STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Northern Illinois Gas Company d/b/a Nicor Gas Company	)))	
Proposed Establishment of Rider 17, Purchase of Receivables with Consolidated Billing.	)))	Docket No. 12-0569

REPLY BRIEF OF NICOR GAS COMPANY

Dated: May 24, 2013

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In accordance with the schedule established by the Administrative Law Judge ("ALJ"), Northern Illinois Gas Company d/b/a Nicor Gas Company ("Nicor Gas" or the "Company") hereby files with the Illinois Commerce Commission ("Commission") this Reply Brief following an evidentiary hearing held on May 6, 2013.

I. EXECUTIVE SUMMARY

Contrary to a recurring theme in the Initial Brief of the Citizens Utility Board / Illinois Attorney General ("CUB-AG"), this proceeding is not a referendum on the current state of the competitive market for natural gas supply in Illinois or the actions of those participating in the market. *See* CUB-AG Corr. Init. Br. at 13-14, 16-19, 25. Instead, the issue is whether to approve Nicor Gas' new proposed tariff – Rider 17 – Purchase of Receivables with Consolidated Billing ("PORCB") – and its cost recovery mechanism. Rider 17 provides Qualifying Alternative Gas Suppliers ("Q-AGS") with the option to have Nicor Gas purchase their receivables for natural gas sales made by the Q-AGS to certain customers and it also provides a mechanism for the Company to recover its costs to provide this service. If CUB-AG have an issue with the competitive market place for natural gas supply, it is clear that this proceeding is not the forum to address such claims.

Not only does CUB-AG fail to grasp the purpose of this proceeding, they also argue for a legal standard to assess proposed Rider 17 that has no foundation in the Public Utilities Act (the "Act"). 220 ILCS 5/1-101, *et seq*. Nothing in the Act even remotely suggests that a proposed rider must pass a "net benefits" test in order to obtain Commission approval. In addition, CUB-AG did not, and could not, cite to any applicable authority to support such a claim. Rather, consistent with the long-standing interpretation of Section 9-201 of the Act, the Commission can approve a tariff pursuant to the "just and reasonable" standard. 220 ILCS 5/9-201. The

Commission Staff ("Staff") presents a similar, flawed legal standard to evaluate Rider 17 by arguing that the rider must be "in the public interest." Staff Init. Br. at 2, 4. This claim too is presented without any statutory citation to support the assertion.

Nicor Gas presented substantial and compelling evidence demonstrating that its proposed Rider 17 holds Nicor Gas' supply and delivery customers harmless in the provision of this new, optional service. The evidence also demonstrates that Nicor Gas developed a mechanism to recover all costs incurred in order to provide the new PORCB service because these costs are not being recovered through current base rates. Finally, the evidence demonstrates that Nicor Gas proposed a balanced PORCB program in response to the request of certain alternative gas suppliers ("AGS") for a PORCB program. The Initial Brief of the Retail Energy Supply Association ("RESA") and Interstate Gas Supply ("IGS") reinforces that "Nicor Gas has put together a good PORCB Program … which incorporates cost recovery within the program and ensures the ability of the utility to terminate for the full amount of the receivable." RESA-IGS Init. Br. at 2.

The Commission also should reject the Staff and CUB-AG alternative recommendations to modify the tariff design as they will put Nicor Gas at risk of not recovering its costs incurred in order to offer its proposed PORCB program.[1] Because Nicor Gas is proposing a voluntary service designed to meet its operational requirements, the Company respectfully requests that the Commission either approve Rider 17 as proposed and modified by the Company in rebuttal testimony (*see* Nicor Gas Ex. 2.2) or reject the tariff altogether. As this proposed service is not statutorily mandated, as Staff and CUB-AG recognize (Staff Init. Br. at 7; CUB-AG Corr. Init.

[1] Although Staff has withdrawn its opposition to Nicor Gas' proposed rate of return related to the PORCB program (Staff Init. Br. at 27-28), Staff's recommended changes to the tariff design continue to put Nicor Gas at risk of not obtaining full cost recovery.

Br. at 8), the Commission should not approve any version of the tariff that would expose Nicor Gas to the risk of less than complete cost recovery of its Rider 17-related costs.

II. ARGUMENT

A. The Public Utilities Act does not Support CUB-AG's and Staff's Novel Legal Standard to Assess Rider 17.

CUB-AG assert that there are two "fundamental grounds" on which the Commission should reject Rider 17: (1) there is no legal authority under which the Commission may approve a PORCB program for a gas utility; and (2) there is no evidence that the benefits of the PORCB program outweigh the costs. CUB-AG Corr. Init. Br. at 2. Both "grounds" rely upon unsubstantiated legal arguments.

CUB-AG's first argument is based on the false premise that there is no statutory authority for the Commission's approval of Rider 17. On the contrary, Nicor Gas made its tariff filing pursuant to Section 9-201 of the Act. 220 ILCS 5/9-201(c) ("the Commission shall establish the rates or other charges … which it shall find to be just and reasonable"). The Commission recognized this statutory authority in the October 17, 2012 Order in this proceeding suspending the proposed establishment of Rider 17. Docket No. 12-0569, Suspension Order at 2 ("IT IS FURTHER ORDERED that pursuant to the provisions of Section 9-201 of the Public Utilities Act, the proposed establishment of Rider 17, stated in the Filed Rate Schedule Sheets, filed by Nicor on September 5, 2012, be, and the same is hereby suspended for a period of 105 days beginning with October 20, 2012, to and including February 1, 2013."). Indeed, in the legal standards section of CUB-AG's Initial Brief, they cite to Section 9-201(c) of the PUA and argue that the tariff "must be just and reasonable" in order for the Commission to approve it. CUB-AG Corr. Init. Br. at 9-11.

Moreover, in a case CUB-AG cite in their Initial Brief (at 6), the Illinois Supreme Court recognized that the Commission has broad authority to set and design utility rates. *Business and Prof'l People for the Pub. Interest v. Illinois Commerce Comm'n*, 136 Ill. 2d 192, 204 (1989) ("BPI"). Included within that authority is the ability to approve riders as a "preferred mechanism" for cost recovery. *Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 140 (1995) ("We find the Commission's approval of a rider as the preferred mechanism for recovery of coal-tar cleanup costs is within the Commission's authority…."). The Illinois Supreme Court has long recognized that the Commission has the power to authorize a rider in a proper case. *City of Chicago v. Illinois Commerce Comm'n*, 13 Ill. 2d 607, 614 (1958). *See also North Shore Gas Company, The Peoples Gas Light and Coke Company, Proposed General Increase in Natural Gas Rates,* Docket Nos. 09-0166, 09-0167 (Cons.) Order at 131-132 (Jan. 21, 2010) ("Peoples 2009 Rate Case Order"); *Commonwealth Edison Company, Proposed General Increase in Electric Rates,* Docket No. 07-0566, Order at 137-38 (Sept. 10, 2008) ("ComEd 2007 Rate Case Order"); *North Shore Gas Company, The Peoples Gas Light and Coke Company, Proposed General Increase in Natural Gas Rates,* Docket Nos. 07-0241, 07-0242 (Cons.) Order at 138-53, 183-84 (Feb. 5, 2008) ("Peoples 2007 Rate Case Order").

Notably, undisputed facts also undermine CUB-AG's statutory authority argument. It is undisputed that Nicor Gas has offered its residential and small commercial customers the option to purchase their natural gas from third-party, AGS for more than a decade through a Commission-approved tariff, Rider 15 – Customer Select Program.[2] At the time the Commission approved the expansion of Rider 15 to all of Nicor Gas' customers, in July 2001, and through and including the present, there has been no specific statutory provision authorizing a gas utility

[2] The Commission approved expansion of Nicor Gas' Customer Select pilot program to all customers of Nicor Gas in Docket Nos. 00-0620, 00-0621 (Cons.). Order (July 5, 2001); Order on Rehearing (Jan. 3, 2002).

to offer choice to customers. Instead, the Commission approved Nicor Gas' offering of the Customer Select Program through Rider 15 pursuant to Section 9-201 of the Act – the same Section applicable to proposed Rider 17.[3] As such, CUB-AG's claim that Rider 17 cannot be approved absent specific statutory authority rings hollow.

CUB-AG's second argument is equally flawed. They advance the unsupported theory that the Commission should only approve Nicor Gas' Rider 17 if it provides "net benefits" to customers. CUB-AG Corr. Init. Br. at 13-16. Staff raises the similar argument that the Commission should only approve Rider 17 "if it believes that the expenditures to implement Rider 17 are prudently incurred." Staff Init. Br. at 4. Staff appears to argue that if the benefits to customers are greater than the costs required to implement the PORCB program, then the Commission may approve Rider 17 as being "in the public interest." *Id*. at 2, 4. Staff also appears to argue that the Commission may entirely reject Rider 17 because Nicor Gas did not have the opportunity to work with RESA and IGS to try to agree upon the form of a sample Billing Service Agreement or title transfer document(s) in the compressed time provided for in this proceeding. *Id*. at 24-26.

Neither the Staff nor the CUB-AG Initial Brief cites any legal authority from which these theories are derived, much less supported.[4] That is because there is no Commission rule or decision, or any other authority supporting a "prudently incurred" or "net benefits" test as

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[3] *See, e.g., Northern Illinois Gas Company, Proposed Changes to Riders 15 and 16 and related provisions*, Docket No. 00-0621, Suspension Order at 2 ("IT IS FURTHER ORDERED that pursuant to the provisions of Section 9-201 of the Public Utilities Act, the proposed rate sheets filed by Nicor on August 11, 2000, be, and the same hereby are, suspended for a period of 105 days….").

[4] CUB-AG argue that investment included in a utility's rates must be "prudently incurred," citing Section 9-211 of the PUA, 220 ILCS 5/9-211. CUB-AG Corr. Init. Br. at 11. However, Section 9-211, which is titled "Investments included in rate base," simply does not apply here because none of the costs that Nicor Gas would incur to provide the new PORCB service would be recovered through Nicor Gas' base rates. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 3:53-55.

applied to approval of a new cost tracker like Rider 17. The Commission should not adopt such a novel, unauthorized test here.[5]

Finally, much of the legal authority that Staff and CUB-AG do cite is inapposite. For example, Staff's reliance on *Governor's Office of Consumer Servs. v. Illinois Commerce Comm'n*, 242 Ill. App. 3d 172 (1992) for a "known and measurable" standard for cost recovery is misplaced. Staff Init. Br. at 10, 13. In that case, the Appellate Court affirmed the Commission's disallowance of postage expenses attributable to a postal rate increase for purposes of establishing base rates in a rate case because the "record contains no proof that the increase in postage costs would occur in the test year." *Governor's Office of Consumer Servs.*, 242 Ill. App. 3d at 190. Unlike that case, this proceeding does not concern the setting of base rates. Rather, Nicor Gas is seeking the approval of a rider that establishes a PORCB program and the cost recovery mechanism for the program. Moreover, Staff's claim that the Company "is in effect asking the Commission to approve a blank check" for PORCB-related costs (Staff Init. Br. at 13) ignores the fact that any cost incurred relative to Rider 17 will be subject to substantial review through the following tariff provisions: Section G – Reconciliation, Section H – Commission Review and Section I – Internal Audit. *See* Nicor Gas Ex. 2.2, Sheets 75.9.12-75.9.13. Thus, the question of whether any particular Rider 17-related cost should be disallowed will be the subject of a future reconciliation proceeding.

In fact, a rider is appropriate for cost recovery in the circumstances where the costs *are not* known and measurable. *See Citizens Util. Bd.*, 166 Ill. 2d at 138 (recognizing that "a rider mechanism is effective and appropriate for cost recovery when a utility is faced with unexpected,

[5] The question of the prudence of any individual costs will be the subject of a future reconciliation proceeding. Here, the Commission should determine whether Nicor Gas should move forward with implementing a PORCB program in the first instance and approve the cost recovery mechanism for the costs that Nicor Gas will incur if it does in fact move forward.

volatile, or fluctuating expenses"). In *Citizens Util. Bd. v. Illinois Commerce Comm'n*, the Court affirmed the Commission's approval of a rider mechanism to recover coal-tar cleanup costs, reiterating the Commission's conclusion that, "given the wide variations and the difficulties in forecasting the costs of investigation and remediation activities, riders can generally be expected to provide a more accurate and efficient means of tracking costs and matching such costs with recoveries than would base rate recovery methods." *Id*. at 138-39.

There also is no legal support for CUB-AG's arguments that PORCB programs only are appropriate for electric utilities. CUB-AG Corr. Init. Br. at 7-9 (citing various sections of the PUA). CUB-AG attempt to infer authority for the Commission's rejection of Rider 17 from the fact that the PUA is silent as to gas utilities while it speaks to the competitive market for electric utilities. They cite *Laborer's Int'l Union of N. Am., Local 1280 v. State Labor Relations Bd.*, 154 Ill. App. 3d 1045 (1987) for the proposition that "the intent of the legislature can be derived not only from the language adopted, but from the language that was not adopted." CUB-AG Corr. Init. Br. at 9. That case is factually distinguishable because the Court found significance in the fact that "the state legislature specifically declined to adopt a certain section of the model federal statute, [which] evidences an intent to achieve a result different from that announced by the decisions of the federal courts" interpreting that federal statute. 154 Ill. App. 3d at 1050. There is no model federal statute at issue here that the Illinois General Assembly has adopted only in part.

Furthermore, the fact that the Illinois General Assembly has not passed a bill regarding gas utility PORCB programs fails to reveal anything about the legislature's intent, much less an "intention to restrict the operation of such a tariff to electric utilities" as CUB-AG argue. CUB-

AG Corr. Init. Br. at 6. The Illinois Appellate Court has explained why there is no legal effect to the "inaction" of the General Assembly:

> While we agree with the general premise that an administrative body is not free to undermine the express intent of our General Assembly, we do not share plaintiffs' claim that rejected legislation unequivocally evinces a wholesale legislative disapproval of the substance of failed legislation. As recognized by the United States Supreme Court, legislative inaction "'lacks persuasive significance because several equally tenable inferences may be drawn from such inaction.'" "A bill can be proposed for any number of reasons, and it can be rejected for just as many others." The legislature "'can not express its will by a *failure* to legislate. The act of refusing to enact a law … has utterly no legal effect, and thus has utterly no place in a serious discussion of the law. … [A legislative body] can no more express its will by not legislating than an individual Member can express his will by not voting.'". The General Assembly's rejection of SB 1275 does not, in our view, reveal a legislative disapproval of the substance of the failed legislation.

S. 51 Dev. Corp. v. Vega, 335 Ill. App. 3d 542, 556 (2002) (citations omitted) (emphasis in original). Thus, the Commission should wholly disregard CUB-AG's reliance on the inaction of the General Assembly with respect to gas utility PORCB programs.

B. The Commission Should Reject Staff's Recommended Changes to Rider 17.

1. Administrative and Operational Costs

Staff states that it "continues to take issue with the 8% overhead factor for Administrative and Operational Costs ("AOCs")" as unsupported by data. Staff Init. Br. at 14. Nicor Gas presented evidence demonstrating that the 8.0% factor is completely different than the AOCs defined in Rider 17. Mudra Sur., Nicor Gas Ex. 3.0, 4:67-77. Sheet 75.9.3 of Rider 17 sets forth the definition for AOCs, which does not include any reference to an "overhead factor." Nicor Gas Ex. 2.2. The Company explained in discovery that the 8.0% overhead factor referenced by Staff was included in the Company's preliminary Information Technology ("IT") design estimate of $3.88 million. Nicor Gas Ex. 3.1 (explaining that the 8.0% was the standard corporate

overhead rate for AGL Resources Inc.'s information technology projects at the time the estimate was prepared). Thus, the AOCs must be considered separate and apart from the 8.0% overhead factor used by Nicor Gas in its estimate of the start-up costs to implement changes required by the PORCB program. To the extent that Staff is dissatisfied with Nicor Gas' data provided in support of the 8.0% factor relating to its IT design estimate, that simply has no bearing on whether the Company has provided sufficient information in support of its proposed mechanism to recover its actual start-up costs.

2. Capital Recovery Costs

Staff maintains that the definition of Capital Recovery Costs ("CRC") should be limited to costs necessary for implementing the program, including incremental costs incurred through one year following the commencement of service, and eliminating the recovery of future system modifications required to maintain IT system integrity and functionality related to the provisions of the PORCB program. Staff Init. Br. at 16-17.

Rider 17 defines CRC as "the revenue requirement necessary to recover the Company's investment in information technology systems necessary for the PORCB Program." Nicor Gas Ex. 2.2, Sheet No. 75.9.3. Subsection (d) of the definition specifically includes future system modifications required to maintain information technology system integrity and functionality. *Id*. This approach insures that the appropriate cost causers (Q-AGS) pay for all of the capital costs required to install and maintain the PORCB system on an ongoing basis. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 14:318-24.

Moreover, the evidence demonstrates that the Company will develop separate IT functionality for the PORCB program. Mudra Sur., Nicor Gas Ex. 3.0, 5:81-86. The Company would only seek to recover system modification costs if required to maintain Information Technology system integrity and functionality related to the PORCB program as explicitly

provided for on 75.9.3. *Id*. The costs at issue do not relate to the Company's existing IT system, but only to costs that would be required for the PORCB Program. *Id*.

If the Company were to ignore the future IT system modification costs, as Staff suggests, presumably Staff would have the Company recover any remaining net investment in plant and a return through a subsequent rate case. This approach has two significant disadvantages: (1) the revenue requirement for the additional investments would not be tracked or charged to the appropriate customer classes (Q-AGS) but rather to all other customers, thereby creating cross subsidies; and (2) due to the infrequent timing of rate cases, the Company would never recover its return on and of capital from the date of the system modification until the next rate case. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 15:327-35. Furthermore, "if it is determined at a later date to include [Percentage of Income Payment Plan] customers in the PORCB program, Nicor Gas would seek to recover its Capital Recovery Costs for the Company's investment in necessary system changes in the same fashion[.]" Mudra Dir., Nicor Gas Ex. 1.0, 8:182-85. Accordingly, the Commission should not adopt Staff's proposed changes to the definition of CRC because it does not improve Rider 17 from a rate design, cost recovery or equity perspective between customer classes.

3. Supply Uncollectible Adjustment

Staff recommends numerous changes to the definition of the Supply Uncollectible Adjustment component of the PORA. Staff Init. Br. at 19-21. Staff's proposal utilizes a formula based on the difference between the uncollectible rate established in the Company's latest rate case (less the 1.0% factor in the discount rate for uncollectibles) multiplied by the total face amount of Receivables purchased from the Q-AGS. Ebrey Dir., Staff Ex. 2.0, 14:305-08. Staff contends that its proposal is less complicated than the Company's proposal. Staff Init. Br. at 21. The Commission should not adopt Staff's SUA formula because the evidence demonstrates that

the Company's proposed rate design formulas are designed to address the complexities and business process changes necessary for Nicor Gas to provide a new service to purchase annually millions of dollars of third-party receivables. Mudra Sur., Nicor Gas Ex. 3.0, 5:90-95.

The Company also identified numerous reasons why Staff's proposal will impede the timely and accurate recovery of the Company's cost to provide the PORCB service. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 16:364-66. First, in the Company's last rate case (Docket No. 08-0363, Order at 31 (Mar. 25, 2009)), the Commission approved an uncollectible rate representing an overall average level of uncollectibles as a percentage of gross revenues for all customer classes of 2.02%. This rate does not reflect the residential class individually or the non-residential class individually. Nicor Gas' proposal to estimate and adjust the $PORA_C$ on a monthly basis for each respective customer class based on actual experience is more precise and equitable for each customer class. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 16:367-17:373.

Second, the Company's proposal uses forward looking estimates, which are more appropriate than historical data points to establish the more accurate and relevant charges for each effective future month of PORCB service. *Id*. at 17:376-78. Furthermore, the Company will monitor its estimates with actual experience on a monthly basis and subsequently adjust the monthly charges based on changing market conditions. *Id*. at 17:378-80.

Third, Nicor Gas' proposal is superior to Staff's approach, which sets an artificial historical cap on SUA recoveries until the two-year reconciliation process is complete. *Id*. at 17:381-83. Staff's method therefore creates additional financial risk to Nicor Gas in the event of rising gas prices, economic downturns, or changing uncollectible rates within the Q-AGS pools, all of which would cause Nicor Gas to be significantly undercollected until the end of its two-year reconciliation process. *Id*. at 17:383-86.

Fourth, Staff's method does not account for actual customer payment experience on a monthly basis as Nicor Gas' proposal does; instead, Staff's proposal utilizes a fixed uncollectible rate of 2.02 % established in 2009. *Id*. at 17:387-91. Finally, Nicor Gas worked with RESA and IGS to develop a structure for Rider 17 that considers the risks and rewards of the PORCB program. Because this is a voluntary program, Nicor Gas is not willing to accept additional financial risks or the uncertainty associated with Staff's proposed SUA formula. Simply put, Staff's formula does not improve upon the proposed rate design or effectiveness of Rider 17. *Id*. at 17:392-18:396.

4. Tracking of Internal IT Costs

Staff argues that the Company should be required to track internal IT employee time that will be capitalized and included in the five-year levelized revenue requirement for the total costs and provide quarterly reports of such costs. Staff Init. Br. at 22-23. Contrary to Staff's assertions about the Company's alleged silence on the point, Nicor Gas presented evidence that the IT programming will be incremental capitalized work; therefore, 100% of the cost should be included for cost recovery. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 19:431-36. Accordingly, the Company should not be required to verify that the internal costs are "incremental" and not otherwise included in recovery under any other tariffs currently in effect.

C. The Commission Should Reject CUB-AG's Recommended Changes to the Tariff Design.

1. Separate Line Item for PORCB Charges

Nicor Gas's Rider 17 proposal provides that the Purchase of Receivables Adjustment ("PORA") would be added to or subtracted from the Monthly Customer Charge along with the Rider 1 "Customer Charge Adjustments." The Customer Charge Adjustments include (a) Energy Assistance Charges for the Supplemental Low-Income Energy Assistance Fund, (b)

Renewable Energy Resources and Coal Technology Development Assistance Charge, and (c) the Rider 26 monthly customer charge adjustments for uncollectible costs. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 36:813-37:818. These adjustments, including the proposed PORA, are not displayed as separate line items on the bill but rather are included in the monthly customer charge. *Id*. at 37:821-22. The evidence demonstrates that a separate line item on the bill for PORA charges and credits, as proposed by CUB-AG (Init. Br. at 20), would not be more beneficial to customers.

As an initial matter, presenting the PORA as a separate line item would create confusion for customers because Nicor Gas currently includes its uncollectible costs within the monthly customer charge. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 37:826-28. It also may increase operating costs in situations when the extra line item creates more two-page bills, or through additional customer calls and inquiries. *Id*. at 37:828-30. Moreover, Nicor Gas publishes its rates and tariffs on its website and provides historical monthly rate information so that market participants can review the relevant costs and credits associated with the Customer Select program. *Id*. at 37:831-33. Nicor Gas will publish the Rider 17 charges and credits monthly on its website and will provide the historical charges for both residential and non-residential customers (similar to the manner in which it currently provides history on items such as Rider 6 – Purchased Gas Adjustment and Rider 26 – Uncollectible Expenses). *Id*. at 37:833-37. Thus, all participants in the competitive marketplace will be able to readily access this information.

2. Price Caps on Monthly PORCB Customer Charges

The Commission should reject CUB-AG's proposal (Corr. Init. Br. at 21-22) to place price caps on the monthly PORCB-related charges because it is based upon a subjective and complicated three-part financial limit. Specifically, CUB-AG's recommendation would require Nicor Gas to (1) calculate a PORA that will be 1.0% of the customer's supply charges, (2) bill

the customer no more than the lesser of 1.0% or a fixed price cap of $0.50 per residential customer and $2.00 per commercial customer, and (3) bill the Q-AGS any remaining expenses. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 38:846-50. The variable per customer price caps proposed by CUB-AG would create operational complexities that are far greater than Nicor Gas had envisioned for itself and its customers in designing the PORCB tariff. *Id*. at 38:850-52. Even if the operational requirements of this recommendation could be implemented, they would introduce significant new billing and computing issues which may delay customer bills and collections, complicate the AGS pool billing process, and significantly increase administrative costs as compared to Nicor Gas' Rider 17 proposal. *Id*. at 38:852-56. Thus, the limits proposed by CUB-AG would add significant computational and billing complexities and would jeopardize the efficient recovery of costs, thereby creating terms that are not commercially acceptable to Nicor Gas.

The evidentiary record demonstrates numerous other reasons to reject CUB-AG's proposal. First, CUB-AG's recommendation ignores the symmetrical nature of Nicor Gas' proposal and arbitrarily caps charges to customers, but does not cap the credits that may be provided to consumers; this makes Rider 17 unrealistically difficult to implement from a business perspective. *Id*. at 38:859-39:865.

Second, CUB-AG's recommendation is based on a premise that there is an intra-class cross subsidy within the residential and commercial customer classes. *Id*. at 39:866-68. However, Rider 17 appropriately allocates costs (*e.g.*, actual uncollectible expenses charged off) directly to the customer class causing the cost (*e.g.*, residential and non-residential) and then recovers the cost on an equal cost per customer basis, which is included in the monthly customer

charge. The Company's approach is consistent with Commission Orders in Docket Nos. 08-0363 and 09-0428. *Id*. at 39:878-82.

Third, CUB-AG's recommendation fails to account for the fact that Q-AGS are already able to design their products and service offerings in a uniquely tailored fashion to small volume and large volume customers because Q-AGS prices charged on a monthly basis are not regulated by the Commission. *Id*. at 40:893-96. Indeed, Q-AGS may make any adjustments in their prices necessary on a monthly basis. *Id*. at 40:896-97.

Finally, CUB-AG's position fails to consider that the competitive retail natural gas industry may significantly change in the future. Municipalities are now aggregating electrical load in the service territory of Commonwealth Edison Company, with Retail Electric Suppliers providing approximately two-thirds of their supply. *Id*. at 41:909-11. Future natural gas prices may be high or low and future economic conditions may dramatically increase (or decrease) uncollectibles. *Id*. at 41:911-12. While Nicor Gas' Customer Select program now serves about 13% of the small volume market, it could dramatically grow or shrink under future legislative or regulatory changes. *Id*. at 41:913-15. Nicor Gas' proposed rate design for Rider 17 will appropriately recover costs under these changing business and economic conditions and the Commission should not modify the rate design to introduce arbitrary pricing limitations that increase risk and administrative complexity.

3. AOC Cost Assignment

Nicor Gas' proposed tariff design recovers AOCs directly from Q-AGS through the Discount Factor to the extent that the Discount Factor is high enough to cover the future expenses. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 41:923-25. If the Discount Factor is not adequate to recover the monthly expenses, then a PORA adjustment, which includes the AOCs, is placed on the customer's bill to recover the difference. *Id*. at 41:925-27. Thus, Rider 17

allocates costs to the appropriate cost causers (Q-AGS and their customers). Likewise, if the Discount Factor is too high, the PORA adjustment will provide credits to customers with the objective of recovering actual costs incurred over the course of the program and through the Commission reconciliation process. *Id*. at 41:927-42:930. In addition, the initial terms and structure of Rider 17 were acceptable to the marketplace as represented by RESA and IGS. All costs of service, including profit, must eventually be included in the end-use customer's bill if a Q-AGS is to be a going concern. *Id*. at 42:934-37. Because the evidence demonstrates that there is nothing inappropriate about recovering the AOCs as proposed in Rider 17, the Commission should reject CUB-AG's proposal to recover the AOCs directly from Q-AGS as a component of the Discount Factor. CUB-AG Corr. Init. Br. at 22-23.

4. Allocation of Costs by Customer Class and Volume

Nicor Gas modified Rider 17 to calculate AOC_C by customer class by including both a common cost per customer component (*e.g.*, for the general administrative labor) plus a class cost per customer component (*e.g.*, for the direct collection agency costs by class). Mudra Reb., Nicor Gas Ex. 2.0 Rev., 44:978-81. The modified proposal reflects Nicor Gas' expectation that AOCs largely would be "common" costs that would be required to administer the program for both residential and non-residential customers (*e.g.*, labor to administer the program and answer Q-AGS and customer questions). *Id*. at 43:973-44:976. It also reflects Nicor Gas' expectation to pay commissions to collection agencies as part of its AOCs, which the Company can allocate to the customer class for which such commissions were paid. *Id*. at 44:976-78. Nicor Gas' modified proposal is consistent with the tariff design intended to ensure that each customer class ultimately pays the appropriate costs caused by that class.

Moreover, PORA costs should not be allocated on a volumetric basis as CUB-AG suggest (CUB-AG Corr. Init. Br. at 22), as that allocation methodology is not superior to Nicor

Gas' proposal to collect bad debt expenses (uncollectible expense) as a "customer" cost included within the monthly customer charge. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 44:985-87. Under Nicor Gas' proposal, costs are first incurred and then tracked by customer class where possible. *Id*. at 42:945-46. The direct costs of residential uncollectibles are recorded directly in the residential customer class and the direct costs of non-residential uncollectibles are recorded directly in the non-residential class. *Id*. at 42:946-48. The common costs of administering the program for both residential and non-residential customers included in the AOCs (*e.g.*, company labor) are recorded and recovered on a per customer basis from all customers. *Id*. at 42:948-50. Recovering these costs on a volumetric basis assumes that higher volume customers cause a greater proportion of the AOCs. However, administrative costs are not likely to be primarily spent on the larger customers; instead, they can be fairly recovered from all customers. *Id*. at 42:951-43:954. Finally, use of a volumetric billing determinant assumption within the tariff design introduces more uncertainty and error because weather and monthly gas volumes change considerably each month and each year making cost/therm charges harder to estimate and collect than cost/customer charges, which are more stable. *Id*. at 43:958-62. Therefore, for all these reasons, the Commission should reject a volumetric rate design for Rider 17 AOCs.

5. Separate Uncollectible Rates for Each Q-AGS

The Commission should reject CUB-AG's proposal to set the uncollectibles portion of the Discount Factor separately for each Q-AGS based on the uncollectibles history of their receivables. CUB-AG Corr. Init. Br. at 24-27. That is because the evidence demonstrates that Rider 17 is properly designed with a uniform discount rate for all suppliers and PORA adjustments based on forward looking rather than historical data. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 46:1027-28. Due to the dynamic nature of the natural gas industry (changing gas prices, weather, competition, municipal aggregation, and other factors) Nicor Gas should not be

required to establish discount rates based on historical information. *Id*. at 46:1028-31. CUB-AG's recommendation also would significantly increase administrative, IT programming, and maintenance costs as compared to Nicor Gas' proposed design. It would require Nicor Gas to segregate receivables by supplier and, by relying on historical information, would not provide Nicor Gas with a timely or efficient cost recovery mechanism. *Id*. at 46:1031-35. In short, it would lead to a burdensome administrative process at higher costs with the potential for more errors and questionable benefit.

Moreover, Nicor Gas' Rider 17 proposal builds in consumer and Q-AGS protections. Only Qualifying Receivables (Q-RECc) by customer class will be purchased by Nicor Gas. *Id*. at 45:1012-13. As explained in the tariff, Qualifying Receivables means that "such receivables have arisen from providing gas supply to Customer Select Participants who were, at the time immediately prior to entering the program, or during the prior billing period, not in arrears with either the Company or the Q-AGS." *See* Nicor Gas Ex. 2.2 at Sheet 75.9.5. This means that Q-AGS will not be able to bring older, difficult to collect, bad debt into the PORCB program. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 45:1017-18. Q-AGS will be incentivized to look for customers with good credit and the ability to pay because otherwise Q-AGS will be dealing with the customer's future uncollectibles. *Id*. at 45:1018-20. Nicor Gas will purchase every receivable (those in good credit standing and those that are not) but only if the customer was previously in good credit standing with both the Company and the Q-AGS. *Id*. at 45:1020-46:1022.

6. Intangible Cost Recovery

Staff and CUB-AG argue against the Company's recovery of intangible costs through Rider 17. Staff Init. Br. at 9-13; CUB-AG Corr. Init. Br. at 20-21. The evidence demonstrates that intangible cost recovery should be permitted for the following reasons: (1) it was part of the

settlement agreement with RESA and IGS wherein the commercial terms of Nicor Gas' proposed Rider 17 were deemed to be acceptable to both the industry participants and the Company and properly identified that Nicor Gas would incur additional costs associated with the program; (2) it provides an incentive for Nicor Gas to keep its PORCB administration costs down; and (3) it encourages innovation in areas where utilities may further support the growth and development of unregulated retail energy markets. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 47:1059-65; Nicor Gas Ex. 2.10; Mudra Sur., Nicor Gas Ex. 3.0, 3:54-4:66; Nicor Gas Init. Br. at 15-16.

Moreover, the intangible cost recovery component of Rider 17 is an important component of the risk/reward structure developed with RESA and IGS. Without this component, Nicor Gas' earnings opportunity on PORCB is limited by the assumption that it will be able to recover its capital investment and required return through sufficient participation in the PORCB program via the Discount Factor or by the assumption that sufficient Q-AGS remain in the program for it to recover any outstanding amounts due through the Capital Recovery Adjustment component. Mudra Reb., Nicor Gas Ex. 2.0 Rev., 48:1075-81. If Q-AGS elect to opt out of the program, Nicor Gas may never recover its initial $3.88 million investment in the program. Due to the concentrated nature of recovering capital costs and return from a limited number of Q-AGS, their customers, and an optional program, the intangible cost recovery component represents a reasonable level of compensation necessary to recover other costs associated with the PORCB program and provide enough incentive for Nicor Gas to agree to participate in such a program. *Id.* at 48:1081-87.

In addition, the purchase of third-party receivables is, in character, a non-utility service that will give rise to intangible costs which are appropriately accounted for "below-the-line," consistent with Account 417, Revenues from Non-Utility Operations. Nicor Gas Ex. 2.2 Sheet

75.9.4; Mudra Sur., Nicor Gas Ex. 3.0, 10:211-13. Below-the-line treatment for intangible cost recovery properly recognizes the non-utility nature of this service (receivables factoring) and its risk while providing Nicor Gas with some opportunity to recover its intangible costs associated with providing the proposed PORCB service. Mudra Sur., Nicor Gas Ex. 3.0, 11:231-35.

7. Below-the-Line Treatment for Intangible Cost Recovery

CUB-AG argue that below-the-line treatment of intangible cost recovery would permit Nicor Gas to earn more than its authorized return. CUB-AG Corr. Init. Br. at 27-28. The Commission should reject CUB-AG's argument as the evidence demonstrates that below-the-line treatment of intangible cost recovery is appropriate.

The purchase of third-party receivables is, in character, a non-utility service that will give rise to intangible costs which are appropriately accounted for "below-the-line," consistent with Account 417, Revenues from Non-Utility Operations. Nicor Gas Ex. 2.2 Sheet 75.9.4; Mudra Sur., Nicor Gas Ex. 3.0, 10:211-13. The Company would only receive $438,609 of return on equity under Rider 17 (Nicor Gas Ex. 2.6, p. 1, sum of ROE column for years 1-5); however, it would incur intangible costs and financial risks associated with purchasing as much as $181,000,000, or significantly more, of receivables. Mudra Sur., Nicor Gas Ex. 3.0, 10:213-17. Therefore, Rider 17 includes an incentive to recover its intangible costs of only up to 0.5% of Q-REC annually if, and only if, Nicor Gas can keep its AOCs at or below 1.0% of Q-REC. Mudra Sur., Nicor Gas Ex. 3.0, 10:217-19. The 1.0% of Q-REC could be approximately $1,000,000 per year (before taxes) if 100% of the current AGS in the Customer Select program elected to participate in the Rider 17 with all of their residential and commercial customer classes. Nicor Gas Ex. 2.10. However, after ten years of full unbundling, only about 13% of Nicor Gas eligible residential and small commercial customers currently participate in Customer Select. Mudra Sur., Nicor Gas Ex. 3.0, 10:222-11:224.

Due to the optional nature of the purchase of receivables service that would be offered to Q-AGS, and the attendant risks and uncertainty of future intangible cost recovery and full cost recovery under Rider 17, recording the intangible cost recovery revenues below-the-line in Account 417, Revenues from Non-Utility Operations is appropriate. *Id*. at 11:225-28. By definition, below-the-line revenues are not included in the net operating income of the utility for ratemaking purposes, so it is impossible for these uncertain potential future intangible cost recovery revenues to cause Nicor Gas to over-earn on its utility rate base. *Id*. at 11:228-30. Below-the-line treatment for intangible cost recovery properly recognizes the non-utility nature of this service (receivables factoring) and its risk while providing Nicor Gas with some opportunity to recover its intangible costs associated with providing the proposed PORCB service. *Id*. at 11:231-35.

III. CONCLUSION

For the above reasons and those set forth in its Initial Brief, Nicor Gas respectfully requests that this Commission enter an Order: (1) consenting to and approving Nicor Gas' proposed Rider 17 as proposed and modified by Nicor Gas in this proceeding in Nicor Gas Exhibit 2.2; and (2) granting such further and additional relief as may be necessary.

Dated: May 24, 2013

Respectfully submitted,

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

By: /s/ Anne W. Mitchell

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