

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

North Shore Gas Company :
 :
The Peoples Gas Light :
and Coke Company :
 : **Docket No. 12-0381**
Petition for an order approving an :
agreement for the provision :
and services between affiliates pursuant :
to Sections 7-101 and 7-102 :
of the Illinois Public Utilities Act :

PROPOSED FORM OF ORDER

By the Commission:

I. PROCEDURAL HISTORY

On June 7, 2012, North Shore Gas Company (“North Shore”) and The Peoples Gas Light and Coke Company (“Peoples Gas”) (together, the “Utilities”) filed a Petition requesting approval of an affiliated interest agreement pursuant to Sections 7-101 and 7-102 of the Public Utilities Act (“Act”). With the Petition, the Utilities also filed the Direct Testimony and exhibit of Richard E. Dobson, Manager of Gas Supply for the Utilities, and the Direct Testimony and exhibits of Denean V. Smith, Manager of Fuel and Supply Accounting for Integry Energy Group, Inc.’s (“Integry”) utilities, including North Shore and Peoples Gas.

On September 19, 2012, the Commission Staff filed the Direct Testimony of Brett Seagle, Gas Engineer in the Energy Engineering Program of the Safety and Reliability Division, and the Direct Testimony of Daniel G. Kahle, Accountant in the Accounting Department of the Financial Analysis Division.

On October 17, 2012, the Utilities filed the Rebuttal Testimony of Denean V. Smith.

There are no intervenors in this proceeding.

An evidentiary hearing was held on October 25, 2012. Admitted into the record, by affidavit, were the Direct Testimony and exhibit of Richard E. Dobson on behalf of the Utilities (NS-PGL Exs. 1.0 and 1.1) and his affidavit (NS-PGL Ex. 4.0); the Direct Testimony and exhibits of Denean V. Smith on behalf of the Utilities (NS-PGL Exs. 2.0, 2.1, and 2.2), Ms. Smith’s Rebuttal Testimony (NS-PGL Ex. 3.0) and her affidavit (NS-PGL Ex. 5.0). Also admitted into the record, by affidavit, were the Direct Testimony of Brett Seagle on behalf of the Commission Staff (ICC Staff Ex. 1.0) and his affidavit (ICC

Staff Ex. 1.1); and the Direct Testimony of Daniel G. Kahle on behalf of the Commission Staff (ICC Staff Ex. 2.0) and his affidavit (ICC Staff Ex. 2.1).

On October 25, 2012 the Administrative Law Judge marked the record "Heard and Taken."

On November 5, 2012, the Utilities filed an agreed form of draft proposed order.

The Commission considers the whole of the record and the arguments presented.

II. ISSUES

A. The Utilities' Position

Utilities witness Mr. Dobson explained that Peoples Gas owns and operates a storage field, located in Champaign County, Illinois, called Manlove Field. It has provided a storage service to North Shore since 1967 under various agreements. The Commission approved the currently effective agreement in Docket No. 87-0401. Mr. Dobson stated that North Shore, under the process permitted in that agreement, reduced its daily contract quantity in each of three supplemental agreements, effective November 1 of each of 1993, 1994, and 1995.

Mr. Dobson stated that the proposed Storage Agreement is necessary to define more accurately and precisely the commercial service that Peoples Gas can provide to North Shore. It is also appropriate to revise the agreement to update references and generally incorporate conventional and more complete contract terms and conditions.

Mr. Dobson testified that the proposal does not change how North Shore recovers costs and how Peoples Gas accounts for revenues it receives from North Shore. Specifically, he said that North Shore would continue to recover costs through its Rider 2, Gas Charge, except for cushion gas that is part of its rate base, which is how North Shore recovers the costs of storage services it purchases from pipelines. Peoples Gas would continue to reflect revenues in its base rate filings.

Mr. Dobson briefly described each article of the agreement, which was included as an exhibit to his testimony, and key changes from the currently effective agreement. He testified:

- Article I is definitions, which include terms that allow a more precise definition of each party's rights and obligations.
- Article II specifies the contract term, including an automatic rollover provision.
- Article III describes the storage service. Unlike the current agreement, it specifies a specific nomination process, locations at which North Shore may deliver gas for injection, and how Peoples Gas makes deliveries to North Shore.
- Article IV defines, in greater specificity than the current agreement, gas quantities in terms of peak day and daily rights and the total storage quantity. A cycling requirement is a key new feature.
- Article V describes the monthly cost of service and charges for over- and under-run and for failing to satisfy the cycling requirement. This article is similar to the existing provision, but it removes obsolete references and clarifies the wording. It also excludes LNG costs from the calculation.

- Article VI defines cushion gas requirements and is more detailed than the current agreement.
- Article VII is an order of deliveries provision.
- Article VIII sets out standard language on measurement, quality and delivery and is more complete and better mirrors the type of language found in pipeline agreements and tariffs.
- Article IX describes the allocation of gas upon contract termination. The current agreement includes such a provision.
- Article X is a *force majeure* provision.
- Article XI is a government regulation provision. Mr. Dobson stated that such a provision is fairly common in commercial agreements and pipeline tariffs, and it is particularly appropriate for an agreement between two regulated companies.
- Article XII includes several common contractual terms and conditions pertinent to the interpretation of the agreement. Again, Mr. Dobson stated that such provisions are common in commercial agreements and pipeline tariffs.

Mr. Dobson stated that the cost to North Shore's customers is competitive with alternatives from pipelines and gave a specific example. He further testified that Peoples Gas will receive appropriate cost recovery under the proposal. Finally, he explained how customers benefit. The proposed Storage Agreement includes commercial terms that accurately reflect the service that Peoples Gas can support with its Manlove Field. New language defining contract quantities, injection and withdrawal rights, cycling requirements, and nomination procedures best reflects these improvements. Mr. Dobson explained that this benefits North Shore's customers by ensuring that North Shore receives specific service rights and allowing it to compare the Peoples Gas service with alternatives. He explained that Peoples Gas' customers benefit by ensuring that North Shore receives and pays for a service that is contractually limited to the physical capability of the asset supporting that service. Also, he stated that the proposed Storage Agreement includes contract terms and conditions that are customary in arm's length contracts. For example, the proposed Storage Agreement includes *force majeure* language and a complete set of definitions. Including such provisions benefits the Utilities' customers by eliminating the ambiguity that may result from omitting common terms and conditions that an independent third party reviewing the agreement would find important in determining the parties' intent.

Utilities witness Ms. Smith addressed certain accounting issues related to the proposed agreement. She stated that the cost will no longer include LNG-related costs and the proposed agreement clarifies the description of the accounts that Peoples Gas uses in billing North Shore.

With respect to cushion gas, Ms. Smith explained that Article VI addresses cushion gas requirements, and the Utilities expect that, when the agreement becomes effective, Peoples Gas will transfer cushion gas to North Shore. She stated that North Shore has reduced its contract quantity, which reduced its cushion gas requirements. However, the proposed agreement no longer provides that LNG assets will support the service to North Shore. These changes would result in Peoples Gas having excess cushion gas. Ms. Smith explained that North Shore is not currently subsidizing Peoples Gas because North Shore bills Peoples Gas for the excess.

With respect to the expected transfer, Ms. Smith stated that it will be approximately 800,000 dekatherms (Dth) and will occur at net book value of Peoples Gas' cushion gas assets at the time of the transaction, which, at December 2011, was approximately \$715,000. Specifically, based on December 31, 2011 data, Peoples Gas would transfer 39,311 Dth recoverable cushion gas and 746,872 Dth non-recoverable cushion gas to North Shore. The actual data will depend on when the transfer occurs. The dollar value of each transfer would be determined at the average cost per dekatherm maintained on Peoples Gas' books for the three following asset classifications: (1) Recoverable cushion gas recorded in Account 117. This gas is not depreciated. (2) Non-recoverable cushion gas recorded as a fixed asset in Account 101. This gas is depreciated. (3) The reserve for depreciation related to the non-recoverable cushion gas recorded as a reduction to fixed assets in Account 108. Ms. Smith sponsored two exhibits illustrating the transfer, including proposed accounting entries.

B. The ICC Staff's Position

ICC Staff witness Mr. Seagle stated that he conducted a review and analysis of the Utilities' filing to determine if approval of the proposed Storage Agreement is in the public interest and that the public will be inconvenienced thereby. He stated that, using the standards set forth in Sections 7-101 and 7-102 of the Act, he found no reason to take issue with the Utilities' request for Commission approval of the proposed Storage Agreement. He reviewed the Utilities' direct testimony and accompanying attachments to the petition. He stated that nothing came to his attention to cause him to dispute the Utilities' assertion that the proposed Storage Agreement is in the public interest or to conclude that approval of the Storage Agreement will not serve the public convenience. Mr. Seagle had no recommendations for the Utilities' Storage Agreement.

ICC Staff witness Mr. Kahle stated that he reviewed the Utilities' Petition for approval of the Storage Agreement. He described the background of the filing. Mr. Kahle noted certain accounting issues associated with the filing. He stated that employee benefits are included in Peoples Gas' charges to North Shore. Citing a Utilities' response to a Staff data request, he stated the response indicated that incentive compensation is included in Peoples Gas' charges to North Shore. Peoples Gas' charges are recovered in North Shore's PGA rates. Mr. Kahle further stated that the response indicated that the Storage Agreement does not provide for exclusion of incentive compensation that might be earnings based, and that Peoples Gas does not make such a determination. Mr. Kahle stated that the Commission has generally not allowed recovery of earnings-based incentive compensation. Citing another data response, he stated that Peoples Gas billed \$32,795 of incentive compensation to North Shore in 2011.

Mr. Kahle also noted that cash working capital ("CWC") is included in Peoples Gas' charges to North Shore calculated at the one-eighth method rather than through a lead/lag study. Mr. Kahle stated that, in recent rate cases, the Commission has required the Utilities to base CWC on a lead/lag study. Citing a Utilities' response to a Staff data request, he stated that Peoples Gas billed \$7,761 of CWC to North Shore in 2011.

Mr. Kahle concluded that, given the small amount of incentive compensation billed to North Shore by Peoples Gas, he was not recommending changes to the Storage Agreement related to incentive compensation. Also, given the cost of a lead/lag study and the small amount of CWC billed to North Shore by Peoples Gas, he was not recommending changes to the Storage Agreement related to CWC. However, Mr. Kahle recommended monitoring tools. Specifically, he recommended that the Commission order the Utilities to submit a report annually to the Manager of Commission's Accounting Department, on or before June 30 of each year, stating the amount of incentive compensation and CWC collected by Peoples Gas from North Shore through the Storage Agreement for each calendar year starting with 2012. The report should also state if the incentive compensation and CWC collected by Peoples Gas through the Storage Agreement was excluded from recovery in rate proceedings. This report should be verified by an officer of the Utilities.

C. The Utilities' Response

Utilities witness Ms. Smith stated that the Utilities accepted Mr. Kahle's recommendations to submit annually, no later than June 30, an officer-verified report that states, for amounts Peoples Gas collected from North Shore through the Storage Agreement:

- the amount of incentive compensation;
- the amount of CWC; and
- if such incentive compensation and CWC were excluded from recovery in rate proceedings.

She stated that the Utilities propose that the first such report be due on June 30 after the Storage Agreement has been in effect for a year. For clarity, Peoples Gas notes that the requested information refers to amounts collected, for which Peoples Gas would use actual costs billed or accrued. She also noted that Peoples Gas' rate proceedings typically use a future test year, so any amounts excluded are based on forecast data in contrast with the actual data that will be the basis for the first two requested items.

III. COMMISSION ANALYSIS AND CONCLUSION

IV. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having considered the entire record and being fully advised in the premises, is of the opinion and finds that:

- (1) North Shore Gas Company is an Illinois corporation engaged in the distribution of natural gas to the public in the State of Illinois and, as such, is a public utility within the meaning of the Public Utilities Act;
- (2) The Peoples Gas Light and Coke Company is an Illinois corporation engaged in the distribution of natural gas to the public in the State of Illinois and, as such, is a public utility within the meaning of the Public Utilities Act;

- (3) the Commission has jurisdiction over North Shore and Peoples Gas and of the subject matter of this proceeding;
- (4) the recitals of fact and the conclusions reached in the prefatory portion of this Order are supported by the record and are hereby adopted as findings of fact;
- (5) North Shore and Peoples Gas filed a Petition pursuant to Sections 7-101 and 7-102 of the Public Utilities Act requesting approval of an affiliated interest agreement under which Peoples Gas would provide a storage service to North Shore;
- (6) Staff recommended, and North Shore and Peoples Gas agreed, to certain reporting obligations associated with the proposed agreement, namely that by June 30 each year, North Shore and Peoples Gas would submit to the Commission's Manager of Accounting Services an officer-verified report that states, for amounts Peoples Gas collected from North Shore through the storage service agreement: (a) the amount of incentive compensation; (b) the amount of CWC; and (c) if such incentive compensation and CWC were excluded from recovery in rate proceedings, with the first such report due on June 30 after the Storage Agreement has been in effect for a year; and
- (7) all motions, petitions, objections or other matters in this proceeding which remain undisposed of should be disposed of consistent with the conclusions herein.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that, pursuant to Sections 7-101 and 7-102 of the Act, consent and approval to the entry by Peoples Gas and North Shore into the Storage Service Agreement, submitted in evidence as NS-PGL Ex. 1.1, is granted.

IT IS FURTHER ORDERED that authority to perform all acts necessary to performance of the Storage Service Agreement that are not contrary to the Act and the Commission's rules and regulations is granted.

IT IS FURTHER ORDERED that each year, on or before June 30, North Shore and Peoples Gas shall submit to the Commission's Manager of Accounting an officer-verified report that states, for amounts Peoples Gas collected from North Shore through the storage service agreement: (a) the amount of incentive compensation; (b) the amount of CWC; and (c) if such incentive compensation and CWC were excluded from recovery in rate proceedings, with the first such report due on June 30 after the Storage Agreement has been in effect for a year.

IT IS FURTHER ORDERED that any objections, motions or petitions filed in this proceeding that remain unresolved should be disposed of in a manner consistent with the ultimate conclusions contained in this Order.

IT IS FURTHER ORDERED that subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Admin. Code Sec. 200.800, this Order is final; it is not subject to the Administrative Review Law.

By Order of the Commission this _____ day of _____, 201__.

(SIGNED)

CHAIRMAN