

December 21, 2005

City of Chicago
Department of Revenue
City Hall, Room 107
121 North LaSalle Street
Chicago, Illinois 60602
Attention: Director of Revenue

Re: Agreement Concerning the Gas Occupation Tax and
Amendment to Tax Collection Agreement for Use Tax

Dear Ms. Reyna-Hickey:

The purpose of this letter agreement (this "*Agreement*") is to set forth the understanding of the City of Chicago, a municipal corporation and home rule unit of local government existing under the Constitution of the State of Illinois (the "*City*"), acting by and through the Director of the Department of Revenue, and The Peoples Gas Light and Coke Company, an Illinois corporation (the "*Company*"), concerning the payment of the Gas Occupation Tax (the "*Occupation Tax*") pursuant to chapter 3-40 of the Chicago Municipal Code (the "*Municipal Code*") and the collection and remittance of the Gas Use Tax (the "*Use Tax*") pursuant to chapter 3-41 of the Municipal Code. Historically, the Occupation Tax has been paid and the Use Tax has been collected and remitted by the Company to the City on the basis of cash receipts actually received by the Company. The Company has proposed, and the City has agreed, that prospectively these taxes will be paid, or collected and remitted, as applicable, on the basis of estimated cash receipts with reference to collection rates determined by the Company as described herein. Consequently, as such agreement relates to the Use Tax, the City and the Company are amending that certain Tax Collection Agreement dated as of January 31, 1994 (the "*Tax Collection Agreement*").

Section 1. Payment of Occupation Tax.

(a) As used in this Section 1, the term "gross receipts" has the meaning given to such term in section 3-20-030 of the Municipal Code. The City and the Company agree that the Occupation Tax which is required to be paid by the Company to the City for any calendar month beginning with the month of November, 2005 (the Occupation Tax for which is due in December, 2005), shall be determined based on monthly estimates of gross receipts, regardless of whether or not the Company actually receives gross receipts.

Thomas A. Nardi • Chief Financial Officer

(b) The Company shall estimate gross receipts based upon a percentage of the amount actually billed to customers with respect to any calendar month for gas service for use or consumption and not for resale. The gross amount billed to such customers shall first be reduced by a percentage (the "*Reserve Percentage*") which is equal to the percentage used by the Company to determine the Company's provision for uncollectible accounts for such calendar month in the course of preparing the Company's financial statements under GAAP, changing when and as such percentage changes as determined by the Company from time to time. As used herein, "*GAAP*" means generally accepted accounting principles in the United States or any successor accounting rules required to be used by issuers of securities listed on a United States securities exchange. At the date of this Agreement, the Reserve Percentage is two and fifty-four one hundredths percent (2.54%). The collection of gross receipts as so reduced by the Reserve Percentage ("*Net Estimated Gross Receipts*") shall then be estimated and deemed received by the Company over a four-month collection period, beginning with the applicable calendar billing month for which the Occupation Tax is being calculated and continuing for the three calendar months immediately following such month. At the date hereof, the Company's determined estimate for the applicable percentages of Net Estimated Gross Receipts to be collected during each month of the four-month collection period is as follows:

- (i) in the initial month of the four month collection period, (*i.e.*, the month customers are billed) twenty-five percent (25%) of the amount billed during such month;
- (ii) for the second month of the collection period, fifty percent (50%) of the amount billed in the initial billing month;
- (iii) for the third month of the collection period, fifteen percent (15%) of the amount billed in the initial billing month; and
- (iv) for the fourth month of the collection period, ten percent (10%) of the amount billed in the initial billing month.

The Company may from time to time, in its reasonable discretion, adjust these collection rate percentages to reflect approximate monthly collection rates based on the Company's observed changes in account receivable collections for all gas service customers of the Company, and may round such percentages to the nearest increment of five percent; provided, however, that the sum of the four monthly percentages must be equal to one hundred percent (100%). The Company will provide the City with prompt written notice upon any change in monthly collection percentages. The Company's monthly collection percentages and the Reserve Percentage are subject to audit by the City in accordance with applicable law.

A hypothetical example of the calculation under this Agreement of Occupation Tax and Use Tax payable to the City is attached hereto as Schedule 1.

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(c) Subject to the City's audit rights referenced in Section 1(b) above, the Company's remittance to the City of the Occupation Tax as calculated pursuant to this Section 1 shall constitute payment of the Occupation Tax in full notwithstanding that the Company's actual gross receipts, if calculated in a different manner, may be less than or in excess of the Net Estimated Gross Receipts.

Section 2. Collection and Remittance of Use Tax.

(a) Notwithstanding anything in the Tax Collection Agreement to the contrary, the Use Tax which is required to be collected and remitted by Company to the City under the Tax Collection Agreement for any calendar month beginning with the month of November, 2005 (payable in December, 2005), shall be determined based on monthly estimates of Use Tax received, regardless of whether or not the Company actually collects payment of the Use Tax from customers.

(b) The Company shall estimate the payment of the Use Tax by Transportation Customers (as defined in the Tax Collection Agreement) based upon a percentage of the total Use Tax actually billed to Non-Certificated Transportation Accounts (as defined in the Tax Collection Agreement) for service during any calendar month. The gross amount billed for a given calendar month shall first be reduced by the Reserve Percentage. The collection of Use Tax as so reduced by the Reserve Percentage ("*Net Estimated Use Tax Collections*") shall then be estimated and deemed received over a four-month collection period, beginning with the applicable billing month for which the Use Tax is being calculated and continuing for the three calendar months immediately following such month. At the date hereof, the Company's determined estimate for the applicable percentage of Net Estimated Use Tax Collections to be collected during each month of the four-month collection period is as set forth in clauses (i) through (iv) of Section 1(b) hereof. The Company may from time to time, in its reasonable discretion, adjust these collection rate percentages as provided in Section 1(b) hereof. The Company will provide the City with prompt written notice upon any change in monthly collection percentages. The Company's monthly collection percentages and the Reserve Percentage are subject to audit by the City in accordance with applicable law and the Tax Collection Agreement.

A hypothetical example of the calculation under this Agreement of Occupation Tax and Use Tax payable to the City is attached hereto as Schedule 1.

(c) The Company shall calculate the Company's "Fee" (as defined in the Tax Collection Agreement) based on the Use Tax to be remitted as calculated pursuant to this Agreement.

(d) Subject to the City's audit rights referenced in Section 2(b) above, the Company's remittance to the City of the Use Tax as calculated pursuant to this Section 2 shall constitute full performance of the Company's obligations to collect and remit the Use Tax under the Tax Collection Agreement notwithstanding that the Company may

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receive cash payments from Transportation Customers of the Use Tax invoiced which are greater than or less than the amount so remitted.

Section 3. Lump-Sum Adjustments to Bad Debt Reserve

It is possible that under GAAP, the Company may be required to revise its reserve for bad debt by means of an adjustment that is not computed in the normal manner of providing for bad debt based upon a Reserve Percentage. In the event that the Company is required under GAAP to make an adjustment to its bad debt reserve for customer accounts receivable, the adjustment, positive or negative, shall be assumed to be fully taxable. The resulting change in Occupation Tax and/or Use Tax shall be deducted from or added to (as applicable) the amount of such tax billed in the month in which the adjustment is made. The Company will provide the City with prompt written notice upon making any such adjustment. These adjustments are subject to audit by the City in accordance with applicable law and, with respect to Use Tax, the Tax Collection Agreement.

Section 4. Transition Period.

(a) The City and the Company expect that as a result of this Agreement, there will be an amount of Use Tax and Occupation Tax which currently is not required to be paid or remitted to the City, but which would have been paid or remitted to the City if this Agreement were in effect during such periods of time. In order to reconcile the Company's Occupation Tax payments and Use Tax remittance prior to the date hereof with the collections and remittance from and after the date hereof, the Company is agreeing to pay such amount. Such amount (the "*Transition Amount*") shall be calculated by the Company according to the worksheet attached hereto as Schedule 2, which contains an example of the calculation solely for illustrative purposes. The Company shall pay to the City the Transition Amount according to the following schedule:

i. If the aggregate Transition Amount of Use Tax and Occupation Tax (the "*Aggregate Transition Amount*") is \$2 million or less, then the Company shall pay the Aggregate Transition Amount to the City in full on December 31, 2005, along with the payment of the Use Tax and Occupation Tax with respect to the month of November 2005;

ii. If the Aggregate Transition Amount is greater than \$2 million but less than \$6 million, then the Company shall pay the Aggregate Transition Amount to the City in two equal monthly installments beginning December 31, 2005, such payments to accompany the monthly payments of Use Tax and Occupation Tax;

iii. If the Aggregate Transition Amount is greater than \$6 million, then the Company shall pay the Aggregate Transition Amount to the City in three equal monthly installments beginning December 31, 2005, such payments to accompany the monthly payments of Use Tax and Occupation Tax.

(b) The Transition Amount paid to the City shall be deemed additional Occupation Tax or Use Tax, as applicable, collected during the calendar month prior to the month such payment is made, and shall not be deemed paid late by customers or remitted late by the Company. With each payment made to the City with respect to the Transition Amount, the Company shall include a cover letter explaining how much of the total amount then being paid to the City relates to payment of the Transition Amount, and not to Occupation Tax or Use Tax payable with respect to the prior calendar month, as well as what portion of the Transition Amount is Occupation Tax and what portion of the Transition Amount is Use Tax. The payments made pursuant to this Section 4(d) shall be sent to the attention of Michael P. Luzzi, Assistant Deputy, Department of Revenue, 333 South State Street, Suite 300, Chicago, Illinois 60604.

Section 5. Representations and Warranties.

(a) The Company represents and warrants that the execution, delivery and performance of this Agreement by the Company has been authorized by all necessary corporate actions and that this Agreement constitutes the legal, valid and binding obligation of the Company, is fully enforceable against the Company in accordance with the terms hereof except as such enforceability may be limited by any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors rights generally or by general principals of equity, will not violate any judgment, law or regulation or agreement binding on or affecting the Company and will not cause or constitute a default under any existing lien, charge, encumbrance or security interest upon any assets of the Company.

(b) The City represents and warrants that the execution, delivery and performance of this Agreement by the City has been authorized by all necessary municipal actions and that this Agreement constitutes the legal, valid and binding obligation of the City, is fully enforceable against the City in accordance with the terms hereof except as such enforceability may be limited by any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors rights generally or by general principals of equity, will not violate any judgment, law or regulation or agreement binding on or affecting the City and will not cause or constitute a default under any existing lien, charge, encumbrance or security interest upon any assets of the City.

Section 6. Miscellaneous Provisions.

(a) Except as amended by this Agreement, the Tax Collection Agreement remains in full force and effect. From and after the date of this Agreement, all references in the Tax Collection Agreement to "this Agreement" and all indirect references such as "hereof" or "herein" shall be interpreted and construed as meaning "this Agreement" (or "of this Agreement" or "in this Agreement", as the case may be) as amended by this Agreement.

(b) This Agreement may be executed in one or more counterparts, each of which shall be deemed an original but all of which shall constitute one and the same instrument.

(c) Each of the City and the Company agree not to file any suit or take any other action challenging or questioning the ability of any party to this Agreement to enter into this Agreement or to agree to determine the amount of Occupation Tax or Use Tax due as provided herein.

(d) If any provision of this Agreement is found by a court of competent jurisdiction to be unenforceable, then the City and the Company agree to negotiate in good faith to revise this Agreement so that its provisions shall be enforceable and shall as nearly as possible give effect to the original provisions and intent of this Agreement.

(e) This Agreement and the schedules hereto constitute the entire agreement between the City and the Company with respect to the subject matter hereof and no other warranties, inducements, considerations, promises or interpretations shall be implied that are not expressly addressed herein.

(f) No changes, amendments, modifications or discharge of this Agreement or any part hereof shall be valid unless the same are in writing and signed by the authorized agent of the Company and by the Director of the City's Department of Revenue or their respective successors and assigns.

(g) This Agreement shall be governed by and construed in accordance with the laws of the State of Illinois without regard to principles of conflicts of law.

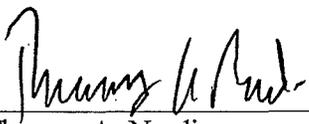
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Please acknowledge the City's agreement to the provisions hereof by signing both counterparts of this Agreement in the space provided below and returning one fully executed original to the undersigned's attention, upon which this Agreement shall be binding upon the City and the Company and their successors and assigns.

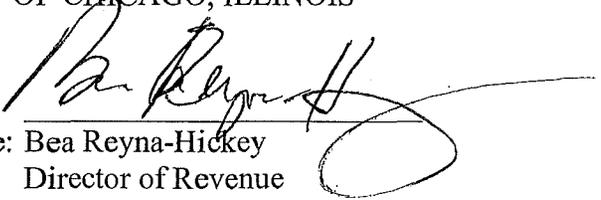
Very truly yours,

THE PEOPLES GAS LIGHT AND COKE
COMPANY

By: 
Thomas A. Nardi
Executive Vice President and
Chief Financial Officer

AGREED as of the date first written above:

CITY OF CHICAGO, ILLINOIS

By: 
Name: Bea Reyna-Hickey
Title: Director of Revenue

Schedule 1

Calculation of Estimated Receipts (Example Only)

August Tax Liability (Payable by Company on or before September 30)

Assume Reserve Percentage = 2.54%

<u>Month</u>	<u>Total Taxes Billed to Customers</u>		<u>100% Minus Reserve Percentage (2.54%)</u>	=	<u>Net Est. Gross Receipts and Net Est. Use Tax Collections</u>		<u>Applicable Monthly Collection Percentage</u>	=	<u>August Tax Liability</u>
August	4,100,000	x	97.46%	=	3,995,860	x	25%	=	\$ 998,965
July	4,200,000	x	97.46%	=	4,093,320	x	50%	=	2,046,660
June	5,900,000	x	97.46%	=	5,750,140	x	15%	=	862,521
May	9,500,000	x	97.46%	=	9,258,700	x	10%	=	925,870
Total August Tax Liability									<u>\$4,834,016</u>

Note: All numbers used are hypothetical and strictly for illustrative purposes.

Schedule 2
Sample Calculation of Transition Amount

Peoples Gas Light & Coke Company
Municipal Revenue Taxes
November 2005 Transition Amount

Chicago Municipal Utility Tax				Chicago Municipal Gas Use Tax				Total
November Balance per SAP			27,377,107	November Balance per SAP			5,587,318	32,964,425
Less: Unbilled Revenue			9,034,526	Less: Unbilled Revenue			2,638,079	11,672,605
Less: November payment due in December			4,777,856	Less: November payment due in December			1,271,491	6,049,347
Adjusted Balance			<u>13,564,725</u>	Adjusted Balance			<u>1,677,748</u>	<u>15,242,473</u>
Balance that should remain in the accrual after the November payment:				Balance that should remain in the accrual after the November payment:				
	Billed	%	Taxes		Billed	%	Taxes	
	Revenue	Outstanding	Uncollected		Revenue	Outstanding	Uncollected	
November	8,367,193	75%	6,275,395	November	1,653,381	75%	1,240,036	7,515,431
October	3,916,869	25%	979,217	October	1,149,495	25%	287,374	1,266,591
September	2,911,487	15%	436,723	September	1,172,821	15%	175,923	612,646
August	2,909,833	0%	-	August	1,107,443	0%	-	-
			<u>7,691,335</u>				<u>1,703,333</u>	<u>9,394,668</u>
Calculation of Transition Amount				Calculation of Transition Amount				
Adj current balance after payment using the percentage method			13,564,725	Adj current balance after payment using the percentage method			1,677,748	15,242,473
Accrual balance should be (using the percentage method)			<u>7,691,335</u>	Accrual balance should be (using the percentage method)			<u>1,703,333</u>	<u>9,394,668</u>
Transition Amount			<u><u>5,873,390</u></u>	Transition Amount			<u><u>(25,585)</u></u>	<u><u>5,847,805</u></u>