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BEFORE THE
ILLINOIS COMMERCE COMMISSION

PUBLIC UTILITY PREBENCH AGENDA

Chicago, Illinois
Tuesday, January 5, 2010

Met, pursuant to notice, at 1:30 p.m. in
the Main Hearing Room, Eighth Floor, 160 North
LaSalle Street, Chicago, Illinois.

PRESENT:

CHARLES BOX, Chairman

LULA M. FORD, Commissioner

ERIN M. O'CONNELL-DIAZ, Commissioner

SHERMAN J. ELLIOTT, Commissioner

JOHN T. COLGAN, Commissioner

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I N D E X

	<u>FROM</u>	<u>PAGES</u>	<u>TO</u>
<u>PUBLIC UTILITY CASES</u>			
09-0166 & 0167	3		21

1 CHAIRMAN BOX: Pursuant to the provisions of
2 the Illinois Open Meetings Act, I now convene a
3 regularly scheduled bench session of the Illinois
4 Commerce Commission. With me in Chicago are
5 Commissioners Ford, O'Connell-Diaz, Elliott and
6 Colgan. I'm Chairman Box, and we have a quorum.

7 Before moving into the agenda this is
8 the time we allow members of the public to address
9 the Commission. Members of the public wishing to
10 address the Commission must notify the Chief Clerk's
11 Office at least 24 hours prior to the bench session.
12 According to the Chief Clerk's Office, there have
13 been no requests to speak.

14 We have one item on today's agenda,
15 Docket 09-0166 and 09-0167 consolidated. This is the
16 North Shore Company and Peoples Gas Light and Coke
17 Company proposed general increase in natural gas
18 rates.

19 Administrative Law Judges Moran and
20 Haynes, can you please brief us on this matter. And
21 if we're not done at 2:00 o'clock, we'll stop and
22 hear oral arguments on the -- two of the issues in

1 this case will commence at 2:00 p.m.

2 JUDGE HAYNES: Okay. And as you know this is
3 the rate increase requested by Peoples Gas and North
4 Shore. And I just wanted to point out that the
5 actual deadline in this case is Sunday, January 24th,
6 but with the possibility of going on to January 25th.
7 And that the PEPO that we've presented to the
8 Commission doesn't have very many substantive
9 changes, just to the cost of equity.

10 And the order that we've presented to
11 you increases the revenue requirement requested by
12 North Shore by 19.9 percent and Peoples Gas by
13 13.8 percent. And although there's many contested
14 issues here, rather than walking you through each
15 one, just touch on a couple of the bigger issues.

16 And under the Companies' rate base one
17 of the more contested issues is the OPEB liabilities
18 and the adjustment to remove the Companies' pensions
19 asset or liability. And the order that we've
20 presented to you follows the Commission's decision
21 from the last rate case and that was -- as proposed
22 by the AG. And it removes the Peoples Gas's pension

1 asset from the -- their rate base calculations and
2 also removes North Shore's pension liability from the
3 rate base calculation. However, it's -- reduces both
4 Companies' rate bases by their -- for their OPEB
5 liabilities.

6 And under operating expenses one of
7 the more contested issues is Staff's proposed
8 adjustment for the Liberty audit-related expenses.
9 And this issue stems from the Commission's prior
10 order in Docket 06-0311 and Staff's interpretation of
11 language in that order. And the order that we've
12 presented to you does not adopt Staff's adjustment
13 and finds that if hasn't -- it hasn't been shown that
14 the Company has incurred any costs above -- over and
15 above those necessary to comply with the Act.

16 And then the next large heading under
17 it would be the rate of return.

18 JUDGE MORAN: And I'll give a quick overview of
19 the cost of equity, which was one of the most
20 contentious issues in this case.

21 We've got testimony of three
22 witnesses, Staff Witness McNally, CUB-City Witness

1 Thomas and Utilities' Witness Moul. All of these
2 witnesses applied the DCF and the CAPM model.

3 What the proposed order did was it
4 accepted the DCFS bids of both Staff and the
5 Utilities, found them both to be reasonable, and
6 included in the calculation. By finding both to be
7 reasonable that meant that while the accepted -- the
8 DCF analysis that the Utilities' witness set out, it
9 was troubling for Staff's DCF analysis in the fact
10 that spot day was used for those results. We thought
11 by averaging them, it would sort of work out.

12 The CAPM estimate of only Staff is in
13 the PEPO, and I'll explain to you why. Before going
14 into the specifics, there was a lot of testimony
15 coming from two witnesses, Steven Fetter and
16 Mr. Bodmer. These witnesses were more giving you a
17 context for how they thought the Commission should
18 consider the models. And the PEPO adopts some of the
19 proposed language that flushes out a little bit of
20 this background, if you will.

21 Now, neither of these witnesses
22 actually applied the models. CUB-City Witness Bodmer

1 made an assessment, as you will see, of the worst of
2 the financial times that shook this country in fall
3 of 2008. He showed that in contrast to other
4 entities utility companies generally were able to
5 hold their own during the height of the financial
6 turmoil. And what Mr. Bodmer most strongly asserted
7 is the Commission should use more caution and greater
8 scrutiny and firmer transparency when evaluating
9 recommendations derived from the data and financial
10 models.

11 So there you have Mr. Bodmer talking
12 about the worst of times. The Utilities also give
13 you background information but it's a little less
14 theoretical. It's a little more forward-looking
15 perspective. Mr. Fetter said, Okay, yes, when things
16 are bad everything is at bottom. But you have to
17 start considering what you're doing at the time that
18 the markets start to return to some type of normalcy
19 during the ramping up process. And he -- if you look
20 at Page 8 of your memo, I will quote the phrase that
21 he used. And that is, But you want to make sure a
22 few weeks later -- and he's talking about "later"

1 referring to their worst periods -- that when the
2 markets are slowly beginning to function again that
3 Peoples/North Shore are able to access capital that
4 they need and won't be able to get.

5 Mr. Fetter also made some comments
6 about accepting Mr. Thomas's DCF and CAPM results,
7 which he found at the low range of a list of 29
8 different electric and gas returns on equity. That
9 list is in the record. That list, during
10 cross-examination, showed that the median for these
11 30 returns is 10.50. The average for these 30
12 returns is 10.36.

13 Now the question is what do you do
14 with that information? In his testimony Mr. Fetter
15 agreed with CUB-City that the list has some value but
16 shouldn't be used for any sort of match-up process.
17 But he maintained -- and this is an interesting
18 concept -- that view must be taken of this list
19 because this is what affects the investor universe.

20 We agree with CUB and City that it
21 should not be used for any type of comparison-based
22 ratemaking. There are other lists. We've pointed

1 those out to you that the Commission might find
2 informative or helpful.

3 We do include new language on the law
4 and that is because CUB-City took issue with what the
5 proposed order did; and, that is, it didn't accept
6 the final recommendations of any particular witness
7 and the proposed order looked at what it considered
8 reasonable. CUB-City saying, No, you got to go --
9 you got to go with the final recommendations. Well,
10 you know, what is the witness proposing? We
11 disagree, and the disagreement is based on the
12 language of the law.

13 The setting of utility rates is a
14 legislative function and not a judicial function.
15 You're not here to pick winners and losers among the
16 different experts. It's well established that the
17 Commission is more than an arbiter and under the
18 complements of a scheme set out in the Public
19 Utilities Act the Commission is supposed to be an
20 active participant. This means that contrary to
21 those arguments by City-CUB, the Commission acts
22 properly in setting its own cost of equity for the

1 utilities. There's only one limitation on your
2 authority at this point and that's the record. And
3 we believe that everything that has -- that has
4 been -- that has evolved on -- from -- on the
5 proposed order and in the PEPO is based on the
6 record.

7 And it actually goes back to CUB and
8 City's own recommendation by Mr. Bodmer who says,
9 Give greater scrutiny to the financial model results.
10 And I think that we have followed that concept.

11 You'll find a DCF analysis. And, as I
12 indicated earlier, the proposed order took the
13 numbers -- the results from both Mr. McNally and
14 Mr. Moul. There was some question about the growth
15 estimates and how they're used.

16 The bigger question and the troubling
17 question in Staff's analysis for us was the spot day.
18 I know that the Commission has used it at times.
19 It's rejected spot day analysis at other times. Spot
20 day is troubling in this financial environment. I
21 mean, you could read the newspapers and every day
22 markets are going up, markets are going down. So

1 what day do you pick? That was the thing we could
2 not get a grasp on, and that's why we did not go with
3 Staff's analysis. And you will -- if you look at the
4 CAPM analyses also, and particularly Staff's, you'll
5 see what happens when you go with the spot day.

6 Again, it seems that that just seems to reverberate
7 both through this proposed order and in these times.

8 COMMISSIONER O'CONNELL-DIAZ: Judge, I know you
9 characterize that as having a distorting effect as to
10 kind of --

11 JUDGE MORAN: I think so. I think it doesn't
12 give you a reliable picture of what is out there, I
13 mean, to the extent you can get an absolutely
14 reliable picture of the markets.

15 CAPM, we did the same thing. We took
16 the CAPM estimate from the Company, which we thought
17 was an unadjusted CAPM estimate based on our
18 readings. We now find out that the beta was
19 leveraged and so, therefore, it's not what we thought
20 it was, an unadjusted figure. Again, we did the same
21 thing. To give some balance we thought it best to
22 take the two numbers. Since then finding out that

1 that Utilities number is -- was leveraged, we have
2 changed the PEPO to go only with Staff's estimate and
3 don't feel comfortable with it.

4 And what makes us uncomfortable is the
5 Utilities' position that if you took a reasonable
6 forecast of 30-year treasury bonds with Staff's CAPM,
7 that would produce an estimate of 10.52 instead of
8 the 9.95 that Staff got with the one-day spot quote.

9 So the Commission can consider
10 averaging these estimates. It can consider taking
11 just Staff's 30-day forecast estimate. We leave that
12 up to you. But we think that it -- that that CAPM
13 analysis needs further consideration by this
14 Commission.

15 COMMISSIONER O'CONNELL-DIAZ: Judge Moran, so
16 what you're suggesting is that the Commission needs
17 to do its own, for lack of a better word, analysis or
18 judgment call with regard to --

19 JUDGE MORAN: It is judgment. That's what it
20 is.

21 COMMISSIONER O'CONNELL-DIAZ: -- it's
22 inexact --

1 JUDGE MORAN: It's much more art than science
2 here. And you have the authority to do that.
3 Mr. Bodmer, himself, says give closer scrutiny. So I
4 propose -- or we propose that you take these figures
5 that we have given you, not just only Staff's 9.5
6 CAPM estimate, which was based on a spot day, but
7 also look at the other number of record, which would
8 have been produced by forecasting and think of where
9 you want to go with those things.

10 I always hesitate with one number, and
11 this is why we average to begin with.

12 COMMISSIONER O'CONNELL-DIAZ: It's my
13 understanding that you find that the 9.95 figure from
14 Staff has gotten --

15 JUDGE MORAN: Exactly, that could be cured or
16 alleviated in some way to produce a fairer or more
17 reliable result. Absolutely.

18 Adjustments, Staff proposed three
19 adjustments. A 20 basis point financial risk
20 adjustment and then it proposed a whole lot of other
21 downward adjustments for the riders -- for Rider VBA,
22 which itself is kind of troubling. And I think that

1 when we were working on the proposed order it was a
2 50/50 call. And it was a 50/50 call -- and I'll tell
3 you why -- because the gas group, which most of the
4 analyses incorporated and it was -- the same gas
5 group was used by all the experts. Most of those
6 companies already had decoupling mechanisms. So it
7 was really iffy putting in that 10 percent basis
8 point adjustment for VBA. If you look at the briefs
9 on exception, you will not find Staff supporting that
10 VBA adjustment.

11 Staff also proposed an adjustment for
12 Rider UEA, which is the uncollectible. We -- in the
13 proposed order put in a 10 basis point adjustment,
14 which is at the low end of Staff's range. But then
15 now you have to think, how does that all work with
16 the risk adjustment? Because we've already adjusted
17 for risk. Why are you adjusting for risk again? Or
18 maybe those rider risks adjustments are the way to go
19 but then you don't need the full-blown rider risk
20 adjustment. I think we would have given that a
21 little more consideration in our PEPO, but we're
22 required to put it in our memo and not change, so we

1 didn't change anything there.

2 You might also want to look at
3 City-CUB's view. City-CUB never argued for that
4 financial risk adjustment. They did, however,
5 support an adjustment for Rider VBA and Rider UEA,
6 but they didn't give you a whole lot of reasons for
7 that. So we don't see a whole lot on the record.

8 So I'll now turn to Rider ICR, which
9 is the next contentious feature in our proposed
10 order. We've changed nothing in our proposed
11 order -- and maybe a little concerned with how
12 parties went about doing the briefs on exceptions.
13 And we will direct you mostly to the language, the
14 proposed language of the different parties in their
15 briefs on exceptions. When we wrote the proposed
16 order we followed your standards. These were not our
17 standards.

18 This Commission set standards in the
19 last Peoples rate case and you validated those
20 standards in the Nicor rate case. So at this point
21 when those standards come to us, we have to accept
22 that you want us to follow those standards. And we

1 took all the evidence of record and the arguments and
2 set it out under each of those standards
3 individually.

4 The disturbing thing when we got
5 parties' briefs on exceptions, is that language threw
6 out almost all your standards. They focus
7 selectively on the positions they wanted to take,
8 mostly theoretical. And it was disturbing for us
9 that they wouldn't give credit to what was flatly and
10 solidly on the record.

11 COMMISSIONER O'CONNELL-DIAZ: Judge Moran, so
12 are you suggesting that in the -- in the briefs that
13 you're talking about the parties ignore the fact that
14 the Commission had set these standards out --

15 JUDGE MORAN: Exactly. Exactly --

16 COMMISSIONER O'CONNELL-DIAZ: -- and in a
17 fashion --

18 JUDGE MORAN: -- they would throw everything
19 out. And that is not a good analysis for this
20 Commission to do even if it finds differently, even
21 if you find differently than what we saw on record.

22 There's something -- I don't want to

1 use the word "dishonest," but just wrong with that
2 kind of analysis. And that's got to give you some
3 pause and some reason to think.

4 There are two questions here. And I
5 think we framed them for you the way you should
6 consider them; that is, whether an accelerated main
7 replacement program should be undertaken by Peoples
8 Gas. Well, interestingly enough in the briefs on
9 exceptions all parties agree that it should be
10 accelerated. When we wrote the proposed order, we
11 figured based on the evidence that we were getting
12 from CUB and from the AG's Office that they didn't
13 agree with that. That they just wanted to maintain
14 the status quo, that they didn't want this
15 accelerated program. And then in the briefs on
16 exceptions they said, Oh, no, we don't disagree with
17 that.

18 Okay. So what's the second question?
19 The second question is, whether the rider recovery
20 mechanism that will enable this undertaking should be
21 adopted. And don't look at the law in a theoretical
22 lens.

1 You have to look at the subject matter
2 of this rider. You can't separate the two. Because
3 one is linked to the other. And that's how our
4 proposed order considered it. What are the
5 alternatives to rider recovery? There's only two.
6 The only two that we could think of, and certainly
7 nothing else was put before this Commission on
8 record, annual rate cases is one of them. Well,
9 who's going to pay for those annual rate cases? It's
10 going to be customers. Okay. If a rider mechanism
11 allows you to get the benefit, allows you to avoid an
12 annual rate case, that's a great idea.

13 Your own Staff is saying, Wow, let's
14 not go with Rider ICR, but let's force the Company to
15 accelerate infrastructure improvements. You can't do
16 that. You cannot do that in this case. You need a
17 separate case, a separate document -- excuse me --
18 docket that gives notice to all the parties that you
19 have intentions to require the Company to accelerate.
20 Then what happens? Then you'll probably have to have
21 another rate case and a whole stream of rate cases.
22 And maybe, maybe that would make a whole lot of sense

1 if you had a company that didn't want to do this.

2 But you have a company that wants to do this.

3 And don't be fooled by arguments that
4 say that they're not little. Because I do remember
5 in some of the briefs on exceptions there is quoted
6 testimony during the cross-examination of Utilities'
7 Witness Jim Schott that's taken out of context.
8 Don't allow yourselves to fall into that. Make sure
9 that you read the whole record and all of the
10 transcript references that surround the quoted
11 testimony because it's much different.

12 The bottom line is we changed nothing
13 to our recommendation. We went through every single
14 one of your standards in the most reasonable, logical
15 and fair way. We went through Staff's
16 recommendations and found Staff wants this too. City
17 wants this. The Union wants this. There are certain
18 benefits and a lot of benefits that you're going to
19 deny consumers if you don't go this way. Yes, you
20 can go another way, but it's not -- it's not helpful.
21 It gives you nothing more and possibly much less.

22 Therefore, we stand on everything that

1 we said in the proposed order and we would direct the
2 Commission to the Utilities' reply brief on
3 exceptions, which answers every single argument and
4 in great detail.

5 COMMISSIONER O'CONNELL-DIAZ: Judge Moran, just
6 with regard to the standards that you were just
7 talking about, those standards -- as they're
8 Commission standards, those standards are also
9 standards that were developed pursuant to rules that
10 were used for our water utilities when they want to
11 come in and have some sort of --

12 JUDGE MORAN: Exactly.

13 COMMISSIONER O'CONNELL-DIAZ: -- so this is not
14 something that's unknown --

15 JUDGE MORAN: -- and we talk about that.
16 You're not reinventing the wheel in a sense because
17 you've got rules for water companies that follow
18 basically the same pattern.

19 COMMISSIONER O'CONNELL-DIAZ: Thank you.

20 JUDGE MORAN: And you -- you know there's a
21 record here that shows the need to do something.

22 CHAIRMAN BOX: Any other questions for Judge

1 Moran or Judge Haynes?

2 Thank you for that brief overview.

3 There will be no 2:00 o'clock break.

4 We'll have some time for the -- thank you very much,
5 Judge. I'm sure there might be additional questions
6 tomorrow at the bench session or next week at the
7 open meeting.

8 JUDGE MORAN: That's fine. That's fine. And
9 we didn't comment on any of the exhibits and we might
10 want to do that. Thank you.

11 CHAIRMAN BOX: Pursuant to --

12 JUDGE WALLACE: Mr. Chairman.

13 CHAIRMAN BOX: Yes.

14 JUDGE WALLACE: Mr. Chairman, do you want to
15 close the bench and then go into oral argument?

16 CHAIRMAN BOX: Anything else to come before us,
17 Judge Wallace?

18 JUDGE WALLACE: No, sir.

19 CHAIRMAN BOX: Meeting is adjourned.

20 (Whereupon the prebench agenda
21 was adjourned.)

