

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.	:	

**REPLY BRIEF ON EXCEPTIONS 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” or “NS-PGL”), in accordance with the schedule set by the Administrative Law Judge (“ALJ”) and Section 200.830 of the Rules of Practice of the Illinois Commerce Commission (the “Commission” or “ICC”), 83 Ill. Adm. Code § 200.830, submit this Reply Brief on Exceptions.

INTRODUCTION

Staff’s Brief on Exceptions requests three changes to the ALJ’s December 9, 2010, Proposed Order (the “Proposed Order”), each of which is not supported by the record and erroneous: (1) to find that the use of the “PAC” (Program Administrator Cost) cost-effectiveness test by the independent Governance Board of the Chicagoland Natural Gas Savings Program was imprudent; (2) to apply the portfolio level standard with an impossibly high bar, essentially transforming it into a measure-level standard; and (3) to punitively disallow all incremental costs associated with wall insulation rebates. The Commission should reject Staff’s Exceptions for the factual and legal reasons discussed below.

Instead, the Utilities’ Exceptions should be approved by the Commission. As discussed in their Brief on Exceptions, the Proposed Order’s recommendations on most subjects are

consistent with the evidence and the law except in three respects. The Utilities urge the Commission to modify the Proposed Order to reflect that: (1) the independent Governance Board's Program decisions should not be a basis for imprudence findings against the Utilities and for disallowances of the Utilities' recovery of costs of implementing the Board's Program decisions; (2) weight should be given to the fact that the Program is determined by an independent Governance Board, which includes major stakeholders; and (3) the inclusion of wall insulation as a measure in the Chicagoland portfolio was not imprudent.

ARGUMENT IN REPLY TO STAFF'S EXCEPTIONS

I. Measuring Prudency: The TRC and the PAC (III.D)

Staff disagrees with the Proposed Order's conclusion (at p. 9) that "it was not generally imprudent" for the independent Governance Board to apply the PAC test, finding the conclusion to be an "unreasonable position". Staff Brief on Exceptions ("BOE"), p. 3. However, the finding is clearly supported by law and the evidence in the record. The Utilities have provided ample evidence that the approach undertaken by the Governance Board, including the use of the PAC test, was reasonable.

The PAC test tallies the costs of efficiency investments incurred by the Program and supported by ratepayers (here, the rebates paid to Program participants that passed through Rider EEP plus administrative costs), and the benefits of avoided gas costs. Plunkett Rebuttal ("Reb."), NS-PGL Exhibit ("Ex.") 5.0, 12:255-259. The PAC test does not include the value to the customer of improved amenity or comfort, or any savings in non-gas resources in the calculation of benefits (*e.g.*, the avoided cost of other resources, such as electricity and water, attributable to the efficiency measures in the Program), nor does it include customers' contributions toward efficiency investments in the calculation of costs (*e.g.*, the customer's cost

of buying or installing efficiency products). *Id.* In other words, the PAC test indicates the extent to which the ratepayers responsible for funding energy efficiency investments benefitting the economy receive reasonable value for the money they provide to support the Program portfolio. *Id.* The test does so by counting only those costs borne by ratepayers supporting the Program and by ignoring the costs borne directly by participants. *Id.*

The independent Governance Board followed the advice of independent energy efficiency experts, and consistent with jurisdictions with leading, mature energy efficiency investments, utilized an approach which considered both the “TRC” (Total Resource Cost) and PAC cost-effectiveness tests in projecting and comparing the benefits and costs of energy efficiency measures and assessing their value. *E.g.*, Plunkett Reb., NS-PGL Ex. 5.0, 10:213 – 15:334. The Board considered not only the results of the TRC and PAC tests, but non-monetary factors as well in order to maximize long-term value from portfolio investment. *Id.* at 13:285 – 14:296.

The Proposed Order correctly points out that Staff does not refute the fact that the PAC has been utilized for evaluating cost-effectiveness in energy efficiency programs outside Illinois, and that Staff even considers the PAC useful for determining rebate levels once an energy efficiency measure has passed the TRC test. Proposed Order at pp. 8-9. Staff’s objection to the PAC test is Staff’s claim that the TRC test is better because it includes costs paid by customers, and Staff cites the Order in *Central Illinois Light Co., et al.*, ICC Docket No. 08-0104 (Order Oct. 15, 2008) (“*Ameren*”). Staff BOE, p. 3. Staff’s witness may disagree with the Governance Board’s decision to follow an approach that considered PAC test cost-effectiveness, but that is no more than a disagreement. In contradiction of prudence review principles, Staff is substituting their witness’ judgment for the reasoned, professional judgment made by experts

with whom the witness disagrees. *E.g.*, Plunkett Reb., NS-PGL Ex. 5.0, 9:184-188; NS-PGL Initial Brief, pp. 2-3 (prudence standard).

Staff's reliance on the 2008 Ameren gas energy efficiency cases Order in *Ameren* is entirely misplaced. In its Order, the Commission found that Ameren's cost-effectiveness analysis using the TRC test was "reasonable". *Ameren*, p. 22. The *Ameren* Order, however, does not stand for the proposition that the use of the TRC test is the only reasonable approach in designing an energy efficiency plan. As stated in the Proposed Order (at p. 8), "the Commission had not ruled out application of the PAC in late 2008 (and did not do so thereafter)."

The law and the evidentiary record simply do not permit a finding of imprudence based on the Governance Board's consideration and use of the PAC test. Staff's difference of opinion with the Board and the Board's independent expert advisors does not establish imprudence. For these reasons, the Commission should reject Staff's request that the Proposed Order be revised to reflect that the use of the PAC test was imprudent.

II. Whether Prudency Should Be Assessed Only at the Portfolio Level (III.E)

In its second Exception, Staff acknowledges that a portfolio-level prudency review is consistent with prior Commission decisions, but nonetheless requests that "the Commission strengthen[] the requirements for cost effectiveness" by indicating that "measure level cost-effectiveness is an appropriate policy on a prospective basis unless there is a clear demonstration that any cost-ineffective measures are likely to provide long-term benefits that are not included in the TRC analysis". Staff BOE, p. 5. Staff's request should be rejected as it is not supported by the law or the evidence.

The independent Governance Board established a portfolio-level cost-effectiveness standard in its governing document, the Chicagoland Policy and Procedures manual, the Board

reaffirmed that standard a year later, and the Board had ample factual basis for adopting that approach. *E.g.*, Beitel Reb., NS-PGL Ex. 4.0, 1:12 – 3:49, 4:71-79, 10:212 – 11:232, 13:289-295, 26:595 – 27:502; Plunkett Reb., NS-PGL Ex. 5.0, 1:7 – 4:88, 14:304-314. Applying portfolio level cost-effectiveness was discussed by the Board and its independent advisors during the Chicagoland Program design phase, and the assigned Staff participating at the time raised no objections. *E.g.*, Beitel Surrebuttal (“Sur.”), NS-PGL Ex. 6.0, 3:65-68. Staff’s position once again is, at most, a disagreement, and it is not a sound position.

Moreover, Staff has already revealed in this proceeding that its interpretation of the standard it urges would set an impossibly and inappropriately high bar for exceptions to the requirement of a measure-level TRC of at least 1.0. The Utilities provided ample evidence to support the benefits of including measures (including but not limited to wall insulation) with a TRC less than 1.0 in a portfolio, including enhancement of consumer awareness, customer comfort in hot and cold weather, and the economic value of the measures over time. *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; Plunkett Reb., NS-PGL Ex 5.0, 5:103 – 6:120. Yet, Staff’s witness asserts that “sufficient justification” was not provided. Brightwell Dir., Staff Ex. 2.0, 9:174-13:248. Staff evidently desires a formal numeric analysis to determine if the sum of the quantifiable benefits plus the non-quantifiable benefits (which may not be quantifiable either by their nature or at a point in time) outweighs the costs (*see* Transcript (“Tr.”), p. 216), but numerical certainty for non-quantifiable factors, made even more uncertain when long-term variables and goals are considered, is an impossibly high bar. It should not be adopted as a standard by the Commission. By any reasonable standard, the Governance Board

acted prudently, both in general, and with regard to the wall insulation measure, discussed in the next section below, in particular.

The evidence is clear that adoption of a conclusive or essentially conclusive measure-level TRC standard would have a detrimental effect on the development and penetration of a robust energy efficiency program, and on greater cost-effective energy savings. *See* Beitel Reb., NS-PGL Ex. 4.0, at 26:595 – 27:502, 13:291-295; Plunkett Reb., NS-PGL Ex. 5.0, 14:311-314. The Illinois Attorney General’s Office’s (the “AG”) Initial Brief (at p. 16) noted that “Staff’s strict approach to measuring cost-effectiveness, if adopted by the Commission, could detrimentally alter other Illinois utilities’ views on what should be included in energy efficiency portfolios.” In the same vein, the Proposed Order (at p. 12) correctly notes that “[s]ome degree of portfolio risk is not imprudent when the likelihood of realizing other important efficiency objectives is enhanced.”

Finally, Staff’s request for a “prospective” or going-forward application of the measure-level TRC standard (with an impossibly high bar for exceptions if the TRC is not at least 1.0) is, practically speaking, moot. The Chicagoland Program ends on June 30, 2011, subject to reconciliation procedures for the final period. Each utility will have a new energy efficiency plan that commences on June 1, 2011, and that will be subject to and evaluated under Section 8-104 of the Public Utilities Act, 220 ILCS 5/8-104, and as noted in the Proposed Order (p. 12, fn. 51), “[n]othing [said]....in this Order is intended to construe what is required by Section 8-104.”

The law and the evidentiary record in the instant cases do not permit the change to the Proposed Order requested by Staff (Staff BOE, p. 8). Accordingly, it should be rejected.

III. Disallowance Calculation (III.[G])

Staff's final Exception urges complete disallowance of the incremental costs incurred by the Utilities on the wall insulation measure. Staff BOE, pp. 9-12. For the reasons discussed in the Utilities' Brief on Exceptions and prior briefs, the Commission should find that it was not imprudent to include wall insulation in the Chicagoland portfolio in the reconciliation period. Indeed, to find imprudence would be reversible error. *E.g.*, NS-PGL BOE, pp. 7-12; *see also* NS-PGL Initial Brief, pp. 30-33; NS-PGL Reply Brief, pp. 16-19. Staff's Exception is erroneous and unreasonable, however, even setting aside the merits of the disallowance.

First, Staff's position lacks internal logic. Under established standards, when the Commission finds imprudence, only the incremental amount spent by the utility due to the imprudence, if any, is to be disallowed. Proposed Order, p. 19 (citing *Central Illinois Light Co., et al.*, ICC Docket No. 94-0040, 1994 Ill. PUC Lexis 577 (Order Dc. 12, 1994)); NS-PGL Initial Brief, pp. 33-34. The results of the PAC test for the wall insulation measure are instructive under that standard. According to the Governance Board's calculations under the PAC test – which Staff's witness does not dispute – the measure of wall insulation in fact provided significant value. Plunkett Reb., NS-PGL Ex. 5.0 at 16. The ratio of benefits to costs under the PAC test for wall insulation was quite high, 3.92; only the measures for high efficiency boilers and ceiling insulation had higher PAC scores. *See* Brightwell Reb., Staff Ex. 3.0, Attachment A. Thus, in the case of wall insulation, it follows that excess of the costs over benefits as calculated by the narrow TRC test if the TRC result is deemed to be below 1.0 was borne by participants (*i.e.*, customers installing wall insulation), not by the Utilities nor ratepayers. Thus, even if there was a TRC of less than 1.0 for the wall insulation measure, that only means that if, hypothetically, any customers were “harmed” (which requires finding that the TRC was below

1.0 and setting aside that the narrow TRC test ignores benefits such as increased comfort), it was the customers who installed wall insulation, not ratepayers. Staff's method of calculating its proposed disallowances, therefore, does not make sense under the prudence standard, even if the narrow TRC test somehow were thought to be conclusive as to cost-effectiveness. To put it another way, the incremental costs incurred by the Utilities contain no "imprudent" dollars, and thus no "imprudent" dollars passed through the rider. So, under the standard, the disallowance of the incremental costs incurred by the Utilities should be zero.

Second, even setting aside all of the above, the Utilities believe that Staff likely has misread the Proposed Order. Staff originally proposed, and, as the Utilities understand it, Staff still proposes, to disallow 100% of the incremental costs incurred by the Utilities on the wall insulation measure, which was \$52,720 as to Peoples Gas and \$12,184 as to North Shore, a total of \$64,904. Hathhorn Dir., Staff Ex. 1.0, Schedules ("Scheds.") 1.2, 1.4; Staff BOE, p. 11 (figure of \$64,904). The Utilities in prior briefing responded, among other things, that, even if the narrow TRC test were the sole determiner of prudence, and assuming that the TRC test result was below 1.0, both of which premises the Utilities contest (*e.g.*, NS-PGL BOE, pp. 2, 7-12 (making a number of points, including that a properly re-calculated, "non-hindsight" TRC for the wall insulation measure would be 1.16, not 0.70)), then the disallowance should only be the percentage of incremental costs incurred by the Utilities that was "imprudent". The Utilities suggested that the percentage of incremental costs incurred by the Utilities that is the difference between the 1.0 and the TRC test result (*e.g.*, a TRC of 0.90 would yield a disallowance of 10% of the incremental costs incurred by the Utilities), would be a suitable method of calculation on the particular facts of this case, assuming any disallowance were warranted. NS-PGL Initial Brief, pp. 33-34. The Utilities interpret the Proposed Order to have adopted that suggested

approach given the particular facts of this case. *See* Proposed Order, pp. 19-21. So, under the Proposed Order, as the Utilities interpret it, the Commission would adopt 30% of Staff's proposed adjustments for the wall insulation measure, *i.e.*, the final Order would disallow \$15,816 out of the \$52,720 of Peoples Gas' incremental costs and \$3,655 of the \$12,184 of North Shore's incremental costs. That may be a relatively unsophisticated calculation, but, given the particular facts of this case, including the amounts of the proposed disallowances, and the Proposed Order's apparent adoption of a TRC of 0.70 for this purpose, this seems a reasonable approach, setting aside the merits of the disallowances.¹ As the Proposed Order (at p. 20) states:

Practically speaking, within the context of designing an energy efficiency portfolio, there would be a range of estimated per-measure outcomes that would be reasonable. It would be unproductive to prolong and complicate this administrative litigation by attempting to map out the boundaries of that range. Given the relatively small amounts involved here, it is sufficient to approve recovery commensurate with the benefit actually provided (70% of costs incurred), while disallowing recovery of remaining costs.

Staff evidently disagrees with a 30% disallowance of the Utilities' incremental costs approach (*see* Staff BOE, pp. 10-11), but Staff's view appears to rest on a much more complicated calculation that is intended essentially to get the TRC test result to 1.0, where the calculation factors in not only the incremental costs paid by the Utilities that were passed through the rider but also the costs incurred by the customers who installed wall insulation that

¹ The Utilities agree to this methodology given the particular facts of this case and solely for purposes of this case, but reserve their rights in future proceedings involving this issue. NS-PGL BOE, p. 12, fn. 2.

were not passed through the rider.² That does not appear to make sense or to be fair on the facts of this case and given the Proposed Order's findings. This proceeding is supposed to be a reconciliation of the costs that passed through the rider with revenues recovered by the Utilities.

Candidly, the Utilities are confused by Staff's Brief on Exceptions as to how Staff reads the Proposed Order. Perhaps Staff reads the Proposed Order to allow the Utilities to recover not only incremental costs spent by the Utilities but also additional costs spent by customers who installed wall insulation (*see* Staff BOE, p. 10), but that is not the Utilities' reading. If the final Order approves 30% of Staff's proposed adjustments for the wall insulation measure, then the Utilities will not be allowed to recover 30% of the incremental costs they incurred on the wall insulation measure. That would be a disallowance, not an added recovery, and it clearly would not mean that, as Staff seems to fear, the Utilities somehow would "collect more revenue than was expended on this program" (*see* Staff BOE, p. 9).

Staff has presented no valid grounds to support its Exception and it is erroneous. Accordingly, the Exception should be rejected by the Commission.

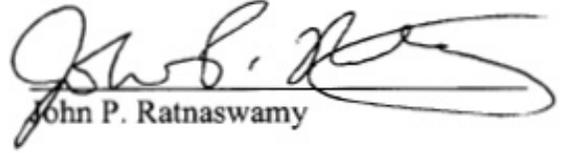
² To illustrate that Staff is taking into account the costs incurred by customers who installed wall insulation that were not passed through the rider, please note that Staff's Brief on Exceptions (at p. 10) relies on a cost figure of \$4,107 per installation, citing Tr. pp. 215-216, but in coming up with that figure Staff's witness makes clear that he is relying on the installation cost of \$1.22 per square foot, which is the cost to the customer who installs the wall insulation. *See, e.g.,* Staff Reply Brief, pp. 9-10. The \$81,690 figure in Staff's BOE (at p. 11 and fn. 21) further illustrates that Staff is including the costs incurred by customers that did not pass through the rider.

CONCLUSION

The proper application of the evidence and the law in this case dictates that Staff's requested changes to the Proposed Order should be rejected.

Dated: February 9, 2011

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