

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

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| NORTH SHORE GAS COMPANY |) | |
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| Proposed General Increase In Rates For |) | |
| Gas Service |) | 12-0511 |
| |) | |
| |) | (Cons.) |
| THE PEOPLE GAS LIGHT AND COKE COMPANY |) | |
| |) | 12-0512 |
| Proposed General Rate Increase In Rates For |) | |
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**REPLY BRIEF ON REHEARING
OF THE CITIZENS UTILITY BOARD
AND THE CITY OF CHICAGO**

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NOW COME the Citizens Utility Board (“CUB”), through its attorneys, and the City of Chicago by Stephen Patton, Corporation Counsel, (“City”, jointly, “CUB-City”), pursuant to section 200.800 of the Rules of Practice of the Illinois Commerce Commission (the “Commission” or “ICC”), (“Rules”), 83 Ill. Admin. Code § 200.800, to file their Reply Brief on Rehearing in the above-captioned proceeding.

I. INTRODUCTION

The Companies¹ raise two issues in their Initial Brief on Rehearing. First, they discuss the appropriate calculation of the net operating loss (“NOL”), assuming it is included in rate base. Second, they discuss the CUB-City and Illinois Attorney General (“AG”) arguments on the appropriateness of the NOL inclusion in rate base. CUB-City do not take issue with the calculations set forth by NS-PGL and ICC Staff. However, the threshold question of whether the 2012 NOLs should be included in rate base for ratemaking purposes must first be answered. The Companies misstate that issue, arguing: “The record demonstrates that a 2012 NOL exists.

¹ North Shore Gas Company and The Peoples Gas Light and Coke Company, collectively “NS-PGL,” the “Utilities,” or “the Companies.”

Further, there is no argument that if an NOL exists, it does not belong in rate base.” NS-PGL Init. Br. on Reh’g at 2 (emphasis added). Though the statement is ambiguous, either meaning is simply untrue. The argument that the 2012 NOL does not belong in rate base plainly was raised. CUB-City and AG argued against including the 2012 NOL in their Applications for Rehearing and discussed it in the CUB-City and AG Initial Briefs on Rehearing. CUB-City App. for Reh’g at 7; AG App. for Reh’g at 10; CUB-City Init. Br. on Reh’g at 8-9; AG Init. Br. on Reh’g at 11-12. The existence of the 2012 NOL was not at issue, but (contrary to NS-PGL’s assertion) though the NOL exists, it *should not be included in rate base*, for several reasons discussed below and in prior briefs. The issue the Commission must decide is this: Should the 2012 NOL be included in the Companies’ rate base for ratemaking purposes? CUB-City, the AG and Staff have shown that it should not.

II. ARGUMENT

A. Inadequate Explanation of Change in Position

The Companies continue to claim that new information came to light when their parent, Integrys, closed its books in January 2013, which information caused their change of position to claim the stand-alone 2012 NOLs. NS-PGL Init. Br. on Rehearing at 11. The Companies knew of and provided evidence about the standalone NOLs in their initial filing on July 31, 2012, in data request responses on October 23 and November 15, 2012, and in testimony on December 18, 2012. *See* NS-PGL Init. Br. on Rehearing at 7-9. They admit that “[t]he evidence demonstrates that the Utilities’ stand-alone 2012 NOLs existed from the time of the Utilities’ direct filing on July 31, 2012, but that it was assumed they would be absorbed, subject to monitoring and updating.” NS-PGL Init. Br. on Reh’g at 11. The Companies acknowledged that the assumptions contained in their financial forecasts -- specifically, in Schedule G-5 for each

utility (which first reported the 2012 NOL) -- were based on those management assumptions. NS Ex. 5.1, Schedule G-5, p. 1; PGL Ex. 5.1, Schedule G-5, p. 1 (“This financial forecast presents, to the best of management’s knowledge and belief, the Company’s expected financial position... for the forecast period. Accordingly, the forecast reflects its judgment as of December 15, 2011... The assumptions disclosed herein are those that management believes are significant to the forecast.”).

For more than a full year thereafter, those management assumptions about how the NOL would be used (i.e. that it would be absorbed by Integrys) were not changed, and they were the basis of the Companies’ filed testimony before this Commission. Predictably, that management position (presented in testimony by the Companies) was relied upon by all other parties in the case. In Rebuttal testimony on December 18, 2012 -- less than two weeks before the year-end closing of books, the Companies continued to testify that “no deferred tax asset exists at the end of 2012 due to the consolidated groups [sic] income.” NS-PGL Ex. 30.0 Rev., 27:651-652.

By claiming that they first “found out” (NS-PGL Init. Br. on Reh’g at 9) in 2013 that the consolidated group could not absorb the 2012 NOLs, the Companies concede that their management assumptions, which they maintained for over a year, turned out to be incorrect. While the Companies imply that their change in position on the 2012 NOLs was no more than a function of their tax sharing arrangement with Integrys, the passive language they use to describe their change in position is curious. For example, they say that it was not until the Integrys books closed for the year that they “found out” Integrys could not absorb the Utilities’ standalone 2012 NOLs. *Id.* They argue that “upon learning” of that fact, they updated their evidence at the first opportunity, in surrebuttal. *Id.* at 13. They argue implicitly that they had no indication less than two weeks before the end of the year that the consolidated group’s tax position might change,

and that they had no obligation to disclose any increased chance of claiming an NOL to the Commission or to other parties. To allow the Companies then to adjust their revenue requirement to recognize a reversal of that assumption after other parties' testimony was complete is patently unfair to ratepayers. That prejudice is not cured by giving the Companies another opportunity (on rehearing) to bolster a position its testimony in the original proceeding could not support.

First, the Companies still have not provided an adequate explanation of why their assumption, maintained for over a year (including through two data request responses and testimony), was incorrect. They do not even address the improbability that NS-PGL's or Integrys' accountants did not recognize any change in accounting circumstances (of the magnitude necessary for the NOLs to become useless to Integrys) two weeks before year-end. They simply state that things changed, and expect the Commission to allow them to update their revenue requirement accordingly. *See* NS-PGL Init. Br. on Reh'g at 11. That bald statement does not meet the necessary burden of proof to establish that the cost of the Companies' including the 2012 NOLs in their own rate bases was prudently incurred and the rates set are just and reasonable.

Second, the Companies claim that other revenue requirement reducing adjustments were made in January 2013, and that CUB-City and the AG only contest this adjustment because it increases rate base. Though that would be a convenient explanation, it is simply not true. The Companies point specifically to the CUB-City and AG proposal to include the impacts of the 2013 bonus depreciation, based on the enactment of the American Taxpayer Relief Act of 2012. NS-PGL Init. Br. on Reh'g at 11. As the Companies acknowledge in that statement, that particular adjustment is appropriate because a *new law* was passed, which affected the

Companies' rate base. No new law affected the Companies' 2012 NOLs. No new facts at all have been presented, other than that management apparently did a poor job in their financial forecasts, failed to recognize an impending multi-million dollar change in tax position two weeks before year-end, and failed to report a potential material revenue requirement change, despite the Commission's test year update rules intended to assure due process to other parties. *See* 83 Ill. Adm. Code 287.30. The Companies have not provided an adequate basis for reversing the assumptions on which intervenors relied for almost the entirety of the case.

In actuality, it is the Companies who are guilty of a self-interested change in position. Just as the Companies suggest that intervenors were motivated to decrease the revenue requirement, management decisions driving the Companies' change in position in January 2013 regarding the allocation of the 2012 NOLs likely were influenced by the revenue requirement impacts of that decision; *i.e. increasing* rate base. In the end, the Commission must review the evidence in light of the legal standards, and should not be held hostage to the Utilities change in position, simply because they indicated there was a remote chance that position would change.

B. The Companies' Change in Position Places an Undue Burden on Ratepayers

Allowing the Companies to make such a significant change to their assumptions at the last possible opportunity, in surrebuttal testimony, places an impossible burden on ratepayer parties to respond meaningfully. The evidentiary hearing began on February 5, 2013, just seven business days after the Companies filed their surrebuttal testimony where they first claimed the NOLs should be included in the Companies' rate bases. Intervenors had no opportunity to present evidence in their direct or rebuttal testimony on the Companies' use of the 2012 NOLs in their rate bases, given that the management decision communicated to parties during all rounds of Staff and Intervenor testimony was that the 2012 NOLs would be absorbed by Integrys.

Furthermore, the Commission has established rules that require consideration of other parties' opportunity to respond in determining whether to allow updates of test year data. 83 Ill. Admin. Code 287.30 ("A determination to . . . allow the submission of an update shall include . . . consideration of: . . . 3) Whether the Illinois Commerce Commission staff and other participants will have an adequate opportunity to review the updated information"). The Commission's rules also require that its discretion be exercised to recognize parties' rights to due process and to avoid the prejudicial result the Companies insist on here. 83 Ill. Adm. Code 200.25(c) ("Fairness – Persons appearing in and affected by Commission proceedings must be treated fairly. To this end, parties which do not act diligently and in good faith shall be treated in such a manner as to negate any disadvantage or prejudice experienced by other parties"). To allow the Companies' last minute change, the Commission must disregard its own rules.

If utilities are allowed to make last minute changes based on the reversal of an internal management decision (like the NOL change the Companies offer in this case), other parties will be placed in an impossible position of rebutting the inclusion of costs incurred on the basis of last-minute decisions without the full benefit of additional discovery, and the Commission's rules will lose their substantive meaning. The Commission should hold the Companies to the only position they held when the other parties had an opportunity to respond meaningfully. To allow any other position is unfair to all other parties in the case.

C. Burden of Proof

In rate cases, the Companies bear the burden of proof to establish the justness and reasonableness of their proposed rates. 220 ILCS 5/9-201(c). The Companies did not meet their burden, in the original case or on Rehearing, and so would prefer to shift it to other parties. By questioning the actions of CUB-City and the AG, the Companies imply that it was up to those

parties (a) to demonstrate that the Companies' assumptions from Direct through Rebuttal testimony were not appropriate or (b) to anticipate a change in the consolidated group's tax status or management decisions by the Companies and Integrys.² The implication is baseless. Utilities have the burden of proving the prudence and reasonableness of costs used to set rates, and they must comply with rules of evidence and procedure (especially those assuring due process) as they do so.

In several places, the Companies inappropriately attempt to divert attention from the true issues and shift the burden of proof on the underlying issue to intervenors. For example, they ask, "[i]f CUB-City had concerns regarding the tax sharing agreement between the Utilities and their parent and the application of the 2012 NOLs, why did they not raise those concerns in direct and rebuttal testimony?" NS-PGL Init. Br. on Reh'g at 13. This question feigns ignorance as to why intervenors would not devote scarce time and resources to what the Companies themselves asserted was a non-issue. In at least 4 pieces of evidence – a schedule, two data request responses, and testimony (NS-PGL Init. Br. on Reh'g at 7-9) –the Companies stated that they were forecasting standalone 2012 NOLs that would be absorbed by the consolidated group. CUB-City did not reject and investigate these repeated assurances, which were made over the course of nearly five months (July 31 through December 18). CUB-City cannot expend already-limited time and resources to question a facially reasonable assumption of the Companies, about which parties were repeatedly assured. The Companies' argument that CUB-City should have anticipated that the Companies would reverse course in surrebuttal, despite unrebutted, consistent testimony from the Companies that the NOLs were not an issue is an obvious and

² There is little doubt that the extensive discovery of the finances and tax positions of the Companies' affiliates required to make such an assessment would be opposed.

desperate attempt to distract from the fact that the Companies' actions prejudiced other parties in this case.

The Companies further complain that Staff's proposal for the Companies to provide "a full quantification of the impact of its position on all pending adjustments" is "unworkable in the time constraints of testimony and the norm in Commission practice." NS-PGL Init. Br. on Reh'g at 4-5. The Companies claim it is impossible that they, with their extensive resources, could comply with Staff's proposal, while simultaneously suggesting that intervenors were responsible for doing just that, to evaluate the reasonableness of the Companies' NOL assumption. Under the PUA, the Commission cannot shift the burden of proof to any other party. The burden of proof "in whole and in part, shall be upon the utility." 220 ILCS 5/9-201(c).

D. Intervenor Testimony on Rehearing

The Companies point out that CUB-City did not file testimony in this rehearing, as if that is somehow evidence of the propriety of including the 2012 NOLs in the Companies' rate base. That claim fails for several reasons. As discussed above, that shifts the burden of proof inappropriately. If a utility does not meet its burden of proof that a particular challenged cost is prudent and reasonable, as well as lawful, then the Commission cannot base rates on that claim – regardless of whether any other party provides testimony. Of course, in this case, CUB-City, the AG and Staff all provided ample demonstrations that the 2012 NOLs should not be included in rate base. Staff and Intervenor concerns about a utility's proposed rates are not limited to only those issues on which they provide expert testimony – particularly in the case of legal issues, such as this.

The Companies improperly suggest that "if CUB-City had questions concerning the tax sharing agreement with Integrys or why the Utilities were not using the 2012 NOLs for

themselves, they should have raised those concerns in either direct or rebuttal testimony.” NS-PGL Init. Br. on Reh’g at 10. The Companies are wrong for two important reasons. First, CUB-City’s decision not to provide testimony respecting a legal issue has no evidentiary significance. As intervenors of record, parties like CUB and the City may file briefs providing an analysis of the record evidence as it applies to the relevant and controlling law, all without ever sponsoring a single witness. Second, CUB-City, the AG and Staff all raised the issue in briefs, which gave the Companies ample notice of their concerns. The CUB-City Application for Rehearing requested that the Commission reconsider its decision on the adequacy of the Companies’ evidence and procedural fairness regarding the 2012 NOLs and that the Commission correct misstatements made in the Final Order. CUB-City App. for Reh’g at 7. The Commission granted that request, and CUB-City have chosen (appropriately) to address the issue in briefs rather than in testimony.

E. Alleged Tax Normalization Violation

The Companies repeat their claims that failure to reflect the 2012 NOLs in their rate bases in this proceeding will lead to a tax normalization violation that will cause the Utilities to lose their ability to claim accelerated depreciation. NS-PGL Init. Br. on Reh’g at 13-17. This claim was addressed in the CUB-City Initial Brief on Rehearing at p.9, and CUB-City will not repeat those arguments here. For the reasons contained in the CUB-City, AG and Staff Initial Briefs on Rehearing (at 9, 9-10 and 6-7, respectively), the Commission should reject the Companies’ unsupported threats of what supposedly could happen if the 2012 NOLs are not included in rate base. Bald references to what could conceivably happen, which do not represent PGL/NS’s actual, historical experience, provide insufficient bases on which the Commission can conclude that the Utilities have met their burden of proof on this issue. The Utilities’ attempt to

bully the Commission into ignoring the burden of proof and the inappropriateness of this late adjustment should be given no weight in this rehearing.

In a final effort to compel the Commission to include the 2012 NOLs in rate base, the Companies imply that the Commission lacks discretion to review utility NOL costs under the otherwise applicable standards of the PUA, because the utility's tax decisions are exempt from such review. *See* NS-PGL Init. Br. on Reh'g at 14-17. However, the Companies have not identified any definitive, controlling law that requires that their tax planning decisions control Commission rate making. That is, the Companies do not cite a specific legal requirement that the Commission is bound to adopt, for ratemaking purposes, the Companies' last-minute decision to use the 2012 NOLs for tax purposes. If the Companies believe that this issue is outside of the Commission's jurisdiction, as a result of supposed tax implications of the decision, they have not met their burden to demonstrate that. The Commission has jurisdiction to decide this issue on the same legal standards as used for any other adjustment. Consequently, the Companies should not be permitted to nullify their failure of proof under the PUA with an internal tax planning decision, to produce rates based on costs that have not been shown to be prudently incurred and reasonable.

Staff's Initial Brief on Rehearing (at 3-4) demonstrates that the miscalculations in the Final Order which gave rise to the Companies' supposed concern about a normalization violation are a consequence of the Company's late and inadequate presentation of the 2012 NOLs. Beyond just prejudicing ratepayer advocates in this proceeding, the Companies' last-minute reversal of their previous assumption regarding the 2012 NOLs burdened the Commission and (so they say) threatened to harm the Companies themselves. It is simply unbelievable that this significant assumption was reversed in the month between their rebuttal and surrebuttal

testimonies, or that the Companies did not at least know that it was a probability. If there were a concern about a normalization violation, it was the Companies' choice to make the 2012 NOL change, at the last possible opportunity, that is the cause.

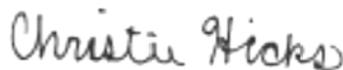
III. CONCLUSION

WHEREFORE, for the reasons discussed herein and in the Initial Brief on Rehearing, CUB and the City respectfully request that the Commission revise its conclusions on the issue of the 2012 NOL and disallow it from the Utilities' rate base.

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Respectfully Submitted,

THE CITIZENS UTILITY BOARD



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