcharges for investment above \$45 million (as adjusted by the Marano-recommended inflationary index) on the Company's revenue requirement needs, expected rider

surcharges and Peoples Gas ratepayers. The response to AG RHG 2.01 fails to provide sufficient information for the Commission to conclude that rates under these conditions are, in fact, just and reasonable. Requiring a company to accelerate main at a rate 11 times greater than the most recent forecasted replacement rate will have significant impacts on the rates customers pay – with or without the reconfigured Rider ICR. In no way can the rates that will be collected under the rider in the coming years, and the trajectory of rate cases that will necessarily follow because of the operation of the rider and the Commission’s ordered-2030 deadline, be considered “just and reasonable” under 9-101 and 9-201 of the Act.

The People urge the Commission to reconsider its approval of Rider ICR and the mandated 2030 deadline in light of the totality of the evidence in this case.

**Conclusion**

WHEREFORE, for all of the reasons stated above, the People of the State of Illinois respectfully request that the Commission enter an Order in accordance with the recommendations presented herein.

Respectfully submitted,

THE PEOPLE OF THE STATE OF ILLINOIS

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