

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

NORTH SHORE GAS COMPANY	:	
	:	No. 09-0436
THE PEOPLES GAS LIGHT AND COKE COMPANY	:	and
	:	No. 09-0437
Petition Pursuant to Rider EEP of Schedule of Rates for	:	(Cons.)
Gas Service to Initiate a Proceeding to Determine the	:	
Accuracy of the Rider EEP Reconciliation Statement.	:	

**INITIAL BRIEF OF NORTH SHORE GAS COMPANY
AND THE PEOPLES GAS LIGHT AND COKE COMPANY**

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North Shore Gas Company (“North Shore”) and The Peoples Gas Light and Coke Company (“Peoples Gas”) (together, “the Utilities”), by their counsel, submit this Initial Brief.

INTRODUCTION

These are reconciliation Dockets under the Utilities’ “Rider EEP - Enhanced Efficiency Program” (“Rider EEP”). The Chicagoland Natural Gas Savings Program (“Chicagoland” or the “Program”) operates a portfolio of energy efficiency measures determined by its independent Governance Board. The Board has five voting members, *i.e.*, the Illinois Attorney General’s Office (the “AG”), the Citizens Utility Board (“CUB”), the City of Chicago (the “City”), the Environmental Law and Policy Center (“ELPC”), and the Utilities, plus Illinois Commerce Commission (the “Commission” or “ICC”) Staff (“Staff”) as a non-voting member. The Utilities fund the Program and recover those costs under Rider EEP. The Program, the Board, and the riders were established by the Commission’s Order in the Utilities’ 2007 rate cases.

The Utilities’ compliance with Rider EEP is uncontested. There is no accounting dispute.

Staff disagrees, however, with the independent Governance Board’s decision to include certain measures in the portfolio and seeks to disallow 100% of the costs the Utilities spent on those measures. Staff’s proposed adjustments are improper. To approve the adjustments would

require the Commission to find both (1) that the Board made imprudent decisions no reasonable person would make *and* (2) that the Utilities should be held responsible for those decisions in the form of disallowances of the associated costs. The law and the facts permit no such findings. Moreover, Staff's proposed adjustments are based on nothing more than Staff's policy disagreements with the Board and also are against the public interest. They also are excessive and punitive. The adjustments should be rejected.

DISCUSSION

The Utilities have presented testimony and reports showing that they complied with Rider EEP, that the funds they spent on the Program were spent as directed by its independent Governance Board, and that the Utilities have correctly accounted for their costs and revenues under Rider EEP. Staff disputes none of those points, as discussed in Section I, below.

The Commission's prudence standard also is undisputed. Under the standard:

- Prudence is the standard of care that a reasonable person would be expected to exercise under the same circumstances encountered by utility management at the time decisions had to be made.
- Hindsight review is impermissible.
- Imprudence cannot be sustained by substituting one's judgment for that of another.
- Reasonable persons can have honest differences of opinion without one or the other necessarily being imprudent.

E.g., Illinois Power Co. v. Illinois Commerce Comm'n, 339 Ill. App. 3d 425, 428, 431-432, 435, 439-444 (5th Dist. 2003) (reversing Commission prudence disallowance as arbitrary and unreasonable and based on hindsight); *Illinois Commerce Comm'n on Its Own Motion v. The Peoples Gas Light and Coke Co.*, ICC Docket No. 00-0720, pp. 5-9 (Order Jan. 24, 2002)

(rejecting City’s proposed imprudence disallowance); Brightwell Direct (“Dir.”), Staff Exhibit (“Ex.”) 2.0, 3:44-56 (citing *Commonwealth Edison Co.*, ICC Docket No. 84-0395, p. 17 (Order Oct. 7, 1987)).

Staff asserts “imprudence” claims, but they really are no more than policy disagreements with the Board and they do not constitute imprudence under the prudence standard. Staff previously opposed both the Program and the vesting of Program decisions in the independent Governance Board. The Commission rejected those two Staff positions, however, in its Order in the Utilities’ 2007 rate cases. Illinois law also now mandates that gas utilities conduct energy efficiency programs. 220 ILCS 5/8-104. Now, Staff disagrees with certain Program decisions of the Board and contends that the Utilities not only should be held responsible for those “imprudent” decisions but should experience draconian 100% disallowances of their costs of complying with those decisions. Staff disagrees with the following Board Program decisions, none of which is a proper basis for an imprudence finding:

- The independent Governance Board, with expert advice, decided to adopt a portfolio of energy efficiency measures, decided that the essential prudence determination was the prudence of the portfolio, and adopted a prudent portfolio.
- The Board, with expert advice, in determining the portfolio, took into account benefits that are difficult to quantify, such as contributing to customer awareness of energy efficiency and market transformation, as well as quantitative benefits.
- The Board, with expert advice, decided that the measures in the portfolio should include, among others, rebates for tankless water heaters, high efficiency clothes washers, and wall insulation.

- The Board, with expert advice, decided to consider the Total Resource Cost (“TRC”) test, which calculates the ratio of certain (not all) of a measure’s incremental benefits to the measure’s incremental costs, as a factor in deciding which measures to include in the portfolio, but also decided not to exclude measures based solely on a TRC test result being below 1.0.

For Staff to seek to substitute its judgment for that of the Board, as Staff seeks to do here, turns upside down the Commission’s prudence standard and the Program governance structure approved by the Commission, as discussed in Section II(A), below.

Furthermore, Staff’s improper rejection of the Board’s decision that portfolio level prudence is what matters, Staff’s disregard for the fact that it is uncontested that the portfolio as a whole is prudent and passes even the TRC test, and Staff’s improper rejection of the Board’s decision that the TRC test should not be used to the exclusion of all else in deciding which individual measures to include in the portfolio, are erroneous and contrary to the public interest, as discussed in Section II(B) through (E), below.

Staff’s proposed adjustments also are excessive and punitive, because Staff seeks to disallow not the amount by which the costs of the challenged measures exceed the subset of benefits that are considered in the TRC test, but rather 100% of the costs, as discussed in Section II(F), below.

Staff’s proposed adjustments should be rejected. They are unlawful and wrong.

II. UNCONTESTED ISSUES

The Program period that is the subject of this consolidated Docket is May 1, 2008, through June 30, 2009. Korenchan Dir., North Shore (“NS”) Ex. 1.0, 3:49-55; Korenchan Dir.,

Peoples Gas (“PGL”) Ex. 1.0, 3:53-55. As to this period, the Utilities complied fully with their obligations under their Rider EEPs,¹ and that compliance is uncontested, as discussed below.

A. Statement of Activity

Each Rider EEP requires the utility to submit a statement of activity for the applicable period. Michalkiewicz Dir., NS Ex. 2.0, 4:55-59; Michalkiewicz Dir., PGL Ex. 2.0, 4:55-59.

Mr. Michalkiewicz presented the Rider EEP Statement of Activity for North Shore (Michalkiewicz Dir., NS Ex. 2.0, 4:63-71; NS Ex. 2.1) and the Rider EEP Statement of Activity for Peoples Gas (Michalkiewicz Dir., PGL Ex. 2.0, 4:63-71; PGL Ex. 2.1.), for May 1, 2008, through June 30, 2009.

The Statements of Activity contain a description of the Program and the portfolio, namely: (1) measures implemented to achieve energy efficiency goals; (2) the performance modeling and cost effectiveness calculator used to screen individual energy efficiency measures and establish the overall program cost effectiveness; (3) community outreach and education efforts; (4) program contract administration; (5) expenses; and (6) goals and performance metrics. NS Ex. 2.1; PGL Ex. 2.1. The measures implemented to achieve energy efficiency goals consisted of certain rebate programs, a multi-family low income program, and whole home scale-up retrofit. NS Ex. 2.1 at pp. 3-4; PGL Ex. 2.1 at pp. 3-4.

Mr. Michalkiewicz also explained, as discussed earlier, that the Program is governed by an independent Governance Board consisting of five voting members: the AG, the City, CUB, ELPC, and the Utilities, with Staff as a non-voting participant on the Board. Michalkiewicz Dir., NS Ex. 2.0, 2:30 - 338; Michalkiewicz Dir., PGL Ex. 2.0, 2:30 – 3:38.

¹ ILL. C. C. No. 17, Fifth Revised Sheet No. 53, *et seq.* (North Shore); ILL. C. C. No. 28, Fourth Revised Sheet No. 54, *et seq.* (Peoples Gas).

Staff witness Ms. Hathhorn reviewed the Statements of Activity and identified no concerns with them, other than referencing the “imprudence” adjustments proposed by Staff witness Dr. Brightwell. Hathhorn Dir., Staff Ex. 1.0, 3:50-65.

B. Statement of Reconciliation Adjustments

Rider EEP calls for the Utilities to file charges (called the “Effective Component”) with the Commission each year. Korenchan Dir., NS Ex. 1.0, 2:35-36; Korenchan Dir., PGL Ex. 1.0, 2:35-36. The Effective Component is a monthly per-customer charge based on the Annual Program Budget approved by the Commission in the utility’s most recent rate case. Korenchan Dir., NS Ex. 1.0, 2:36-38; Korenchan Dir., PGL Ex. 1.0, 2:36-38. Rider EEP is applicable to Service Classifications (“SC”) Nos. 1 (Small Residential Service) and 2 (General Service), and there is a separate Effective Component for each Service Classification. Korenchan Dir., NS Ex. 1.0, 3:38-40; Korenchan Dir., PGL Ex. 1.0, 3:38-40.

Each Rider EEP also calls for the utility to submit a report on their reconciliation adjustments (“RA”), reconciling the costs and revenues accrued under the riders for the applicable period and addressing any reconciling adjustments. Korenchan Dir., NS Ex. 1.0, 3:40-48; Korenchan Dir., PGL Ex. 1.0, 3:40-48.

Mr. Korenchan presented the Statement of Reconciliation Adjustment for North Shore (Korenchan Dir., NS Ex. 1.0, 4:62-67; NS Ex. 1.1) and the Statement of Reconciliation Adjustment for Peoples Gas (Korenchan Dir., PGL Ex. 1.0, 4:62-67; PGL Ex. 1.1), for May 1, 2008, through June 30, 2009.

Page 2 of each Statement of Reconciliation Adjustment demonstrates how the Utilities calculated the RA for each Service Classification. NS Ex. 1.1 at p. 2; PGL Ex. 1.1 at p. 2; Korenchan Dir., NS Ex. 1.0, 4:78-5:96; Korenchan Dir., PGL Ex. 1.0, 4:78-5:96. For each

Classification, the following information was included in the RA calculations: (1) the Carry Over Budget Amount; (2) the Total Reconciliation Adjustment dollar amounts, including Carry Over amount and applicable Interest; and (3) the monthly per-customer RA. *Id.*

C. Correctness of Accounting

There is no dispute over the correctness of the Utilities' accounting for their costs and revenues under the riders and the RAs. Staff witness Ms. Hathhorn reviewed the Utilities' Statements of Reconciliation Adjustments for the May 1, 2008, to June 30, 2009, period. Hathhorn Dir., Staff Ex. 1.0, 3:50-65. Ms. Hathhorn testified that she recommends that the Commission accept the reconciliations of SC No. 2. *Id.* at 6:116-119. She also recommends that the Commission accept the reconciliations of SC No. 1, except for the "imprudence" disallowances recommended by Staff witness Dr. Brightwell, described below. *Id.* at 4:67 – 6:113 and Schedules ("Sched.") 1.1, 1.2, 1.3, and 1.4.

II. CONTESTED ISSUES

A. The Independent Governance Board's Program Decisions Should Not Be Subject to Prudence Review and Should Not Be a Basis for Denying the Utilities Recovery of Their Costs of Complying With Those Decisions

Staff's claims of imprudence are based entirely on Staff's contentions that the independent Governance Board made non-cost-effective decisions in including three measures in the Program's portfolio and that the Utilities should be subject to disallowances of their costs of complying with those decisions.

The Board's Program decisions (decisions about what measures to include in the portfolio and other policy decisions) should not be a basis for imprudence findings against the Utilities and for disallowances of the Utilities' cost recovery, for two different reasons.

- First, the Commission should give deference to the Board’s Program decisions. The Commission established the governance structure of the Program to ensure prudence. Staff has identified no legitimate basis for second-guessing the Board’s Program decisions. There is no claim of misappropriation of funds.
- Second, because Staff’s disagreements with Board Program decisions are the sole basis of Staff’s imprudence claims, but the question in this proceeding is whether to disallow costs incurred by the Utilities, any prudence review in these Dockets should be limited to two questions: (1) Did the Utilities act prudently in proposing that the Board be in charge of Program decisions? and (2) Did the Utilities act prudently in paying costs of measures in compliance with the Board’s Program decisions? The answer to both questions can only be yes.

Each of those reasons independently should conclude the contested issues in these Dockets.

1. Background

Because the disputed question in these Dockets is whether, under the prudence standard, the Utilities should be denied recovery of certain amounts they spent in compliance with Program decisions of the Board, it is important to understand the genesis of the Program and the Board, including the Commission’s role in establishing them in prior Dockets.

a. The Reorganization Docket

In ICC Docket No. 06-0540, the Commission considered and approved, with certain specified conditions, the transaction by which Integrys Energy Group, Inc. (f/k/a WPS Resources Corp.) became the ultimate parent company of the Utilities. *WPS Resources Corp., et al.*, ICC Docket No. 06-0540 (Order Feb. 7, 2007) (“*WPS Order*”). The intervenors in the reorganization Docket included the AG, the City, CUB, ELPC, the Cook County State’s Attorney’s Office

(“CCSAO”), the Utility Workers Union of America, AFL-CIO, and UWUA Local Union No. 18007 (“UWUA”), Constellation NewEnergy – Gas Division, LLC, and an *ad hoc* group of five retail gas suppliers. *WPS Order* at p. 2.

One of the issues originally contested in the reorganization Docket was ELPC’s proposal that the Commission should order the Utilities to adopt various energy efficiency programs as a condition of approval of the transaction. *WPS Order* at pp. 16-18, 20-23.

The AG, the City, CUB, ELPC, CCSAO, UWUA, and the Utilities ultimately entered into and proposed a Memorandum of Agreement (“MOA”) that proposed resolutions of all contested issues in the Docket among those parties, including the ELPC proposal. *WPS Order* at pp. 3, 16, *et seq.* Among the provisions of the MOA (as specified in more detail in the MOA) were that the Utilities agreed to propose in their then-upcoming 2007 rate cases an energy efficiency program or programs, including spending at an aggregate annual level of \$7.5 million, a third party administrator to implement the program(s), and a mechanism for the recovery of the costs of the program(s), with the proviso that the Utilities would not be obligated to fund the program(s) beyond the amount of cost recovery provided for by the Commission in the rate cases. *WPS Order* at p. 24. The MOA also noted that Staff and intervenors could oppose, or propose changes to, the program(s) and the cost recovery mechanism in the rate cases. *Id.* Staff was not a party to the MOA, but Staff signed it to memorialize that Staff did not oppose the MOA. *Id.* at p. 3.

The Commission’s final Order approved the MOA, and, accordingly, directed, among others, the above terms (as specified in more detail in the Order). *WPS Order* at pp. 23-25 and Appendix (“App.”) A (“Conditions of Approval”) at Condition Nos. 27-30.

Although the MOA and the *WPS Order* provided for a third party administrator, neither provided for the independent Governance Board. *See WPS Order* at pp. 16-18, 20-25, and App. A at Condition Nos. 27-30.

The MOA also provided in part that the intervenors that were parties to the MOA and the Utilities agreed to engage in post-Order discussions in good faith to develop the details of the energy efficiency programs to be proposed in the rate cases, and the *WPS Order* directed the Utilities to participate in those discussions. *WPS Order* at p. 25 and App. A at Condition No. 28.

After the *WPS Order*, the parties to the MOA discussed the specifics of the energy efficiency program that the Utilities would propose in their 2007 rate cases, as indicated in the next subsection of this Brief.

b. The 2007 Rate Cases

In their 2007 rate cases, pursuant to the *WPS Order* and the post-*WPS Order* discussions with the MOA parties, the Utilities proposed an energy efficiency program (now known as the Chicagoland Natural Gas Savings Program), including the independent Governance Board consisting of five voting members, *i.e.*, the AG, the City, CUB, ELPC, and the Utilities, plus Staff as a non-voting member, and also including an independent Contract Administrator, an independent Program Administrator, and an independent Program Evaluator. *North Shore Gas Co., et al.*, ICC Docket Nos. 07-0241, 07-0242 (Cons.), pp. 163-167 (Order Feb. 5, 2008) (“*2007 RC Order*”). The Utilities also proposed riders to provide for their recovery of the costs they incurred under the Program. *Id.*

Staff opposed the proposed energy efficiency program on the merits, including on the theory that even if the overall program were cost-effective efficiency required that each individual measure have net benefits, and also objected to the administrative structure and urged

that, if the program were adopted, the Board appoint a single Director with clear authority over the program and that personnel and administrative costs should be capped at 5%. *2007 RC Order* at pp. 167-168. Staff also argued that, if the program were adopted, the Utilities should recover their costs through base rates. *Id.* at pp. 168-170.

ELPC strongly disagreed with Staff's claims regarding the merits of the program, and with Staff's proposal of a Director. *2007 RC Order* at pp. 171-174. Among other things, ELPC contended that the governance structure of the program, including the independent Governance Board, and the numerous audits and evaluations, assured that the program costs would be prudent. *Id.* at p. 172. ELPC also argued for cost recovery through base rates. *Id.* at p. 174.

The AG, CUB, and the City, together as "GCI", also strongly disagreed with Staff's claims regarding the merits of the program, and disagreed with Staff's proposal of a Director, although CUB and the City said they would not object if the Commission were to prescribe additional oversight. *2007 RC Order* at pp. 174-180. GCI also argued for cost recovery through base rates. *Id.* at pp. 181-182.

The Commission rejected Staff's positions, other than Staff's proposed administrative cost cap and Staff's alternative proposed language changes for the riders, which the Utilities did not oppose. *2007 RC Order* at pp. 183-184. The Commission found, among other things, that

- "Energy efficiency programs are socially desirable".
- "[T]he proposed governance structure for the program should ensure independence from the Utilities and will likely result in representation of all or substantially all relevant interests."
- "With proper independent governance and oversight, and with the selection of appropriate, cost-effective efficiency measures, the Commission believes that the

proposed programs will make a significant positive contribution to the benefit of all ratepayers. Accordingly, the Commission orders the Utilities to implement the energy efficiency program as proposed. We find the structure to be fair and reasonable”.

- “More important in our decision to adopt the Utilities’ rider treatment is that the manner in which this money will be spent is far beyond the Utilities’ control. [Citation omitted.] As set out on record, the Governance Board’s voting procedure ensures the independence of the board from the Utilities. Because the Utilities do not “control” how much of the \$7.5 million will be spent each year, it is not appropriate for the program costs to be included in rate base.”
- “Further, knowing that the energy efficiency program will be administered by an independent board lessens our concern over the costs of administering Rider EEP. In other words, and given the composition of this body, we expect that that [*sic*] any reconciliation proceedings would likely not be litigious because most, if not all interested parties, would have had a say in the efficiency program spending process.”

Id. The Commission’s rulings did not include any requirement that each individual measure in the Program had to have net benefits in order to be included in the portfolio.

2. Deference Should Be Given to the Independent Governance Board’s Program Decisions

The evidence confirms that the independent Governance Board in fact plays the role in the Program that the Commission directed. The Board, not the Utilities, is responsible for establishing Program goals and performance criteria, overseeing the creation and issuance of requests for proposals, and selecting the various experts who design and implement the Program,

namely the independent Contract Administrator, the independent Program Administrators, and the independent Program Evaluator. Michalkiewicz Dir., NS Ex. 1.0, 3:39-48; Michalkiewicz Dir., PGL Ex. 1.0, 3:39-48. The Board also formed an Operating Committee, with one representative for each voting member of the Board, to assist it in analyzing Rider EEP measures. Schott Reb., NS-PGL Ex. 3.0, 4:47-50. Staff has been a regular and active participant in Board meetings. *Id.* at 4:55-59.

The Board received and considered extensive information and advice from its independent expert advisors in making the decisions that Staff challenges, as witnesses Ms. Beitel and Mr. Plunkett have testified in great detail. Ms. Beitel testified that the Chicagoland Natural Gas Savings Program was designed by highly experienced energy efficiency professionals, including her firm, Future Energy Enterprises, whose two principals have a combined four decades of experience with energy efficiency program design, administration and implementation for the largest energy efficiency portfolio in the world; Resource Solutions Group, which also has decades of experience with energy efficiency program design, administration and implementation; the Center for Neighborhood Technology, which provided expertise on local building characteristics, findings from numerous home energy retrofit projects, and energy modeling for several measures; the Midwestern Energy Efficiency Alliance, which provided benchmarking from other Midwest energy efficiency programs and additional information on Chicago area residential buildings; and Mr. Plunkett's firm, Green Energy Economics Group, to which he brings over 30 years in utility planning, concentrating on energy efficiency. Beitel Reb., NS-PGL Ex. 4.0, 8:169 - 9:188; Plunkett Reb., NS-PGL Ex. 5.0, 1:4 - 4:88. She explained the prudence of the Program design: the design team employed their experience and best judgment, conducted measure analysis, cost-effectiveness analysis, and

developed benchmarks of other residential gas programs throughout the Midwest. Beitel Reb., NS-PGL Ex. 4.0, 9:189-194; *see also* Plunkett Sur., NS-PGL Ex. 7.0, 9:190-197. Staff does not and cannot deny the facts regarding the information and advice received by the Board from its independent expert advisors.

The Board, by unanimous vote, with the input of and consistent with the recommendations of its independent expert advisors, approved the overall portfolio of measures as a portfolio, including the three measures that are the subject of Staff witness Dr. Brightwell's proposed "imprudence" disallowances. Schott Reb., NS-PGL Ex. 3.0, 4:60-63; Beitel Reb., NS-PGL Ex. 4.0, 4:71 – 6:127.

Mr. Schott testified that, given the Commission-approved governance structure, the Commission should deem the decisions of the Governance Board to be prudent, absent some sort of hypothetical misappropriation of funds scenario such as a Board decision to spend Program funds on a Board junket to Europe. Schott Reb., NS-PGL Ex. 3.0, 5:70-82; Schott, Tr. at pp. 41, 43, 46-47. The very creation and selection of the Board established prudence as to Board decisions. Schott, Tr. at p. 46.

Because deference should be given to Board Program decisions, and there is no claim of misappropriation, there is no basis for an imprudence finding, much less one that can be ascribed to the Utilities to justify disallowing recovery of the costs of complying with those decisions.

3. The Utilities Acted Prudently in Proposing the Board and Complying With Its Program Decisions

Staff's rationale for claiming that the Utilities should be held responsible for the prudence of the independent Governance Board's Program decisions is fatally flawed, even if, in the abstract, prudence review of Board Program decisions is not barred. Staff's rationale ignores

the underlying history here, including the roles of the MOA intervenors and the Commission, and does not logically and fairly lead to Staff's conclusion.

Staff witness Dr. Brightwell argues that the Utilities should be held responsible for the prudence of the Board's decisions on the following basis:

Q. Why should the Companies be held responsible for the prudence of decisions made by an independent Governance Board?

A. The Companies are the parties who filed this plan and recommended the independent Governance Board. Since they filed the plan, the risk of imprudence should be their responsibility not the ratepayers.

Brightwell Dir., Staff Ex. 2.0, 4:74-78. Dr. Brightwell gives no weight at all to the fact that the Program is determined by an independent Governance Board or to the role of other stakeholders in the proposal. Brightwell, Tr. at pp. 220, 222.

Staff's rationale cannot withstand examination in light of the history discussed in Section II(A)(1), above. The original proposal for an energy efficiency program was made by the ELPC in the reorganization Docket. The MOA intervenors and the Utilities ultimately agreed to recommend to the Commission that the Utilities propose an energy efficiency program in their 2007 rate cases, subject to cost recovery. The MOA intervenors and the Utilities discussed what should be in the proposal. The Utilities then proposed the Program and the Board in the 2007 rate cases. The Commission approved the Program and the Board.

Moreover, the Board's five voting members include three entities, a voting majority, that represent customers: the AG, CUB, and the City. In addition, the vast majority of the costs sought to be recovered by the Utilities, *i.e.*, everything but the small amount of administrative costs, consists of amounts paid out to customers. *See* NS Ex. 2.1, p. 15; PGL Ex. 2.1, p. 15. Holding the Utilities responsible for the alleged imprudence of Program costs, and on that basis

denying them recovery of the amounts they paid out to customers and of the small associated administrative costs, is not logical and it is not fair.

Rates must be just and reasonable to utilities and their shareholders, as well as to customers. 220 ILCS 5/9-201(c); *Bus. and Prof. People for the Pub. Interest v. Illinois Commerce Comm'n*, 146 Ill. 2d 175, 208-209 (1991).

Under all of the circumstances, it is not reasonable or just that the Utilities and their shareholders bear the risk of allegedly imprudent Board Program decisions, absent a hypothetical misappropriation of funds that no one claims occurred here.

Because Staff's disagreements with Board decisions are the sole basis of Staff's imprudence claims, but the question in this proceeding is whether to disallow costs incurred by the Utilities, any prudence review in these Dockets should be limited to two questions: (1) Did the Utilities act prudently in proposing that the Board be in charge of Program decisions? and (2) Did the Utilities act prudently in paying costs of measures in compliance with the Board's Program decisions? The answer to both questions can only be yes. That should conclude the contested issues in these Dockets.

The earlier discussion of the history shows that there can be no conclusion other than that the creation of the Board was prudent, and, accordingly, the Utilities cannot be said to have acted imprudently in proposing the Board. *See also* Schott, Tr. pp. 44-45.

There also can be no conclusion other than that Utilities acted prudently in paying costs of measures in compliance with the Board's Program decisions. The Commission ordered an independent Governance Board and stressed its independence. There is no basis now for suggesting that the Utilities were imprudent in complying with the Board's Program decisions.

Mr. Schott made clear that he was not advocating that there could be no prudence review at all in these Dockets, but that Program decisions of the Board should not be subject to prudence review and that, in any event, the Utilities should not be subject to cost recovery disallowance for them. Schott, Tr. pp. 40-41. Prudence review should be limited to implementation issues and the Utilities' role in them, such as did the Utilities administer the contracts properly and pay out the correct amounts for rebates. *Id.* at pp. 41, 43-44. Similarly, the independent Contract Administrator, Ms. Beitel, testified that there should be prudence review, but it should be for concerns such as misappropriation of funds. Beitel, Tr. at pp. 88-89. Staff, however, does not claim that there was any imprudence (or misconduct) in the Utilities' implementation of the Board's decisions. Thus, once more, that should conclude the contested issues in these Dockets.

B. Prudence Should Be Assessed Only at the Portfolio Level

Even if the independent Governance Board's Program decisions were to be subject to prudence review and, in theory, could be a basis for denying the Utilities' cost recovery, the prudence review should be performed only at the portfolio level, because that is what the independent Governance Board determined should be the approach, and that approach is consistent with the Commission's approach to electric utility energy efficiency programs. Dr. Brightwell's disagreement with the Board about that approach is not a lawful basis for an imprudence finding.

Ms. Beitel, the independent Contract Administrator with vast energy efficiency program knowledge and experience, testified that the independent Governance Board established a portfolio-level cost-effectiveness standard in its governing document, the Chicagoland Policy and Procedures Manual, and reaffirmed that standard a year later. Beitel Reb., NS-PGL Ex. 4.0, 1:12 – 3:49, 4:71-79, 10:212-216. That standard is consistent with the standard adopted by the

Commission for Illinois electric utility energy efficiency programs, and it is used by leading energy efficiency jurisdictions. *Id.* at 4:79-84, 10:217 – 11:232, 13:289-291. For example, when the Commission approved Commonwealth Edison Company’s (“ComEd”) and the Illinois Department of Commerce and Economic Opportunity’s (“DCEO”) energy efficiency and demand response plan, the Commission found, among other things that:

Calculation of the TRC test at the portfolio level provides utilities with greater flexibility to ensure that measures with less short-term energy savings value, but greater value over several years, will be included in any overall portfolio of measures and programs. This contention is reasonable and hereby is approved. However, the utilities and DCEO are not precluded from applying the TRC test at the “measure” or program level if they choose.

Commonwealth Edison Co., ICC Docket No. 07-0540, p. 28 (Order Feb. 6, 2008). *Accord Central Illinois Light Co., et al.*, ICC Docket No. 07-0539, p. 21 (Order Feb. 6, 2008).² Under the portfolio level standard, individual measures that are not cost-effective under the TRC test still may be included in the portfolio as long as the portfolio is cost-effective. Beitel Reb., NS-PGL Ex. 4.0, 4:84-87. Ms. Beitel further testified that the portfolio level standard will lead to greater cost-effective energy savings and a more diverse, robust portfolio that will provide value over time, while limiting portfolios only to individual measures that pass the TRC test will curtail innovation, limit customer value, and prevent Illinois from being a best practices jurisdiction. *Id.* at 26:595 – 27:502. Ms. Beitel explained that the portfolio-base approach allows for a broad range in products in various stages of market penetration/maturity which reduces lost opportunities, maximizes consumer exposure to efficiency, and helps to transform

² The statutory provisions for electric and gas utility energy efficiency programs require the use of a TRC test as defined in the statute, 220 ILCS 5/8-103(b), 8-104(b), but they do not require use of the TRC test at the individual measure level. In the above Commonwealth Edison Company and Ameren Illinois electric utility Dockets, considering parallel statutory language of 220 ILCS 5/12-103(b) before it was recodified in 220 ILCS 5/8-103(b), the Commission expressly found that applying the TRC test at the portfolio level was proper and beneficial, as cited and quoted above.

markets by building demand and therefore increasing cost effectiveness of lower penetration products. *Id.* at 13:291-295.

Ms. Beitel further noted that applying portfolio level cost-effectiveness was discussed during the Chicagoland Program design phase with the independent Governance Board, and the assigned Staff participating at the time raised no objections. Beitel Sur., NS-PGL Ex. 6.0, 3:65-68.

Mr. Plunkett, another independent expert with vast energy efficiency program experience, testified that analyzing cost-effectiveness at the portfolio level to maximize economic value is the standard approach adopted by jurisdictions with leading, mature energy efficiency investments. Plunkett Reb., NS-PGL Ex. 5.0, 1:7 – 4:88, 14:304-311. He concluded that this approach -- not the measure-level standard espoused by Staff witness Dr. Brightwell -- will produce the greatest amount of cost-effective energy savings over time from both the perspective of both the TRC and Program Administrator Cost (“PAC”) tests. *Id.* at 14:311-314. The PAC test counts only the costs of efficiency investments incurred by program administrators and supported by customers, and only the benefits of avoided gas costs; it does not include the value of non-gas resources in the calculation of benefits nor include customers’ contributions toward efficiency investments in the calculation of costs. *Id.* at 12:254-259.

Dr. Brightwell may disagree with the independent Governance Board’s decision to determine prudence at the portfolio level, and not based on the measure-level standard, but that is no more than a disagreement. Dr. Brightwell, in asserting his view, “is substituting his judgment for the reasoned, professional judgment made by experts with whom he disagrees – exactly what the Commission’s definition excludes from consideration of whether a utility decision is prudent.” Plunkett Reb., NS-PGL Ex. 5.0, 9:184-188.

C. The Portfolio Was Prudent

The portfolio determined by the independent Governance Board was prudent as a portfolio, even under the TRC test. Even Staff admits that the portfolio had a TRC test result of over 1.0. Staff offered an arbitrary calculation that mixed projections and actual data to arrive at a hypothetical scenario in which the portfolio could have a TRC test result of 0.99, which means that every dollar spent had 99 cents of benefits, without counting the benefits that are excluded from the TRC test, but that only underscores that the portfolio was prudent and illustrates the improper and extreme nature of the Staff position in leveling imprudence charges.

Ms. Beitel and Mr. Plunkett testified in great detail about the numerous independent experts who advised the Board and the detailed information and advice that they gave to the Board, as discussed in Section II(A)(2), above. Staff does not and cannot deny those facts.

Ms. Beitel further testified that it was reasonable and prudent to include the three measures contested by Staff in the portfolio because the measures were included as part of a portfolio that collectively had a TRC test result greater than 1.0 (and also because all of the measures individually are cost-effective under the PAC test, which indicates that the measures provide positive economic value to customers). Beitel Reb., NS-PGL Ex. 4.0, 3:65 – 4:70, 4:87-89, 27:611-614, 27:613 – 28:625. When launched, the portfolio had a TRC of 1.3 and PAC of 3.27. *Id.* at 7:141-148. The Program was launched to achieve energy savings of 865,973 therms per year, while actual savings were 1.3 million therms. *Id.* at 7:144-153.

Ms. Beitel reported that Program Year 1 (the reconciliation period) also served to lay the groundwork for future efforts in energy efficiency. Beitel Sur., NS-PGL Ex. 6.0, 3:49-51. Program Year 1 made a significant impact on product availability and awareness in the Chicagoland region, developed an effective network of trained contractors, and laid the

groundwork for successful future energy efficiency programs. Beitel Reb., NS-PGL Ex. 4.0, 28:626 – 29:655.

Dr. Brightwell has never disputed that the portfolio had a TRC test result of over 1.0, as forecasted and in terms of actual results. Rather, he presented an elaborate calculation that arbitrarily mixed forecast data with actual results data to arrive at a hypothetical scenario that, at worst, reduced the TRC test result to 0.99 (as corrected in his post-hearing “Attachment F”). *See* Brightwell Reb., Staff Ex. 3.0, Attachment F; Brightwell, Tr. at pp. 212-214. As stated above, that only underscores that the portfolio was prudent and illustrates the improper and extreme nature of the Staff position in leveling imprudence charges. Moreover, again the TRC test only includes certain benefits, *e.g.*, it does not include the Program Year 1 benefits referenced above that Ms. Beitel identified.

Thus, the amounts that the Utilities recovered under Rider EEP that are the subject of these Docket are amounts paid out on a Program, and a portfolio, that, it is undisputed, were cost-effective taken as a whole. To impose any “imprudence” disallowances in these Dockets would be unlawful as contrary to the prudence standard discussed earlier and would be arbitrary and capricious. *See, e.g., Illinois Power Co. v. Illinois Commerce Comm’n*, 339 Ill. App. 3d 425, 428, 431-432, 435, 439-444 (5th Dist. 2003) (“*Illinois Power*”) (reversing Commission prudence disallowance as arbitrary and unreasonable and based on hindsight). In *Illinois Power*, the Appellate Court found, among other things, that it was arbitrary and unreasonable for the Commission, with hindsight, to disallow costs of a project on the theory that the utility should have performed a certain analysis when the Commission previously had not ordered such an analysis in similar situations. *Id.* Similarly, here, the Staff theory would have the Commission find that the independent Governance Board should have used a measure-level TRC test to

exclude individual measures, even though the Commission recently had reached the opposite conclusion in the 2008 electric utility energy efficiency program Dockets. On this evidentiary record, that would be reversible error.

D. Disallowances Based Solely on “TRCs” Are Inappropriate

As discussed in the preceding subsection, the facts that the independent Governance Board decided to adopt a portfolio of energy efficiency measures, decided that the essential prudence determination was the prudence of the portfolio, and adopted a prudent portfolio are conclusive, under the prudence standard as well as the law governing arbitrary and capricious Commission actions. There also is further extensive evidence, however, that disallowances of costs of individual measures based solely on TRC test results are inappropriate, once more rendering Staff witness Dr. Brightwell’s contrary opinion a matter of disagreement, but not one that can be a basis for a finding of imprudence.

Ms. Beitel testified that it is a very common practice for some individual measures to be included in an energy efficiency portfolio because they offer significant benefits not covered by the TRC (such as contributing to consumer awareness and increasing customer comfort in hot and cold weather, among many other examples) or will likely at some point become cost-effective. *E.g.*, Beitel Reb., NS-PGL Ex. 4.0, 3:65 – 4:70, 4:82-87, 6:121-127, 13:278-295, 17:381 – 18:398, 19:417 – 21:480, 24:535-538, 26:576-580, 26:595 – 27:613. Ms. Beitel testified program managers can manage measure mix to manage overall program and portfolio cost effectiveness, even if the program contains individual measures that do not have a TRC greater than 1.0. Beitel Sur., NS-PGL Ex. 6.0, 17:362-375. Ms. Beitel acknowledged that Staff in many Board and Operating Committee meetings had opposed individual measures that do not meet the TRC test, but that Staff had never explained why its position was consistent with the

Commission's decisions as to electric utility energy efficiency programs nor why a different standard should be applied as to gas utilities. Beitel Reb., NS-PGL Ex. 4.0, 11:233-243.

Mr. Plunkett also testified that Dr. Brightwell's cost-effectiveness methodology fails to take into account the positive economic benefits of the measures to customers (as calculated under the PAC test), the economic value of the measures over time using the TRC test, and other benefits provided by the measures. Plunkett Reb., NS-PGL Ex 5.0, 5:103 – 6:120.

Mr. Plunkett explained that, consistent with jurisdictions with leading, mature energy efficiency investments, the independent Governance Board followed a two-pronged approach to assess the cost-effectiveness of the Program portfolio. The Board considered both the TRC and PAC cost-effectiveness tests to project and compare the benefits and costs of the purpose of the energy efficiency measures and assess their value from the perspectives of the economy (society) and of customers and the Board also took into account benefits that are not captured by the two tests and benefits that occur over time and not just in the individual Program period. Plunkett Reb., NS-PGL Ex 5.0, 10:213 – 15:334. Mr. Plunkett supported the Board's approach, explaining, among other things, that the TRC test does not capture everything of value to customers or society, including non-monetary benefits or non-resource benefits; consequently, it is not the sole or dispositive criterion used by energy efficiency program designers and administrators. *Id.* Indeed, Mr. Plunkett stated that using the TRC test alone is unduly restrictive and inconsistent with "best practices" in energy efficiency design and implementation. *Id.* at 11:237-241. Mr. Plunkett also explained that the Board also considered non-monetary factors not included in either the TRC or PAC tests in order to maximize long-term value from portfolio investment. *Id.* at 13:285 – 14:296. These included the potential to drive down future efficiency costs by raising demand, the need to build and maintain long-term business relationships

throughout the supply chain for high-efficiency products and services in order to influence market behavior, and the importance of including measures that would build awareness and support for energy efficiency in the Chicagoland marketplace. *Id.*

Mr. Plunkett testified regarding other shortcomings in using the TRC test alone, and of excluding those measures with a benefit-cost ratio under 1.0. The TRC test does not consider the dynamic effect that programs are designed to have on the future costs of high-efficiency measures with current low market penetration. Plunkett Reb., NS-PGL Ex. 5.0, 20:430 – 23:500. Sustained national, regional and even state level efforts have increased demand for expensive high-efficiency products by offering financial incentives to customers and/or suppliers. *Id.* at 20:435-441. Over time, the increase in volume led to major cost reductions, which led to greater market penetration. *Id.* at 20:441-443. Example cited by Mr. Plunkett included compact fluorescent lamps and high efficiency refrigerators and washers. *Id.* at 20:444 – 22:485.

Mr. Plunkett testified that other energy efficiency programs have justifiably included measures with a TRC less than 1.0 – “lost-opportunity” measures - where the inclusion prevented a potential loss of savings from such measures over the long lifetimes of the inefficient measures. Plunkett Reb., NS-PGL Ex. 5.0, 19:412-420. High-efficiency clothes washers, wall insulation, and tankless water heaters represent “lost-opportunity” measures. *Id.* at 19:421 – 20:429.

Mr. Plunkett also testified that if the Commission approved Staff’s recommended individual measure TRC governs cost-effectiveness standard, that would discourage the Board and other Illinois energy efficiency plan administrators from taking aggressive steps to maximize long-term benefits from their investments. Plunkett Reb., NS-PGL Ex. 5.0, 26:585-595. They would take no chances on front end investments that do not promise to pay off within the first

year of implementation. Plunkett Sur., NS-PGL Ex. 7.0, 16:334-347. That would lead to lower levels of cost effective gas savings to customers over the long term. *Id.* at 16:347-348.

Dr. Brightwell's view that all that matters in these Dockets is the TRC test results of the individual measures is, at best, a view, and, the evidence indicates, a misguided one. Even if it were persuasive, however, that view cannot somehow be the only reasonable view, and thus the basis of an imprudence finding. Indeed, Dr. Brightwell himself showed reticence about offering the opinion that the Board had made decisions that no reasonable person could make, even though that would be required as part of an imprudence finding under the Commission's prudence standard. His direct and rebuttal testimony never contained a plain statement that the Board had made decisions that no reasonable person could make. Even when he was presented with a point blank data request that asked whether that was his opinion, he still avoided making an express statement to that effect, and even on cross-examination, he continued to exhibit that reticence, only offering that opinion when pressed, and even then he limited his opinion to the Board's conclusion that further review was not needed. *See* Brightwell, Tr. at pp. 224-226.

The law and the evidentiary record simply do not permit a finding of imprudence based solely on the measure level TRC tests. Dr. Brightwell's difference of opinion with the Board and its independent expert advisors does not establish imprudence.

E. Staff's Specific Proposed Disallowances Are Inappropriate

Staff's criticisms of the three individual measures at issue do not show imprudence.

1. Tankless Water Heaters

The Chicagoland Natural Gas Savings Program provided customer rebates for tankless water heaters of \$400 per customer during the applicable period. (NS Ex. 2.1, p. 7; PGL Ex. 2.1,

p. 7.) The cost of these rebates was included in the SC No. 1 reconciliation amounts presented by Mr. Korenchan. (NS Ex. 1.1, p. 2; PGL Ex. 1.1, p. 2.)

Ms. Beitel testified that tankless water heaters were included in the Program for several reasons. The Program was designed to leverage the ENERGY STAR brand, which included tankless water heaters at the time of the Program launch. Water-heater manufacturers had long supported an ENERGY STAR label for their product category, and it was expected that the combination of industry support and leverage of the ENERGY STAR label, combined with consumer recognition and value of the label, would help drive awareness and demand in this product category. Beitel Reb., NS-PGL Ex. 4.0, 19:420-421. Ms. Beitel also stated that tankless water heaters represent tremendous potential for energy savings --- four times as much -- compared to ENERGY STAR storage water heaters (78 vs. 19 therms annually); indeed, tankless water heaters offer the highest energy savings in the water heating category. *Id.* at 19:422-423. Ms. Beitel also stated that tankless water heaters have additional consumer benefits, including very rapid hot water and water savings associated with not needing to run faucets while waiting for hot water, and the smaller space required to install the heaters. *Id.* at 21:473-476. Ms. Beitel noted that many other Midwest-based energy efficiency programs offer incentives for tankless water heaters in amounts from \$100 to \$420. *Id.* at 23:515-523.

Ms. Beitel recognized the relative high cost of tankless water heaters, but explained that it was expected that the cost would decrease over time with increased volume through market transformation (market transformation occurring through several programs, including ENERGY STAR and the Chicagoland Program). Beitel Reb., NS-PGL Ex. 4.0, 19:423-424. Offering tankless water heater rebates in Program Year 1 was the first step in a long-term market transformation strategy. *Id.* at 22:504 – 23:508.

Ms. Beitel acknowledged that tankless water heaters need a minimum delivered gas pressure to achieve proper water temperature rise, and that the Governance Board did not know of the fact that portions of the Peoples Gas system in Chicago were at low pressure until Program Year 2. Beitel Reb., NS-PGL Ex. 4.0, 22:483-488; Beitel Sur., NS-PGL Ex. 6.0, 9:184-191. She also testified, however, that over 50% of Peoples Gas' customers in Chicago do have sufficient gas pressure and all customers in North Shore's service territory have adequate pressure. Beitel Reb., NS-PGL Ex. 4.0, 22:497-500; Beitel Sur., NS-PGL Ex. 6.0, 9:185-191. Ms. Beitel stated that the rebate application clearly states that products must be installed according to manufacturer specifications, and the installation manual for tankless water heaters requires the installer to verify adequate gas pressure before installation. Beitel Sur., NS-PGL Ex. 6.0, 10:125 – 11:238. She further noted that manufacturers offer frequent training to their trade ally networks on proper installation. *Id.* at 11:239-247.

Ms. Beitel testified that, to her knowledge, no one with low pressure gas service installed the tankless water heaters or received the rebate under the Program. Beitel, Tr. at p. 119. She further noted that Staff has provided no evidence that the Utilities paid rebates for tankless water heaters in homes with low gas pressure, or that customer incurred costs over the estimated total purchase price or incremental measure cost (such as the cost of boosters); that is, there is no evidence that tankless water heaters were any less cost-effective than the Program's estimates. Beitel Sur., NS-PGL Ex. 6.0, 13:271-276.

The TRC for tankless water heaters was calculated as 1.01 when the Board made its decision to include tankless water heater rebates in the Program in the applicable period. Brightwell Dir., Staff Ex. 2.0, 17:316-318. Dr. Brightwell opined that the possibility that Peoples Gas customers with low pressure service would pay for boosters would bring the TRC

below 1.0 (*id.* at 17:319-328), but, as indicated above, he has never provided any information that substantiates his speculation that any Peoples Gas customer paid for a booster. Thus, even under the TRC test, standing alone, there is no basis for an imprudence finding. Moreover, he admitted that even half the Peoples Gas service territory is still an ample market for the offering of an efficiency measure. Brightwell, Tr. at p. 247. Finally, Dr. Brightwell's explanation of why he made the same proposed adjustment as to North Shore, which has no low pressure system, is unpersuasive. His explanation is pure speculation that if the Board had looked at the low pressure issue it would not have adopted the tankless water measure as to either service territory. *See id.* at pp. 247-248. That illustrates the arbitrary and unreasonable nature of Staff's proposed adjustments.

2. High Efficiency Clothes Washers

The Program provided customer rebates for high efficiency clothes washers of \$100 per customer during the applicable period. (NS Ex. 2.1, p. 7; PGL Ex. 2.1, p. 7.) The cost of these rebates was included in the SC No.1 reconciliation amounts presented by Mr. Korenchan (NS Ex. 1.1, p. 2; PGL Ex. 1.1, p. 2.)

Ms. Beitel testified that high efficiency clothes washers were included in the Chicagoland portfolio because the TRC was very close to 1.0 (it was 0.91, later corrected to 0.94), clothes washers provided high visibility to consumers and led to a retail-based awareness of gas efficiency measures, and leveraged the extensive retailer-based outreach and awareness of energy efficiency measures that was already underway in the market through the ComEd energy efficiency program. Beitel Reb., NS-PGL Ex. 4.0, 13:280-285. She also testified that clothes washers incentives appear regionally and nationally, and are the cornerstone of many energy efficiency programs. *Id.* at 13:285-286.

Ms. Beitel explained that clothes washers were the only significantly visible product in the Chicagoland portfolio. Beitel Reb., NS-PGL Ex. 4.0, 14:310-311. Unlike heating and water heating measures, people touch and see clothes washers several times a week. *Id.* at 14:311-314. Moreover, clothes washers have features that can get people excited about efficient products, like using less water and detergent, and causing less wear and tear on clothes. *Id.* at 14:314-317. She explained that including in a portfolio measures like clothes washers that have valuable features beyond saving energy helps to build excitement and momentum for efficient products generally; the opportunity to generate consumer excitement about efficiency was a critical factor in the Program team's recommendation to include clothes washers in the Program. *Id.* at 14:317 – 15:323.

Ms. Beitel also noted that the Chicagoland Program could achieve a significant level of visibility and therefore overall Program participation with retail support and promotion of the Program in appliance departments. The Program design was aligned with ENERGY STAR whenever possible in order to leverage consumer familiarity and confidence in that label, and to set up the connection between clothes washers and other efficient products covered by the label, including water heaters and heating equipment. Beitel Reb., NS-PGL Ex. 4.0, 15:330-336. Ms. Beitel further noted that the inclusion of clothes washers in the Chicagoland Program led to retailer support and increased visibility. All retailers allowed store visits by Program representatives, and leading retailers participated in sales associate training that led to increased visibility and sales at those locations. *Id.* at 15:340 – 16:349. Ms. Beitel testified that inclusion of clothes washers in the Chicagoland Program resulted in over 1 million therms saved annually. *Id.* at 7:150-153. In addition, there was a significant advertising benefit with very little direct expenditure on marketing. *Id.* at 17:386 – 18:392.

Mr. Plunkett testified that the marketing benefit for this measure refers to all measures, not just clothes washers, using a marketing channel (retailers) that had already been developed by the electric efficiency programs. Plunkett Sur., NS-PGL Ex. 7.0, 4:75-78. Therefore, he noted, the market share of clothes washers prior to the Program's existence is not relevant in determining whether such a benefit was achieved. *Id.* at 4:78-83.

Once again, Dr. Brightwell has presented his opinion that the TRC test result of below 1.0 means that the Board should not have included high efficiency clothes washers in the Chicagoland portfolio, but there is extensive evidence that his opinion is erroneous and, at most, presents a reasonable difference of opinion. His opinion cannot support an imprudence finding.

3. Wall Insulation

The Chicagoland Program provided customer rebates for wall insulation of 75% of total cost, up to \$750 per home, during the applicable period. (NS Ex. 2.1, p. 7; PGL Ex. 2.1, p. 7.) The cost of these rebates was included in the SC No. 1 reconciliation amounts presented by Mr. Korenchan (NS Gas Ex. 1.1, p. 2; PGL Ex. 1.1, p. 2.)

Ms. Beitel acknowledged that when the Program was originally designed, the assumption was that wall insulation would be self-installed. Beitel Reb., NS-PGL Ex. 4.0, 23:527-528. She explained that at the time the Program was being designed in October 2008, one of the Board's key considerations was the rapidly declining economy. Consumers were losing jobs and home equity and had very little disposable income to invest in discretionary spending such as energy efficiency upgrades. *Id.* at 9:196-202. That led to several key design recommendations by the Program team, including the assumption that customers undertaking home improvements as economically as possible when feasible, rather than through contractors. *Id.* at 9:202 - 10:209.

The TRC for wall insulation originally was calculated to be 2.5, based on no incremental labor cost. Beitel Reb., NS-PGL Ex. 4.0, 23:527-530.

Ms. Beitel testified that when Program assumptions were reviewed in May 2009, it was discovered that, contrary to the Program prediction, about two-thirds of wall insulation was being installed by contractors. The cost-effectiveness was recalculated with the actual Program experience of \$1.22 per square foot, with a resulting TRC of 0.70. Beitel Reb., NS-PGL Ex. 4.0, 23:531 – 24:534. She stated that although the original assumption about how the measures would be installed was incorrect, it was not imprudent given the severe economic conditions at the time the portfolio was designed. *Id.* at 24:551 – 25:556.

Ms. Beitel further testified that even when the TRC was revised to 0.70, the Governance Board voted to maintain wall insulation in the Program. She stated that the Board considered wall insulation an essential part of the Program because it presents significant energy savings and comfort improvements, and reduces lost opportunities. Beitel Reb., NS-PGL Ex. 4.0, 24:535-538. She explained that wall insulation reduces convection, conduction, and radiant heat loss. Beitel, Tr. at p. 65. Ms. Beitel noted that many homes in Chicago have no wall insulation (homes built in Chicago before 1970 have little to no insulation, and seventy-seven percent of homes in Chicago were built before 1970). Beitel Reb., NS-PGL Ex. 4.0, 5:559-562. She testified that in most cases, residents install wall insulation when walls are already open as part of other remodeling or repair projects. She explained that the Program intended to increase the likelihood that customers would install insulation when the opportunities arose. *Id.* at 25:566-569.

Ms. Beitel testified that wall insulation incentives appear regionally and nationally. Beitel Reb., NS-PGL Ex. 4.0, 26:583-585.

Ms. Beitel testified that wall insulation was promoted through all readily available channels, including retailer outreach and contractors. Beitel Sur., NS-PGL Ex. 6.0, 5:109-113. Her testimony described the extensive retailer promotion efforts, including over 300 site visits and retail display materials developed for home improvement and hardware stores. *Id.* at 15:321-323. She also described promotion through additional channels, including contractor training and outreach. *Id.* at 15:329-332. As it turned out, the contractors' channel was more successful; Year 1 results show that 2/3 of wall insulation applications through contractor installation, and 1/3 through self-installation. *Id.* at 15:333-337. She noted that even if a contractor-installed component had been factored into original cost estimates, given the economic conditions, it would not have been expected that the contractor-installed share would be greater than 1/3. *Id.* at 16:338-344. Using this figure in a TRC analysis would have resulted in a TRC of 1.16. *Id.* at 16:345-348.

Ms. Beitel testified that the cost of contractor installed wall insulation can decrease over time with high-volume, because contractors can develop efficiencies in marketing, scheduling and installation practices, which reduces their cost. Beitel Sur., NS-PGL Ex. 6.0, 16:349-351.

Mr. Plunkett echoed that testimony, noting that in New England wall insulation costs declined over time as installation techniques became more widely practiced by contractors. Plunkett Sur., NS-PGL Ex. 7.0, 11:237-239.

Mr. Plunkett noted that the Program Administrator could refine program design and marketing to improve the cost effectiveness of including wall insulation. Plunkett Sur., NS-PGL Ex. 7.0, 11:239-241.

As with the other two measures of which he complains, Dr. Brightwell has presented his opinion that a TRC test result of below 1.0 means that the Board should not have included wall

insulation in the Chicagoland portfolio, but there is extensive evidence that his opinion is incorrect and, at best, presents a reasonable difference of opinion. His opinion cannot support an imprudence finding.

F. Staff's Specific Proposed Disallowances Are Excessive and Punitive

Staff's proposed adjustments disregard long-established principles on the calculation of disallowances, if any, in the event of a finding of imprudence. In *Central Illinois Light Co.*, ICC Docket No. 94-0040, 1994 Ill. PUC Lexis 577 (Order Dec. 12, 1994) ("*CILCo*"), based on the evidence in the record in that Docket, the Commission found both that the utility had been imprudent and that the utility's imprudence had caused significant incremental amounts to be spent that otherwise would not have been spent. Staff there submitted evidence, and the Commission specifically found, that the utility's imprudence required the utility to spend more to fix the problems than the utility would have spent if it had acted prudently. *CILCo* at **25, 27, 29, 30. Accordingly, Staff there proposed to disallow the incremental portion of the amounts spent by the utility that were due to imprudence, and the Commission agreed that that was the correct measure of the disallowance. *Id.* at **30, 35, 40, 42. The Commission expressly rejected an intervenor's contention that the entire amount spent (apart from a certain amount already scheduled to be spent), rather than the incremental amount spent due to the imprudence, should be disallowed, finding not only that disallowing more than the incremental amount was unwarranted but also that it would create an incentive to put off dealing with dangerous situations. *Id.* at **37-41. The Commission's adoption and application of the principle that only incremental amounts due to the imprudence should be disallowed could not be clearer. For example, the Commission held: "Here, the Commission concludes that the disallowances should

be imposed only to the extent that the expenses and investment exceed the levels that would have been incurred absent imprudence on the part of CILCO.” *Id.* at *40.

Here, Dr. Brightwell is of the view that no costs should have been incurred on the measures, but that does not alter that customers received substantial benefits as calculated under the TRC test, even setting aside the benefits not captured under the TRC test because they do not fall within it or occur over a longer period, as discussed earlier.

Accordingly, even if the law and the record permitted imprudence findings as to the Board’s decisions here, which they do not, and even if those warranted disallowance of the Utilities’ cost recovery, which they do not, there should be no disallowance. The TRC test results are 1.01 or not much below 1.0, as discussed earlier, and there are numerous other customer and societal benefits outside the narrow boundaries of the TRC test.

In addition, the cross-examination of Dr. Brightwell further illustrates the excessive and punitive nature of his proposed adjustments. If a TRC is 1.0, he would propose no disallowance, but if it is 0.99, he would propose to disallow 100% of the rebate costs, despite the fact that even under the narrow TRC test there were 99 cents of incremental benefits for each \$1 of incremental spending. *See* Brightwell, Tr. at pp. 227-231.

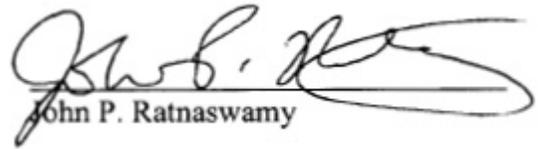
In the alternative, even treating the TRC test as the “be all and end all”, the amount of the disallowances should be zero for tankless water heaters given the TRC of 1.01. The fractions by which the TRC test result figure was below 1.0 times the costs of each of the other two measures should be the maximum amount of those disallowances, *e.g.*, if the TRC was 0.90, then, if any costs were to be disallowed at all, only a maximum of 10% of the costs would be disallowed. To have disallowances that disregard the customer benefits, including even the benefits that count under the TRC test, as Staff proposes, is excessive and punitive.

CONCLUSION

The Commission can have been presented with few prior Dockets, if any, in which it was so clear that imprudence disallowances were being proposed based on nothing more than a difference of opinion. Staff's opinions seem to be entirely wrong, but even if they fall within the zone of reasonable opinions, they certainly do not negate the reasonable conclusions reached by the Board with advice and information from independent experts. The Commission should approve the Statements of Reconciliation Adjustments and reject Staff's proposed adjustments. Staff's proposed adjustments would constitute reversible error.

Dated: October 20, 2010

By:



John P. Ratnaswamy

John P. Ratnaswamy
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