

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

NORTHERN ILLINOIS GAS COMPANY)
d/b/a NICOR GAS COMPANY)
)
Petition Pursuant to Rider 29 of Schedule of) Docket No. 10-0567
Rates for Gas Service to Initiate a Proceeding to)
Determine the Accuracy of the Rider 29)
Reconciliation Statement)

**BRIEF ON EXCEPTIONS OF
NICOR GAS COMPANY**

October 31, 2012

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Northern Illinois Gas Company d/b/a Nicor Gas Company (“Nicor Gas”) respectfully submits its Brief on Exceptions to the Administrative Law Judge’s (“ALJ”) Proposed Order dated October 17, 2012 (“Proposed Order” or “PO”). Pursuant to Section 200.830 of the Rules of Practice of the Illinois Commerce Commission (“Commission”), 83 Ill. Adm. Code 200.830, suggested replacement language is provided as Exceptions in Exhibit A to this brief.

I. INTRODUCTION

The Illinois General Assembly declared in 2009 that it is “the policy of the State that natural gas utilities ... are required to use cost-effective energy efficiency to reduce direct and indirect costs to consumers.” 220 ILCS 5/8-104(a) (P.A. 96-33, eff. 7-10-09). The Illinois General Assembly further declared that it “serves the public interest to allow natural gas utilities to recover costs for reasonably and prudently incurred expenses for cost-effective energy efficiency measures.” *Id.* To further these policies, the legislature mandated that natural gas utilities implement energy efficiency measures. 220 ILCS 5/8-104(c).

More than a year before Section 8-104 of the Public Utilities Act (the “Act”) became effective, Nicor Gas voluntarily proposed a pilot Energy Efficiency Plan in the Company’s rate case filed in 2008, Docket No. 08-0363 (“2008 Rate Case”). The Commission approved Nicor

Gas' voluntary Energy Efficiency Plan in the 2008 Rate Case Final Order. Docket No. 08-0363, Order at 156-59 (Mar. 25, 2009 and Oct. 7, 2009, collectively "Rate Case Order").

In this reconciliation proceeding, which arises under the voluntary program, the Company calculated that a credit of more than \$2 million was due to the relevant customer groups under Nicor Gas' Rider 29 – Energy Efficiency Plan ("EEP") for the first plan year. Importantly, there is no dispute in this proceeding about Nicor Gas' compliance with the Commission-approved Rider 29 or Nicor Gas' accounting under the rider. However, the Proposed Order adopts proposals made by the Citizens Utility Board ("CUB") and the Office of the Attorney General ("AG") (collectively "CUB/AG") and the Commission Staff ("Staff") to exclude certain costs from recoverable EEP expenses. Nicor Gas respectfully submits that the adjustments relating to consultant and employee costs are improper and unsupported by the record evidence. Nicor Gas addresses these two adjustments below and proposes related replacement language in its Exceptions. The Commission should issue a Final Order accepting Nicor Gas' revisions to the Proposed Order.

II. ARGUMENT

A. Exception No. 1 – The Proposed Order Should Be Revised To Permit Recovery Of All Consultant Costs

Nicor Gas respectfully submits that the Proposed Order errs in concluding that certain of the consultant costs incurred by Nicor Gas related to the development of its EEP in 2009 should be disallowed because they were not approved by the Advisory Board established to oversee the EEP. PO at 5. There is nothing in the record showing that the Advisory Board must approve EEP-related expenditures. Moreover, there is no requirement that the Advisory Board approve the EEP expenses in order for them to be recoverable under Rider 29, whether in any statutory authority, Commission rule or Order. Instead, Nicor Gas is entitled to recover its prudent and

reasonable expenses. *See, e.g., Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 121 (1995). Finally, the Proposed Order's conclusion ignores the fact that the very expenses it disallows were incurred as a direct result of demands placed upon the consultants by the Advisory Board, including specifically the AG and CUB representatives. Accordingly, as a matter of law and fundamental fairness, as further discussed below, Nicor Gas should be permitted to recover the prudent and reasonable consultant costs it incurred in implementing the voluntary and Commission-approved EEP.

1. No Approval Of The Expenditures Was Required

The Proposed Order relies upon the Rate Case Order to reject recovery of \$58,375 in consultant costs as such result is "in keeping with the delegation of authority to the Advisory Board for 2009." PO at 15. However, in approving Rider 29, the Commission recognized that the authority of the Advisory Board was limited to "determining what programs best suit ratepayers in Nicor's service territory" and beginning "the process of setting up those programs." Rate Case Order at 162. Thus, the authority of the Advisory Board did not extend to "oversight on expenditures during 2009" as described in the Proposed Order (at 15). As support for this conclusion, the Proposed Order quotes language from the Rate Case Order relating to a risk of imprudent or malfeasant expenditures. *Id.* In fact, as demonstrated in the full quote below, the Commission concluded in the Rate Case Order that EEP expenses were highly unlikely to be imprudent or malfeasant to the extent they were spent on setting up energy efficiency programs:

Logically, in the beginning the Advisory Board will be determining what programs best suit ratepayers in Nicor's service territory. It will also commence the process of setting up those programs. Thus, the funds spent during this period of time would largely be on setting up energy efficiency programs. Therefore, in the beginning of the program there is less risk of imprudent or malfeasant expenditures.

Rate Case Order at 162. And there is no dispute that the expenses at issue were spent on the exact activities contemplated by the Commission for the first year of the EEP, *i.e.*, “setting up energy efficiency programs.” *See, e.g.*, Jerozal Sur., Nicor Gas Ex. 6.0, 6:126-31.

The Proposed Order also refers to a “purposeful decision by the Board not to approve the RFP expenses when it approved the rest of the budget.” PO at 15. Yet, unlike with individual EEP expenses, there is record evidence demonstrating that the Advisory Board had the responsibility to approve an overall budget for 2009. The Bylaws state that the duties of the Advisory Board include “approval of the annual plan and budget for 2009.” CUB/AG Ex. 1.01 at 3. Thus, approval of the budget by the Advisory Board does not demonstrate that that individual EEP expenses also must be approved.

Put simply, the Commission did not mandate Advisory Board approval as a prerequisite to recovery of otherwise prudent and reasonable EEP expenditures, a fact that CUB/AG—the proponents of the adjustment—have expressly conceded: “[Nicor Gas witness] Jerozal is correct in that the Final Order does not specifically require the Board to approve expenditures.” CUB/AG Init. Br. at 5. Accordingly, the Proposed Order should be revised to permit recovery of the full amount of the consultant costs.

2. The Commission Has Authority To Approve Recovery Of Prudent And Reasonable EEP Expenses

Regardless of Advisory Board approval of EEP expenses, the Commission “must allow the utility to recover costs prudently and reasonably incurred.” *Citizens Util. Bd. v. Ill. Commerce Comm’n*, 166 Ill. 2d 111, 121 (1995) (citing 220 ILCS 5/1-102(a)(iv)). As such, the Commission has authority to review and approve recovery of Nicor Gas’ prudent and reasonable EEP expenses. There is no evidence refuting Nicor Gas’ evidentiary showing, summarized

below, that the consultant costs at issue were prudent and reasonable, nor did the Proposed Order conclude otherwise.

The costs at issue were paid to KO Solutions from May 2009 to December 2009, inclusive of amounts paid to Bass. Devens Reb., CUB/AG Ex. 2.0, 8:168-69; Devens Dir., CUB/AG Ex. 1.0 Corr., 8:158-9:163. This amount is inclusive of work KO Solutions performed as a consultant, as the Board Facilitator elected by the Advisory Board on July 21, 2009, and as the developer of Requests For Proposal (“RFPs”) for the Plan Administrator and for implementation contractors. Jerozal Reb., Nicor Gas Ex. 4.0, 3:57-60. Bass assisted KO Solutions with the development of these RFPs as reflected in the Advisory Board’s minutes as “RFP Consultant Support.” *Id.* at 3:61-62.

The evidence shows that KO Solutions and Bass brought much needed knowledge and expertise to the process of implementing the EEP as demonstrated by the fact that the Advisory Board unanimously elected KO Solutions to take on multiple roles and tasks throughout the process, including that of operating as the Board Facilitator. *Id.* at 5:102-04, 6:125-7:133; Nicor Gas Exs. 4.1-4.2. The Commission approved Rider 29 with the understanding that every attempt would be made to implement programs for the coming heating season, which accordingly required significant effort to start-up the EEP. Jerozal Reb., Nicor Gas Ex. 4.0, 6:107-10. Because Nicor Gas did not yet have sufficient experience or capability to implement the EEP (*see* Rate Case Order at 160), KO Solutions, with Bass as a subcontractor, provided the necessary experience and capabilities to guide Nicor Gas in (a) understanding how an Advisory Board would be constituted and who would be involved, (b) performing research and planning on the Advisory Board’s design, and (c) coordinating the Advisory Board’s initial efforts.

Jerozal Sur., Nicor Gas Ex. 6.0, 6:126-31. CUB/AG presented no evidence contesting these facts.

Nicor Gas Exhibit 6.1 provides a full description of the services provided by Bass during the fall of 2009:

In this engagement we provided on-demand support to Nicor Gas that included management advice, technical research, and a review of specific deliverables that evolved over a two-month engagement. The initial scope of the engagement was to write two implementation RFPs. Eventually the scope came to include a plan administrator RFP and new implementation RFPs that were developed in conjunction with Chicagoland Natural Gas Program. Each of these changes in scope required negotiation with new parties and often a re-negotiation of RFP content with existing parties, as well as added coordination with a separate organization. The initial intent was to develop implementation RFPs such that some new programs could be launched during the fall—a key time for customer enrollment in gas energy efficiency programs.

Nicor Gas Ex. 6.1, NR29 000149. As specifically detailed in Nicor Gas Exhibit 6.1, Bass expended tremendous time and effort to achieve the goal of establishing and implementing Nicor Gas' EEP. Without this assistance and that of KO Solutions, the start-up process for Nicor Gas' EEP would have been considerably lengthier and would have pushed the starting date for the EEP back many more months. Jerozal Sur., Nicor Gas Ex. 6.0, 6:131-7:133.

Although the Proposed Order (at 10) references CUB/AG's argument that delays in implementing the EEP weigh against a finding of prudence and reasonableness, the Proposed Order correctly refuses to adopt CUB/AG's position in this regard. That is because any delay in implementing Nicor Gas' EEP was due to the fact that the consultants were trying to follow and implement directives from the Advisory Board. Jerozal Sur., Nicor Gas Ex. 6.0, 10:215-16. For example, the AG and CUB representatives on the Advisory Board demanded that Nicor Gas partner with or make EEP offerings similar to those offered by Chicagoland Natural Gas

Program (“Chicagoland”), the then existing energy efficiency program affiliated with The Peoples Gas Light & Coke Company and North Shore Gas Company. Jerozal Sur., Nicor Gas Ex. 6.0, 10:219-22; Nicor Gas Ex. 6.1, NR29 000149-154. The evidence shows that the Advisory Board’s efforts to align with Chicagoland changed the scope of work and, by necessity, the timing of deliverables. Jerozal Sur., Nicor Gas Ex. 6.0, 11:234-40; Nicor Gas Ex. 6.1. Additional work included Bass serving as “the primary drafting agent for both Chicagoland and Nicor for the joint RFP creation, review and finalization process” and supporting “the review and vetting process of these joint RFPs with Chicagoland Plan Administrator, Chicagoland Board, Illinois Stakeholders, and the Nicor EEP Advisory Board.” Nicor Gas Ex. 6.1, NR29 000150-51. It was the very effort undertaken at the request of the AG and CUB representatives on the Advisory Board that caused the delay criticized by CUB/AG. And it was the additional work necessary to follow the directives of the Advisory Board, including, for example, trying to partner with or mirror the efforts of Chicagoland, which caused the amount payable to Nicor Gas’ consultants to increase above the original \$50,000 estimate. Jerozal Sur., Nicor Gas Ex. 6.0, 13:294-14:307. None of these facts have been refuted.

The evidence shows that the expenditures for Nicor Gas’ outside consultants were prudent and reasonable, and they should be approved without the adjustment adopted in the Proposed Order.

B. Exception No. 2 – The Proposed Order Should Be Revised To Permit Recovery Of Wages And Benefits

EEP expenses are defined in the rider as “the actual amount of EEP expenses accrued by the Company during the Previous Plan Period.” Ill. C. C. No. 16-Gas, 2nd Revised Sheet No. 82.1. There is no dispute here that the energy efficiency employee costs were prudently incurred, reasonable and necessary, or that they were actually incurred by Nicor Gas in

connection with the administration of its EEP during the first plan year. Martino Reb., Nicor Gas Ex. 3.0, 3:45-47, 3:49-54. Accordingly, those costs qualify as “EEP Expenses” under Rider 29 and are recoverable under the provisions of the rider. *Id.* at 3:47-48.

Nevertheless, the Proposed Order rejects Nicor Gas’ recovery of \$17,936 in wages and benefits for one employee who worked on the administration of the EEP. In particular, the Proposed Order concludes that Nicor Gas cannot recover these employee costs because Nicor Gas did not sufficiently counter Staff’s contention that such costs “were part of base rates and ... no new expense was incurred by the transfer of an employee whose previous responsibilities were absorbed by the existing workforce.” PO at 7. Nicor Gas respectfully submits that this conclusion is wrong in several respects, as set forth below, and urges that the Proposed Order be revised to reject Staff’s contention, particularly in light of the impact it may have on reconciliations beyond the first plan year of the EEP.

First, the assumption that the wages and benefits at issue were recovered through Nicor Gas’ existing base rates is inconsistent with general ratemaking principles. PO at 7. Nicor Gas’ base rates are set in a general rate case using a Commission-approved revenue requirement. Martino Reb., Nicor Gas Ex. 3.0, 5:99-6:107. That revenue requirement is based, in turn, on the amount of just and reasonable utility expenses that Nicor Gas is able to support for the particular representative test year used for that rate case. *Id.* Unlike certain riders, base rates established in a general rate case do not track and recover actual costs incurred by Nicor Gas in future periods. *Id.* Base rates do not assure Nicor Gas that it will earn any particular rate of return in any year or be able to recover any specific actual expenses incurred in any year. *Id.* In approving Nicor Gas’ revenue requirement in the 2008 Rate Case, the Commission examined the total costs to conduct Nicor Gas’ operations over a forecasted test year period, which costs were assumed to

be representative of the costs Nicor Gas would incur in the future. Martino Supp., Nicor Gas Ex. 7.0, 3:51-55. As the Illinois Supreme Court has recognized, “[i]n order to accurately determine the utility’s revenue requirement, the Commission established filing requirements under which a utility must present its rate data in accordance with a proposed one-year test year. The purpose of the test-year rule is to prevent a utility from overstating its revenue requirement by mismatching low revenue data from one year with high expense data from a different year.” *Bus. & Prof. People for the Pub. Interest v. Ill. Commerce Comm’n*, 146 Ill. 2d 175, 237-38 (1991). Thus, the suggestion that the salary of any individual employee can be traced to Nicor Gas’ Commission-approved base rates is contrary to the very philosophy behind using a representative test year in a rate case proceeding.

Second, there is no requirement in Rider 29 that Nicor Gas demonstrate it incurred “additional expense” in the administration of its EEP before such expense may be recovered. And, even if Nicor Gas were required to demonstrate that the employee costs were “additional,” Nicor Gas presented evidence demonstrating that these were new costs incurred specifically related to the administration of the EEP. More specifically, Nicor Gas’ current base rates were established using a forecasted 2009 test year in the 2008 Rate Case and the financials used for that test year did not include any expenses related to the Energy Efficiency Department. Martino Sur., Nicor Gas Ex. 5.0, 2:37-40. As a result, the Commission-approved base rates did not include any costs associated with recovery of expenses for the new department. *Id.* at 2:40-41. Staff agrees that the “revenue requirement for the test year in Nicor’s most recent rate proceeding did not include any expenses specific to the new Energy Efficiency Department.” Jones Supp., Staff Ex. 3.0, 3:48-50. Thus, the wages and benefits associated with employees in the Energy Efficiency Department, and as to which recovery is at issue, represent entirely new

costs that Nicor Gas incurred as a result of establishing and implementing its EEP. Martino Sur., Nicor Gas Ex. 5.0, 2:41-44. Staff conceded as much by approving the cost of one employee's salary "in allowable Rider 29 expenses." Jones Reb., Staff Ex. 2.0, 4:79-80. That this particular employee's former position was filled by another employee does not change the fact that both employees in the Energy Efficiency Department during the first plan year began working solely on the EEP after their transfer to that department, and their former activities are entirely performed by other Nicor Gas personnel or have been discontinued. Martino Sur., Nicor Gas Ex. 5.0, 3:50-53.

Nicor Gas presented additional evidence demonstrating that these were new costs that Nicor Gas incurred specifically related to the administration of the EEP in the form of its annual internal audit results. Nicor Gas Ex. 3.1. Section F of Rider 29 provides that Nicor Gas is to perform an annual internal audit of the operation of the rider. Martino Reb., Nicor Gas Ex. 3.0, 4:65-66. One of the tests to be conducted as part of the audit is whether the costs being recovered under the rider are not otherwise being recovered through other existing, Commission-approved tariff mechanisms. *Id.* at 4:66-69. Nicor Gas conducted the required internal audit and the final audit report concluded that the costs being recovered through Rider 29 for the first plan year are not being recovered through other existing, Commission-approved tariffs. *Id.* at 4:70-72; Nicor Gas Ex. 3.1. This conclusion refutes Staff's contention, quoted in the Proposed Order (at 7), that there was nothing in the audit workpapers indicating "consideration was given to whether any of the costs incurred by or assigned to the Energy Efficiency Department are recovered in base rates." The contents of the audit workpapers do not change the Rider 29 audit tests or the ultimate conclusion of the audit that the costs being recovered through Rider 29 for the first plan year are not being recovered through other existing, Commission-approved tariffs.

Nicor Gas Ex. 3.1. The audit report was filed with Staff on January 26, 2011 and no party contested its conclusions. Martino Reb., Nicor Gas Ex. 3.0, 4:73-74.

In short, the Proposed Order should be revised to permit Nicor Gas' recovery of all energy efficiency employee costs incurred in connection with the administration of the EEP because Nicor Gas demonstrated that the wages and benefits at issue are properly recovered under Rider 29.

C. Exception No. 3 – Conforming Corrections

Nicor Gas offers revisions to the Findings and Orderings Paragraphs of the Proposed Order consistent with Nicor Gas' position on the two issues described above.

In addition, Nicor Gas notes that, if the Commission adopts any of the adjustments reflected in the Proposed Order, the Final Order should provide for the mechanism by which Nicor Gas would credit the relevant customer groups given that Rider 29 is no longer in effect. Nicor Gas suggests that such credits could be made through the Company's current Rider 30 – Energy Efficiency Plan Cost Recovery reconciliations. Nicor Gas also offers language to address this issue in Exception No. 3.

III. CONCLUSION

WHEREFORE, for each of the reasons set forth herein and within its Initial and Reply Briefs, Northern Illinois Gas Company d/b/a Nicor Gas Company respectfully requests that the Commission revise the Proposed Order consistent with the positions set forth herein and with the replacement language set forth in Exhibit A.

Dated: October 31, 2012

Respectfully submitted,

NORTHERN ILLINOIS GAS COMPANY
D/B/A NICOR GAS COMPANY

By: /s/ Anne W. Mitchell
One of its attorneys

John E. Rooney
Anne W. Mitchell
Rooney Rippie & Ratnaswamy LLP
350 West Hubbard Street, Suite 600
Chicago, Illinois 60654
(312) 447-2800
john.rooney@r3law.com
anne.mitchell@r3law.com