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May 18, 2015

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Daniel P. Wolf
Executive Secretary
Minnesota Public Utilities Commission
350 Metro Square Building
121 Seventh Place East
St. Paul, MN 55101

Re: In the Matter of the Report of Minnesota Energy Resources Corporation on the Merger of Wisconsin Energy Corporation and Integrys Energy Group, Inc.
Docket No. G011/PA-14-664

Dear Mr. Wolf:

Minnesota Energy Resources Corporation ("MERC") respectfully submits its Update on Proceedings in Other Jurisdictions.

By copy of this letter all parties of record have been served.

Very truly yours,

Briggs and Morgan, P.A.

/s/ Michael C. Krikava

Michael C. Krikava

MCK/rlr

Cc: Service list

CERTIFICATE OF SERVICE

IN THE MATTER OF MERC 011 – REPORT OF MERC ON THE MERGER OF WISCONSIN ENERGY CORPORATION AND INTEGRYS ENERGY GROUP, INC.

MPUC DOCKET NO. G011/PA-14-664

Roshelle L. Herstein hereby certifies that on the 18th day of May, 2015, she served copies of **MERC'S UPDATE ON PROCEEDINGS IN OTHER JURISDICTIONS** by posting the same on www.edockets.state.mn.us. Said document is also served via U.S. Mail or e-mail as designated on the attached Official Service List on file with the Minnesota Public Utilities Commission in the above-referenced docket.

s/Roshelle L. Herstein
Roshelle L. Herstein

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STATE OF MINNESOTA
BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Beverly Jones Heydinger	Chair
Nancy Lange	Commissioner
Dan Lipschultz	Commissioner
John Tuma	Commissioner
Betsy Wergin	Commissioner

In the Matter of the Report of Minnesota Energy Resources Corporation on the Merger of Wisconsin Energy Corporation and Integrys Energy Group, Inc.	Docket No. G011/PA-14-664

MERC'S UPDATE ON PROCEEDINGS IN OTHER JURISDICTIONS

I. INTRODUCTION

Minnesota Energy Resources Corporation (MERC or the Company) provides the Minnesota Public Utilities Commission (Commission) with this Update to inform the Commission of recent developments in related proceedings in Wisconsin and Illinois, and to provide the Commission with additional information in response to the Department of Commerce – Division of Energy Resources' (Department) May 12, 2015, Supplemental Comments in this proceeding.

First, in its Supplemental Comments, the Department restates its recommendation to approve the merger between Wisconsin Energy Corporation (WEC) and Integrys Energy Group, Inc. (Integrys) (the Proposed Transaction) with conditions and provides additional information on potential conditions. We agree that the Proposed Transaction is consistent with the public interest and should be approved. While MERC can agree to most of the Department's proposed conditions, a few of them are inconsistent with the record and relevant legal standard, and have been rejected by other States who have approved the Proposed Transaction. Therefore, those

conditions should not be adopted by this Commission. MERC respectfully requests that the Commission approve the merger subject to the set of conditions set forth in Attachment A of MERC's April 27, 2015 filing. That set of conditions is consistent with the record in this case as well as the outcomes achieved in the other States.

Second, we are pleased to report that the Public Service Commission of Wisconsin (PSCW) has approved the Proposed Transaction on terms substantially consistent with MERC's requested approval in this proceeding. The PSCW adopted a series of conditions that are consistent with those proposed by MERC in Attachment A of our April 27, 2015 filing, along with two additional conditions, which we describe below and which are inapplicable to MERC's circumstances. In addition, the PSCW rejected a number of additional conditions proposed by a variety of parties. We anticipate a written order from the PSCW by the end of May, and will submit that written order into the record promptly upon receipt.

Third, on May 14, 2015, the Administrative Law Judge (ALJ) in the related Illinois proceeding issued a Proposed Order recommending approval of the merger as being consistent with the public interest.[1] A copy of that Proposed Order is included with this filing as Attachment A. The Illinois ALJ adopted conditions that are substantially consistent with those proposed by MERC in Attachment A of our April 27, 2015 filing, along with one additional condition that we describe below and which is already addressed by conditions agreed-to by MERC. We anticipate the Illinois Commerce Commission (ICC) will issue its approval of the merger by the end of June, and not later than July 6, 2015, consistent with the Illinois statutory deadline.

[1] As described in our earlier filings, the Michigan Public Service Commission and the Federal Energy Regulatory Commission (FERC) have already approved the merger.

Finally, MERC respectfully requests that the Commission consider and decide this proceeding as promptly as possible. MERC requests that the Commission approve the merger with a written order effective by the end of June to allow for the timely closing of the Proposed Transaction. To facilitate that schedule, the Company respectfully requests that the Commission calendar this matter for an agenda meeting no later than June 12, 2015, with a written order to be issued and effective by the end of June to coincide with the resolution of the Illinois proceeding.

II. UPDATE ON DEPARTMENT'S SUPPLEMENTAL COMMENTS

MERC appreciates the Department's Supplemental Comments and discussion of conditions to include in the Commission's approval.[2] In its Supplemental Comments, the Department recommends that the Commission approve the Proposed Transaction and impose the thirty conditions listed in Attachment B of the Department's April 20, 2015 comments.[3] In addition, the Department recommends the Commission adopt Condition 32 of the Attorney General Antitrust and Utilities Division (OAG) from its April 20, 2015 comments in lieu of the three conditions the Department previously proposed in its April 20, 2015 filing[4]:

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[2] *In the Matter of the Report of the Minnesota Energy Resources Corporation on the Merger of Wisconsin Energy Corporation and Integrys Energy Group, Inc.*, Docket No. G011/PA-14-664 ("*WEC/Integrys Merger*"), Supplemental Comments of the Minnesota Department of Commerce Division of Energy Resources (May 12, 2015) (Department Supplemental Comments).

[3] *Id.* at 2.

[4] The three conditions the Department proposed that it believes are unnecessary if the OAG Condition 32 is adopted are:

> 1. The Commission will deny MERC recovery of increased financing costs due to any rating agency downgrades in any subsequent general rate proceeding for the first three years following the merger.
>
> 2. Any increased capital costs determined by the Commission to be related to downgrading or other credit degradation of the holding company and-or non-utility affiliates should be removed from the cost of capital for MERC.
>
> 3. Cost allocated or assigned from IBS, or its successor, cannot increase above the level approved in MERC's most recent general rate case (Docket E-011/GR-13-617) for rate-making purposes for the first three years after the Proposed Transaction is executed.

Department Supplemental Comments at 1.

> If MERC's cost of debt increases during the next three calendar years, Minnesota ratepayers will be held harmless from any rate impact unless MERC can demonstrate that its increased cost of debt was not caused by the proposed transaction.[5]

MERC appreciates the Department's attempt to streamline the Commission decision-making process. Nevertheless, MERC continues to support only those conditions proposed in MERC's April 27, 2015 Reply Comments, which provide an appropriate balance and ensure the Proposed Transaction is consistent with the public interest.[6] MERC has concerns over some of the Department's proposed conditions, particularly since those conditions were not adopted by other States, and continues to have concerns about the OAG's Condition 32 for the reasons stated in its Reply Comments.[7] Notably, the conditions proposed by MERC are consistent with the conditions adopted in other States based on the extensive records developed in those proceedings.

III. STATUS OF OTHER PROCEEDINGS

The Commission indicated during the February 5, 2015 Agenda Meeting on this matter that it was interested in the records being developed in the other States and the types of conditions that were being adopted or rejected there. In prior filings, we have provided information about the conditions adopted and rejected by FERC and in Michigan. After conferring with the Department and the OAG, we agreed to provide additional information about the conditions adopted and rejected in Wisconsin and Illinois.

A. Wisconsin

During its April 30, 2015 discussion of the record, the PSCW determined that WEC's acquisition of Integrys satisfied Wisconsin's statutory requirement that the acquisition be in the

[5] *Id.* at 2.

[6] *See WEC/Integrys Merger*, MERC Reply Comments on Proposed Conditions (Apr. 27, 2015).

[7] *Id.* at 7-9, 19.

best interests of utility consumers, investors, and the public. We expect the PSCW's formal written decision by the end of May, and will submit it to the Commission when it is issued.

1. Conditions Adopted By PSCW

The PSCW adopted a series of conditions that are consistent with the conditions MERC is proposing in this matter and are substantially similar to the conditions proposed by MERC in Attachment A of its April 27, 2015 filing. These conditions address topics such as accounting, treatment of transaction and transition costs, and a variety of ratemaking issues. In an effort to maintain consistency across jurisdictions, MERC respectfully requests that the Commission adopt the conditions it has proposed, which are consistent with the conditions adopted by the PSCW.

The PSCW also adopted two additional conditions that it found were supported by the record and applicable law in that proceeding. Neither of these conditions are relevant to MERC or Minnesota.

First, the PSCW conditioned approval on adoption of a revenue sharing mechanism for the next three years at Wisconsin Electric Power Company and Wisconsin Gas Company. Under this mechanism, any earnings above the utilities' authorized return on equity (ROE) would be shared between customers and shareholders. Specifically, the first 50 basis points over the authorized ROE would be split between customers and shareholders, and above that all over-earnings would be returned to customers. With respect to Wisconsin Electric Power Company, the shared earnings would be applied to an accrued transmission escrow account. For Wisconsin Gas Company, the shared earnings would be applied to reduce the cost of a gas lateral that is currently under construction in Wisconsin. This earnings sharing mechanism arose out of the unique circumstances existing in Wisconsin and the fact that the utilities had specific costs (e.g., transmission escrow and gas lateral construction) that could be offset by any over-earnings.

MERC notes that an earnings sharing mechanism would not be appropriate for Minnesota or for MERC's service territory. MERC has historically under-earned its authorized rate of return, without adjustment for unusual circumstances. In addition, the record in this proceeding does not support the type of cost information that the PSCW used to support imposing that mechanism; instead, such an earnings mechanism is more appropriately evaluated in the context of a rate case. Finally, the merger is consistent with the public interest without such a sharing mechanism, meeting the relevant legal standard.

A second condition adopted by the PSCW has no applicability to Minnesota. It relates to an Integrys electric utility subsidiary, Wisconsin Public Service Company (WPSC), and would prohibit WPSC from proceeding with an application to construct a new combined cycle power plant -- Fox 3 -- until the newly combined company files a joint resource planning analysis demonstrating the need for the plant. Again, this condition is unique to Wisconsin and has no application to a gas utility in Minnesota.

2. Conditions Rejected by PSCW

As described in earlier filings, parties to the proceeding in Wisconsin proposed over 90 conditions addressing a number of important topics. The PSCW rejected the following additional conditions, concluding that they were substantially duplicative and overlapping, they merely reaffirmed the utility's obligations under existing law, the record did not support them, or the Proposed Transaction met the applicable legal test without them:

- A condition imposing a "most favored nations" clause.[8] We note that previously both the Department and the OAG agreed that such a clause is unnecessary.[9]

[8] Department Condition 13 from Attachment B of its April 20, 2015 Comments proposes a most favored nation condition. All references to Department Conditions refer to Attachment B of the Department's April 20, 2015 Comments.

- Conditions that preclude the utilities from seeking recovery of "transition" costs.[10]
- Conditions prejudging the treatment of service company issues.
    - The Department's proposed Condition 21 seeks to prejudge cost allocation within the service company structure.
    - The Department's proposed Condition 23 seeks to prejudge the use of the service company structure. PSCW adopted a modified Condition 23 to consider both qualitative, as well as quantitative, factors when determining which services should be performed by the service company.[11]
- Overlapping and duplicative conditions on accounting practices, cost allocations, charitable contributions, low income programs and treatment of severance costs. The Department's proposed Conditions 4, 6, 8, 10, 15, 19 and 29 all fall in this category of unnecessary conditions that have not been adopted elsewhere.

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[9] *See WEC/Integrys Merger*, Comments of the Office of the Attorney General - Residential Utilities and Antitrust Division, at 6 (Apr. 20, 2015); *WEC/Integrys Merger*, Comments of the Minnesota Department of Commerce, Division of Energy Resources, at 4 (Apr. 20, 2015). However, Department of Commerce Condition 13 reintroduces the "most favored nations" concept.

[10] Department proposed Conditions 26, 27, 28, and 30 seek to limit "transition" cost recovery. Note that MERC agrees that it is precluded from seeking recovery of "transaction" costs (i.e., the costs incurred in consummating the Proposed Transaction). However, "transition" costs (i.e., the downstream costs incurred to fully integrate operations and to maximize economies of scale and other efficiencies) are different and should be treated differently.

[11]The PSCW adopted the following formulation of this condition: "The service company should be limited to performing services where there are efficiencies and economies of scale that could not be achieved if the service were not performed by the service company, or where qualitative factors justify performance of services by the service company." MERC is willing to accept this language.

B. Illinois

On May 14, 2015, the Illinois ALJ issued a Proposed Order recommending that the ICC approve the Proposed Transaction.[12] In so deciding, the ALJ adopted a "no harm" legal standard – *i.e.*, examining the merger to determine that it will not detrimentally affect the status quo of the utility's operations and service – finding that this standard is the proper statutory standard the ICC should apply when determining whether to approve the merger.[13] The legal standard in Illinois is substantially similar to the "consistent with the public interest" standard applicable to this proceeding.

The Illinois ALJ concluded that the merger should be approved, as it "will not adversely affect either Peoples' Gas or North Shore's or ATC's ability to perform its duties under the [Illinois Public Utilities] Act," based upon findings including, but not limited to, that the Proposed Transaction will not "diminish" their abilities "to provide adequate, reliable, efficient, safe and least-cost public utility service."[14] MERC anticipates that the ICC will approve the Proposed Transaction at the end of June, with a decision required by the July 6, 2015, Illinois statutory deadline. A copy of the Illinois ALJ's Proposed Order is attached to this filing.

Except for one condition that is inapplicable to Minnesota, and some less significant changes in two conditions, the Proposed Order adopts the condition language proposed by the Illinois Joint Applicants and rejects the onerous conditions requested by the other parties. The conditions adopted by the ALJ encompass the same type of conditions proposed by MERC in

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[12] *Wisconsin Energy Corporation, Integrys Energy Group, Inc., Peoples Energy, LLC, The Peoples Gas Light and Coke Company, North Shore Gas Company, ATC Management, Inc., and American Transmission Company, LLC; Application pursuant to Section 7-204 of the Public Utilities Act for authority to engage in a Reorganization, to enter into agreements with affiliated interests pursuant to Section 7-101, and for such other approvals as may be required under the Public Utilities Act to effectuate the Reorganization*, Docket No. 14-0496, Proposed Order (May 14, 2015). The Illinois ALJ Proposed Order is attached as Attachment A to this filing.

[13] *Id.* at 30.

[14] *Id.* at 103.

this proceeding but also include conditions that are unique to the gas utilities in Illinois. Specifically, the Proposed Order contains conditions relating to cost recovery, the allocation of savings, the honoring of existing labor agreements, and maintaining community involvement.

The one significant instance where the Proposed Order adopts the ICC staff's requested language rather than the Illinois Joint Applicants' proposal is inapplicable to Minnesota. In this instance, the Joint Applicants had proposed a condition with a minimum level of full time equivalent employees (FTEs) required to be maintained in Illinois for two years after closing without specific requirements for FTEs being enumerated for each company.[15] The Proposed Order, however, adopts the ICC staff's proposed language for a condition that requires minimum FTE levels at each company for a period of two years after closing.[16] This altered condition is unique to Illinois and does not affect this proceeding because the Proposed Transaction in Minnesota does not involve multiple companies as it does in Illinois. Further, MERC has already committed that no workforce reductions will occur as result of the Proposed Transaction, except through normal attrition.

IV. REQUEST TO EXPEDITE SCHEDULING OF THE COMMISSION MEETING

MERC hopes to close the Proposed Transaction at the end of June. As noted, we expect to have a final written order from the PSCW by the end of May. And, we anticipate that the ICC is likely to address the Illinois ALJ Proposed Order during its June 24 Bench Session, which is the last regularly scheduled meeting of the ICC prior to the July 6 Illinois statutory deadline. We expect to receive a written decision within a day or two of that session if the ICC votes on the Proposed Order at that time. If we can obtain an effective written Minnesota order in that same timeframe, it will facilitate the timely closing of the Proposed Transaction. Under the merger

[15] *Id.* at 32-33.

[16] *Id.* at 37.

agreement, the transaction must close within two business days after receipt of the required regulatory approvals.

Closing the Proposed Transaction by the end of June will also lock in the benefits of the Proposed Transaction for Minnesota ratepayers and enable ratepayers to begin reaping the benefits as quickly as possible. To facilitate closing the Proposed Transaction by the end of June, MERC would greatly appreciate if the Commission could calendar this matter as soon as reasonably possible. In particular, MERC respectfully requests that the Commission consider this matter at a Commission meeting on or before June 12, 2015. Additionally, MERC respectfully requests that the Commission promptly issue its order following the Commission meeting and state in its order that the order is "effective immediately."

V. CONCLUSION

MERC appreciates the time and attention given to this matter by the Commission, its Staff, the Department, and the OAG. We recognize that this is an important matter to the State and to MERC's customers and that it has required considerable resources to process. A robust and complete record has been developed that supports granting approval for the merger, subject to the conditions proposed in Attachment A to MERC's April 27, 2015 filing.

Dated: May 18, 2015

Respectfully Submitted,

/s/
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MINNESOTA ENERGY RESOURCES CORPORATION

7095513

Attachment A

Illinois Commerce Commission
May 14, 2015 Proposed Order

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Wisconsin Energy Corporation, Integrys Energy Group, Inc., Peoples Energy, LLC, The Peoples Gas Light and Coke Company, North Shore Gas Company, ATC Management Inc., and American Transmission Company LLC	:	
Application pursuant to Section 7-204 of the Public Utilities Act for authority to engage in a Reorganization, to enter into agreements with affiliated interests pursuant to Section 7-101, and for such other approvals as may be required under the Public Utilities Act to effectuate the Reorganization.	:	**14-0496**

PROPOSED ORDER

May 14, 2015

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STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Wisconsin Energy Corporation, Integrys Energy Group, Inc., Peoples Energy, LLC, The Peoples Gas Light and Coke Company, North Shore Gas Company, ATC Management Inc., and American Transmission Company LLC	:	
Application pursuant to Section 7-204 of the Public Utilities Act for authority to engage in a Reorganization, to enter into agreements with affiliated interests pursuant to Section 7-101, and for such other approvals as may be required under the Public Utilities Act to effectuate the Reorganization.	:	**14-0496**

PROPOSED ORDER

By the Commission:

I. PROCEDURAL HISTORY

On August 6, 2014 an application was filed by Wisconsin Energy Corporation ("Wisconsin Energy"), Integrys Energy Group, Inc. ("Integrys"), Peoples Energy, LLC ("PELLC"), The Peoples Gas Light and Coke Company ("Peoples Gas"), North Shore Gas Company ("North Shore") (collectively, Peoples Gas and North Shore are referred to herein as the "Gas Companies"), ATC Management Inc. ("ATCM") and American Transmission Company LLC ("ATCLLC") (operated as a single entity and referred to collectively herein as "ATC") (all, collectively, the "Joint Applicants" or "JA") asking the Illinois Commerce Commission ("Commission"), for approval, pursuant to Sections 7-204 and 7-204A of the Public Utilities Act ("Act"), of reorganization (the "Reorganization") by which Integrys will merge into a subsidiary of Wisconsin Energy and the Gas Companies will become wholly-owned subsidiaries of a newly formed holding company, WEC Energy Group, Inc. ("WEC Energy Group"). The Joint Applicants also seek approval pursuant to Sections 7-102 and 7-204A (b) of the Act for entry by the Gas Companies into an affiliated interest agreement by which they may receive services from and provide services to WEC Energy Group and its subsidiaries. The Joint Applicants request additional approvals and findings in connection with the Reorganization, as more fully discussed in this Order.

The City of Chicago ("City") filed an appearance pursuant to Section 10-108 of the Act. 220 ILCS 5/10-108.

Petitions to intervene were filed by: the Citizens Utility Board ("CUB"); the People of the State of Illinois by the Office of the Attorney General ("AG"); the Retail Energy Supply Association ("RESA"); the Environmental Law and Policy Center ("ELPC"); and Utility Workers United of America, AFL-CIO, Local 18007 ("UWUA"). All of these petitions to intervene were granted by a duly authorized Administrative Law Judge ("ALJ") of the Commission.

Pursuant to notice as required by law and by the rules and regulations of the Commission, prehearing conferences were held in this matter before the ALJ at the Commission's offices in Chicago on September 4, 2014, September 18, 2014, October 9, 2014, January 6, 2015, January 20, 2015, March 16, 2015, and March 19, 2015.

On January 2, 2015, the AG and City filed a motion to extend the deadline by ninety days for the Commission to issue an order approving or denying the Reorganization pursuant to Section 7-204(d) of the Act. 220 ILCS 5/7-204(d). The Joint Applicants and Staff opposed the motion, while CUB supported the motion. On January 14, 2015, the ALJ issued a Notice of ALJ's Ruling denying this motion. The ALJ's Ruling also limited the scope for which an interim report prepared by Liberty Consulting Group ("Liberty") regarding Phase I of their ongoing investigation of Peoples Gas' Accelerated Main Replacement Program ("AMRP") being conducted at the direction of the Commission ("Interim Report") could be used in this proceeding. (The Commission directed that this investigation of the AMRP be conducted in its Final Order in Peoples Gas' 2012 rate case, issued on June 18, 2013. *North Shore Gas Co., et al.*, Docket Nos. 12-0511/12-0512 (Consol.), Order at 61 (June 18, 2013)). On February 4, 2015, the AG, City, and CUB jointly filed a petition for interlocutory review of the ALJ's decision denying the request for an extension of the approval deadline and limiting the use for which the Interim Report could be used in this proceeding. Staff and the Joint Applicants filed responses in opposition to this petition for interlocutory review. On March 11, 2015, the Commission denied this petition for interlocutory review.

On January 22, 2015, the AG, City, and CUB jointly filed a motion requesting the removal of Staff's confidential designation placed on the Interim Report. Staff and the Joint Applicants filed responses opposing this motion. On February 11, 2015, the ALJ issued a Notice of ALJ's Ruling denying this motion. On February 17, 2015, the AG, City, and CUB jointly filed a petition for interlocutory review of the ALJ's decision denying the motion to remove the confidential designation of the Interim Report. Staff and the Joint Applicants filed responses in opposition to this petition for interlocutory review, although the Joint Applicants withdrew their opposition prior to the Commission's ruling. On March 11, 2015, the Commission denied this petition for interlocutory review.

On February 11 and 13, 2015, the AG, City, and CUB jointly filed verified requests for subpoena to be issued on Liberty. Staff and the Joint Applicants filed responses opposing these requests and Liberty filed a special appearance and motion

to quash the subpoena requests. On February 18, 2015, the ALJ issued a Notice of ALJ's Ruling denying the requests for subpoena and granting Liberty's motion to quash.

On February 17, 2015, the AG filed a motion to compel additional information concerning the AMRP and the Interim Report. The Joint Applicants filed a response in opposition to this motion. On March 5, 2015, the ALJ issued a Notice of ALJ's Ruling denying the AG's motion to compel.

On February 18 and 19, 2015, an evidentiary hearing was held before the ALJ at the Commission's offices in Chicago. The Joint Applicants, Staff, AG, City, CUB, UWUA, and RESA entered appearances. The Joint Applicants presented testimony and exhibits from Allen L. Leverett, President for Wisconsin Energy; Scott J. Lauber, Vice President and Treasurer for Wisconsin Energy; John J. Reed, CEO, Concentric Energy Advisers, Inc.; James F. Schott, Executive Vice President and Chief Financial Officer for Integrys; David D. Giesler, Senior Project Manager for Integrys Business Support, LLC ("IBS"); Thomas J. Webb, Compliance Manager for Peoples Gas; and Andrew Hesselbach, Project Director for Wisconsin Energy.

The AG presented testimony and exhibits from the following witnesses: David J. Effron, a utility regulatory consultant; and Sebastian Coppola, President, Corporate Analytics, Inc.

The City and CUB (collectively "City/CUB") presented testimony and exhibits from the following witnesses: Christopher Wheat, Deputy Director of the Innovation Delivery Team for the City; Karen Weigert, Chief Sustainability Officer for the City; William Cheaks, Jr., Deputy Commissioner, Chicago Department of Transportation ("CDOT") – Division of Infrastructure Management; and Michael P. Gorman, Managing Principal, Brubaker & Associates, Inc.

RESA presented testimony and exhibits from Joseph Clark, a member of the government affairs team for Direct Energy Services, LLC.

UWUA presented testimony and exhibits from Richard Passarelli, business manager for UWUA.

Staff presented testimony and exhibits from the following witnesses: Harold Stoller, Director, Safety and Reliability Division; Eric Lounsberry, Supervisor, Gas Section of the Energy Engineering Department, Safety and Reliability Division; Matthew Smith, Pipeline Safety Analyst II, Safety and Reliability Division; David Sackett, Economic Analyst, Policy Division; Daniel Kahle, Accountant, Financial Analysis Division; Dianna Hathhorn, Accountant, Financial Analysis Division; Michael McNally, Senior Financial Analyst, Financial Analysis Department; and Alicia Allen, Rate Analyst, Financial Analysis Division.

All of the foregoing testimony and exhibits were admitted into the record during the February hearings, along with certain cross-examination exhibits.

On March 11, 2015, the Commission issued Commissioners' Data Requests to be answered by the Joint Applicants. On March 18, 2015, the Joint Applicants filed responses to Commissioners' Data Requests. On March 24, 2015, Staff, the AG, and City/CUB filed replies to the Joint Applicants responses to the Commissioners' Data Requests. The Joint Applicants' responses and the replies from Staff, the AG, and City/CUB were admitted into the record pursuant to an ALJ ruling on April 27, 2015.

On March 24, 2015, the AG, City, and CUB filed a second motion for extension of the deadline for the Commission to enter an order approving or denying the Reorganization and motion to hold open the record for additional evidence. Staff and the Joint Applicants filed responses opposing the motion. On April 21, 2015, the ALJ issued a Notice of ALJ's Ruling denying this motion.

On March 27, 2015, the Joint Applicants, Staff, the AG, and City/CUB each filed their respective Initial Briefs ("IB"). On April 10, 2015, the Joint Applicants, Staff, the AG, and City/CUB each filed their respective Reply Briefs ("RB").

On March 27, 2015, Staff filed a motion for administrative notice of the Commission's corrected Initiating Order and the Staff report from Docket No. 15-0186. On April 27, 2015, the ALJ issued a Notice of ALJ's Ruling Granting Staff's motion.

On April 13, 2015, the Joint Applicants, Staff, the AG, and City/CUB each submitted a Draft Proposed Order or statement of positions.

On April 27, 2015, the record was marked "Heard and Taken" by the ALJ.

On May 14, 1015, the ALJ filed and served on the parties a Proposed Order addressing the Joint Applicants' application and Staff and Intervenor objections and recommendations.

II. THE PROPOSED REORGANIZATION

A. Identification of the Parties to the Reorganization and Their Affiliates

1. Wisconsin Energy and its Affiliates

Wisconsin Energy is a holding company with a number of wholly owned subsidiaries. In fiscal 2013, Wisconsin Energy had operating revenues of approximately $4.5 billion, net income of approximately $577.4 million, and employed approximately 4,300 people. Through its subsidiary utilities, Wisconsin Electric Power Company ("WEPCO") and Wisconsin Gas LLC ("WG") (both doing business as "We Energies"), Wisconsin Energy serves 1.1 million electric customers and 1.1 million natural gas customers throughout Wisconsin and the Upper Peninsula of Michigan. Wisconsin Energy's utility assets include 20,967 miles of gas transmission and distribution lines, 6,021 megawatts ("MW") of electric generation capacity, and 45,597 miles of electric distribution lines.

2. Integrys and Its Affiliates

Integrys is a holding company that was originally formed in 1994, and established in its current structure on February 21, 2007 with the merging of WPS Resources Corporation and Peoples Energy Corporation (now Peoples Energy, LLC). Integrys presently owns and operates six regulated natural gas and electric utilities that serve a total of 2.1 million customers in Illinois, Wisconsin, Minnesota, and Michigan, plus a services company, Integrys Business Support, LLC. The Illinois utilities are The Peoples Gas Light and Coke Company and North Shore Gas Company, which are Illinois public utilities within the meaning of Section 3-105 of the Act. 220 ILCS 5/3-105. Integrys also presently owns Trillium CNG, a leading provider of compressed natural gas fueling services. Integrys had total revenues in 2013 of $5.6 billion, with a net income of $350 million, and it employed approximately 5,000 people.

3. ATC

ATCLLC is a Wisconsin limited liability company managed by a corporate manager, ATCM, a Wisconsin corporation. Together they operate as a single entity, ATC, which owns and operates a high-voltage electric transmission system in an area from the Upper Peninsula of Michigan, throughout the eastern half of Wisconsin and small portions of Minnesota and Illinois. ATC is owned primarily by the electric utilities in eastern Wisconsin that contributed transmission facilities to it, including Wisconsin Energy subsidiary WEPCO and Integrys subsidiary Wisconsin Public Service Corporation.

ATC is an Illinois public utility that owns and operates two 345 kilovolt ("kV") transmission lines and associated facilities, each less than two miles in length, that interconnect with the 345 kV system of Commonwealth Edison Company, as well as a 69 kV transmission line and associated facilities that form a nine-mile loop in Winnebago County and serves four distribution substations. *American Transmission Co. L.L.C. and ATC Management Inc.*, Docket 01-0142, Order (Jan. 23, 2003); *American Transmission Co. LLC*, Docket 11-0661, Order (April 10, 2012). ATC does not charge any retail rates to Illinois end-user customers, or have any retail customers in Illinois. ATC's transmission service rates are regulated exclusively by the Federal Energy Regulatory Commission ("FERC").

B. The Reorganization

Wisconsin Energy and Integrys have entered into an Agreement and Plan of Merger, dated June 22, 2014 ("Merger Agreement"). Pursuant to the Merger Agreement: 1) Wisconsin Energy will acquire 100% of the outstanding common stock of Integrys, with Integrys shareholders receiving 1.128 Wisconsin Energy shares plus $18.58 in cash for each Integrys share; 2) the current Integrys holding company will merge with a subsidiary that Wisconsin Energy will create and Integrys will be the surviving company in that merger; 3) Integrys will then merge into a second subsidiary created by Wisconsin Energy, with the second subsidiary surviving after the merger; and 4) the surviving entity, labeled the "Subsequent Merger Subsidiary" in the Merger

Agreement but expected to be called Integrys Energy Group, will then be a wholly-owned subsidiary of WEC Energy Group (the "Merger" or "Transaction"). Upon consummation of the Reorganization (the "Closing"), Peoples Gas and North Shore will become wholly-owned subsidiaries of WEC Energy Group. Peoples Gas and North Shore will retain their current names, corporate forms, and headquarters in Chicago and Waukegan, respectively, and continue to operate as Illinois public utilities, subject to the Commission's jurisdiction and applicable Illinois law and regulation.

As a result of the Reorganization, WEC Energy Group will gain a majority ownership interest in ATC. Currently, Integrys owns 34.07% of the outstanding shares of ATC's manager, ATCM, and Wisconsin Energy owns 26.24%. Following the Reorganization, WEC Energy Group will own 60.31% of the outstanding shares of ATCM.

III. COMMISSION AUTHORITY

A. Joint Applicants' Position

The Joint Applicants argue that Section 7-204 of the Act provides the sole comprehensive scope of the Commission's authority to approve the Reorganization, as the Commission determined when interpreting Section 7-204 in *SBC Communications, Inc., et al.*, Docket No. 98-0555, 1999 Ill. PUC LEXIS 738 (Sept. 23, 1999) at *26.

The Joint Applicants state that City/CUB, however, attempt to argue that when it approves a proposed reorganization subject to Section 7-204, the Commission must go beyond the comprehensive required findings set forth in Sections 7-204(b) and (c) of the Act to make a general determination as to whether or not a merger meets some general "public interest" standard. In particular, City/CUB rely on the Act's general declaration of findings and intent, Section 1-102, to support their assertion that the Commission must go beyond the requirements of Section 7-204 when determining whether to approve a proposed reorganization. The Joint Applicants contend that Illinois Courts, however, have held that these declarations are "prefatory," and of no substantive or positive legal force. *See Monarch Gas Co. v. Illinois Commerce Comm'n*, 261 Ill. App. 3d 94, 99 (5th Dist. 1994). Moreover, it is ironic in the Joint Applicants' opinion that while City/CUB rely on the canon of statutory construction that requires a statute to be interpreted so as not to render a word or phrase superfluous, City/CUB's interpretation would ignore Subsection (e) of Section 7-204, which expressly provides: "No other Commission approvals shall be required for mergers that are subject to this Section." 220 ILCS 5/7-204(e). The Joint Applicants believe that City/CUB's standard for Commission review of a proposed reorganization would effectively render Section 7-204(e) a nullity, and thus, must be rejected based on the case law cited by City/CUB. *See Kraft, Inc. v. Edgar*, 138 Ill. 2d 178, 189, 149 Ill. Dec. 286, 561 N.E.2d 656 (1990).

The Joint Applicants note that City/CUB further rely on Section 7-204(f) in support of their position that the Commission must make a general "public interest" finding when determining whether to approve a proposed reorganization, asserting that

Section 7-204(f) "requires" the Commission to impose conditions on a reorganization. The Commission, however, rejected a similar argument made by intervenors in Docket No. 98-0555, determining that Section 7-204 does not require a specific "public interest" finding and that the seven specific findings required by Section 7-204(b) will have the effect of protecting the interests of the utility and its customers. Docket No. 98-0555, Order at *26-27. Indeed, City/CUB's attempt to expand the scope and interpretation of Section 7-204(f) in this manner would again make superfluous the express language of this provision that gives the Commission permissive authority to impose conditions – using the word "may" instead of "must" or "shall" – when in the Commission's "judgment" such conditions are "necessary to protect the interests of the public utility and its customers." The Joint Applicants argue that City/CUB's interpretation of Section 7-204(f) would violate the primary rule of statutory construction, which is to effectuate the true intent and meaning of the legislature by giving a statute's language its "plain and ordinary meaning." *Wisnasky-Bettorf v. Pierce*, 2012 IL 111253 at ¶ 16.

The Joint Applicants contend that the AG's and City/CUB's attempt to use Section 7-204(f) as a basis for arguing that the Commission should impose numerous conditions to enhance the Gas Companies' service or the interests of customers likewise is contrary to the plain and ordinary meaning of the statute's language, as well as the Commission's interpretation of this subsection. In Docket No. 98-0555, the Commission examined the scope of Section 7-204 and, in particular, the interplay between subsections (b) and (f). The Joint Applicants note that the Commission concluded that Section 7-204(b) establishes the minimum findings that "encompass most, if not all, of the interests in need of protection" in a proposed reorganization, and that any additional findings made by the Commission and conditions based upon those findings must have "a reasonable relationship to the Section 7-204(b) interests articulated by our legislature." Docket No. 98-0555, at *97-*98. The Commission went on to find that, based on the statutory language of Section 7-204(f) "as the best indicator of legislative intent," any conditions imposed on a proposed reorganization be, "in [the Commission's] good and informed judgment, of a type necessary to protect the interests of the company and its customers consistent with the interests outlined by Section 7-204(b)." *Id*. at *98-99.

The Joint Applicants argue that the interests outlined in Section 7-204(b) are focused on ensuring that a proposed reorganization will not have an adverse impact on the ability of the Gas Companies to perform their obligations under the Act and provide service to their customers. *See GTE Corp. and Bell Atlantic Corp.*, Docket No. 98-0866, 1999 Ill. PUC Lexis 825 at *28 (Oct. 29, 1999) ("At the outset, it must be noted that the standard contained in the statute requires the Commission to evaluate whether the impact of the proposed reorganization will be to diminish service quality, not whether the proposed merger will enhance service quality."). Accordingly, to be consistent with those interests, conditions imposed under Section 7-204(f) likewise should be designed to prevent diminishment of existing service quality and not focused on enhancements or improvements. The Joint Applicants maintain that the Commission has previously determined this is the plain and ordinary meaning of the word "protect" as used in Section 7-204(f). *See* Docket No. 11-0046, Order at 77 (concluding that the

Commission would not alter the status quo in its order approving a reorganization because Section 7-204(f)'s authorization to issue conditions "to protect" the public interest is distinct from "enhancing the public interest"). This is consistent with the definition of "protect," which is "to cover or shield from that which would injure, destroy, or detrimentally affect," and does not include the concept of improving or enhancing the item which is to be protected. Webster's Third New International Dictionary 1822 (1993).

The Joint Applicants conclude that the authority relied upon by the AG and City/CUB does not support their interpretation of Section 7-204 and, in particular, subsection (f). Thus, the AG's and City/CUB's proposed interpretations as to the scope of Section 7-204 and subsection (f) should be rejected.

B. The AG's Position

The AG states that Section 7-204(b) of the Act provides that no reorganization shall take place without prior Commission approval and certain findings must be made. 220 ILCS 5/7-204(b). In addition, Section 7-204(c) provides that the Commission "shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated." 220 ILCS 5/7-204(c). The burden of proof is on the Joint Applicants to demonstrate that these provisions have been satisfied. Finally, the AG notes, and of particular importance to Peoples Gas and North Shore ratepayers, subsection (f) provides that "[i]n approving any proposed reorganization pursuant to this Section the Commission may impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f).

The AG argues that the Joint Applicants' interpretation of Section 7-204 is unlawfully narrow and should be rejected. The AG points to the Joint Applicants' statement in their Initial Brief that the Commission should reject the additional conditions sought by the AG and City/CUB "because they are not related to any of the findings required under Section 7-204." JA IB at 31.

According to the AG, the argument betrays a fundamental misunderstanding of the requirements of Section 7-204 and the Commission's obligations under the entire statute. Section 7-204(b) outlines the minimum service, safety and rate impact requirements that the Commission must conclude have been satisfied before approving a merger. 220 ILCS 5/7-204(b)(1)-(7). But in addition to Section 7-204(b), Section 7-204(f) creates a further obligation on the Commission to protect the public interest – not one that must be tied to the subsection 7-204(b) requirements.

The AG adds that in ascertaining the legislature's intent, courts begin by examining the language of the statute, reading the statute as a whole, and construing it so that no word or phrase is rendered meaningless or superfluous. *Kraft, Inc.*, 138 Ill. 2d at 189; *Wal–Mart Stores, Inc. v. Industrial Comm'n*, 324 Ill. App. 3d 961, 965, 258 Ill.

Dec. 17, 755 N.E.2d 98 (2001). Illinois courts cannot view words or phrases in isolation but, rather, must consider them in light of other relevant provisions of the statute. *In re E.B. et al.*, 231 Ill. 2d 459, 899 N.E.2d 218, 2008 WL 4943447 (2008). The AG concludes that these statutory interpretation precepts require rejection of the JA's flawed statutory analysis.

The AG states that while it is true that Section 7-204(f) conditions, in effect, can be used to help ensure that the Section 7-204(b)(1)-(7) requirements are, in fact, satisfied post-merger, Section 7-204(f) also provides the Commission with an obligation to impose conditions that it believes are necessary and appropriate to protect the public interest. Adoption of the Joint Applicants' restricted interpretation of Section 7-204 would, contrary to accepted statutory interpretation principles, render this subsection meaningless.

The AG notes that prior Commission orders related to proposed utility mergers support its position. For example, the AG points out that the Commission applied a condition designed to improve service quality in its 1999 Order approving the merger between Ameritech, Inc. and SBC Communications, Inc. In that decision, the Commission imposed a condition that it specifically noted was necessary to improve Ameritech's existing service quality found to be deficient by the Commission – not unlike the evidence in this case of mismanagement by Peoples Gas of its AMRP, and the requested intervenor conditions designed to set the AMRP operation on a better operational course. *See* Docket No. 98-0555, Order at *21-22.

The AG contends that this merger condition in Docket 98-0555, the Ameritech/SBC case, demonstrates that the Commission has authority under Section 7-204(f) to premise merger approval on the conditions it believes are necessary to protect the public interest, including conditions that would create improvements in existing service. It also aligns with the argument that should the Commission approve the merger here, additional conditions are needed to improve the existing deficient management of the Peoples Gas AMRP. In other words, the AG claims that even if the Joint Applicants had satisfied the requirements of Section 7-204(b) designed to ensure that the quality, reliability and cost of utility service is not negatively impacted, the Commission has an obligation to attach any additional conditions that "in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f). The AG concludes that the imposition of commitments that will help protect customer interests – interests that WEC has made clear are not its priority – is unquestionably appropriate and consistent with the Commission's obligations under the Act.

With respect to the specific Commitments made by the Joint Applicants, the AG asserts that the Joint Applicants' claim of future benefits is vague and offers no tangible value to Peoples Gas and North Shore customers. The AG notes that the Joint Applicants have committed to establish a new training center within the City of Chicago, the extension of funding of technical training for future gas utility workers at Chicago's City Colleges (JA Ex. 15.1 REV, nos. 37 and 38), and to contribute $5 million over five years to the Gas Companies' Share the Warmth Fund. While the AG appreciates these

commitments, the promises are insufficient in light of the risks of rate shock associated with the Joint Applicants' assumption of the AMRP.

In addition, the AG states, filing commitments for both the Joint Applicant-proposed AMRP activity and other merger-related monitoring and ratemaking activities represent standard, boiler-plate filing requirements that are necessary but unremarkable in scope. See, e.g., JA Ex. 15.1 REV, Commitment Nos. 3, 4, 6, 7, 8, 9-13, 16, 17-25. These commitments represent business-as-usual activity that is either already happening under Integrys' leadership or is standard practice when acquisitions are approved by the Commission. Also, the AG states that the acquisition premium commitment is standard, and nothing more than business-as-usual merger treatment. The AG explains that the Joint Applicants have committed to exclude the goodwill from the determination of the Gas Companies' rates, irrespective of whether push down accounting is required or not. The balance of goodwill on the Gas Companies' balance sheet, if any, will not be included in rate base and amortization of goodwill will not be included in operating expenses. JA Ex. 1.0 at 22. The AG points out that these accounting treatments are appropriate and essential, but are standard practice and thus of limited value as merger conditions.

Also, the AG points out that the Joint Applicants have not proposed any service quality improvements. Coupled with their failure to create a transition plan for the AMRP, the Joint Applicants' "commitments" will result in a deterioration of service and rate shock, and do not protect the public interest, according to the AG. The AG argues that these Commitments do not go far enough and are, in some instances, practically meaningless.

C. City/CUB's Position

City/CUB note that the Joint Applicants argue that an applicant need only address the listed requirements of subsection (b) of Section 7-204 to gain approval. In support of their position, the Joint Applicants rely on the Commission's 1999 decision in the SBC Merger. Docket No. 98-0555, Order at *26. The Joint Applicants draw from that decision a conclusion that subsection (f) of Section 7-204 has no independent significance, and that meeting the mandatory requirements of subsection (b) has the substantive effect of protecting utility and ratepayer interests as subsection (f) requires. City/CUB state that the Joint Applicants selectively acknowledge and apply the provisions of Section 7-204 and do not acknowledge or properly apply the substantive requirements of Section 7-204(f). As a result, City/CUB argue, the Joint Applicants applied incorrect legal standards, making their evidentiary and legal conclusions flawed.

City/CUB claim that the Joint Applicants' interpretation is unlawful, since their statutory interpretation would completely nullify the legislature's explicit grant of authority to impose conditions necessary to protect the interests of Illinois utilities and ratepayers under Section 7-204(f). City/CUB assert that under binding Illinois Supreme Court precedent, every provision of Section 7-204 must be given substantive meaning. *Kraft, Inc.*, 138 Ill. 2d at 189 ("A statute should be construed so that no word or phrase is rendered superfluous or meaningless.").

City/CUB argue that even if, at one time, the Commission accepted the Joint Applicants' position, the Commission has since recognized its error and abandoned that interpretation. City/CUB cite the Nicor Merger proceeding, in which the Commission examined the statute's meaning and application in some detail. The Commission found that the public interest provisions of Section 7-102 and Section 7-204 provide independent authority that does not depend on, and is not subsumed by, Section 7-204(b)'s list of threshold criteria. *AGL Resources Inc., et al.*, Docket No. 11-0046 (Dec. 7, 2011). The Commission further stated that "Subsection 7-204(f) does not exempt any component of utility operations from its purview." Using its broader Section 7-204(f) authority in that case, the Commission ordered corrective conditions independent of the requirements of Section 7-204(b).

Moreover, City/CUB argue that if commitments are made by the Joint Applicants or conditions are imposed by the Commission, to help meet statutory requirements for reorganization approval, those commitments or conditions must meet additional standards. City/CUB maintain that they must permit effective Commission oversight and compliance enforcement; and define consequences that effectively deter non-compliance. See City/CUB Ex. 4.0 at 23. They argue further that since the required Commission findings must be made in this proceeding -- not at some later date -- the commitment or conditions must be (a) defined and in-place, (b) effective in preventing adverse impacts, and (c) immediately operative. They conclude that if the Commission cannot make the required findings now, the mandated level of protection for Illinois utility and customer interests is not achieved. City/CUB emphasize the timing of the required Commission findings; the Commission must find that the statutory requirements are met now. If terms or conditions that involve future action (whether proposed or imposed) are part of the basis for approval, the Commission must find that the future action is sufficiently clear, certain, and timely that the Commission can make a sustainable finding that statutory requirements (at the specified level of proof) have been satisfied.

D. Commission Analysis and Conclusion

There is an issue with the parties pertaining to the extent of the Commission's authority to impose conditions on the Joint Applicants from other Sections of the Act. This Petition for Reorganization was brought by the Joint Applicants pursuant to Section 7-204. The Joint Applicants argue that the Commission should look only at the requirements of Section 7-204(b). According to the Joint Applicants, this is the only section that should be reviewed in determining this Reorganization. However, subsection 7-204(f) provides that "[i]n approving any proposed reorganization pursuant to this Section, the Commission may impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f). Subsection 7-204(f) does not exempt any component of utility operations from the Commission's consideration of the proposed Reorganization.

The Commission finds that Section 7-204(f) conditions can be used to ensure that the Section 7-204(b)(1)-(7) requirements are, in fact, satisfied post-merger. Section 7-204(f) also provides the Commission with an obligation to impose conditions that it believes are necessary and appropriate to protect the public interest. The Joint Applicants' interpretation of the statute's requirements reads out that portion of Section 7-204 and is contrary to the Commission's interpretation of the Act. The Commission therefore concludes that the power to impose merger conditions extends to all aspects of a utility's operation.

The Joint Applicants made many commitments that were accepted by Staff. These commitments are adopted as conditions to the Commission's approval of the proposed merger and are listed in the attached Appendix. Staff, the AG and City/CUB each request that the Commission impose additional conditions on its approval of the Reorganization in this proceeding pursuant to subsection 7-204(f).

IV. SECTION 5/7-204(b)

> No reorganization shall take place without prior Commission approval. The Commission shall not approve any proposed reorganization if the Commission finds, after notice and hearing, that the reorganization will adversely affect the utility's ability to perform its duties under this Act. In reviewing any proposed reorganization, the Commission must find that:

220 ILCS 5/7-204(b).

A discussion follows of the statutory requirements for approval of the Reorganization and parties proposed conditions on approval of the Reorganization.

A. Section 5/7-204(b)(1)

> the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service;

220 ILCS 5/7-204(b)(1).

1. AMRP

a. Joint Applicants' Position

The Joint Applicants assert that the Commission has determined that with respect to this subsection, "[t]he intention of the statute is to sustain the utility's service quality status quo, not to achieve quality improvements." Docket 11-0046, Order at 13. In particular, with respect to Section 7-204(b)(1)'s required finding, the Joint Applicants note that the Commission has stated:

> Significantly, this subsection focuses on whether the impact of the reorganization will "diminish" [a utility's] ability to provide certain aspects of service, not on whether the merger will improve or enhance those aspects.

Docket No. 98-0555, Order at *48.

The Joint Applicants argue that the record evidence in this proceeding demonstrates that the proposed Reorganization meets the standard set forth in Section 7-204(b)(1). The Joint Applicants state that they have the experience, ability, and financial resources to maintain the Gas Companies' service quality. Wisconsin Energy has a proven track record of successfully managing and operating electric and natural gas utilities, including the implementation and management of large-scale capital programs on time, on budget, and in compliance with applicable laws and regulations. JA Ex. 1.0 at 4, 8, 19-20; JA Ex. 14.0 at 10; JA Ex. 14.1; AG Cross Ex. 8; Tr. at 324, 363-364.

Moreover, the Joint Applicants assert that they have made several commitments designed to ensure continuity in the Gas Companies' service so that the Reorganization will be seamless for Illinois customers. Peoples Gas and North Shore will continue as separate operating utilities, maintain their respective names, and maintain their operating headquarters in Chicago and Waukegan, respectively. The Joint Applicants note that they have committed that there will be at least one non-employee individual resident of Illinois on WEC Energy Group's board of directors, similar to what the Commission ordered in its approval of the AGL Resources Inc. - Nicor Gas ("AGL/Nicor") merger. The Joint Applicants also note that they have committed to honoring the Gas Companies' existing philanthropic pledges and maintaining Integrys' existing levels of involvement in the communities that the Gas Companies serve. The Joint Applicants state that in furtherance of their commitment to the Gas Companies' communities, they have agreed to provide $5 million in shareholder funds over the next five years to Peoples Gas' Share the Warmth Fund, starting with $1 million in 2015.

Further, the Joint Applicants note that they have committed to honoring the Gas Companies' existing labor agreements and maintaining the Gas Companies' existing training programs for at least two years after the close of the Reorganization. Additionally, the Joint Applicants have agreed to continue to support the recent five-year extension, from April 2015, of the Gas Utility Workers Training Program in which Peoples Gas works with the Power 4 America Training Trust Fund, in cooperation with UWUA Local 18007, at the Kennedy-King College's Dawson Technical Institute. Furthermore, in response to a request from the City of Chicago, the Joint Applicants note that they have committed that the Gas Companies will build a new, state-of-the-art training facility in the City of Chicago.

The Joint Applicants assert that they worked to reach agreement with Staff on four additional areas with respect to Section 7-204(b)(1): (1) due diligence concerning

the AMRP, (2) commitments regarding continuation of the AMRP and the implementation of recommendations from the Commission-ordered investigation of the project, (3) capital expenditure commitments, and (4) commitments regarding minimum levels of full time equivalent employees ("FTEs"). The Joint Applicants state that they have presented evidence and agreed to conditions on all of the areas of concern that Staff has with respect to Section 7-204(b)(1) that establish that the Reorganization will not diminish the Gas Companies' service quality. The Joint Applicants emphasize that even with respect to two conditions on which they disagree with Staff concerning the specific language and proper scope of the conditions, there is no disagreement with Staff that conditions should be imposed by the Commission.

The Joint Applicants state that prior to entering into the Merger Agreement with Integrys, Wisconsin Energy conducted the standard due diligence for a transaction of this nature. It assessed the material condition of Integrys, analyzed whether the financial and economic projections are reasonable, and evaluated the business, financial and regulatory risk of Integrys. JA Ex. 6.0 at 14; JA Ex. 8.0 at 12-13. This involved a review of material, non-public financial information and projections, operational data, capital investment plans, and strategic outlooks. The Joint Applicants assert that, as is customary for mergers such as the Reorganization where the intention is for the acquired utilities to remain in current form without any large reductions in force, Wisconsin Energy's pre-merger due diligence did not include investigation into the specifics of the Gas Companies' "on-the-ground" operations, such as detailed work plans for the AMRP. JA Ex. 6.0 at 14; JA Ex. 8.0 at 13; AG Cross Ex. 3.

The Joint Applicants note that Staff, as well as the AG and City/CUB, argue that they should have performed due diligence concerning the details of the implementation and management of the AMRP. During the course of this proceeding, however, the Joint Applicants state that Wisconsin Energy's management reviewed an Interim Report prepared by Liberty Consulting Group which contains preliminary findings and recommendations made during its Phase I investigation of the AMRP that had been ordered by the Commission in Docket Nos. 12-0511/12-0512 (Consol.). The Joint Applicants state that Wisconsin Energy's management agrees with the approach for management and implementation of large capital programs as Liberty outlines in the Interim Report. Management also supports the current commitments and initiatives undertaken by Integrys and Peoples Gas in response to the Interim Report, and it is ready, willing and able to implement the AMRP consistent with Liberty's ultimate recommendations in its Final Report expected to be issued in mid-2015.

The Joint Applicants express their understanding that the AMRP is an important capital project for Peoples Gas that will modernize its distribution system, thereby increasing safety and reliability of service for customers, as well as reduce O&M costs over time and help reduce greenhouse gas emissions. JA Ex. 4.0 Rev. at 8. They explain that the AMRP as planned is a 20-year program in which Peoples Gas intends to complete the replacement of its cast-iron and ductile-iron natural gas mains and service pipes, as well as upgrade its distribution system from a low pressure system to

a medium pressure system and relocate gas meters from inside customer facilities to outside by 2030. JA Ex. 1.0 at 18; JA Ex. 4.0 Rev. at 8.

The Joint Applicants assert that they have made several commitments to address concerns that the Reorganization could impact the continuation of the AMRP, and thereby diminish the level of service Peoples Gas' customers would have received in the absence of the merger. The Joint Applicants have committed to ensuring that Peoples Gas works with the City on the coordination of AMRP and for the Joint Applicants to review and attempt to improve their performance with respect to the AMRP on a continuing basis as work on the project progresses. Additionally, the Joint Applicants assert that Wisconsin Energy reviewed Liberty's Interim Report and it is ready, willing, and able to implement the AMRP consistent with Liberty's ultimate recommendations in its Final Report, in accordance with the procedures set forth in the conditions agreed to with Staff in this proceeding.

The Joint Applicants state that they have agreed with Staff on the language of three conditions originally proposed by Staff that will ensure, post-Reorganization, that the Joint Applicants will continue to work with Liberty on the proper implementation of the recommendations Liberty will make in its final investigation report, as well as report any changes to their implementation after Liberty completes its two-year Phase II verification process ordered in Docket Nos. 12-0511/12-0512 (Consol.). The Joint Applicants note that they have agreed to several conditions that address Staff's concerns that the Reorganization should not interfere with or diminish work that is to be done with respect to implementing recommendations from the report from Phase I of Liberty's investigation. Staff Ex. 2.0 at 17-18; JA 14.0 at 5-6; JA Ex. 6.0 at 15-17; Staff Ex. 9.0 at 8-9; JA Ex. 15.0 at 8; JA Ex. 15.1 REV. at Nos. 9-11.

Furthermore, the Joint Applicants note that commitments and other requirements exist to ensure that the Commission will be kept apprised of progress on the implementation of Liberty's final recommendations on an ongoing basis. Staff will be involved in the implementation process, and there are annual proceedings with respect to Peoples Gas' Rider QIP, Qualifying Infrastructure Plant, in which AMRP investments will be reviewed and thus, to the extent relevant, findings and recommendations from Liberty's Final Report may be considered in those proceedings. The Joint Applicants also note that because the implementation of Liberty's final recommendations will be governed by the conditions agreed to by the Joint Applicants discussed above, the Joint Applicants will be required to file a semi-annual compliance report regarding their progress on satisfying this condition and have such compliance addressed by the WEC Energy Group's CEO in an annual report to the Commission.

The Joint Applicants assert that one area of disagreement they have with Staff is on the wording of a condition with respect to a completion date for the AMRP. Staff has recommended that the Commission impose a condition worded as follows:

> Joint Applicants will reaffirm Peoples Gas' commitment to the Commission in Docket Nos. 09-0166/09-0167 (Consol.)

> to complete the Accelerated Main Replacement Program ("AMRP") by the end of 2030.

In response, the Joint Applicants argue that the problem with this proposed condition is that Peoples Gas did not make a commitment to the Commission in Docket Nos. 09-0166/09-0167 (Consol.) to complete the AMRP by the end of 2030 that it can "reaffirm" in this proceeding. The Joint Applicants assert that, in Docket Nos. 09-0166/09-0167 (Consol.), one of Peoples Gas' witnesses presented various cost-benefit analyses for acceleration of the company's main replacement program, which used three different completion years – 2025, 2030 and 2035 – for purposes of supporting a cost recovery rider. Peoples Gas' witness concluded that a 2030 completion date was the most feasible based on his cost-benefit analysis and used the results of his analysis to show that acceleration of main replacement could provide benefits that would not be outweighed by its costs, so that a cost recovery rider should be granted to support acceleration. Thus, the Joint Applicants aver that Peoples Gas did not make any commitment in Docket Nos. 09-0166/09-0167 (Consol.) to accelerate its main replacement independent of obtaining an automatic cost recovery rider. *Id*. Consequently, the Joint Applicants argue that the wording of the condition sought by Staff here could lead to uncertainty in the future over what, if any, commitment from Docket Nos. 09-0166/09-0167 (Consol.) was reaffirmed in this condition.

The Joint Applicants point out that they submitted testimony from Integrys to show Peoples Gas' current state of commitment to completing the AMRP by 2030. The testimony established that "it remains Peoples Gas' intention, assuming it receives and continues to receive appropriate cost recovery, to complete the AMRP by 2030." JA Ex. 9.0 REV. at 4. Relying on Commission decisions stating that the purpose of Section 7-204(b)(1) is to maintain the status quo and to prevent a reorganization from causing service quality to diminish, the Joint Applicants proposed the following commitment as an alternative to Staff's, asserting that it would maintain this status quo as required by the statute:

> Peoples Gas will continue the [AMRP] assuming it receives and continues to receive appropriate cost recovery, with a planned 2030 completion date.

Because of the potential for future confusion and uncertainty over the meaning and application of Staff's proposed language for this condition, the Joint Applicants urge the Commission to adopt their version set forth above which, they argue, maintains the pre-Reorganization status quo and thus, meets Section 7-204(b)(1)'s requirement with respect to the planned AMRP completion date.

The Joint Applicants state that Staff also sought a commitment from them concerning future levels of capital expenditures for the Gas Companies to ensure that there is no diminishment in their ability to provide adequate, reliable, efficient, safe and least-cost public utility service as required by Section 7-204(b)(1). In response to Staff's concerns, the Joint Applicants note that they have made a commitment to make at least

$1 billion in capital expenditures for Peoples Gas and at least $43 million in capital expenditures for North Shore during the 2015 through 2017 time period, with a running total to be provided in the Gas Companies' semi-annual compliance report to the Commission.

The Joint Applicants maintain that the AG's and City/CUB's arguments are based on an incorrect standard for Section 7-204(b)(1) that would require the Joint Applicants to demonstrate that the Reorganization will result in improvements to existing Gas Companies' operations, namely remedying what the AG and City/CUB witnesses perceive to be problems with the AMRP, in order for the Commission to approve the Reorganization. See, e.g., AG IB at 9; City/CUB IB at 27. The Joint Applicants assert that the AG's and City/CUB's position flies in the face of Section 7-204(b)(1)'s plain language, which the Joint Applicants argue does not require a showing that a reorganization will improve or enhance a utility's service quality.

The Joint Applicants argue that the appropriate forum in which to evaluate the AMRP, determine what issues may exist, and implement corrective actions is the ongoing, two-phase Liberty investigation ordered by the Commission in Docket Nos. 12-0511/12-0512 (Consol.). The Joint Applicants state that the Commission already has established a process and procedure for this investigation in which the Commission's expert consultant will make recommendations and work with Staff and Peoples Gas on their appropriate implementation, which includes a two-year period in which implementation of recommendations will be monitored. The Joint Applicants aver that they have submitted evidence demonstrating that the Reorganization will not disrupt this Commission-established process. The Joint Applicants rely on evidence of the new management's experience in implementing large-scale capital programs on time, on budget, and in compliance with applicable laws and regulations, noting that contrary to suggestions by City/CUB, the evidence demonstrates that Wisconsin Energy has not been found to be out of compliance with the City of Milwaukee's regulations. The Joint Applicants claim that with its experience managing large capital projects, Wisconsin Energy has and will bring a culture of performance tracking and accountability to the AMRP management.

Significantly, the Joint Applicants emphasize that in addition to remaining subject to the Commission's jurisdiction, the conditions they have agreed to with Staff will ensure that Peoples Gas takes action to accomplish the goals of each recommendation in Liberty's Final Report barring agreement with Staff or, if needed, a determination by the Commission, that a particular recommendation would be imprudent, impractical, unreasonable or impossible to implement. Thus, the Joint Applicants maintain that contrary to the AG's and City/CUB's arguments, these conditions are not overly conditioned or weak, but rather a reasonable approach to ensure that recommendations are appropriate and appropriately implemented.

Further, the Joint Applicants assert that they have reviewed Liberty's Interim Report and submitted testimony demonstrating that while its conclusions and recommendations are preliminary, it gave the Joint Applicants an awareness of the

possible scope and scale of the obligations that will be undertaken if the Reorganization is approved. The Joint Applicants state that they are ready, willing and able to implement the AMRP consistent with additional remedies that may be recommended by Liberty. The Joint Applicants argue that in light of the preliminary nature of the Interim Report and it being subject to change, the Commission should give the AG's and City/CUB's arguments made in substantive reliance on findings contained in the document little, if any, weight.

Furthermore, the Joint Applicants contend that the evidence demonstrates that the fact that Wisconsin Energy does not have a transition plan currently completed and in place will not cause any diminishment in the Gas Companies' service quality. The Joint Applicants note that they presented unrebutted testimony from an expert witness who testified that in a merger of this nature, a detailed transition plan typically is not prepared until a month prior to the transaction's closing. Tr. at 364-365; JA Commissioners Data Request Response ("DRR") No. 1. The Joint Applicants explain that Wisconsin Energy does not intend to fundamentally change, interfere with or abandon the initiatives started by current Integrys management in response to preliminary recommendations or expressed concerns from Liberty's Interim Report. JA Ex. 12.0 at 5-6. Moreover, the Joint Applicants aver that the evidence demonstrates that there will be significant continuity in the employees making daily decisions about the Gas Companies' operations. JA Ex. 6.0 at 10. The Joint Applicants' Commissioners' Data Request Response No. 1 shows no intent to "fully replace" current AMRP management, but rather, that there is an expected inclusion of at least three persons from Wisconsin Energy's current management team with extensive experience in natural gas operations and construction as part of Peoples Gas' post-closing senior leadership. The Joint Applicants note that consistent with the Liberty Interim Report's preliminary recommendations, the president of Peoples Gas will be reporting to the top executive of the WEC Energy Group. Further, Wisconsin Energy is currently in the process of reviewing and evaluating the current management and personnel involved with the AMRP and will make decisions regarding their retention and/or role based upon what will be in the best interests of the utility and its customers given the performance and skill-set of those employees to demonstrate that there will be a seamless transition on "Day 1" after the Closing.

The Joint Applicants note City/CUB's assertion that merely because a holding company's management is physically headquartered in a different state, the service quality of its utilities will suffer. The Joint Applicants state that it is not uncommon for the parent company of a utility to be located in a different state, and the residency of its board members or location of its headquarters has no impact on the company's focus on making sure each of its utilities provide high-quality service to their service territories. JA Ex. 6.0 at 10-11. The Joint Applicants further aver that the residency of a utility holding company's board members is not predictive of whether or not the interests of the utility's customers will be protected, and this is especially true in a situation like the present case where the Gas Companies will maintain local headquarters and have local management running the day-to-day operations of the utilities.

The Joint Applicants maintain that the evidence does not support imposing a condition requiring Peoples Gas to participate in the City's "dotMaps" website. The Joint Applicants assert that this proposal has no relation to Wisconsin Energy's acquisition of Integrys, addresses a pre-existing City request of Peoples Gas that is not related to the Reorganization, and is an improper effort to impose an enhancement to Peoples Gas' operations that is contrary to the intent of Section 7-204. Moreover, the Joint Applicants note that they have identified specific concerns which Peoples Gas has previously communicated to the City regarding Integrys' and the Gas Companies' computer systems being incompatible with the Google-based dotMaps website, and customer privacy and data security concerns that putting information into dotMaps would entail. JA Ex. 6.0 at 22; City Group Cross Ex. 1 at 15-16 (DRRs JA City 10.43 and JA City 10.44).

The Joint Applicants oppose City/CUB's and the AG's proposed condition that would require Peoples Gas to provide additional reporting and to improve its performance in six operational categories with financial penalties for failing to improve. These operational categories include adherence to schedule, adherence to budget, change order spending and communication, management reserve spending and budgeting, time to close Field Order Authorizations and Change Orders, and contractor hits on facilities. The Joint Applicants assert that this proposal goes beyond the scope of Section 7-204's purpose, which is to prevent diminishment of service quality or adverse impacts as a result of the Reorganization. The Joint Applicants maintain that City/CUB's proposed reporting and penalty system is aimed at addressing existing problems the City is complaining about with respect to past AMRP and operational performance by Peoples Gas and fails to identify any adverse impact or diminishment of service that otherwise would be caused by the Reorganization.

The Joint Applicants argue that there are specific problems with the additional conditions proposed by the AG and City/CUB. For example, the Joint Applicants note that they presented evidence that the additional reporting requested by the AG and City/CUB is either duplicative of existing AMRP reporting requirements, or would add little value to the massive amounts of information that Peoples Gas already provides to the Commission regarding AMRP, as well as the information already being provided to the City. Thus, the Joint Applicants assert that the Commission should deny the AG's and City/CUB's requests because the Commission already receives or can readily obtain the information at issue.

Further, the Joint Applicants maintain that both the AG's and City/CUB's proposed conditions would create practical problems. The AG's suggested evaluation and scaling of the AMRP with a focus only on "high risk segments" of pipe would lead to inefficiencies and duplication of effort in the project. The Joint Applicants assert that City/CUB's requested condition on the production of Field Order Authorizations and Change Orders within 24 hours of their approval to the CDOT would create unnecessary burdens, and possibly conflict with confidentiality restrictions contractually imposed on Peoples Gas by its contractors. For these reasons, the Joint Applicants assert that it would be best to wait for Liberty to complete its investigation and a

comprehensive implementation of corrective action taken, rather than attempting to impose potentially conflicting requirements on the Joint Applicants before it is issued.

Thus, for these reasons, the Commission should deny this AMRP-related condition requested by City/CUB, as well.

b. Staff's Position

Staff witness Lounsberry proposed seven conditions to determine whether the Joint Applicants' application met the requirement of Section 7-204(b)(1). Staff Ex. 9.0 at 3-7. The Joint Applicants agreed to five of the conditions. JA Ex. 15.1 REV #9; Staff IB, Appendix A, #1; JA Ex. 15.1 REV #10; Staff IB, Appendix A, #2; JA Ex. 15.1 REV #11; Staff IB, Appendix A, #3; Condition #24 from Docket No. 06-0540; JA Ex. 15.1 REV #12; Staff IB, Appendix A, #4; JA Ex. 15.1 REV #13; Staff IB, Appendix A, #5. Staff submits that all of Mr. Lounsberry's conditions must be imposed on the Joint Applicants in order for the Reorganization not to diminish the utility's ability to provide adequate, reliable, efficient and safe and least-cost public utility service. The Joint Applicants did not agree with Mr. Lounsberry's condition for a recommitment by Joint Applicants for Peoples Gas to complete AMRP by 2030.

Staff contends that approval of the petition should be conditioned upon the Joint Applicants recommitting to complete Peoples Gas' AMRP by 2030 and that such a recommitment would be consistent with the Commission's Order in Docket Nos. 09-0166/09-0167 (Consol.). Staff Ex. 2.0 at 13. Without such recommitment, there will be a diminution in Peoples Gas providing adequate, reliable, efficient, safe and least-cost public utility service. According to Staff, the AMRP was ordered by the Commission only for pipeline safety reasons and AMRP's end date should not be extended without giving serious consideration to the pipeline safety implications of an extension. Staff Ex. 8.0 at 8-9.

Staff notes that the Joint Applicants claim Peoples Gas' commitment to AMRP in Docket Nos. 09-0166/09-0167 (Consol.) was to a 20-year program, but dependent upon certain cost recovery. The Joint Applicants argue that the Commission's Order in Docket Nos. 09-0166/09-0167 (Consol.) linked the timeline for AMRP completion with the approval of the Rider ICR cost recovery mechanism. JA Ex. 9.0 at 3. The Joint Applicants assert that because the Illinois Appellate Court held that the Commission lacked the authority to approve Peoples Gas' Rider ICR, the Commission direction for completion of AMRP by 2030 is no longer applicable. *People v. Illinois Commerce Comm'n*, 2011 IL App (1st) 100654.

Staff counters that the Joint Applicants' argument should be rejected. The Order in Docket Nos. 09-0166/09-0167 (Consol.) determined that completion of AMRP by 2030 was necessary and in the public interest. Staff Ex. 9.0 at 11. Having made that determination, the Commission required that Peoples Gas complete the AMRP by the year 2030. *Id*. Only then did the Order authorize Rider ICR to allow Peoples Gas a means to obtain recovery of its AMRP costs. *Id*. According to Staff, the issue of whether there is a need to accelerate replacement of cast and ductile iron mains is and always has been separate and distinct from the issue of the appropriate recovery mechanism.

Staff Ex. 9.0 at 11-12. Staff argues that nothing in the Order in Docket Nos. 09-0166/09-0167 (Consol.) states or even suggests that AMRP's 2030 end date was dependent upon rider cost recovery. Instead, the Order provides that any change from that 2030 end date would require Commission approval. Staff contends that this is not the appropriate case for the Commission to grant that approval.

Staff notes that the Joint Applicants proposed the following commitment regarding this issue:

> Peoples Gas will continue the Accelerated Main Replacement Program ("AMRP"), assuming it receives and continues to receive appropriate cost recovery, with a planned 2030 completion date.

JA Ex. 15.1 REV #5. Staff argues that the Commission should reject the Joint Applicants' commitment because it is not consistent with the Commission's Order in Docket Nos. 09-0166/09-0167 (Consol.) and the Commission instead should adopt Staff's proposed language for this issue. Staff's proposed commitment language is as follows:

> Joint Applicants will reaffirm Peoples Gas' commitment to the Commission in Docket Nos. 09-0166/09-0167 (Consol.) to complete the Accelerated Main Replacement Program ("AMRP") by the end of 2030.

Staff Ex. 9.0 at 15.

Staff mentions as well that the AG does not support a 2030 end date for AMRP and proposes the condition that the AMRP 2030 completion timeline be reassessed. Staff witness Stoller testified that the AG (and other intervenors) ignore the pipeline safety implications of any decision to delay AMRP completion beyond the Commission's mandated 2030 date. Staff Ex. 8.0 at 3. Specifically, the AG ignores the nature of the cast and ductile iron piping materials that lose their strength over time through the processes of graphitization and corrosion. *Id*. at 5. The age of the cast iron, chemistry of the soil around the pipe, electrical current resistivity or conductivity of the soil, stray electrical current presence in the soil, soil moisture and aeration fluctuations, and corrosion rates are factors that all can contribute to unpredictable graphitization rates. *Id*. at 4-5. Both cast and ductile iron are also subject to corrosion which causes the iron pipe in any gas system to become less strong and more brittle. *Id.* Additionally, the congested utility underground in Chicago, combined with the frigid winter climate, causes soil disturbances that only further compromise the integrity of these obsolescent and in some cases, ancient piping materials. *Id*. at 7-8. This confluence of factors has profound public safety implications, potentially compromising the life, health, safety and property of Peoples' customers and those who reside in its service territory. *Id*. And, that risk, while it cannot be precisely quantified, and regardless of how unquantifiable it might be, increases with the passage of time. *Id*. at 8. In Staff's opinion, extending the

end date for AMRP will most certainly increase that risk, and the AG's proposed condition should also be rejected. *Id*. at 9.

c. The AG's Position

The AG argues that the evidence shows that the Joint Applicants do not meet the requirements of Section 7-204(b)(1) because they did not address the problems with Peoples Gas' multi-billion dollar main replacement program. According to the AG, the Joint Applicants marginalized the significance of the AMRP in this proceeding. The AG alleges that the AMRP has been beset by poor management since the Commission approved the program in Docket Nos. 09-0166/09-0167 (Consol.), Peoples Gas' 2009 rate case. The first indication of the extent of the problems with Peoples Gas' project management was identified in Docket Nos. 12-0511/12-0512 (Consol.), the utility's 2012 rate case. The Commission was so concerned about the poor state of the program, it ordered "a two-phase investigation of the AMRP [be conducted] under Section 8-102 of the Act (220 ILCS 5/8-102) ending in a public document report." Docket 12-0511/12-0512 (Consol.), Order at 61. The AG holds that Liberty's AMRP audit (and the Interim Report filed in January, 2015) are the result of the Commission's Order in Docket 12-0511/12-0512 (Consol.).

The AG points out that in response to an AG/City motion to extend the schedule in this case to incorporate the results of Liberty's Interim Report and the Joint Applicants' response to the report, the ALJ issued a ruling requiring the JA (and other parties) to submit supplemental testimony addressing: (1) whether the Joint Applicants are aware of the scope and scale of the potential obligations under AMRP; and (2) whether Joint Applicants are ready, willing and able to implement the AMRP consistent with additional remedies as recommended by the Liberty audit. ALJ Ruling, January 14, 2015. The AG alleges that the JA's supplemental testimony, as well as the other evidence of record, demonstrates that the JA have not shown that they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit." In fact, the AG asserts that the JA have shown a startling lack of concern about a multibillion infrastructure program that has been beset with poor management from its inception and has resulted in substantial cost overruns that threaten to double a typical customer's base rates by 2024. AG Ex. 2.0 at 15. The AG argues that the JA's apparent indifference to remedying the AMRP's many problems has manifested in many ways.

First, and perhaps most important, the AG explains that the JA have no transition plan for assuming ownership of Peoples Gas and oversight of the AMRP. This point was made clear in the JA's Responses to the Commissioners' Data Requests, wherein they admitted that no transition plan has been developed. JA DRR at 2-3. The Commissioners' question on this point sought this information "to ensure a seamless changeover that avoids any diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public service both leading up to and after closing the proposed reorganization, if approved." Notice of Commissioners' Data Request at 2. The AG states that in an apparent effort to excuse their lack of a transition plan, the JA

highlighted a customer outreach program that WEC has initiated in Wisconsin that they say could be made part of the AMRP. JA DRR at 7.

The AG points out that in the last major energy merger case decided by the Commission, the Commission stressed the importance of the transition plans that the Illinois utility and its proposed purchaser had in place so that no "diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public utility service" would occur as a result of the acquisition. The AG states that in the AGL/Nicor merger case, the Commission stressed the significance of the integration planning process the joint applicants in that case conducted. *See* Docket No. 11-0046, Order at 11-12, 13.

Besides the lack of transition plans, the AG maintains that there is another important distinction between the record in this case and the record in the AGL/Nicor merger. In the earlier case, the Commission found that "[a]fter [the] merger, staffing levels will be maintained, generally by the same people in place now." *Id*. at 13-14. In response to the Commissioners' Data Requests in this case, the JA were unable to identify the person or persons who would be responsible for overseeing the AMRP if the transaction is approved. See, e.g., JA DRR at 3, see also Tr. at 84, 256, 314. The JA were also unable to describe the process for evaluating whether Peoples Gas and Integrys employees currently overseeing the AMRP will be retained or replaced. JA DRR at 2-3; Tr. at 214.

The AG states that the Liberty auditors in their Interim Report found that the proposed merger was having an impact on Peoples Gas' efforts to make changes to the AMRP. The AG argues that the witnesses who testified on behalf of JA in response to the ALJ's Ruling that the JA demonstrate in supplemental testimony that they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit" had minimal familiarity with the AMRP. The AG continues that, although Integrys and Peoples Gas are two of the Joint Applicants seeking merger approval, those two entities did not submit supplemental testimony as to whether they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit." The lack of any testimony from Peoples Gas is remarkable, particularly because, as AG witness Coppola testified, "Peoples Gas (1) is the company that is implementing the AMRP now, and (2) will continue to be implementing it post-merger, should the proposed acquisition be approved." AG Ex. 6.0 at 5.

The AG notes that Peoples Gas has stated that the AMRP was the main driver for its need for increased rates in each of its last two rate increase requests. AG Ex. 4.0 at 17. According to the AG, the project's estimated costs have swelled from $2.2 billion in 2009 to $4.6 billion in May, 2013. AG Ex. 2.0 at 6. The AG states that, of note, is that Peoples Gas' May 2013 estimate did not include the cost impact of new City of Chicago regulations scheduled to go effect in January 2014 as well as other factors. *Id*. at 19-20. Thus, the $4.6 billion price tag is likely to increase. AG witness Coppola projected that

the main replacement program will cause the average residential customer's base rates to double from "$555 annually to more than $1,100 per year by 2024." AG Ex. 2.0 at 7.

According to the AG, the Joint Applicants have the burden of satisfying the statutory criteria of Section 7-204 of the Act before the Commission can approve any proposed merger. 220 ILCS 5/7-204. The AG continues that the record evidence is clear that the Joint Applicants failed in presenting the necessary evidence to satisfy that statutory standard. The AG emphasizes that the Commission's analysis of the evidence must begin with the Joint Applicants' admission that they failed to prove that they are ready and able to step into the shoes of Peoples Gas/Integrys to manage the day-to-day operations of Peoples Gas, and in particular to seamlessly oversee the operation and management of the Peoples Gas AMRP. The AG argues that the Commission's assessment of the quality and depth of the acquiring company's due diligence review is directly relevant to its evaluation of claims by WEC that the Reorganization will not adversely affect the utility's ability to perform its duties under the Act. 220 ILCS 5/7-204(b).

The AG submits that whether WEC engaged in an adequate due diligence process has implications for not only shareholders, but also utility customers, whose interest the Commission is charged with protecting. 220 ILCS 5/7-204(b)(1)-(7), (b)(f). As Mr. Lounsberry noted, WEC's claims that the resulting combined company "will strengthen the WEC Energy Group's operating companies, including the Gas Companies (Peoples Gas and North Shore), by integrating best practices in distribution operations, larger capital project management, gas supply, system reliability, and customer service" must be scrutinized by the Commission in light of evidence of whether the JA actually understood the capital investment commitments and problems of the companies they seek to acquire. Staff Ex. 2.0 at 19. The AG argues that the record evidence in this case reveals a troubling lack of due diligence by WEC related to the Peoples Gas AMRP both in terms of a basic understanding of the AMRP as an ongoing infrastructure project within the City of Chicago as well as the past and ongoing problems identified by the Commission and the utility's internal auditors in the operation of the program. JA witness Leverett confirmed this conclusion during cross-examination when he stated, "WEC didn't do a specific examination of the AMRP" as part of its due diligence analysis. Tr. at 177.

Importantly, the AG notes that Staff witness Lounsberry's direct testimony concluded that the Joint Applicants had not met their burden of satisfying Section 7-204(b)(1) of the Act. Staff Ex. 2.0 at 23. The AG notes that AG witness Coppola, who performed a detailed assessment of the Peoples Gas AMRP and concluded, among other findings, that project costs have doubled since originally approved by the Commission in 2010 due to rampant mismanagement, and that the project lacked an overall plan and any sort of cost controls, likewise concluded that WEC failed to conduct due diligence in its bid to acquire Integrys and, in particular, Peoples Gas.

The Joint Applicants responded by arguing that concern about AMRP and other "on the ground" operations before a reorganization is approved "is not customary." JA

Ex. 8.0 at 13. The AG counters that Peoples Gas ratepayers and, indeed, the Commission, are, however, interested in the AMRP capital expenditure plans of a WEC-owned Peoples Gas. In Peoples Gas' 2012 rate case (Docket Nos. 12-0511/12-0512 (consol.), Order at 61) the Commission ordered that an independent audit of the AMRP be conducted in order to identify and remedy integral operational flaws, including the lack of an overall plan for the project, budget or cost controls. From the ratepayers' perspective, the AMRP has been the primary driver in Peoples Gas' constant rate increase requests. In the four years since Peoples Gas initiated the AMRP, it has filed three base rate cases and received approval for increases in rates of $57.8 million, $59.8 million, and $71.1 million. The AG maintains that the largest driver of these actual and proposed rate increases has been the actual and forecasted capital investment and expenses tied to the AMRP.

The AG notes that Mr. Lounsberry, inexplicably went on to testify in rebuttal testimony that he was somehow satisfied that the Joint Applicants now understand the breadth of the infrastructure and operational challenges the AMRP presents to the acquiring company. Staff Ex. 9.0 at 27. He added that the Joint Applicants' commitment to "various conditions," including those related to implementation of the Liberty audit, assuaged him of his early concerns about the quality of the Joint Applicants' due diligence. According to the AG, this change in Staff's position is startling given the importance of the AMRP to Peoples Gas' customer service and rate levels.

Section 7-204(b)(1) requires that the Commission examine WEC's ability to ensure that the proposed merger would not diminish Peoples Gas' ability to provide adequate, reliable, efficient, safe and least-cost public utility service. The AG suggests that whether WEC is able to immediately step into the role of current Peoples Gas/Integrys management – particularly the management team currently overseeing the AMRP – is a critical question for that assessment.

The AG argues that the Commission must not blindly adopt the JA's commitment to complete the AMRP by 2030 – a date that the record makes clear has no validity in terms of safety assessment or law. To do so would not ensure the safety and reliability of the Peoples Gas delivery system and lead to rate shock. Even the current pace has resulted in huge cost overruns and unrelenting rate increases since the AMRP was approved in 2010. The AG asserts that the Commission must require the JA to commit to improving the current operation of the AMRP by reassessing the scale and timeline of the program to a manageable level. In addition, the AG states that the JA must be required to commit to implementing all findings – both Interim and Final – of the Commission-ordered Liberty audit now being conducted. The AG continues that any approval of the merger should be conditioned on the JA committing to the following AMRP improvements:

i. Peoples Gas shall perform a thorough evaluation of the AMRP and scale the program to a level of cast iron/ductile iron replacement and related infrastructure upgrades that is manageable, targets high priority, high risk

segments first, cost- effective, and minimizes the impact on customer rates.

ii. Peoples Gas shall commit to a transparent process of providing annual reports to the Commission, reconciling its actual vs. forecasted AMRP investments, and provide an accounting of financial and non-financial benefits realized from the AMRP to date.

iii. Peoples Gas will present to the Commission an annual, detailed, work plan for the remainder of the AMRP program that shows: (1) the planned infrastructure replacement segments for the upcoming 12-month period and their related cost; (2) the Main Ranking Index ("MRI") of each planned targeted segment; (3) a list of the mains and other infrastructure that are still in need of replacement, along with their respective MRI ranking and projected cost to complete; (4) the total projected annual cost to complete the program and quantity of mains, services, meters and other infrastructure to be replaced and installed; (5) an explanation and detailed corrective action/implementation plan for improved coordination with the City of Chicago permit and public works activities; and (6) a detailed corrective action plan and status report for implementation of the approved final recommendations from the pending outside audit.

iv. Peoples Gas shall credit customers for all construction fines and penalties paid from the beginning of 2011 to date to the City of Chicago, plus any fines and penalties incurred through the close of the merger, that were recovered in base rates or infrastructure riders. The credits could be flowed through Peoples Gas' Rider QIP during a single month or alternatively contributed by Peoples Gas to its "Share the Warmth" fund.

v. Going forward, Peoples Gas shareholders should bear the costs of any such City of Chicago fines and penalties associated with AMRP and other construction activity.

vi. The Joint Applicants shall commit unconditionally to implement all audit recommendations of both the Interim and Final Liberty audit reports.

vii. The Joint Applicants shall commit to fully cooperating with the Commission's investigation into allegations of misconduct and improprieties in the Peoples Gas AMRP (Docket No. 15-0142), and implementing any corrective actions, including customer refunds of AMRP costs deemed imprudent by the Commission, as ordered by the Commission in that and any other docket related to review of the AMRP and Peoples Gas' Rider QIP.

viii. The Joint Applicants shall commit to City of Chicago witness Cheaks' proposed conditions that are designed to revamp Peoples Gas' coordination with CDOT. They include:

- Requiring a weekly, block-by-block schedule of construction activities be given to CDOT and the ICC, provided on a five-year, annual, and monthly basis.
- Requiring that any Field Order Authorizations or Change Orders be communicated within 24 hours to CDOT.
- Requiring the newly formed entity to actively participate in CDOT's dotMaps website in order to better collaborate with all occupants of the Public Way.
- Requiring that Peoples Gas improve their performance in the following categories, with financial penalties for failure to improve that cannot be recovered from Peoples Gas' ratepayers:

  - Permitted timeframe adherence (being on schedule more often)
  - Approved capital and O&M spend adherence (being on budget more often)
  - Change order spending and communication
  - Management reserve spending and budgeting
  - Time needed to close Field Order Authorizations and Change Orders
  - Contractor "Hits" on City facilities.

According to the AG, these conditions will help to ensure both the safety and reliability of the Peoples Gas distribution network and that the impact of the AMRP on future customer rates will be minimized, thereby ensuring least cost utility service in accordance with Sections 7-204(b)(1) and (b)(7).

d. City/CUB's Position

City/CUB argue that the Act's reorganization provisions expressly grant the Commission authority and broad discretion to "impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers," in approving any proposed reorganization. 220 ILCS 5/7-204(f). In addition, City/CUB detail that the Act prohibits the Commission from approving any reorganization that it finds "will adversely affect the utility's ability to perform its duties under this Act." 220 ILCS 5/7-204(b). City/CUB note as well that the Commission is also prohibited from approving a reorganization unless it finds that "the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service." *Id*.

City/CUB emphasize that this is the only proceeding in which the Commission can impose conditions on the continued operation of AMRP, in the context of the proposed Reorganization, to protect the interests of Peoples Gas' ratepayers. In fact, the Joint Applicants concede that the ability of the new owner to manage AMRP

properly is relevant to this proceeding, and that, if left uncorrected, the acknowledged AMRP mismanagement can worsen performance (an expectation that does not satisfy the threshold statutory requirements for approval). Tr. at 328, 329. City/CUB witness Cheaks illustrated the negative public safety, reliability, quality-of-life, and infrastructure coordination impacts that a poorly managed AMRP can impose on Chicago's ratepayers.

City/CUB contend that the proposed Reorganization will change the management and operation of AMRP. Tr. at 137; also Tr. at 151-152, 20-22. The Joint Applicants have stated their intention to change (1) the management responsible for AMRP at Peoples Gas itself, and (2) the parent company's management responsible for AMRP. JA DRR at 3. City/CUB explain the modifications will include changes in lobbyists who influence legislation affecting AMRP, changes in design and engineering personnel who work directly on AMRP, changes in who decides the budgetary and financial aspects of AMRP, as well as changes to policies and procedures applicable to AMRP construction activities. Absent concrete commitments from the Joint Applicants, City/CUB maintain, knowledgeable employees who work on AMRP now may not be the same employees who work on AMRP in the future. In this same vein, Mr. Cheaks testified that it does not "give [him] confidence that Peoples Gas' AMRP will be managed any better than it already is." City/CUB Ex. 3.0 at 914-915.

City/CUB offer that neither WEC nor any other Joint Applicant requested Peoples Gas to provide a detailed work plan of the AMRP as part of its due diligence review. CUB Ex. 3.1 (JA-AG 4.01). WEC has no transition plan for AMRP and "no specific plans at the present time with respect to the use of WEC Energy Group's cash flows for the funding of Peoples Gas' AMRP." CUB Ex. 3.1 (JA-City 2.22). To this point, Mr. Cheaks testified that "[u]nsafe or inefficient implementation could actually harm Illinois ratepayers' interests, if the Commission does not act to compel correction of AMRP deficiencies and to disallow imprudent expenditures." City/CUB Ex. 7.0 at 193-195. Mr. Cheaks continued that "[t]he Audit Report provides strong, unsolicited, and independent support for imposing conditions regarding AMRP performance as a condition of any approved reorganization." City/CUB Ex. 9.0 at 22-24.

City/CUB add that if the Commission fails to act on the Liberty's audit report in this proceeding, it may have to wait until 2020 for the next Peoples Gas rate case before it has the opportunity to act on the cost and service implications of Peoples Gas' response to that report. City/CUB Ex. 9.0 at 24-27. City/CUB state that Wisconsin Energy's witnesses have already admitted their disagreement with some of the findings of the Interim Report. Tr. at 91.

Finally, City/CUB note that while WEC admits that "developing an integrated scheduling approach" appears reasonable and is likely to lead to an increase in efficiency for both AMRP and non-AMRP work, the Joint Applicants have failed to commit to develop such an approach. JA Ex. 13.0 at 132-134. City/CUB submit that the record is replete with instances of poor AMRP management that have already led to construction problems. In order to ensure that Peoples Gas will be able to provide

reliable, adequate, and least-cost service, City/CUB conclude that the Commission should require Peoples Gas to participate in the dotMaps website and provide weekly block-by-block schedules.

e. Commission Analysis and Conclusion

Pursuant to Section 7-204(b)(1), the Commission must conclude whether the evidence supports the finding required by Section 7-204(b)(1) that the impact of a proposed Reorganization will not diminish service quality, not whether the proposed merger will enhance service quality. Thus, it is necessary for the Commission to evaluate whether the service quality of the Gas Companies will be reduced by the proposed Reorganization.

With this standard in place, it is necessary to examine the evidence presented by the Joint Applicants and determine whether the standards have been met. The Joint Applicants have presented some voluntary commitments and have agreed to some conditions as proposed by Staff. The evidence demonstrates that Peoples Gas and North Shore Gas will remain largely unchanged. The Gas Companies will retain their local headquarters and will maintain local management on site. The customers will continue to interact with the Gas Companies as they did pre-Reorganization and will not suffer any disruption of service or adverse impact on the quality of their service as a result of the Reorganization.

The Commission finds that the mere location of the Gas Companies' holding company's corporate headquarters being in a neighboring state does not give rise to any concerns that the interests of the Gas Companies and their customers will be slighted. The management and headquarters of the Gas Companies will remain in Illinois. There has been nothing developed in the record to show that the service quality of the Gas Companies will be impaired by the approval of this Reorganization. The Commission finds that this evidence supports finding that the Reorganization will not diminish the Gas Companies' service quality.

The Commission agrees with Staff that the proposed condition in which the Joint Applicants commit to a minimum amount of capital expenditures will ensure that the Gas Companies continue to make necessary investments in their infrastructure.

Concerning the issue of the AMRP, the Commission agrees with the Joint Applicants that the language of the condition proposed by Staff requiring the Joint Applicants to "reaffirm" Peoples Gas' "commitment" from Docket No. 09-0166/09-0167 would lead to possible problems for AMRP. The Joint Applicants correctly point out that they did not make any commitment in that proceeding that can be reaffirmed here. The Commission directed Peoples Gas to complete this program by 2030 and any change to the completion date requires Commission approval. The Commission will continue to hold Peoples Gas to this condition that any changes will require Commission approval. The Commission expects that Peoples Gas will be attentive to the prudent operation of its system.

However, the Commission agrees with the opinions expressed by Staff and the Joint Applicants in this proceeding that this is not the proper forum for either evaluating or implementing specific corrective action with respect to the AMRP, or examining the ongoing Liberty investigation. Doing so is beyond the scope of a Section 7-204 proceeding, which is focused on maintaining the service quality of a utility's operations, not developing specific improvements to its management and operations. The Commission already has established a process and procedure for an expert evaluation of the AMRP and a process to implement recommendations developed from that evaluation in the two-phase Liberty investigation initiated by the Commission in Docket 12-0511/12-0152 (Consol.), the 2012 Peoples Gas/North Shore rate case. Adoption of the conditions agreed to by the Joint Applicants and Staff for the implementation of the recommendations from Liberty's Final Report and cooperation with Staff and Liberty in the verification process will protect the interests of ratepayers pursuant to Section 7-204(b)(1). The Commission wants to ensure that the Reorganization does not diminish or otherwise interfere with the process established by the Commission with respect to implementation of recommendations resulting from Liberty's investigation. Moreover, the Commission wants an orderly plan for Peoples Gas and Staff to work collaboratively on the appropriate implementation of Liberty's recommendations.

The Commission finds that the evidence supports the conclusion that the Joint Applicants have demonstrated that they will be ready, willing and able to undertake the implementation of the AMRP with the scope and scale of the additional remedies likely to be seen in Liberty's Final Report. The Joint Applicants presented evidence demonstrating that Wisconsin Energy's management has experience operating large capital projects successfully with emphasis on performance tracking and accountability needed for the AMRP. Wisconsin Energy's management reviewed the Liberty Interim Report and demonstrated that it will agree to implement the AMRP consistent with the findings that will be included in Liberty's Final Report. Significantly, Wisconsin Energy expressed its commitment to support and continue initiatives being made now by Peoples Gas to address Liberty's preliminary findings, such that corrective actions that can be made before the Final Report is issued are not being impeded.

Because the preliminary finding and recommendations of the Interim Report are subject to change, the Commission agrees that it should not impose a condition requiring the implementation of recommendations from the Interim Report.

Additionally, the Commission finds that the Joint Applicants are working appropriately towards a transition plan and integration of operations in light of the evidence that there will be significant continuity in the employees making daily operational decisions for the Gas Companies. Wisconsin Energy is actively involved in the process of reviewing and evaluating the current management and personnel involved with the AMRP to ensure that there will be a seamless transition after Closing. The Commission also notes that AMRP would continue to be a major capital works project for Peoples Gas whether this Reorganization took place or not.

Consequently, to maintain the status quo here with respect to Peoples Gas' current commitment to continue the AMRP and the planned 2030 completion date, the

evidence in the record supports adopting the language of the Joint Applicants' proposed condition, which is based upon the current status of Integrys' plans to continue and complete the AMRP:

> Peoples Gas will continue the Accelerated Main Replacement Program ("AMRP"), assuming it receives and continues to receive appropriate cost recovery, with a planned 2030 completion date.

The Commission adopts this condition 5 in Appendix A, as proposed by the Joint Applicants.

The Commission declines to impose a condition requiring Peoples Gas to participate in the CDOT's "dotMaps" website as requested by City/CUB. The Joint Applicants submitted testimony establishing the existence of real technical issues concerning the compatibility of Peoples Gas' computer systems with CDOT's dotMaps system, as well as security concerns, that were not resolved in this proceeding. Moreover, this is the type of enhancement or improvement to a utility's service that is not consistent with Section 7-204(b)(1)'s focus on maintaining the service quality of the utility. Accordingly, we will adopt the language of the commitment offered by the Joint Applicants requiring them to continue to work with CDOT on resolving the outstanding technical and security issues as well as coordinating the AMRP with the City. (Appendix A, Condition #40).

The Commission finds that the various AMRP-related conditions that the AG and City/CUB requested pursuant to Section 7-204(f) are not going to be imposed on the Joint Applicants as part of this Reorganization. As stated above, this major capital project is necessary for Peoples Gas whether the Reorganization is approved or not. The Commission is concerned that imposing additional conditions as proposed by the AG and City/CUB in this docket could conflict with the findings in Liberty's Final Report. The conditions to be imposed on Peoples Gas will be determined from the Final Report. The Joint Applicants have already agreed to comply with the recommendations of the Final Report and pending investigation. The Commission expects the Joint Applicants to honor those commitments.

The Commission, therefore, finds that subject to the conditions (Conditions # 5, 7, 9, 10, 11, 13, 35, 37, 38, 39 and 40) adopted by the Commission as discussed above and in Appendix A, the Reorganization will not diminish either Peoples Gas' or North Shore's ability to provide adequate, reliable, efficient, safe and least-cost public utility service. Accordingly, the Commission finds that the proposed Reorganization satisfies the criteria of subsection 7-204(b)(1) of the Act.

2. Full Time Equivalent Employees ("FTEs")

a. Joint Applicants' Position

The Joint Applicants assert that unlike what occurs in many corporate consolidations, they are not planning a large-scale reduction in force after the close of the Reorganization. Rather, the Joint Applicants state that the vast majority of any reductions in employee headcount are expected to occur over time through attrition, i.e., voluntary decisions by employees to leave the company, such as retirements and voluntary departures. The Joint Applicants aver that this will minimize disruptions to the workforce and the local communities, and will allow the combined company the time necessary to develop, implement and realize the benefits of a prudent integration plan. JA Ex. 3.0 at 33.

To demonstrate their commitment to this approach, the Joint Applicants point out that they proposed an enforceable commitment to maintain a minimum floor-level of employment in Illinois of 1,953 FTEs for at least two years after the close of the Reorganization. The Joint Applicants state that this would include, in the aggregate, the employment levels at the Gas Companies and Illinois-based employment levels at the shared services company, IBS. The Joint Applicants explain that this commitment is not designed to set the target employment levels at the Gas Companies or IBS; actual employment levels at each of Peoples Gas, North Shore, and IBS in Illinois will be determined based upon what levels are needed to provide adequate, reliable, efficient, safe, and least-cost utility service and may, in the aggregate, require more than 1,953 FTEs in Illinois. For the Gas Companies in 2015 and 2016, the target employment levels that the Joint Applicants plan to have in place to provide adequate, reliable, efficient, safe, and least-cost utility service are 1,356 FTEs for Peoples Gas and 177.7 FTEs for North Shore, based upon the FTE levels approved for recovery in rates by the Commission in its final Order in the Gas Companies' most recent rate case in Docket Nos. 14-0224/14-0225 (Consol.).

In response to a proposal raised by Staff and other parties to require a specific minimum FTE level at the Gas Companies that reflects the level of employment approved by the Commission in Docket Nos. 14-0224/14-0225 (Consol.), the Joint Applicants argue that contrary to the reason underlying Staff's proposed language, there is no evidence that the Joint Applicants' proposal would result in a reduction or departure from the FTE levels approved by the Commission for Peoples Gas and North Shore in Docket Nos. 14-0224/14-0225 (Consol.). The Joint Applicants point to their testimony explaining how the 1,953 FTEs level in the Joint Applicants' proposed condition represents an aggregate floor-level commitment below which the overall, aggregate WEC Energy Group headcount in Illinois will not be allowed to fall for two years after the close of the Transaction, and that the 1,953 FTE level does not constitute the intended, forecasted, or targeted level of post-merger employment at Peoples Gas and North Shore. Consistent with the concerns expressed by Staff and other parties, the Joint Applicants state that they have been clear that they fully expect and intend for the FTE levels at Peoples Gas and North Shore to be those approved for the Gas Companies by the Commission in Docket Nos. 14-0224/14-0225 (Consol.) – 1,356 FTEs for Peoples Gas and 177.7 FTEs for North Shore.

Additionally, the Joint Applicants argue that including a specific FTE level for IBS in the condition as proposed by Staff is not required to be consistent with Docket Nos. 14-0224/14-0225 (Consol.) because the Commission did not base its IBS-related cost allocations to the Gas Companies on any FTE level for IBS in the rates it set in that case, but rather, only determined certain labor costs for the Gas Companies based on specific FTE levels. Moreover, the Joint Applicants contend that the language of Staff's proposed FTE condition would alter the nature of the commitment originally proposed by the Joint Applicants. It would remove the requirement that the FTEs at issue be employed in Illinois and limit the flexibility the WEC Energy Group will need to operate its business efficiently to seek savings by reducing potential duplication in the shared services company.

Finally, the Joint Applicants argue that the language Staff proposed for the FTE condition that excludes extra hiring that may be required in response to the recommendations from the Liberty Final Report from the initial FTE commitment could have negative, unintended consequences. The Joint Applicants state that the additional language suggested by Staff presupposes that any Liberty recommendation for the hiring of additional personnel must be in addition to the forecasted 2015 test year FTE levels. The Joint Applicants also aver that it is possible, however, that Liberty could recommend additional hires as a replacement for existing personnel with incorrect or inadequate skillsets, or else propose eliminating certain positions to increase efficiency, leading to the recommendations that, as a whole, provide for no net change in employment levels. Consequently, the Joint Applicants conclude that it would be better to allow the general conditions concerning implementation of final Liberty audit recommendations agreed to by Staff and the Joint Applicants to address all of Liberty's potential recommendations, including those involving the hiring of personnel.

b. Staff's Position

Staff asserts that the number of employees the Joint Applicants will retain after the close of the Reorganization transaction is vital in determining whether the proposed Reorganization will diminish the Gas Companies' ability to provide adequate, reliable, efficient, safe and least-cost public utility service. 220 ILCS 5/7-204(b)(1). Reducing employee levels below the levels approved by the Commission from the Gas Companies' most recent rate case could cause detrimental results for ratepayers. As a condition for approval of the Reorganization, the Commission should require the Joint Applicants to enter into a commitment to retain for two years after the closing of the proposed Reorganization the FTE levels the Commission approved in Docket Nos. 14-0224/14-0225 (Consol.). Related to that condition and commitment, the Commission should order that any recommendations from the Liberty review of Peoples Gas' AMRP that result in additional headcount shall not count toward the existing FTE commitment values.

Staff points out that the Joint Applicants proposed a commitment to maintain 1,953 full time FTE positions in Illinois for two years after the closing of the proposed Reorganization. This proposal, according to Staff, was lacking in clarity for several reasons. First, the Joint Applicants' proposed FTE amounts were an aggregate amount,

not broken out between North Shore, Peoples Gas, and Integrys Business Support. Second, the number of FTEs proposed by the Joint Applicants was not consistent with the projected FTE levels that the Gas Companies forecasted in Docket Nos. 14-0224/14-0225 (Consol.). Finally, the potential exists that the Liberty audit of Peoples Gas' AMRP could result in recommendations to increase staffing levels in some areas of the Company. Staff witness Lounsberry requested the Joint Applicants add that, "Peoples Gas agrees and commits that it shall implement any increased staffing levels recommended by Liberty audit recommendations as an overall increase in the agreed upon FTE levels for Peoples Gas" to address this concern.

In response to the Joint Applicants' statement that their 1,953 FTE commitment is a "floor level" commitment, Staff explains that the Joint Applicants' "floor level" commitments break down to 1,294 FTE for Peoples Gas and 166 FTE for North Shore. Staff Ex. 9 at 17. Significantly, these figures represent reductions of 4.6% and 6.6%, respectively, in Peoples Gas' and North Shore's 2015 forecasted manpower levels from Docket Nos. 14-0224/14-0225 (Consol.). *Id*. Staff states that the Joint Applicants have failed to provide any rationale behind why the Commission ordered levels should be departed from.

Staff argues that the Joint Applicants have never provided any definitive plans for how they will operate the Gas Companies going forward, or what if any staffing level reductions they identified. In fact, Staff argues that the Joint Applicants provided insufficient information to form a conclusion regarding any longer-term effect of the proposed Reorganization. What is known is that the Gas Companies argued in Docket Nos. 14-0224/14-0225 (Consol.) for specific FTE levels, and these are the same levels that the Commission should hold the Joint Applicants to maintain in their proposed FTE commitment language. Finally, Staff's proposed FTE commitment levels for IBS (493 FTEs) equal those originally proposed by the Joint Applicants for IBS when the Joint Applicants' aggregate totals are broken down into the individual components. *See also*, Staff Ex. 9.0 at 21.

c. The AG's Position

The AG avers that the Joint Applicants' employee retention commitment is non-specific and of no value. The commitment, while based on assumed FTE numbers for each Gas Company and IBS, is made in the aggregate, not by company. Further, as Mr. Effron notes, there is no description of how this commitment breaks down between administrative support and front line operational employees. Moreover, Mr. Effron noted that in Docket Nos. 14-0224/0225 (consol.), North Shore and Peoples Gas forecasted 178 and 1,356 FTEs, respectively, for the 2015 test year. The Joint Applicants, in response to Mr. Effron's observation, asserted that these higher headcount numbers "represent the FTEs that will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016." JA Ex. 6.0 at 26. The JA added, however, that the 1,953 FTEs represent "a 'floor-level' of FTEs, below which the post-merger company, WEC Energy Group, will not allow its employment levels in Illinois to fall for a period of two years after the closing of the Transaction." *Id*. at 8-9.

In light of this information, Mr. Effron concluded that "[i]f, as claimed in the rate cases, the Gas Companies really expect to have 178 FTEs for North Shore and 1,356 FTEs for Peoples Gas in 2015, then the Joint Applicants' employee complement commitment in this case has little, if any substantive value, as there is little or no chance that the 'floor-levels' will ever be a factor in the Gas Companies' actual employee headcounts." *Id*. at 9. He noted that if the commitment to maintain designated employee headcounts is to have any value to customers and the Illinois communities the Gas Companies serve, "then further conditions must attach to this commitment." AG Ex. 3.0 at 3.

Thus, in order to provide any value to the WEC employee number commitment, Mr. Effron recommended that the Commission condition merger approval on the proper crediting to ratepayers of any savings due to the difference between the headcounts for the Test Year reflected in the revenue requirements presented by the Gas Companies in Docket Nos. 14-0224/14-0225 (consol.) and the Joint Applicants' employee headcount commitment in the present case. One option recommended by Mr. Effron would be to credit to customers the savings associated with a decreased employee complement post-merger, as compared to the FTE numbers Peoples Gas and North Shore forecasted in the rate case – a number that is reflected in current customer rates. Mr. Effron proposed that the differential in expense associated with these conflicting numbers be returned to Peoples Gas/North Shore customers by means of a rider that would commence at the closing of the Transaction and would continue until the rates in the Gas Companies' next base rate case go into effect. AG Ex. 1.0 at 20. The rider would be no different than any other merger commitment; it would exist because the JA had agreed to implement it to ensure that customers were not financially harmed by the merger, consistent with Section 7-204(b)(1) and (7) of the Act.

As AG witness Effron noted, the Joint Applicants' characterization of the minimum employee headcount commitment as a benefit to customers in the present case is inconsistent with the test-year employee headcounts presented by the Gas Companies in the rate cases as being necessary to provide safe and reliable service. Mr. Effron's rider credit proposal is an effort to give some substance to the Joint Applicants' minimum employee headcount commitment, on a forward looking basis. While the Joint Applicants and Staff complained that the ratemaking prohibition against single-issue ratemaking is triggered by the proposal, it is in fact an effort to resolve the inconsistency that Peoples Gas and North Shore created by forecasting higher FTE numbers in the rate case (thereby maximizing revenues) and the Joint Applicants' commitment in this docket to a lower combined FTE number post-merger – a number that the JA admit is lower than the FTE amount that "will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016." JA Ex. 6.0 at 26. Importantly, it demonstrates that this JA commitment neither ensures the maintenance of existing service quality nor least cost rates, according to the AG.

The AG argues that Mr. Effron's proposal (or a modification of that proposal that captures this revenue difference) should be adopted as a condition of any Commission merger approval, pursuant to Section 7-204(f).

d. Commission Analysis and Conclusion

The Commission finds that the operation of the Gas Companies is dependent upon the necessary support of its employees. There must be adequate levels of staff to ensure that the Gas Companies continue to provide reliable service. It is necessary for the Commission to address the number of employees the Joint Applicants will retain after the close of the Reorganization transaction in determining whether the proposed Reorganization will diminish the Gas Companies' ability to provide adequate, reliable, efficient, safe and least-cost public utility service. 220 ILCS 5/7-204(b)(1). The Gas Companies provided evidence in the recent rate cases as to the number of FTEs that are required to provide reliable service to ratepayers. Reducing employee numbers below the levels approved by the Commission from these recent rate cases could cause detrimental results for customers. The evidence demonstrates that the Reorganization is not based upon and will not involve a large involuntary reduction in the workforce to achieve savings, but rather gradual attrition over time. As a condition for approval of the Reorganization, the Commission will require the Joint Applicants to enter into a commitment to retain for two years after the closing of the proposed organization the FTE levels the Commission approved in Docket Nos. 14-0224/14-0225 (Consol.). Further the conditions agreed to by the Joint Applicants with respect to implementation of recommendations from Liberty's Final Report will ensure that any additional employees that need to be hired are made in addition to any employees currently needed for other functions. Both of the alternatives as proposed by the Joint Applicants are less than what was just approved in the recent rate case. There was no explanation by the Joint Applicants as to why the number of FTEs changed. Accordingly, the Commission will adopt the following language for condition 2 on minimum FTEs:

> Joint Applicants agree to maintain a minimum of 1,356 full time equivalent employees ("FTEs") for Peoples Gas, 177.7 FTEs for North Shore, and 493 FTEs for Integrys Business Support for two years after the close of the transaction. The Joint Applicants also agree to the extent they implement any recommendations in the final report on the Liberty Consulting Company's Accelerated Main Replacement Program ("AMRP") investigation that require the hiring of additional personnel, those additional personnel shall not count toward the FTE values previously identified and the Joint Applicants shall track them separately.

The AG requested that the Commission adopt a rider concerning the level of FTEs to provide proper credit to ratepayers of any savings due to the difference between the headcount approved in the most recent Gas Companies rate case and the Joint Applicants' commitment in this case. Staff pointed out that a rider is only appropriate if the utility cannot influence the cost and the cost does not affect the utility's revenue requirement. Neither condition can be satisfied with a rider related to FTE. Since the Commission agreed with Staff and will adopt their proposed condition, it will not be necessary to consider the AG's proposed rider tied to FTE.

B. Section 5/7-204(b)(2) and (b)(3) and Section 7-101

> the proposed reorganization will not result in the unjustified subsidization of non-utility activities by the utility or its customers;

220 ILCS 5/7-204(b)(2).

> costs and facilities are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes;

220 ILCS 5/7-204(b)(3).

1. Joint Applicants' Position

The Joint Applicants contend that the proposed Reorganization meets the requirements of Sections 7-204(b)(2) and (b)(3). The Joint Applicants state that the Reorganization will not affect the existing relationship between Integrys' shared services company, IBS and the existing Integrys companies, including the Gas Companies. At or shortly after closing, IBS will become a direct subsidiary of WEC Energy Group and be renamed WEC Business Services, LLC ("WBS") and maintain the existing IBS affiliated interest agreements with today's Integrys companies. The Joint Applicants state that it is expected that WEC Energy Group and today's Wisconsin Energy subsidiaries will execute interim affiliated interest agreements that will allow, but not require, these companies to take services from WBS. The Gas Companies will not be parties to those agreements, and thus, Commission approval is not required for those agreements.

The Joint Applicants request approval of a proposed WEC Energy Group Affiliated Interest Agreement ("WEC Energy Group AIA") to be entered into by WEC Energy Group and all of its subsidiaries, including the Gas Companies, that is based upon the existing Integrys Affiliated Interest Agreement approved by the Commission in Docket No. 10-0408 (the "Integrys AIA" or "10-0408 AIA"). The WEC Energy Group AIA will allow services to be provided by Wisconsin Energy companies to Integrys companies, including the Gas Companies, and vice-versa, all pursuant to appropriate contractual requirements, allocation standards and compliance processes. The Joint Applicants note that Staff recommended that the WEC Energy Group AIA should be approved on an interim basis in this docket, to be updated after the completion of the ongoing investigation of the Integrys AIA in Docket Nos. 12-0273/13-0612 (Consol.). The Joint Applicants explain that this is the best approach because this investigation may lead to changes in that agreement being agreed to by the Gas Companies and/or ordered by the Commission.

Further, with respect to issues of non-utility subsidization and allocation, the Joint Applicants assert that the record evidence demonstrates that after the Reorganization, non-utility operations will represent a very low percentage of WEC Energy Group's revenue (1.46%), EBIT (0.09%), assets (1.21%), and operating cash flow (0.47%), and proportionally less than currently exists within the Integrys holding company system. JA Ex. 5.0 at 4-6. The percentages provided are based upon the application of definitions and calculations provided by Wisconsin's public utility holding company statute, Wis. Stat. § 196.795. The Joint Applicants point out the fact that Wisconsin Energy's Elm Road Generating Station and Port Washington generating units and ownership interest in ATC are not considered non-utility affiliates pursuant to this statute. *See* Staff Group Cross Ex. 1 at 3-4.

The Joint Applicants note that Staff recommended that the Commission approve the Reorganization as to Sections 7-204(b)(2) and (b)(3), subject to three conditions, which the Joint Applicants state that they have accepted. The Joint Applicants further argue that the record evidence demonstrates that the proposed Reorganization meets the requirements of Sections 7-204(b)(2) and (b)(3). The Joint Applicants assert that it will not materially change the contractual arrangements in place with respect to the Gas Companies that, where appropriate, have been reviewed and approved by the Commission to ensure that there will not be unjustified subsidization of non-utility activities by the Gas Companies or their customers. Moreover, the allocation of costs and facilities will be done in a manner that will allow the Commission to properly identify them for ratemaking purposes.

In reply to arguments by City/CUB that Sections 7-204(b)(2) and (b)(3) cannot be met because the Joint Applicants have not presented a detailed tracking mechanism, the Joint Applicants state that the evidence demonstrates that City/CUB's arguments are not well-founded. Based on the conditions agreed to with Staff, the Joint Applicants state that they will bear the burden of identifying and tracking transaction costs and transition costs, and in future rate cases they must identify any transaction costs included in the test period and demonstrate that they are not included in the rate case for recovery. Moreover, the Joint Applicants assert that the Gas Companies will only be able to recover transition costs to the extent they can establish that they produce savings. To track and monitor transition costs and savings, the Joint Applicants explain that they will use a spreadsheet model operating in parallel with their existing accounting systems similar to what has been used in other utility mergers. The Joint Applicants further explain that as with other mergers, the model will be multi-layered allowing granular as well as higher-level tracking to occur.

Further, the Joint Applicants argue that while City/CUB's concern is focused on the accuracy of the tracking – i.e., the quantification – of transition costs and savings, Sections 7-204(b)(2) and (3) are concerned with ensuring that costs within the WEC Energy Group holding company system are allocated so as to ensure that the Gas Companies' customers do not unjustly subsidize non-utility activities and that the costs to be included by the Gas Companies in their rates are fairly identified as being proper utility costs. A tracking mechanism for transition costs and related savings will not be the mechanism that makes these allocation determinations. Rather, the Joint

Applicants state that the determination of which costs are appropriately identified as utility activities and the basis upon which any shared transition costs are to be fairly allocated between the WEC Energy Group companies will be done pursuant to the WEC Energy Group AIA, which will apply the same identification and allocation rules and processes as the Commission approved for the present affiliated interest agreement in place for the Integrys holding company system. Accordingly, the Joint Applicants conclude that City/CUB's arguments are inapposite to the determinations to be made by the Commission pursuant to Sections 7-204(b)(2) and (3).

2. Staff's Position

Staff notes that in order to approve the Joint Applicants' Reorganization, the Commission must find under Section 7-204(b)(2) that there is no unjustified subsidization of non-utility activities by the utility or its customers and the Commission must find under Section 7-204(b)(3) that there is a fair and reasonable allocation of costs and facilities between the utility and non-utility activities and the facilities and costs must be identifiable and properly included for ratemaking purposes. *See* 220 ILCS 5/7-204(b)(2), (b)(3).

As part of any reorganization application and as required by the Act, the Joint Applicants requested approval under Section 7-101 and 7-204A for the WEC Energy Group AIA. Application at 25; JA Ex. 2.4. The WEC Energy Group AIA is a two-way agreement that provides the mechanism for charges from Wisconsin Energy companies to Integrys companies, including Peoples Gas and North Shore, and by Integrys companies, including Peoples Gas and North Shore, to Wisconsin Energy companies. The WEC Energy Group AIA includes various reporting and auditing requirements and is based upon the Gas Companies' 10-0408 AIA. *Id*. at 4. The WEC Energy Group AIA and the 10-0408 AIA come into play when addressing the requirements of Sections 7-204(b)(2) and 7-204(b)(3)).

Staff notes that the Commission has a pending investigation in Docket Nos. 12-0273/13-0612 (Consol.) of the 10-0408 AIA. In the Initiating Order for Docket No. 13-0612, the Commission broadened the scope of Docket 12-0273 to consider interactions between the Companies and their affiliates. *Illinois Commerce Comm'n v. North Shore Gas Co., et al.,* Docket No. 13-0612, Initiating Order at 2 (November 6, 2013). Staff maintains that the Commission should approve the plan proposed by Staff (Staff Ex. 6.0 and 12.0) and agreed to by the Joint Applicants (JA Ex. 16.0 at 6) to enable the Commission to make the findings required by Sections 7-204(b)(2) and 7-204(b)(3). Staff states that if the plan and conditions agreed to by Staff and the Joint Applicants are acceptable to the Commission, Staff suggests that specific findings should be included in the Order. As the plan and conditions discussed above are all agreed to by the Joint Applicants, there is no dispute between the two parties with respect to Sections 7-204(b)(2) and (b)(3) and Section 7-101.

3. City/CUB's Position

City/CUB argue that the deficiencies in the readiness and effectiveness of the Joint Applicants' accounting and ratemaking protocols for transition costs, in particular those incurred at proposed affiliates but allocated to Illinois utilities for rate recovery, creates uncertainties that preclude a finding that "the proposed reorganization will not result in unjustified subsidization of nonutility activities by the utility or its customers." City/CUB address this issue further in the discussion in this Order concerning Section 7-204(b)(7).

4. Commission Analysis and Conclusion

In order to approve the merger, the Commission must determine under Section 7-204(b)(2) that there is no unjustified subsidization of non-utility activities by the utility or its customers and must also find under Section 7-204(b)(3) that there is a fair and reasonable allocation of costs and facilities between the utility and non-utility activities and the facilities and costs must be identifiable and properly included for ratemaking purposes. The Joint Applicants request approval under Section 7-101 and 7-204A for the WEC Energy Group AIA. The WEC Energy Group AIA is an agreement that provides for charges between Wisconsin Energy Companies and Integrys Companies, including Peoples Gas and North Shore. The WEC Energy Group AIA includes various reporting and auditing requirements and is based upon the Gas Companies' Affiliated Interest Agreement approved in Docket No. 10-0408. Both of these agreements must be reviewed when addressing the requirements of whether there is unjustified subsidization of non-utility activities by the utility or its customers and whether costs and facilities are fairly and reasonably allocated between utility and non-utility activities and whether those costs and facilities are identifiable and properly included for ratemaking purposes.

The Commission does not agree with City/CUB's arguments that the Joint Applicants need to present a completed, detailed tracking mechanism for transition costs and related savings for the Commission to make the findings under this section. The Commission will impose conditions on the Joint Applicants concerning the allocation of costs and savings resulting from the Reorganization. The burden will be on the Joint Applicants to track those costs and savings and prove them to the Commission before any transition costs can be recovered in future rate cases. This provision protects against any concern that there will be unjustified subsidization of non-utility activities or an inability of the Commission to identify that any transition costs included in rates are properly allocated to a utility activity.

With the conditions proposed by Staff and accepted by the Joint Applicants, the Commission concludes that the Joint Applicants have satisfied the requirements of Section 7-204(b)(2) and (b)(3) of the Act (Appendix A, Conditions # 22, 23, 24, 25, and 26). Additionally, the WEC Energy Group AIA is approved on an interim basis, subject to the conditions accepted by the Joint Applicants, which the Commission hereby adopts.

C. Section 5/7-204(b)(4)

> the proposed reorganization will not significantly impair the utility's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure;

220 ILCS 5/7-204(b)(4).

1. Joint Applicants' Position

The Joint Applicants argue that the evidence demonstrates that after the Reorganization, the Gas Companies will be able to continue funding their operations and raise capital on the same basis as before the Reorganization. After the announcement of the proposed Reorganization, the Credit Rating Agencies reaffirmed the current credit ratings for Wisconsin Energy, Integrys, and their operating utility subsidiaries, including the Gas Companies. Indeed, the Joint Applicants aver that it is anticipated in the long-term that the Gas Companies may have enhanced access to capital as a result of the Reorganization. The Joint Applicants assert that the post-merger capital structures targeted for Peoples Gas and North Shore are the same as those approved by the Commission in Docket Nos. 14-0224/14-0225 (Consol.). The Joint Applicants state that WEC Energy Group will work to maintain those approved capital structures, through equity contributions from the parent company if necessary.

The Joint Applicants note that City/CUB appear to argue that because it is possible that the debt to be incurred by Wisconsin Energy to finance the Reorganization could lead to a downgrade by one credit rating agency – Standard & Poor's ("S&P") – of the Gas Companies' long-term issuer rating, the Commission should find that Section 7-204(b)(4) has not been met. The Joint Applicants argue that this analysis lacks any evidence suggesting that in the event such a downgrade were to occur, it would impair, let alone "significantly impair" the ability of the Gas Companies to raise necessary capital or to maintain a reasonable capital structure. The Joint Applicants state that the evidence shows that S&P did not downgrade the Gas Companies' credit ratings, but rather, indicated that their outlook was "negative" because the debt to be incurred would leave less room for underperformance in S&P's rating model. The Joint Applicants further argue that City/CUB ignore the evidence from the Moody's Investors Service ("Moody's") credit rating agency that kept the Gas Companies' ratings stable and found that the merger overall would allow Wisconsin Energy to benefit from a larger size, complementary operations in Wisconsin, and a more diversified operational and geographical footprint. Accordingly, the Joint Applicants conclude that City/CUB has failed to rebut the evidence presented by the Joint Applicants and Staff that the Reorganization will not significantly impair the ability of the Gas Companies to raise necessary capital.

The Joint Applicants also argue that the Commission should deny City/CUB's and the AG's request for a ring-fence condition on its approval of the Reorganization that limits WEC Energy Group's ability to require the Gas Companies to make dividend payments, or any other cash transfer to WEC Energy Group, before the Gas

Companies fulfill their obligations (both in amount and as to timing) to make distribution system modernization capital improvements. As an initial matter, the Joint Applicants contend that City/CUB's analysis of dividend payments and capital expenditures fails to address how this stated concern, even if accurate, would create any impairment in the ability of the Gas Companies to raise necessary capital. According to the Joint Applicants, the evidence demonstrated that the payment of dividends up from the Gas Companies to the WEC Energy Group would have no impact on the ability of the Gas Companies to raise capital necessary to finance their capital programs. Thus, the Joint Applicants argue City/CUB's requested ring-fence condition, also known as "dividend payout restrictions", is not necessary to protect the interests embodied in Section 7-204(b)(4).

Moreover, the Joint Applicants maintain that there are at least three additional reasons, based on the record evidence, that the Commission should deny City/CUB's proposal. First, the evidence reveals that the Reorganization is expected to result in a stronger more financially stable holding company with both greater financial liquidity and improved access to capital markets. The Joint Applicants assert that the credit rating agency S&P does not expect that the additional debt used to finance the merger will result in WEC Energy Group's inability to maintain its current credit ratings or impact its cash flows. Indeed, City/CUB's witness does not dispute the fact that the Joint Applicants' projections and S&P's outlook suggest that the Joint Applicants will have adequate cash flows both to support their acquisition-related debt and to fund their planned capital improvement programs. The Joint Applicants argue that the original cash flow analysis prepared by City/CUB's witness incorrectly assumed how the acquisition-related debt would be financed and failed to reflect WEC Energy Group's actual cash flows. According to the Joint Applicants, City/CUB's analysis also incorrectly assumes that the only capital available to spend on the Gas Companies' capital programs is internally generated funds, as funds paid to a parent company as dividends can be returned as equity, or external capital markets are available for debt and for the parent company equity.

Second, the Joint Applicants urge the Commission to deny City/CUB's proposal because they have made several enforceable commitments in this proceeding that provide adequate assurance that the Gas Companies will continue investing in their infrastructure as is reasonable and appropriate. In particular, the Joint Applicants aver that they have committed to continue the AMRP, assuming Peoples Gas receives and continues to receive appropriate cost recovery, with a planned 2030 completion date and to spend minimum amounts on capital expenditures for both Peoples Gas and North Shore during the 2015 through 2017 time period. Further, the Joint Applicants assert that their commitments to implement Liberty's final recommendations for improving the AMRP, to ensure Peoples Gas works to coordinate with the City in the execution of the AMRP, and to review and attempt to improve their performance with respect to the AMRP on a continuing basis as work on the project progresses also demonstrate a strong assurance that investment in the AMRP will continue after the Reorganization is closed. The Joint Applicants argue that City/CUB's analysis is flawed

because it fails to address or respond to the question of why such a restriction is necessary in light of these agreed upon conditions.

Third, City/CUB's proposal should be rejected in the Joint Applicants' view because Section 7-103 of the Act provides protection and empowers the Commission to take action to stop a parent company from requiring dividends from a utility that would impair its ability to perform its duty to render reasonable and adequate service, as would occur if WEC Energy Group forced the Gas Companies to make dividend payments to the detriment of their necessary capital investments. The Joint Applicants explain that Section 7-103(2) of the Act prohibits a utility from paying any dividend unless its earnings and earned surplus are sufficient to declare and pay such dividend after provision is made for reasonable and proper reserves, and unless such dividend can be paid "without impairment of the ability of the utility to perform its duty to render reasonable and adequate service at reasonable rates." 220 ILCS 5/7-103(2). Accordingly, the Gas Companies are already subject to provisions of the Act which preclude the types of actions that concern City/CUB and the AG. Additionally, the Joint Applicants further explain that Section 7-103(1) of the Act authorizes the Commission to order a public utility to cease and desist the declaration and payment of any dividend if the Commission finds the utility's capital has or would become impaired. 220 ILCS 5/7-103(1). The Joint Applicants assert that based on their agreement to a condition requested by Staff to file all reports by credit reporting agencies specific to the Gas Companies or WEC Energy Group, the Commission will be kept apprised of information that would allow it to act pursuant to Section 7-103(1) to prohibit dividends from the Gas Companies if their credit and financial situation indicated that they would be unable to fund their capital expenditures adequately.

The Joint Applicants assert that, based upon the record evidence, the Commission should deny the ring-fencing condition proposed by City/CUB and the AG, and find that the Reorganization meets the requirements of Section 7-204(b).

2. Staff's Position

Staff states that the proposed transaction satisfies the statutory requirement of Section 7-204(b)(4) of the Act. S&P's has assigned the Gas Companies an A– issuer rating, indicative of an obligor with a strong capacity to meet its financial commitments. Staff Ex. 7.0 at 4. Moody's has assigned the Gas Companies an A2 issuer rating, which Moody's considers upper medium grade and subject to low credit risk. *Id*. Following the merger announcement, S&P, whose ratings generally reflect a group credit profile, revised the Gas Companies' credit outlook from stable to negative due to the weakened financial measures at WEC resulting from the increased debt used to finance the transaction. Likewise, Moody's, whose ratings reflect a stand-alone credit profile, also notes that "the amount of holding company debt compared to Integrys' consolidated indebtedness will remain significant." However, Moody's apparently does not expect the transaction to have a detrimental effect on the Gas Companies' stand-alone credit profiles, as it maintained the Gas Companies' stable rating outlook.

According to Staff, the Gas Companies might be assigned a lower S&P long-term issuer credit rating than today as a result of the proposed Reorganization, but it will likely be no lower than BBB+. Staff Ex. 7.0 at 6. BBB+ rated utilities, while slightly less creditworthy than an A– utility, still have access to the long-term capital markets on reasonable terms. As such, the effect of the proposed Reorganization on the Gas Companies' long-term credit ratings will not significantly impair their ability to raise necessary long-term capital on reasonable terms.

Additionally, Staff notes that the Joint Applicants intend to maintain the Gas Companies' current sources of short-term debt, including their money pool with each other and Integrys; Peoples Gas' credit facility, which does not expire until June 2017; and Peoples Gas' commercial paper program. Further, it is unlikely that the proposed Reorganization will harm Peoples Gas' commercial paper rating. As such, the proposed Reorganization will not significantly impair the Gas Companies' ability to raise necessary short-term capital on reasonable terms. Thus, Staff states that the proposed Reorganization satisfies Section 7-204(b)(4) of the Act.

In response to the City/CUB dividend restriction proposal, Staff notes that, as a primary benefit of the proposed transaction, the Joint Applicants repeatedly cite their expectation that the Gas Companies will have enhanced access to capital markets on reasonable terms as a result of the scale of the newly formed corporation. Staff concludes that, assuming this emphasis on the benefits of the greater scale of the newly formed corporation is warranted, it would be unnecessary to apply an adjustment to the cost of common equity in future rate cases on the basis of the Gas Companies' relatively small size. Thus, Staff recommends that the Joint Applicants commit to not seek recovery of any costs related to time spent by witnesses on the development or presentation of cost of common equity size adjustments in future rate cases. Staff Ex. 7.0 at 17-18. Staff and the Joint Applicants were able to reach agreement on a modified version of that commitment. JA Resp. to Staff DR MGM 5.06; Staff IB, Appendix A, #24.

Finally, with respect to the Joint Applicants' argument that City/CUB witness Gorman's proposed condition to restrict dividends is unnecessary, as the Commission already is empowered to restrict dividends by Section 7-103 of the Act, Staff notes that, unlike Mr. Gorman's proposal, the authority granted the Commission under Section 7-103 is not preemptive. Therefore, Staff recommends that, if Mr. Gorman's proposed condition is rejected, the Commission should require the Joint Applicants to file copies of all credit rating agency reports for the Gas Companies and WEC Energy Group within five days of publication, so that the Commission can act on its authority under 7-103 in a timely manner should those reports indicate a deterioration in the companies' creditworthiness. Staff Ex. 13.0 at 6-7. Staff and the Joint Applicants were able to reach agreement on a modified version of that condition. JA Resp. to Staff DR MGM 5.05; Staff IB, Appendix A, #25. Nonetheless, Staff is not taking any position on Mr. Gorman's proposal to condition dividends on AMRP targets.

3. The AG's Position

The AG supports City/CUB witness Gorman's recommendation that should the Commission approve the merger, a dividend ring-fencing provision should be a condition of the approved Reorganization. While the Joint Applicants reject the need for any "ring-fence" protections to ensure that the Gas Companies are able to fund their planned capital improvements before sending money up to the corporate parent for shareholder dividend payments, City/CUB witness Gorman viewed them as essential. The AG agrees and support this as a necessary condition to merger approval to protect the interests of both of the Gas Companies, particularly Peoples Gas, given its AMRP commitment in the City of Chicago.

4. City/CUB's Position

City/CUB note that the financing structure of the Joint Applicants' proposed Reorganization will result in a significant increase in the amount of debt for the parent company, WEC Energy Group. It is uncontested that the financing plan accommodates the premium above prevailing book value that WEC agreed to pay to acquire Integrys' common stock. WEC Energy Group will take on $1.5 billion of acquisition debt to fund the purchase. City/CUB note that the cash to service that debt will come from its utility subsidiaries, including Peoples Gas and North Shore. City/CUB Ex. 4.0 at 13. City/CUB aver that the analysis of whether ratepayers are at risk of adverse rate impacts includes consideration of the utility's access to capital and its other obligations due to existing and future debt. *Illinois Consol. Tel. Co.*, Docket. No. 02-0502, Order at 25-26 (December 17, 2002).

City/CUB state that Peoples Gas and North Shore currently access capital markets on reasonable terms. Prior to the announcement of the proposed Reorganization, City/CUB note that S&P had assigned the Gas Companies an A- issuer rating (strong capacity to meet financial commitments, but somewhat more susceptible to adverse circumstances than higher rated entities), and Moody's had assigned the Gas Companies an A1 issuer rating (upper-medium grade and subject to low credit risk). However, state City/CUB, following the announcement of the proposed Reorganization in June 2014, S&P revised its forward-looking credit outlook for the Gas Companies from "stable" to "negative." S&P cited expectations that "the incremental debt associated with this transaction will weaken WEC's financial measures," and indicated that the credit ratings of the Gas Companies will be aligned with that of their new parent (WEC Energy Group). CUB Cross Ex. 3, JA MGM 1.15 Attach 02 at 3, 5-6; *see also* Staff Ex. 7.0 at 5. Further, note City/CUB, S&P elaborated that the consolidated company could fall into the "weaker end of our 'significant' financial risk profile…leaving little cushion for underperformance relative to our forecast." *Id*.

City/CUB point out that Fitch Ratings ("Fitch") had a similar response. Fitch placed WEC on "Rating Watch Negative" the day following the proposed Reorganization announcement, going as far as to say that "[g]iven WEC's projected incremental leverage and pending acquisition of Integrys, a positive rating action is unlikely in the near to immediate term." CUB Cross Ex. 3, JA MGM 1.15 Attach 03 at 1-2. Fitch further noted that regulatory actions like rate freezes as a reorganization approval condition could lead to negative rating actions. City/CUB elaborate that Fitch stated that

the merger would result in a "meaningful increase in consolidated leverage compared to WEC's current and projected pre-acquisition financial position," and noted its additional concern about the "aggressive dividend policy adopted by management." *Id*. Fitch added that it "expects leverage metrics of the combined entities to be weak for the current rating category and significantly weaker than WEC's stand-alone credit profile." *Id*. at 2. Similarly, note City/CUB, Moody's changed its rating outlook for WEC from stable to negative following the proposed Reorganization announcement, though they have not yet revised their outlooks for the Gas Companies. CUB Cross Ex. 3, JA MGM 1.15 Attach 01 at 1.

City/CUB state that the most recent financial press available prior to the evidentiary hearing in this case, UBS Reports -- an equity analyst on which Joint Applicant witness Reed relies (Tr. at 419, 430) -- considered the investment risks of WEC. In that report, dated February 12, 2015, UBS stated, with regard to the industry in general, "We expect cost-cutting and strategic planning to be a theme across both regulated and competitive companies… We believe utilities with high parent leverage will disproportionately suffer, as they are unable to recoup from rising interest rates." CUB Cross Ex. 2 at 2. City/CUB aver this analyst expectation directly applies to the proposed Reorganization, as WEC intends to fund the Reorganization transaction by significantly increasing its debt obligations at the corporate level and its only source of cash to service the acquisition debt will come from its utility subsidiaries (including Peoples Gas and North Shore). City/CUB Ex. 4.0 at 12, 13. Mr. Reed agreed that interest rates are indeed expected to rise in coming years. Tr. at 418. Thus, state City/CUB, the warning from the UBS Report applies here – where there is high parent leverage and rising interest rates. At worst, then, the Gas Companies' ability to access capital on reasonable terms is likely to be negatively impacted. At best, state City/CUB, cost-cutting measures that are harmful to the Gas Companies' ratepayers appear inevitable.

City/CUB point out that, the Joint Applicants' own witness, Mr. Scott Lauber, acknowledged that the credit rating agencies downgraded their outlooks for WEC following the proposed Reorganization announcement, (JA Ex. 5.0 at 9), but the Joint Applicant's Initial Brief emphasizes only that the current, pre-Reorganization credit ratings were affirmed. *See* JA IB at 24. Likewise, argue City/CUB, Joint Applicant witness Reed noted the ratings agencies outlook downgrades in his testimony, but that information is also missing from the Joint Applicants' arguments in brief. See JA Ex. 3.0 at 24-26.

City/CUB argue that the Joint Applicants have not proposed any Reorganization terms or conditions that would alter those cost of service (and rate) dynamics, or that would provide the statutory level of protection to Illinois utility ratepayers. City/CUB aver that the Joint Applicants' proposed financial commitments (Commitments 27-34) do not provide the certainty ("will not") or low risk ("not likely") that the statute requires. Some of the proposed commitments impose vague restrictions of uncertain meaning and effect. *See* Commitment 27 ("to the extent they existed prior to the entry of the final order"); Commitment 28 and 29 (prohibitions on loans and guarantees, but only to "non-

utility affiliates"). The others serve mainly to require that the Joint Applicants file reports or studies with the Commission. *See* Commitment 30 and 31 ("shall file"), 32 ("shall present"), 33 ("should . . . be presented"), and 34 ("shall be filed"). City/CUB maintain that, since the Commission may be unwilling or unable to act in a timely manner to prevent the Section 7-204(b) harms noted, the required statutory findings depend on future independent actions of entities not involved in the Reorganization, thus, the threshold requirements for approval are not met.

City/CUB contend that there is real risk that the proposed WEC Energy Group will be forced to extract additional cash from its utility affiliates, above and beyond what has been proposed in this case, if cash flow is not realized as projected by the Joint Applicants. City/CUB Ex. 4.0 at 13; City/CUB Ex. 8.0 at 13. Aside from the negative impacts on the Gas Companies' costs of capital, such additional withdrawals could negatively impact the Gas Companies' ability to fund important capital projects, including critical system modernization and improvement plans. *Id*. City/CUB argue that, given the credit rating agency outlooks and the Joint Applicants' failure to provide any evidence regarding the existence or significance of any negative effects, the Commission cannot find, at this time, that the Reorganization will not significantly impair the Gas Companies' ability to raise capital. City/CUB aver that the Reorganization should be denied as failing to meet the statutory criteria of 7-204(b)(4).

City/CUB witness Gorman suggests that, if the proposed Reorganization is approved, "ring-fence protections" (also known as "dividend payout restrictions") should be adopted to assure that utility cash flows will be used first to avoid diminished utility service, before paying dividends to serve parent company financial obligations. Specifically, Mr. Gorman recommended that dividend payouts of Illinois utilities should be restricted if Illinois utilities do not fulfill their obligations (both in amount and as to timing) to make capital improvements to their distribution systems. City/CUB Ex. 4.0 at 21-22, City/CUB Ex. 8.0 at 7. This would ensure prioritization of the Gas Companies' ability to fund capital programs, which enhance system safety and reliability, above funding the acquisition-related debt created by this proposed Reorganization. City/CUB Ex. 4.0 at 22. Otherwise, say City/CUB, Illinois ratepayers will be less protected from the effects of this proposed Reorganization than Wisconsin ratepayers, and less protected than they are currently. *Id.*

City/CUB point out, as an initial matter, that WEC is a holding company, completely dependent for its debt coverage on the ability of its subsidiaries to pay amounts to WEC through dividends or other payments. City/CUB Ex. 4.0 at 14. WEC currently pays public dividends to its shareholders. Post-Reorganization, WEC has indicated its intention to pay increased dividends per share at the same time that it will also have to pay the debt service (principal and interest) on the $1.5 billion of new reorganization debt. *Id*. If WEC requires its utility subsidiaries to pay up higher dividends to cover increased obligations, the cash flow available for those utilities' modernization investment and service operations is reduced. *Id*. at 15; also Tr. at 133-134, 137. City/CUB aver that, if the dividend payments from Peoples Gas, specifically, are

increased, reduced funds available for Peoples Gas' system investment could delay implementation of the necessary and Commission-required AMRP.

Alternatively, as the Joint Applicants witness Mr. Reed suggests, Peoples Gas could go to the market for external debt to fund AMRP. However, state City/CUB, that alternative could erode their credit rating and increase its cost of debt. Such adverse effects on the utility's financial position would preclude satisfying the threshold Section 7-204(b)(4) requirements, and the resulting harm to the ratepayers who will have to pay increased capital costs in rates would violate the Section 7-204(b)(7) criterion. *Id*. at 15.

City/CUB witness Gorman assessed whether the projected level of dividend payouts from the utilities to WEC could support both WEC's increased dividend payouts and service on the Reorganization debt service, under the proposed Reorganization. Mr. Gorman compared the forecasted level of utility dividend payments up to WEC (post-merger) with the amount of cash WEC needs to (1) pay its public dividends and (2) service the $1.5 billion acquisition-related debt. City/CUB Ex. 4.0 at 15. WEC will also have to service parent company debt that existed prior to the merger, meaning that WEC's incremental Reorganization debt service will have to be funded from new subsidiary payments. Even when Mr. Gorman's very conservative assessment left that consideration out of his analysis, thus understating the pressure on WEC's utility subsidiaries for cash flow, the analysis shows a persistent need to extract more in payments from the utilities. *Id*. at 15-16. City/CUB argue that, since the Commission cannot find that the proposed Reorganization financing "will not diminish" the utilities' ability to meet its statutory service obligations, the proposal presents an unlawful risk that bars approval.

City/CUB point out that the Joint Applicants' current dividend projections already assume that the Illinois utilities will pay out more of their earnings as dividends than they currently do—a projected total of 89% of their earnings. For Peoples Gas, that is in comparison to an average of 59% of their earnings over the past five years. City/CUB note that such dividend payouts leave less internal cash available to the Gas Companies to support their own needs, such as critical capital investment programs, including AMRP.

Moreover, argue City/CUB, the danger of service-affecting cash extractions is greater for Illinois utilities than for other utility subsidiaries. S&P, Moody's, and Fitch have all remarked on the magnitude of WEC Energy Group's increased financial obligation following the merger and on the fact that WEC Energy Group's only source of cash will be its utility subsidiaries. However, the Public Service Commission of Wisconsin has the authority to restrict Wisconsin subsidiary utility payouts in the form of dividends if certain financial metrics are not met. City/CUB point out that Illinois has no comparable regulatory mechanism in place. Fitch observed that the credit ratings of the Wisconsin utilities will be unaffected, because "[r]egulatory restrictions regarding upstream dividend distributions to WEC provide some level of credit protection and mitigate contagion risk to the utilities from higher leverage at the parent." CUB Cross Ex. 3, Att. 03 at 1. As the ratings agencies have noted, WEC Energy Group's level of post-Reorganization debt will be so great that under-performing projections will require

more from the utility subsidiaries. *Id*. at 21. Thus, say City/CUB, Illinois subsidiaries could be in the position of shouldering an even greater burden when Wisconsin subsidiaries and their customers are protected by dividend restrictions and -- absent Mr. Gorman's proposed reorganization approval conditions -- Illinois companies and customers are the principal remaining source of cash.

City/CUB note the Joint Applicants' suggestion that their proposed commitments make Mr. Gorman's proposal unnecessary. The Joint Applicants' financing experts identified those commitments as the proposed AMRP commitments, "most specifically Commitment No. 5." City/CUB respond that the proposed Commitment No. 5 is a conditional, unmeasurable promise to "continue the Accelerated Main Replacement Program ("AMRP"), assuming it receives and continues to receive appropriate cost recovery." Additionally, say City/CUB, the Joint Applicants' capital investment commitments are only effective for three years – 2015 through 2017, a small fraction of the remaining AMRP implementation period. The Joint Applicants' commitment to implement recommendations in Liberty's Final Report is also heavily conditioned (recommendation will be implemented if it is possible, practical, reasonable, cost-effective, as determined by Peoples Gas). City/CUB acknowledge that the Joint Applicants commit to cooperate with Staff, but only to the extent that "cooperation" meets their 82-word definition. They commit to provide reports regarding any change in implementation of the recommendations in Liberty's Final Report, but only to the Commission – not to the essential stakeholder, the City of Chicago. City/CUB point out that the Joint Applicants' commitment to "review and attempt to improve" their AMRP performance is without a single metric or benchmark. Clearly, say City/CUB, the commitments cited by the Joint Applicants as purportedly obviating the need for ring-fence provisions do not provide anywhere near the level of assurance of continued infrastructure improvement investment as Mr. Gorman's proposals.

Moreover, City/CUB note that the statutory provision in the Act authorizing the Commission to limit the payment of dividends is not adequate to ensure that system improvements for safety and reliability are given higher priority than parent-company dividends. First, the Commission may order a utility to cease and desist payment of dividends only if the Commission finds that the capital of a utility has (effectively) already become impaired. 220 ILCS 5/7-203(1), (2). If a wholly owned utility subsidiary is compelled to pay out dividends despite not meeting any of the statutory requirements, this provision becomes operative. Though the utility is required to give the Commission at least thirty days' notice if it plans dividends while under financial stress, no notice is required if the utility does acknowledge that the dividend would trigger the Section 7-203 constraints. In either case, note City/CUB, Staff's finance expert testified that the extraordinary assessment required to support a Commission order stopping the dividend payments would likely take longer than the brief period provided by the notice. City/CUB maintain that dividend restrictions in the Act only protect the financial integrity of a utility during specifically defined periods of financial distress, and even that protection may not be timely.

In sum, City/CUB aver that, as a condition of any Commission-approved reorganization, funding for the Gas Companies' capital programs should be prioritized over dividend payments up to WEC Energy Group, in a clear commitment with defined and enforceable consequences for violation. To the extent that the Gas Companies' obligations regarding system modernization capital programs are not met, City/CUB contend that the Gas Companies' dividend payouts should either be limited or eliminated. The dividend restrictions, which would prevent dividends that compromise infrastructure investment in the first instance, should remain in effect as long as the Qualifying Infrastructure Plant rider program is in effect. City/CUB emphasize that the safety and reliability of the Gas Companies' distribution systems should be prioritized over dividend payouts to the out-of-state parent company.

5. Commission Analysis and Conclusion

Under Section 7-204(b)(4) of the Act, the Commission must find that "the proposed reorganization will not significantly impair the utility's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure." The burden is on the Joint Applicants to show that this is the case. While there are some questions concerning the credit ratings of the various companies, overall the Commission finds that the Joint Applicants satisfy this requirement.

The Joint Applicants agreed to conditions, including Staff's proposal requiring the filing of credit reports specifically concerning the Gas Companies or WEC Energy Group. (Appendix Conditions # 34 and #45). The Joint Applicants also agreed to the conditions in connection with Section 7-204(b)(1) discussed above with respect to minimum capital expenditures and implementation of recommendations from Liberty for the AMRP. The Commission concludes that Peoples Gas' and North Shore's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure will not be significantly impaired by the Reorganization.

Section 7-103 of the Act provides the Commission with the authority to restrict the payments of dividends and since the Joint Applicants agreed with Staff to file reports from all credit agencies reports within 10 days, the Commission does not feel it is necessary to adopt City/CUB witness Gorman's proposed condition to restrict dividends. There has not been a sufficient showing that the ring-fence provision requested by City/CUB and the AG is necessary for the protection of the public utility or its customers with respect to the ability of the Gas Companies to raise necessary capital on reasonable terms. The Commission finds that City/CUB's and the AG's request for the ring-fence provision is not required especially in light of the enforceable conditions requiring that such investments will be made to which the Joint Applicants already have agreed. Therefore, the ring-fencing provision as requested by City/CUB and the AG will not be imposed as a condition of the Reorganization.

Accordingly, the Commission finds that the proposed Reorganization satisfies the criteria of Section 7-204(b)(4) of the Act.

D. Section 5/7-204(b)(5)

> the utility will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities

220 ILCS 5/7-204(b)(5).

1. Joint Applicants' Position

The Joint Applicants argue that the unrebutted evidence is that under the proposed Reorganization, the Gas Companies will remain separate Illinois public utilities regulated by the Commission and remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities. Accordingly, the Joint Applicants assert that the Commission should find, based on the evidentiary record, that the proposed Reorganization complies with Section 7-204(b)(5) of the Act.

The Joint Applicants challenge City/CUB's requests in its Initial Brief that the Commission impose a number of energy efficiency-related conditions on the Reorganization under the auspices of Section 7-204(b)(5) that had been the subject of City/CUB testimony unrelated to this provision. The Joint Applicants maintain that City/CUB fail to explain how forcing the Joint Applicants to engage in conduct beyond what is required under the legislatively prescribed energy efficiency measures provided in Section 8-104 of the Act (220 ILCS 5/8-104), would be consistent with the requirement in Section 7-204(b)(5) that the Gas Companies remain subject to the laws and regulations governing Illinois public utilities. While City/CUB cite to Docket No. 04-0299 (*FairPoint Communications*, Docket No. 04-0299, Order (May 26, 2004)) in apparent support of its position, the Joint Applicants state that this citation is confusing because nowhere in this Order did the Commission impose a reorganization condition pursuant to Section 7-204(b)(5) of the Act. Indeed, the Commission's Order in Docket No. 04-0299 reflects only a finding by the Commission that the requirement of Section 7-204(b)(5) was met by testimony similar to that provided by the Joint Applicants in this proceeding. The Commission's decision in Docket No. 04-0299 thus does not support City/CUB's request for energy efficiency conditions pursuant to Section 7-204(b)(5). Rather, the Joint Applicants argue that it supports the position of the Joint Applicants and Staff that the Commission should make the finding required by Section 7-204(b)(5) based on the evidence presented in this proceeding.

As the Joint Applicants discuss in connection with the standard for Section 7-204 and with respect to Section 7-204(f), the conditions imposed on a proposed reorganization should be "of a type necessary to protect the interests of the company and its customers consistent with the interests outlined by Section 7-204(b)." Docket No. 98-0555, Order at 98-99. The Joint Applicants assert that none of the energy-efficiency conditions proposed by City/CUB in this proceeding bear any relationship to the interests identified in Section 7-204(b). The Joint Applicants assert that the evidence is unrebutted that the Gas Companies presently are in compliance with the

energy efficiency requirements of Section 8-104 of the Act, and there is no evidence that this will change after the Reorganization. The Joint Applicants state that they have no plans to change the Gas Companies' energy efficiency programs. Regardless of their ultimate owner, the Gas Companies will be bound to both follow the statutory requirements of Section 8-104 of the Act and the Commission's final Orders approving their energy efficiency plans.

Furthermore, the Joint Applicants aver that the record evidence supports denying the proposed conditions for additional reasons. With respect to the request for an additional $10 million in shareholder funding for additional energy efficiency programming, the Joint Applicants argue that the proposal would be contrary to the comprehensive statutory requirements in Section 8-104 of the Act for gas utility energy efficiency programs, and it likely would create a situation where the statutory program and the "extra-statutory" program sought by City/CUB would compete or conflict with each other. Critically, the two previous Commission decisions relied upon by City/CUB to support the notion that the Commission has imposed conditions with respect to funding energy efficiency programs, both pre-date the legislature's enactment of Section 8-104. Consequently, the Joint Applicants contend that while City/CUB rely on the fact that there was a voluntary agreement by utilities in the reorganization that created Integrys in Docket No. 06-0540 to implement and fund an energy efficiency program, City/CUB ignore the fact that at that time, neither Section 8-104 nor any other state-mandated energy efficiency programs existed. Also, the Joint Applicants note that the energy efficiency program that resulted from Docket 06-0540 allowed cost recovery pursuant to a rider mechanism.

With respect to City/CUB's request for the Gas Companies' On Bill Financing ("OBF") programs to be expanded, the Joint Applicants state that Peoples Gas is expanding the range of weatherization measures that will be eligible for OBF. However, the Joint Applicants contend that Peoples Gas cannot unilaterally expand the program as requested by City/CUB to allow customers with lower credit scores to participate because the credit requirements for the program are contractual in nature and set by third-party financiers not under Peoples Gas' control (or the Commission's jurisdiction). The Joint Applicants explain that the credit score to be applied by the financier when it assesses loan requests is stated in the contract and the financier has a statutory obligation to conduct credit checks or undertake other appropriate measures to limit credit risk. Further, if higher risk customers are allowed to use OBF, the Joint Applicants assert that Peoples Gas' other customers ultimately may have to pay more through increased amounts under Peoples Gas' uncollectible expense rider. Also, while Peoples Gas could terminate its contract with its current financier, there is no assurance that a new entity source would be willing to negotiate terms allowing for lower credit scores to be accepted.

With respect to City/CUB's proposed condition requesting the development of a study regarding the potential costs and benefits of a third-party administrator, the Joint Applicants argue that this request is based upon an incorrect factual assumption that the Gas Companies have an incentive to deliver more natural gas. The Joint Applicants

assert that the Gas Companies have full, symmetrical decoupling in place through its Rider Volume Balancing Adjustment ("Rider VBA") and thus do not have any throughput incentive to reduce their energy efficiency goals. Moreover, such a study would be applicable to all gas utilities, not just the Gas Companies, so requiring them to incur the expense and burden of developing the report would be unfair.

Finally, the Joint Applicants aver that the proposed conditions to require the development of an energy usage database for use in helping building owners comply with the City's energy "benchmarking" ordinance and to work with the City and researchers to create a database of the customers' usage patterns not only would be burdensome on Peoples Gas, requiring a significant investment of IT resources, but is unnecessary because Peoples Gas already makes the necessary information available to building owners and managers. The Joint Applicants state that Peoples Gas continues to explore ways to assist building owners and managers in complying with the requirements of the City's benchmarking ordinance, but it is the building owners and managers who have the obligations under this ordinance.

Accordingly, based on the evidentiary record and the foregoing reasons, the Joint Applicants recommend that the Commission reject the various energy efficiency conditions requested by City/CUB and find that the proposed Reorganization complies with Section 7-204(b)(5) of the Act.

2. Staff's Position

Staff notes that the Joint Applicants state that Peoples Gas and North Shore will each remain Illinois public utilities following the Reorganization and will, therefore, remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities. Application at 21. Additionally, Section 7-204(b)(5) of the Act is explicitly addressed in the direct testimony of Mr. Leverett, President of Wisconsin Energy Corporation, who states that Peoples Gas and North Shore will retain their current names, will continue to operate as Illinois public utilities in their current service areas, will retain their current Illinois headquarters, and will continue to be subject to Commission jurisdiction and applicable Illinois law and regulations. JA Ex. 1.0 at 16. Staff finds the Joint Applicants to meet the requirement of Section 7-204(b)(5) of the Act. Staff Ex. 1.0 at 7.

3. City/CUB's Position

City/CUB note that under Section 7-204 of the Act, the Commission has conditioned approval of a reorganization on the commitment of Peoples Gas and North Shore to propose $7.5 million of energy efficiency programs. City/CUB also observe that the Commission has conditioned approval of a reorganization on a requirement that the subject utilities ensure certain specific funding levels for energy efficiency. City/CUB also note that the Commission has issued its own report making clear that the Commission has an active role, even in non-Energy Efficiency Portfolio Standards ("EEPS") proceedings, to contemplate the effect on energy efficiency of its various orders.

City/CUB argue that, as a condition of any approved reorganization, the Commission should require:

- an additional contribution of $10 million in energy efficiency programming funded by Wisconsin Energy's shareholders
- changes to the Gas Companies' OBF programs to allow more ratepayers to access the program and to fund a greater number of measures
- the creation and maintenance of an electronically accessible energy use database for aggregated, building-level energy use
- the creation of an updatable database of actual usage patterns for all of the Gas Companies' ratepayers; and
- the issuance of a public report examining the costs and benefits of implementing energy efficiency programming through a third party.

City/CUB Ex. 3.0 at 40-53.

City/CUB witness Weigert asserts that Peoples Gas and North Shore can achieve greater savings, even within the budget constraints of the legislation by pursuing more energy efficiency programming. City/CUB point out that the proposed Reorganization "presents the possibility that the excess of ratepayer contributions over delivered utility programs will become just another revenue stream flowing out of Chicago to the proposed acquiring company." City/CUB Ex. 2.0 at 122-124. City/CUB note that it is discretionary whether to use EEPS funds to achieve additional savings and how to achieve those additional savings once reduced EEPS targets have been met. City/CUB Ex. 6.0 Rev. at 56-59. Even with Rider VBA intact, City/CUB argue, the Joint Applicants have not rebutted the fact that demand drives additional investment in the gas distribution infrastructure on which the utility earns a mandated return and that removing a disincentive against lowered consumption is not the same as incentivizing additional energy efficiency savings. *Id*. at 163-167. City/CUB observe that the record contains no indication that Wisconsin Energy, after approval of a reorganization, will be more inclined (than Peoples Gas has been) to honor the aims of Section 8-104 and use all the funds collected from Peoples Gas ratepayers for effective programs to reduce energy use and to lower bills.

City/CUB also note that low participation has been a problem for Peoples Gas' OBF program. City/CUB observe that the Commission has indicated that it shares the concern around low participation and looks forward to ways to address that problem. *Illinois Commerce Comm'n vs. Commonwealth Edison Co., et al*, Docket. No. 11-0689, Order at 7 (May 15, 2013). City/CUB argue that given the extraordinarily low rate of loss (less than 1 percent), Peoples Gas' OBF program should be expanded to include those ratepayers who may not qualify based on their credit history but may qualify based on their bill payment history. City/CUB Ex. 2.0 at 311, 314. City/CUB conclude that the Gas Companies have more than enough precedent to request the changes Ms. Weigert recommended.

City/CUB observe that while Peoples Gas created a system earlier this year to offer basic aggregate energy usage data for buildings, it is only partially automated and does not offer the year round functionality of ComEd's Energy Usage Data System ("EUDS"). *Id*. at 236-238. The manual process in place today, which requires a user to wait up to a week for data, requires input, time, and effort of actual personnel, note City/CUB. City/CUB Ex. 6.0 Rev. at 172-174. Thus, City/CUB argued, the Joint Applicants should be required to offer a ComEd EUDS-like system to access aggregated natural gas usage data for buildings that is fully automated, timely, and offers billing quality data and which includes full technical support. In addition, City/CUB argued, the Joint Applicants should be required to work with the City and its academic research partners to create an ongoing, updatable database of actual natural gas usage data that protects the privacy of ratepayers.

City/CUB also argue that the third party administrator model of energy efficiency removes the overarching disincentive to reduce energy use and allows the administrator to champion and implement programs that will be successful in reducing overall energy use. City/CUB Ex. 2.0 at 189-191. A third-party administrator would maximize reductions in energy use, would align closely with the common goals defined by the General Assembly for the gas EEPS and the recent decisions of the Commission to encourage greater energy efficiency, City/CUB observe. *See* Docket No. 13-0550, Order at 26-27, 64. Thus, argue City/CUB, the Commission should order that that the Joint Applicants fund a study of the potential costs and benefits of third party administration of Peoples Gas and North Shore EEPS programs. City/CUB note that Illinois ratepayers deserve no less than Wisconsin ratepayers in terms of effective energy efficiency initiatives.

4. Commission Analysis and Conclusion

Section 7-204(b)(5) provides that the Commission must find that "the utility will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities."

The evidence of record, including the conditions agreed to by the Joint Applicants, establishes that the Reorganization will not affect Peoples Gas' or North Shore's status as an Illinois utility and that it will remain subject to all applicable laws, regulations, rules, decisions, and policies governing the regulation of Illinois utilities. Accordingly, based on this undisputed evidence, the Commission finds that the Reorganization will satisfy the criteria of Section 7-204(b)(5).

City/CUB request that a separate energy efficiency program be funded by WEC Energy Group. There is no provision in Section 7-204(b)(5) for the Commission to impose an additional requirement to establish such a program. This request may well be in conflict with the Gas Companies' compliance with Section 8-104. It is undisputed that the Gas Companies are in compliance with the requirements of Section 8-104 and the Commission assumes they will remain in compliance. That is what Section 7-204(b)(5) requires. Further, City/CUB requested that a database be required of Peoples Gas to assist building owners and managers with compliance issues related to an

ordinance particular to the City of Chicago. This requirement would only pertain to Peoples Gas, as the distribution company for the City, and not other Illinois utilities. This requirement will not be placed on the Joint Applicants. City/CUB also requested that more applicants be accepted under the OBF program. Since these programs are financed by third-party vendors, the Commission cannot force a third-party financier to accept OBF applicants with lower credit scores and doing so likely would impose additional costs on other customers. Thus, the Commission will decline to adopt the energy efficiency conditions requested by City/CUB.

E. Section 5/7-204(b)(6)

> the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction;

220 ILCS 5/7-204(b)(6).

1. Joint Applicants' Position

The Joint Applicants argue that they have presented evidence that the Reorganization is not likely to have any significant adverse effect on competition in the markets over which the Commission has jurisdiction. The Joint Applicants state that the Reorganization will cause no changes to the Gas Companies' tariffs or programs offering retail choice to their customers. Moreover, in response to concerns raised by intervenor RESA, the Joint Applicants note that they have committed to maintain the Gas Companies' existing large and small volume transportation programs in substantially the same form as they exist now for at least two years after the close of the Reorganization, to reinstate intraday nomination rights in Rider P of their rate schedules, and to discuss additional matters of interest with RESA post-merger. The Joint Applicants assert that they also reported in their Reply Brief that they had reached a settlement in principle with RESA, which includes commitments and provides further structure with respect to the actions to be taken and/or discussions to be had.

The Joint Applicants note that none of the parties argued that the Reorganization fails to satisfy the criteria of Section 7-204(b)(6). Thus, the Joint Applicants urge the Commission to find that the proposed Reorganization complies with Section 7-204(b)(6) of the Act.

2. Staff's Position

Staff notes that the relevant markets which the Commission needs to be concerned with are not just the gas markets but rather all competitive retail utility markets in the state, which include gas and electric. Staff Ex. 4.0 at 5. The Commission must consider any effect this Reorganization might have on any retail electric markets in Illinois or retail gas markets in other utility service territories. *Id*. A significant adverse impact on competition "would likely increase the ability of a firm or firms in the market to, all else equal, increase prices above costs." *Id*. A review of the Joint Applicants'

testimony and response to data requests reveals that the proposed Reorganization is not likely to have a significant adverse effect on competition. Staff recommends that the Commission find that the Joint Applicants have met the requirement of Section 7-204(b)(6) of the Act. *Id*. at 4.

3. Commission Analysis and Conclusion

The Commission is required to determine under Section 7-204(b)(6) of the Act whether the proposed Reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction. It is necessary for the Commission to look at the potential effect of this proposed Reorganization on all of the utilities in Illinois. Staff has reviewed the evidence in the record, the conditions agreed to by the Joint Applicants and have indicated that the proposed Reorganization is not likely to have a significant adverse effect on competition in Illinois. The Commission also approves the conditions agreed to between the Joint Applicants and RESA. (Appendix # 42, 43 and 44). No other party commented on this section. Accordingly, the Commission finds that the proposed Reorganization satisfies the requirements under this section of the Act.

F. Section 5/7-204(b)(7)

> the proposed reorganization is not likely to result in any adverse rate impacts on retail customers.

220 ILCS 5/7-204(b)(7).

1. Joint Applicants' Position

The Joint Applicants state that the evidentiary record in this proceeding demonstrates that the proposed Reorganization meets the requirements of Section 7-204(b)(7). The Joint Applicants have committed that they will not seek to recover any portion of the "acquisition premium" Wisconsin Energy is paying to acquire Integrys in the Gas Companies' base rates, nor the amortization of the premium in future cost of service determinations. Nor will the Joint Applicants seek the recovery of any transaction costs incurred in connection with the execution of the Reorganization. The Joint Applicants explain that transaction costs are the costs associated with executing the transaction at issue, such as banker's fees, legal fees, or severance costs incurred as a result of the transaction (i.e., executive change-in-control payments as identified in an SEC Form S-4). Further, the Joint Applicants have committed that they will not seek any change in the base rates set by the Commission for the Gas Companies in Docket Nos. 14-0224/14-0225 (Consol.), to be effective any earlier than two years after the Reorganization is closed. The Joint Applicants assert that the evidence demonstrates that in the long-term, five to ten years after the close of the Reorganization, the Reorganization will generate 3% to 5% net savings in non-fuel O&M costs compared to what the Gas Companies' non-fuel O&M costs would have been absent the Reorganization. The Joint Applicants also state that there could be long-term reductions in the Gas Companies' debt costs as the Reorganization may enhance the

Gas Companies' access to capital due to the larger size of the combined holding company.

Additionally, the Joint Applicants state that Staff recommended several conditions to mitigate against the potential effects that a credit downgrade of Wisconsin Energy might have (i.e. increased debt costs) if such a downgrade were to occur after the close of the Reorganization. As modified and clarified through negotiations with Staff, the Joint Applicants have agreed to the conditions as requested by Staff. *See* Appendix A, Conditions 27, 28, 29, 30 and 32.

The Joint Applicants assert that the AG's and City/CUB's argument that continuing the AMRP as planned will cause rates to increase does not undermine the evidence showing that the Reorganization is not likely to cause adverse rate impacts. The Joint Applicants aver that the Intervenors' argument is flawed because it is not the Reorganization that is causing rates to increase, which is what Section 7-204(b)(7) addresses, but rather, the AMRP itself. The Joint Applicants believe that the AG's and City/CUB's complaint is with the AMRP as it has existed prior to the Reorganization proposal, and that they are trying to use the reorganization approval process as a forum to make changes to the AMRP.

The Joint Applicants state that with respect to the pace of the AMRP, contrary to the AG's suggestion, Wisconsin Energy has committed only to continue the AMRP on the same basis as Peoples Gas' current pre-existing plan. This entails continuing the AMRP with the intention of completion by 2030, assuming it receives and continues to receive appropriate cost recovery. *See* JA Ex. 15.0 at 9. Thus, the Joint Applicants argue that if the Reorganization is approved, this maintenance of the status quo with respect to the planned completion date of the AMRP will not cause rates to be impacted any differently than if there was no Reorganization. Accordingly, the Joint Applicants state that the AG's and City/CUB's arguments should be rejected and the Commission should find, based on the record as a whole, that the Reorganization will meet the requirements of Section 7-204(b)(7).

The Joint Applicants assert that there is no evidence that the Reorganization is likely to cause the Gas Companies' costs of capital to increase due to higher debt costs. The Joint Applicants state that S&P putting the Gas Companies' credit ratings on a "negative" outlook does not mean that their S&P credit ratings are certain to fall, or even that such an occurrence is likely. The Joint Applicants emphasize that Section 7-204(b)(7)'s standard does not require that the Joint Applicants must prove that there is no "possibility" of a rate increase, only that an adverse rate impact is not "likely." The Joint Applicants aver that when the S&P outlook information is examined with the whole of the record, the evidence supports the conclusion that a credit downgrade is not likely, and, if one occurs, then an adverse rate impact resulting from that downgrade is not likely. The Joint Applicants highlight the fact that another credit rating agency - Moody's - kept the Gas Companies' ratings stable and found that the merger overall would allow Wisconsin Energy to benefit from a larger size, complementary operations in Wisconsin, and a more diversified operational and geographical footprint. Further, the Joint

Applicants state that there is significant evidence that there likely could be long-term reductions in the Gas Companies' debt costs as the Reorganization may enhance the Gas Companies' access to capital. City Group Cross Ex. 1 at 6 (DRR JA City 2.21 sub. (b)(iv)). In the event of a credit downgrade by S&P, the Joint Applicants assert that the conditions put in place by agreement between the Joint Applicants and Staff will work to prevent increased costs of debt from likely having an adverse impact on the Gas Companies' rates.

The Joint Applicants assert that City/CUB's arguments regarding the Joint Applicants' mechanism for tracking transition costs being likely to cause an adverse rate impact are unfounded and should be rejected. The Joint Applicants assert that City/CUB unfairly extrapolates a statement about when two of the Joint Applicants' witnesses talked about how to respond to a data request on treatment of hypothetical transaction costs and savings (Tr. at 408-409) into a conclusion that the Joint Applicants had "neglected" the development of a process for the tracking of transaction costs and related savings. The Joint Applicants state that they had described their model for tracking transition costs and savings in their testimony, describing how the Joint Applicants will use a spreadsheet model operating in parallel with their existing accounting systems similar to what has been used in other utility mergers to track transition costs and related savings. As used with other mergers, the model to be used will be multi-layered allowing granular as well as higher-level tracking to occur.

The Joint Applicants state that transition costs will have no impact on rates unless and until there is a rate case in which a transition cost is approved for recovery by the Commission. Before that can happen, the Joint Applicants assert that they must bear the burden of proving to the Commission's satisfaction that: an identified transition cost has been incurred (or, for a future test year rate case, that like other costs it is based upon a reasonable forecast); that the cost is prudent and reasonable; and that the transition cost has generated savings equal to or greater than the cost being recovered. These obligations are based on conditions agreed to by the Joint Applicants with Staff. *See* Conditions #17, #19, and #21 (numbering is from Appendix A).

Moreover, the Joint Applicants aver that City/CUB's concern also is unfounded because the Joint Applicants will not seek to recover any transition costs that are incurred prior to the test year for the first post-reorganization rate cases, which must provide for no increase in rates to be effective earlier than two years after closing of the Reorganization. *See* Tr. at 405-406.

The Joint Applicants have committed that they will not to seek any change in the base rates set by the Commission for the Gas Companies in the final Order of their recent rate cases issued on January 21, 2015, as modified by the Commission's February 11, 2015 Second Amendatory Order in that proceeding, to be effective any earlier than two years after the Reorganization is closed. The Joint Applicants state that City/CUB's and AG's requests to extend this period for up to five years is unfounded and should be rejected for four main reasons.

First, the Joint Applicants state that the purpose of the Commission's evaluation of a proposed reorganization under Section 7-204 is not to create benefits or other enhancements in a utility's service quality before approving a reorganization Rather, the standard under Section 7-204 is that the Commission should make the required findings and approve a reorganization if it will at least maintain the utility's status quo and not diminish or adversely impact the utility's service quality or rates. Accordingly, the Intervenors' stated reasons for this proposed modification are not appropriate grounds for the Commission to impose a condition under Section 7-204. *See* Docket No. 11-0046, Order at 77 (conditions should protect interests to maintain the status quo, not enhance those interests).

Second, the Joint Applicants aver that while Intervenors rely upon Peoples Gas' Rider QIP as a reason why the Gas Companies could withstand a longer period before seeking to increase their rates, their analysis fails to account for the fact that North Shore does not have a Rider QIP or any other means to recover capital expenditures between rate cases. Moreover, Intervenors fail to account for the cap in Rider QIP recoveries that can only be reset by the filing of a rate case.

Third, the Joint Applicants state that Intervenors' analysis fails to account for how various updates to CDOT's regulations have led to dramatic increases in the costs of performing operational work on Peoples Gas' facilities in the City. These increases have caused a significant amount of costs that Peoples Gas will incur in 2015 but will be unable to recover in the rates set in Docket Nos. 14-0224/14-0225 (Consol.) due to the timing of the City's regulations being updated. Because these costs are operational in nature, they are not recoverable under Rider QIP.

Finally, the Joint Applicants state that an extended commitment not to seek a change in base rates is unnecessary and not the vehicle by which customers may derive benefits from the Reorganization. The Joint Applicants expect that there will be net savings, over time, as they integrate their management, systems and operations, and these savings will be reflected in future rate proceedings for the benefit of Illinois customers by way of reduced operating expenses or lower capital costs.

2. Staff's Position

Staff states that it is not clear whether the Gas Companies' costs of capital are likely to increase because of the proposed Reorganization, but that it is certainly possible. Staff Ex. 7.0 at 9. Specifically, as a consequence of the proposed Reorganization, the Gas Companies' credit ratings have been assigned a negative rating outlook from S&P. *Id*. If their credit ratings are ultimately downgraded, it would lead to higher capital costs, which would have an adverse impact on rate payers. *Id*. at 10. In order to mitigate the effects of a potential credit rating downgrade of WEC, Staff and the Joint Applicants agreed to conditions on approval. *See* Appendix 27, 28, 29, 30, 32. Staff asserts that with these conditions, the Joint Applicants' proposal will satisfy the requirements of Section 7-204(b)(7) of the Act, and the Commission should apply those conditions to any approval of the proposed Reorganization.

3. The AG's Position

Both Staff and the Joint Applicants propose that the Joint Applicants commit, as part of the proposed Reorganization, to complete the AMRP by 2030. The Joint Applicants add the caveat that the commitment be conditioned on "appropriate cost recovery." The AG alleges that this commitment would virtually ensure that Peoples Gas' rates will continue to increase at the alarming rate that persists currently - and will continue to do so without any guarantee that the 2030 date will ensure the safety and integrity of Peoples Gas' distribution system.

The AG states that when the Commission originally ordered the AMRP in Docket Nos. 09-0166/09-0167 (Consol.), the Commission first approved the institution of an infrastructure cost recovery rider known as Rider ICR for purposes of supporting an accelerated main replacement program for Peoples Gas' pipelines. The Commission then approved Peoples Gas' proposed AMRP and required completion of the program by 2030 - an end date that Peoples Gas had proposed in an effort to secure approval of the rider.

The AG argues that the Commission's directive to have Peoples Gas complete the AMRP by 2030 was made only in the context of approving Rider ICR. Rider ICR was overturned by the Appellate Court in 2011. *People ex rel. Madigan v. Illinois Commerce Comm'n*, 2011 IL App (1st) 100654 at 42 (Sep. 30, 2011). According to the AG, the Commission recognized that the 2030 completion date was no longer operative in its next rate order for Peoples Gas, Docket Nos. 12-0511/12-0512 (Consol.), in which it noted Peoples Gas' lack of progress on the AMRP, and it ordered an investigation to determine the "shortest reasonable time" in which the AMRP could be completed.

The AG asserts that the record is clear that if Peoples Gas were to now follow through on a goal of completing the AMRP by 2030, the effect on residential customer rates would be large and financially burdensome for Chicago residents. Calculations by AG witness Coppola in this case show that, if a 2030 completion date for the AMRP is assumed, the incremental contribution of AMRP costs - including rate base effects and Rider QIP recovery - to the typical residential customer bill will reach $529 by 2023 (up from $10 in 2011 and $180 today). AG Ex. 2.0 at 28-29. The AG notes that for context, a typical residential customer's annual Peoples Gas bill as of 2013 includes around $555 related to base rates. *Id*. at 28. The AG states that no Joint Applicant witness refuted Mr. Coppola's findings.

The AG argues that both Section 7-204(b)(1) and Section 7-204(b)(7) of the Act are salient in evaluating whether the Commission should order a commitment to the 2030 completion date. Subsection (b)(1) requires that a reorganization not diminish a utility's ability to provide (inter alia) least-cost service; subsection (b)(7) requires that a reorganization be not likely to result in any adverse rate impacts for retail customers. The AG notes that as Mr. Coppola's findings show, a re-commitment to the 2030 completion date would scale the AMRP far beyond Peoples Gas' capabilities, requiring it to expand its construction activities at a runaway pace that, if history is any guide, will lead to large cost overruns. The AG argues that Peoples Gas is not currently

conducting the AMRP on a pace anywhere close to completing the work by 2030 and has shown no plans in this proceeding for how it might cost-effectively accelerate its pace of activity commensurate with such an ambitious goal. The AG further suggests that it was, in part, Peoples Gas' poor track record over its first two years of AMRP activity in 2011 and 2012 that led the Commission to order the Liberty audit in Docket Nos. 12-0511/12-0512 (Consol.). Thus, the AG argues that if this reorganization is approved and if it entails a re-commitment to the 2030 completion timeline, accelerating the pace of the project over that of the status quo would lead to severe rate impacts for retail customers, violating the reorganization approval standard of Section 7-204(b)(7).

The AG avers that the 2030 date was originally selected somewhat arbitrarily in Docket Nos. 09-0166/09-0167 (Consol.) without any consideration of optimizing safety or minimizing the effect on customer rates. Staff witness Lounsberry admitted during cross-examination that neither he nor anyone at Staff had conducted an analysis of how the 2030 would impact customer rates. Tr. at 566-567. The AG argues that the Joint Applicants' promise to resurrect the 2030 AMRP completion date without a realistic assessment of whether that date is achievable would have clear, adverse rate impacts on Peoples Gas retail customers - a phenomenon Section 7-204(b)(7) prohibits for any merger applicant.

The AG argues that the Joint Applicants' proposal to complete AMRP by 2030, subject to appropriate cost recovery is a harbinger of the rate shock to come should the Commission approve their proposed AMRP completion date. The AG sought to clarify the meaning of "appropriate cost recovery" through discovery and cross-examination to identify exactly what circumstances would cause the JA's proposed commitment to be effective. The AG notes that in discovery, Mr. Schott stated that, after Rider QIP expires after 2023 pursuant to Section 9-220.3 of the Act, appropriate cost recovery could come through rate case filings, but that "[w]hat the appropriate cost recovery is in future years remains to be seen." AG Cross Ex. 1 at 1. As the AG observes, when invited to clarify the precise type of rate case treatment he was referring to, Mr. Schott stated in cross-examination only that he did not feel comfortable answering a question about events nine years hence. Tr. at 98-99. The AG alleges that putting aside the inappropriateness of saddling both Peoples Gas and its ratepayers with constant rate increases in order to achieve the unsupported 2030 deadline, the Commission should not approve a merger with an ambiguous condition whose predicate has not been clearly defined.

The AG alleges that the evidence shows that Peoples Gas simply has been unable to manage an AMRP with a 2030 completion date, and a condition in this proceeding that requires a resumption of that goal would violate the statutory requirements of maintaining least-cost service and causing no adverse retail rate impacts. 220 ILCS 5/7-204(b)(1), (b)(7). AG witness Coppola concluded in his direct testimony that "[t]he scale of the AMRP seems to have overwhelmed the utility's resources." AG Ex. 2.0 at 20. The AG further notes that after reviewing the Liberty Interim Report, Mr. Coppola concluded that the "lack of proper on-site management of the program, the hesitancy on the part of senior level management to make decisions

about the organization and structural changes to the program, compounded by cost overruns and delays in completing scheduled projects, all point to an inability to complete the AMRP by 2030." AG Ex. 5.0 at 15.

The AG notes that Mr. Coppola also observed that holding the Joint Applicants to a 2030 completion date for the AMRP will not "achieve completing the program 'at the lowest reasonable cost' - one of the listed goals of the Liberty audit examination." *Id*. The AG also notes that as Mr. Coppola noted in testimony, the Liberty Interim Report does not mention anywhere in its pages a goal of completing the AMRP by 2030. AG Ex. 5.0 at 15-16. According to the AG, the Commission-hired auditors have not thus far recommended any acceleration of the AMRP to a 2030 completion timeline, and the Commission should not second-guess the auditors by imposing such a condition.

The AG alleges that while the Joint Applicants have stated repeatedly that they will commit to complete the AMRP by 2030 (with "appropriate cost recovery"), they have not explained how they matched that goal with the Section 7-204 statutory standards. The AG notes that as JA witness Schott agreed in cross-examination, an effectively managed AMRP should minimize the impact on customer rates. Tr. at 95. The AG states that Mr. Schott, Chief Financial Officer of Integrys Energy Group, stated during cross-examination that (using his example) near-term customer rates would be lower when $100 million is prudently spent in a given year on capital expenditure, compared to capital expenditure of $200 million (Tr. at 104-105), and he agreed generally that the annual rate of AMRP investment increases customer rates in the near term. Tr. at 105-106.

The AG notes that despite this correlation, JA witness Lauber, who is Vice President and Treasurer of WEC, stated during cross-examination that WEC did not ask Peoples Gas or Integrys to calculate a rate impact associated with different AMRP completion timelines. Tr. at 462. Similarly, as the AG notes, Mr. Leverett, President of WEC, stated that neither he nor any other JA witness had performed any recent analysis or assessment to conclude that the 2030 completion date is still feasible and achievable in a cost-effective manner for ratepayers. Tr. at 221. Additionally, as Mr. Coppola found, "there is no evidence that the Joint Applicants have performed the due diligence necessary to understand the infrastructure investment rate involved in achieving that [2030] deadline [and] the impact on customer rate." AG Ex. 2.0 at 30.

According to the AG, in light of the General Assembly's statutory mandate in Section 7-204(b)(7) of the Act to consider retail rate impacts, it is difficult to see how the Commission could approve this proposed Reorganization with a 2030 AMRP completion condition when the only rate impact study related to the proposed condition, presented by AG witness Coppola, suggests that customer rates would roughly double, before considering any non-AMRP factors that inform the setting of rates, within the next decade if the 2030 completion date is required.

According to the AG, the evidence is clear that neither safety nor reliability is linked to the proposed 2030 completion timeline. The AG notes that as JA witness

Schott observed, the Commission's decision authorizing the AMRP with a 2030 targeted completion date in Docket Nos. 09-0166/09-0167 (Consol.) was based on the testimony of Peoples Gas witness Marano, who provided cost-benefit analyses for a possible accelerated main replacement program using three possible completion dates: 2025, 2030, and 2035 - and then from those alternatives concluded that a 2030 completion date was most feasible. JA Ex. 18.0 at 3. The AG notes that a careful look at the direct testimony filed by Mr. Marano in Docket Nos. 09-0166/09-0167 (Consol.) regarding a proposed 2030 completion date shows that he focused only on cost-benefit analyses and did not consider customer rate impacts, pipeline safety issues or the Peoples Gas' ability to manage an accelerated program. AG Ex. 4.0 at 30; AG Cross Ex. 2 at 51-59. The AG states that in light of the Commission's decision calculus from Docket Nos. 09-0166/09-0167 (Consol.), AG witness Coppola correctly noted in his rebuttal testimony that there is nothing "magical or critical" about a 2030 completion date. AG Ex. 4.0 at 30.

While Mr. Stoller alleged in his rebuttal testimony that "AMRP was not ordered by the Commission for reasons other than pipeline safety" (Staff Ex. 8.0 at 8), the AG notes that he later admitted in cross-examination that he was not a Commissioner at the time the Order in Docket Nos. 09-0166/09-0167 (Consol.) was issued and agreed that he is not suggesting that he is a legal expert in the interpretation of prior Commission orders. Tr. at 500-501. In fact, as Mr. Stoller agreed during cross-examination, the Commission approved Rider ICR, which enabled Peoples Gas to collect a return of and on AMRP investment over a designated dollar amount each year between rate cases, at the same time as it ordered a 2030 completion date in Docket Nos. 09-0166/09-0167 (Consol.). Tr. at 504. The AG notes that Mr. Stoller also agreed (Tr. at 506) that the Commission's Order in Docket Nos. 09-0166/09-0167 (Consol.) expressly rejected "Staff's persistent claim that Rider ICR is not needed." According to the AG, the Commission's Order in Docket Nos. 09-0166/09-0167 (Consol.) speaks for itself and clearly demonstrates that it approved the 2030 AMRP completion date in the context of also approving Rider ICR. The AG observes that, as Mr. Stoller agreed, after the Illinois Appellate Court reversed the Commission's approval of Rider ICR in September, 2011, Peoples Gas was unable to collect a return of and on AMRP investment between rate cases until 2014 when Rider QIP was initiated pursuant to the new Section 9-220.3 of the Act. Tr. at 507-508.

The AG advances the proposition that Mr. Stoller's direct testimony from Docket Nos. 09-0166/09-0167 (Consol.) shows that the genesis of his support for a 2030 completion date was nuanced and based on the expectation of further Commission review. There, Mr. Stoller recommended that (1) Peoples Gas should be ordered to conduct an in-depth study of the (then-proposed) AMRP since the program appears to be necessary for the long-term safety of Peoples Gas' system; (2) Peoples Gas should present the Commission with an AMRP implementation plan in a separate docket, with the plan to be analyzed by an independent consultant, and obtain Commission approval before commencing the AMRP; and (3) following Commission approval, Peoples Gas should be ordered to return to the Commission with updated analysis of the AMRP every three years. Tr. at 511-512. The AG suggests that the Commission looked to Mr. Stoller's recommendations in Docket Nos. 09-0166/09-0167 (Consol.) in formulating its

conclusion in that case that the AMRP should be concluded by 2030. The AG notes, however, that as Mr. Stoller admitted under cross-examination in this case, the Commission never adopted his second or third recommendation from his testimony in Docket Nos. 09-0166/09-0167 (Consol.). Tr. at 513. The AG argues that it is not clear how Mr. Stoller's 2030 completion date recommendation is still tenable when the Commission never executed the second and third steps that Mr. Stoller recommended in his testimony in Docket Nos. 09-0166/09-0167 (Consol.). The AG deems it also noteworthy that Mr. Stoller admitted in this case that he performed no analysis of the impact on customer rates when he prepared his testimony in Docket Nos. 09-0166/09-0167 (Consol.) and he did not know if any other Staff member did. Tr. at 517.

The AG asserts that Mr. Stoller's support for the 2030 completion date is complicated by looking to his statements in the evidentiary hearing of Docket Nos. 09-0166/09-0167 (Consol.), where he admitted that 2030 is not a "magic bullet" and is not necessarily the year that the AMRP must be completed. AG Cross Exhibit 15 at 15; Tr. at 514. The AG notes that Mr. Stoller admitted in that 2009 hearing that no evidence in Docket Nos. 09-0166/09-0167 (Consol.) supported the notion that the AMRP must be completed by 2030 (AG Cross Exhibit 15 at 15; Tr. at 515) and that he also admitted that he did not "know if it's 2029 or 2030 or 2031." AG Cross Exhibit 15 at 15; Tr. at 515. Finally, Mr. Stoller also admitted in that 2009 hearing that the issue of a particular completion date would be something that should be addressed in the future Commission proceeding that he had recommended in his direct testimony in that case. AG Cross Exhibit 15 at 15; Tr. at 516. The AG avers that if the Commission wished to rely in this proceeding on Mr. Stoller's position as it determines an appropriate AMRP completion date, Mr. Stoller's statements under cross-examination and re-direct examination in Docket Nos. 09-0166/09-0167 (Consol.) do not provide sturdy ground for a finding that a 2030 completion date is imperative. In short, according to the AG, neither Mr. Stoller nor Mr. Lounsberry were able to justify the inclusion of a 2030 AMRP completion date as a condition to the requested merger.

The AG notes that its expert witness in this proceeding, Mr. Coppola, recommended scaling the pace and scope of AMRP activity to a level that, inter alia, targets high-priority and high-risk segments (AG Ex. 4.0 at 35), in light of evidence that Peoples Gas has not been historically tracking the risk level (known as the Main Rank Index) of each of its mains replaced (AG Ex. 4.0 at 9-10, 22). The AG suggests that this merger condition would address safety needs far more effectively than blithely instructing Peoples Gas to accelerate its AMRP to a timeline determined without any reference to safety considerations.

The AG also argues that because of their failure to engage meaningfully - if at all - regarding the fate of the AMRP, the Joint Applicants failed to make the necessary showing under Section 7-204(b)(7) that the proposed reorganization will not have adverse retail rate impacts. As described above, the AMRP has had - and will continue to have - severe adverse consequences on Peoples Gas' customers' bills. The AG observes that Peoples Gas has stated that the AMRP was the main driver for its need for increased rates in each of its last two rate increase requests. AG Ex. 4.0 at 17.

The AG points out that neither the Joint Applicants nor Staff considered the impact of the Joint Applicants' passive approach towards the AMRP in their respective assertions that the proposed transaction meets Section 7-204(b)(7)'s requirement that the Commission find that any proposed reorganization "is not likely to result in any adverse rate impacts on retail customers." The AG pointed out that Staff's Section 7-204(b)(7) analysis focuses solely on the impact the proposed merger would have on Peoples Gas' and North Shore's respective costs of capital. The Joint Applicants mention the potential impacts on the utilities' respective costs of capital as well as their agreement to not seek recovery of (1) any portion of the acquisition associated with the transaction and (2) the transaction costs incurred to accomplish the merger. The AG states that whatever the merits of JA's and Staff's arguments on those points, neither party mentioned the flawed AMRP and the impact it will have on rates if the transaction were approved. The AG conclude that as much as the Joint Applicants may prefer to ignore the rate impacts of the AMRP, the Commission must account for adverse rate impacts the troubled program is likely to have on Peoples Gas' customers' bills if the proposed merger is approved.

The AG argues that in sum, the Joint Applicants' remarkable lack of detail as to how they plan to conduct a seamless transition to managing the troubled AMRP and Mr. McNally's testimony regarding the proposed transaction's potential impact on the Companies' cost of capital demonstrate that the Joint Applicants have not proved that the proposed Reorganization "is not likely to result in any adverse rate impacts for retail customers." 220 ILCS 5/7-204(b)(7).

With respect to the Joint Applicants two-year rate freeze offer, the AG notes that this approximates Peoples Gas' current rate case filing timeline. The Joint Applicants also commit to not seek increases in their base rates just approved in January in Docket Nos. 14-0224/14-0225 (cons.) "any earlier than two years after the Transaction closes." JA Ex. 1.0 at 21; JA Ex. 15.1 REV, par. 1. This commitment is heavily conditioned, as it is contingent on "the right to request that the Commission waive this base rate limitation if the financial integrity of Peoples Gas and/or North Shore is jeopardized to the extent of negatively affecting customers," the AG points out. *Id*. The evidence shows that this, too, has little tangible value to ratepayers, according to the AG. During cross-examination, JA witness Leverett, who sponsored the JA's list of merger commitments, confirmed that a rate case could be filed by the Gas Companies 11 months prior to the two-year anniversary of the merger closing, or as early as August of 2016. Tr. at 169. Given that the Gas Companies have filed a rate case, on average, every 16.6 months since their 2007 rate case filing, this commitment does not suggest that the time period between the Gas Companies' rate case filings would be extended significantly beyond a business-as usual frequency, the AG points out.

Moreover, the Joint Applicants' rate freeze commitment falls short compared to the most recent Illinois-based natural gas utility reorganization commitment, that of the joint applicants in Docket No. 11-0046, according to the AG. There, the AGL/Nicor joint applicants agreed to a three-year rate freeze as a merger commitment, a full year

longer than what the JA in this docket promise. Docket No. 11-0046, Order of December 11, 2011, Appendix A, Condition No. 21. Here again, the AG states, the Joint Applicants' asserted benefits of the merger are underwhelming, at best. The AG argues that the Joint Applicants should be required to adopt a five-year rate freeze as a condition of the merger, particularly in light of the Gas Companies' revenue stabilizing mechanisms.

In response to the City/CUB proposed five-year rate freeze merger commitment proposal, the JA again argue that this proceeding "is not to create benefits or other enhanc[e]ments in a utility's service quality before approving a reorganization." JA IB at 44. In the JA's view of the case, if the Commission concludes that the required findings under subsection (b) of the statute that the proposed merger "will at least maintain the utility's status quo and not diminish or adversely impact the utility's service quality or rates" the merger must be approved. *Id*.

Again, as noted repeatedly above, this interpretation of the Commission's obligations under Section 7-204 of the Act is simply wrong, and would render subsection (f) of the statute meaningless, according to the AG. That viewpoint runs counter to well-established rules of statutory interpretation.

The JA also argue that the proposal does not take into account the 5.5% annual cap included in Rider QIP or that City of Chicago regulations "have led to dramatic increases in the costs of performing operational work" that will not be recovered in either the Rider or the 2014 rate case, citing JA witness Leverett's Rebuttal testimony. JA IB at 45. These arguments, too, should be rejected, the AG states. A review of the cited testimony that proffers these arguments (JA Ex. 6.0 at 34) includes no specific discussion of dollar amounts tied to either the Rider QIP claim or the amount of extraordinary expenses incurred as a result of the new City regulations. Moreover, given Mr. Leverett's lack of knowledge about either the AMRP or Rider QIP revealed in cross-examination, these arguments ring hollow. See, e.g., Tr. at 146-237.

In addition, the Joint Applicants suggest that rather than committing to a rate freeze, net savings will occur over time, citing the testimony of JA witness Reed. JA IB at 45. But Mr. Reed's claimed savings were so vague as to be meaningless, and his comparison of savings that occurred in other mergers proved to be irrelevant to the instant proceeding, the AG points out. See AG Initial Brief at 49-50; Tr. at 343-345.

In sum, the AG urges the Commission to adopt Mr. Gorman's five-year rate freeze commitment recommendation as a condition of merger approval.

4. City/CUB's Position

City/CUB argue that the protocols for ratemaking treatment of the costs of integrating the Joint Applicants into a single reorganized entity -- which the Joint Applicants call transition costs -- are an essential, but poorly defined process that cannot support the required Commission finding that adverse rate impacts are not likely. 220 ILCS 5/7-204(b)(7). In fact, according to City/CUB, development of a cogent

process was an after-thought, wholly neglected until the Joint Applicants were prodded by advocates for affected ratepayers. Tr. at 408. The details of the process are few and hastily cobbled together; basic cost identification, tracking, and accounting processes are still lacking, according to City/CUB and the Joint Applicants propose to leave tens of millions in potential rate increases subject to ad hoc processes to be defined during a future rate case. Tr. at 403.

City/CUB argue that the Joint Applicants' proposal, commitments, and evidence do not provide adequate support for the required statutory findings for merger approval. On examination of the record, it appears to City/CUB that the Joint Applicants' preparations are not adequate to assure that post-Reorganization rates will not improperly recover costs prohibited by Section 2-704, or by the Joint Applicants' own commitments.

City/CUB contend that the Joint Applicants' proposal presents problematic identification, tracking, and rate recovery issues related to costs for the post-closing process of melding separate corporate entities into an integrated organization. According to City/CUB, these issues relate directly to the rate impacts of the proposed Reorganization, and many of the problematic issues are direct results of the Joint Applicants' strategic decision to delay planning and preparation for that assimilation process. *See* Joint Applicants-Commissioners DRR No. 1. City/CUB assert that the Joint Applicants' decision not to develop transition plans and estimates of costs or savings avoids any up-front allocation of estimated savings and risk to the Joint Applicants, but that decision necessitates far more complex and uncertain ratemaking mechanics. City/CUB assert that the most important consequence is the need to have in place -- from the beginning of the transition (the Closing) -- rigorous protocols for accurate identification, classification, and calculation of costs eligible for rate recovery, to assure that adverse rate impacts on retail customers are not likely.

City/CUB assert that the Joint Applicants' ill-defined proposals do not assure the result required by the statute. They argue that because of the structure of the proposal in this case, if the record is inadequate on any one of several points, the statutory requirement for a Commission finding that adverse rate impacts are "unlikely" cannot be met, and the reorganization cannot be approved. City/CUB observe that whether intended or not, the Joint Applicants' tactical delay in serious implementation planning has the effect of making all transition costs potentially recoverable through utility rates. Thus, they argue, to satisfy the threshold rate impact criterion for reorganization approval, the Joint Applicants' evidence must assure the Commission of (a) the improbability of reorganization related cost recovery that has an adverse impact on utility customers, (b) the certainty of compliance with transition cost commitments incorporated in a reorganization approval order, and (c) the Commission's ability to accurately identify and quantify recoverable transition costs for lawful ratemaking, even in the absence of Commission-reviewed protocols for identifying and tracking transition costs and any associated savings.

Adding another layer of complexity in any of the above circumstances City/CUB say, anticipated net savings may not be realized. City/CUB observe that where reliance on projected but un-achieved savings results in premature and improper recovery, meaningful enforcement of the commitment to cap transition costs at net savings would require an adjustment to past rate recovery, but that no such mechanism is available in current ratemaking processes or any Joint Applicants record testimony.

City/CUB observe that the Joint Applicants concede that the expected magnitude of the Joint Applicants' transition costs is significant; the Joint Applicants' Reorganization expert, Mr. Reed, estimated that they could amount to "tens of millions" of dollars. Tr. at 369. City/CUB argue that timely establishment of rigorous accounting and classification protocols for such large amounts -- which the utilities plan to include in rates -- is essential to avoid severe, adverse impacts on utility customer rates, as well as misallocations of costs and possible cross-subsidization of non-utility activities. *See* Section 7-204(b)(2), (3), and (7).

City/CUB note that the Joint Applicants suggest that the necessity of Commission approval in ratemaking proceedings virtually guarantees that adverse rate impacts are not likely. JA Ex. 8.0 at 8. That is not correct, since the burden of identifying and challenging improper reorganization costs buried in various tracking schemes would be shifted to ratepayer advocates in future rate cases. In City/CUB's view, the complexities of determining properly recovered costs when costs and savings do not advance in lock step may be practically insurmountable. It cannot be cured by a process that depends on Staff or under-funded ratepayer advocates finding and correcting improper recovery requests.

According to City/CUB, the Commission should reasonably expect that the Joint Applicants would (at the very least) be able to explain the framework of the process they claim can assure proper rate treatment of transition and transaction costs, thereby preventing adverse rates impacts, but the Joint Applicants were unable to do so. City/CUB found it telling that even with the uncertainty about the efficacy of their undefined protocols, the Joint Applicant witnesses rejected City/CUB proposals for firmer, more detailed commitments as a way to reduce the likelihood of adverse rate impacts.

City/CUB argue that the Joint Applicants' lack of diligence and thoroughness on transition cost/savings issues extinguishes any claim of reasonableness for a speculative assumption that the Joint Applicants will timely develop and implement the protocols needed to satisfy the statutory standards. According to City/CUB, the lack of diligence was established through the testimony of the Joint Applicants' own witnesses, and their admissions are evidence that distinguish this case from any prior reorganization proceeding. Here, City/CUB argue, there is no basis to speculate that whatever scheme the Joint Applicants ultimately cobble together will be adequate to assure that the Reorganization "is not likely to result in any adverse rate impacts on retail customers," even though the rate impact could be in the tens of millions. 220 ILCS 5/7-204(b)(7). City/CUB add that even if the Joint Applicants could actually develop such a process, its deployment would not be timely and the Commission could

not look back to identify transition costs and savings that were not properly tracked in the years before an approved process was in place.

City/CUB emphasize that they do not oppose recovery of all transition costs, only transition costs that fail to produce savings for customers. "Allowing for recovery of transition costs that are not fully offset by savings created specifically by those activities, will result in an increase (inconsistent with the JAs' commitment) in the revenue requirement and retail rates within a rate case." City/CUB Ex. 8.0 at 5-7. Moreover, in his testimony, Mr. Gorman insisted that the Joint Applicants have the burden of demonstrating that no transition costs are improperly being recovered in rate cases.

According to City/CUB, despite the deficiencies of the Joint Applicants' undefined methods for identifying and determining transition costs and savings highlighted during the cross-examination of their experts, the Joint Applicants experts declined any action to remedy the problems. *See generally* Tr. at 367-409, 463-484. In a particularly telling refusal, City/CUB say, the Joint Applicants' witness Scott Lauber (the executive in charge of implementing the transition cost protocols) would not modify the Joint Applicants' transition cost commitment (Commitment 21) to match the language of the transaction cost ratemaking commitment (Commitment 16) -- specifically to conform the commitments so that the utilities would "demonstrate that such costs are not included in the rate case for recovery." Tr. at 478-480. The Joint Applicants' apparent desire to preserve ambiguity in their transition cost commitment, which could affect tens of millions of dollars in costs and savings, is (according to City/CUB) a danger sign the Commission should heed.

If the Commission nonetheless approves the proposed Reorganization, despite the undisputed lack of developed transition cost protocols, City/CUB ask that the Commission impose very clear, enforceable conditions to produce an order of even marginal sustainability. With respect to transition costs, City/CUB assert those conditions must have at least the following features.

- Assure that any risk that the Joint Applicants' yet-to-be-developed transition cost recovery protocols are inadequate falls squarely on the utility. At a minimum, the Joint Applicants' transition cost commitment (Commitment 21) must be modified to add a clear requirement that the utility seeking inclusion of transition costs in rates must "demonstrate that transition costs in excess of associated savings are not included in the rate case for recovery."

- The Joint Applicants must present for approval fully-developed transition cost protocols for Commission review and approval (in a contested proceeding) within 90 days of closing, so that valid accounting procedures are in place for the maximum feasible portion of the transition period.

- The Joint Applicants should be required to report on an annual basis an accounting of all transition costs and all savings (to date) that may later be

used to justify transition cost recovery in a rate case. They should be accumulated on the same basis (e.g., initiative, asset, or baseline measurement) that will be used to define the net savings cap on cost recovery, as this is the only way to avoid later result-oriented calculations hidden in the complexity of overlapping (and possibly inconsistent) ratemaking concepts. For example, dealing with transition costs net savings that are realized at different rates would otherwise be impossible.

- The Joint Applicants should identify all transition costs in a rate case's test year costs, whether or not they are proposed for recovery, providing the Commission with a check on the accuracy and completeness of the defined protocols.

- "The Joint Applicants have committed that they will not seek to recover any portion of the "acquisition premium . . . ." JA IB at 26. However, the Joint Applicants are taking no steps to identify and track effects of the acquisition premium on the utilities' costs of capital. City Group Cross x. 1, JA-City/CUB DRR 2.08. They should be required to provide this information.

With respect to the proposed rate freeze, the Joint Applicants lead their objections to City/CUB's proposed extension of the rate freeze with a diversion into yet another restatement of their commitment not to improve the Illinois utilities, referring to their oft-repeated assertion that the Act requires only that the utility status quo be maintained - not improved. The Joint Applicants' first objection to City/CUB's proposed extension of the rate freeze demonstrates to City/CUB, once again, that the Joint Applicants' perception of the Commission's authority and obligations in this proceeding is unlawfully narrow. City/CUB claim it also shows that their arguments are illogically broad. City/CUB aver that the Joint Applicants fail to connect their objection to the rate freeze commitment they offered to help meet statutory approval requirements or to City/CUB's proposed modification. Assuming, arguendo, some statutory basis for the Joint Applicants' "no harm" standard, it cannot apply to improvement of the Joint Applicants' own proposed conditions; at most, it applies to current utility operations.

More importantly, say City/CUB, the Joint Applicants miss the mark. What City/CUB and the AG seek in supporting an extension of the rate freeze in not an inequitable benefit for customers. City/CUB assert that the rate freeze is supported by the tremendous revenue stability provided to Peoples Gas through multiple risk-reducing rider mechanisms, (City/CUB Ex. 4.0 at 8), as well as by the Joint Applicants' claim that net savings are expected to accrue as a result of the merger (see JA Ex. 17.0, 5). City/CUB point out that the proposed transaction will benefit Peoples Gas' ultimate investors, and a longer base rate freeze will provide a concomitant benefit in the form of a consumer protection intended to protect utility customers from the burden of a fifth rate increase in just 7 years.

City/CUB argue that the Joint Applicants' arguments ignore two relevant provisions in the Act that support the rate freeze extension. First, the Commission is required to find that the proposed reorganization is "not likely to result in any adverse rate impacts on retail customers." 220 ILCS 5/7-204(b)(7). If the post-reorganization company is operating as the Joint Applicants project, say City/CUB, it will be a stronger, more financially stable holding company, (JA Ex. 2.0 at 28-29), it will benefit from multiple revenue-stabilizing riders, and it will generate long-term net savings in non-fuel O&M expense. In such conditions, City/CUB aver it is not unreasonable to request a longer rate freeze period. Second, according to City/CUB, the Joint Applicants ignore the public interest standard explicitly referenced in Section 7-204(f), which allows the Commission to impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers. 220 ILCS 5/7-204(f). City/CUB therefore conclude that it is entirely appropriate for the Commission to protect utility ratepayers from paying higher rates that could result if the Reorganization does not produce the outcomes the Joint Applicants project.

Next, City/CUB point to the Joint Applicant's argument that Mr. Gorman's proposal does not account for the fact that North Shore does not have a Rider QIP and that the cap in Rider QIP recoveries can only be reset by the filing of a rate case. JA IB at 45. According to City/CUB, though North Shore does not have a rider like Rider QIP in effect currently, it has other mechanisms, including Rider VBA, that coupled with savings from the Reorganization, make a five year rate freeze reasonable for North Shore as well. *Id*. at 4. City/CUB conclude that the Joint Applicants' reasons for objecting to the proposed five year rate freeze stand in opposition to the evidence on the entire record.

City/CUB challenge the Joint Applicants claim that updated CDOT regulations have imposed costs on Peoples Gas in performing operational work on its infrastructure located under the City's Public Ways that it will not recover in current rates. JA IB at 45. This point is unpersuasive for several reasons, according to City/CUB. City/CUB demonstrate that the fees, fines, and penalties Peoples Gas incurs are largely within Peoples Gas' control. If Peoples Gas improved its AMRP construction management to achieve better coordination with the City of Chicago to take advantage of savings opportunities in the new CDOT regulations, and to better monitor and control its budgets, schedules, and quality of work, as City/CUB recommend, its additional costs would be minimized. City/CUB showed that just as a five-year freeze could incent the Joint Applicants to maximize reorganization savings (City/CUB Ex. 8.0 at 4), it could also provide an incentive to Peoples Gas to reduce its construction costs through more effective and efficient management of its AMRP program.

City/CUB reiterate the point that the Joint Applicants have ignored the savings opportunities included in new CDOT regulations. City/CUB IB at 62; City/CUB Ex. 8.0 at 4. City/CUB say that the Joint Applicants have failed to quantify, or even acknowledge, the management efficiencies provided for in the CDOT regulations and through the Project Coordination Office process. City/CUB Ex. 3.0 at 421-425. If properly managed and communicated, claim City/CUB, Peoples Gas could complete AMRP and other

construction work as scheduled and budgeted, which should result in reduced costs for Peoples Gas' ratepayers, as well as for the City's taxpayers. Such prudent management also could avoid having to ask that Chicago ratepayers pay even higher rates. City/CUB Ex. 3.0 at 589-603. Since the Joint Applicants have not defined protocols to identify and track transition costs/savings and propose to address them only in a rate case, City/CUB showed that savings achieved by Peoples Gas and North Shore during a freeze would likely accrue to the utilities' shareholders. If that approach is allowed, the onus should be on those companies to maximize savings, and a longer rate freeze creates greater incentives for the companies to do so.

The Joint Applicants oppose Mr. Gorman's proposed rate freeze extension by claiming that such a measure is unnecessary. The Joint Applicants "expect that there will be net savings, over time, as they integrate their management, systems and operations, and these savings will be reflected in future rate proceedings for the benefit of Illinois customers by way of reduced operating expenses or lower capital costs." JA IB at 45, citing JA Ex. 17.0 at 5. However, City/CUB argue that the Joint Applicants have declined to do transition planning to capture available savings, delayed their transition (precluding near-term savings), and neglected development of protocols to identify, quantify and to track transition costs and savings that could be produced by the Reorganization. Thus, aver City/CUB, adverse rate impacts could result from the Joint Applicants' disincentive to achieve and account for cost-saving synergies prior to the time the rate freeze ends.

City/CUB further maintain that the Joint Applicant's proposed problematic treatment of transition costs and a short freeze period would encourage the Joint Applicants to put off integration plans that could benefit customers until the freeze period ends. At the end of the freeze, cost recovery risks associated with expenditures for integration planning and execution (to achieve Reorganization savings) are transferred from shareholders to ratepayers through the proposed scheme for transition cost recovery in rate cases. City/CUB aver that ratepayers would pay for implementing the management/shareholder Reorganization decision, and shareholders would be insulated from the possibility of large losses from failed synergy expectations or a poor reorganization gambit. Tellingly, say City/CUB, under the Joint Applicants' proposed time lines, the transition is projected to begin, costs are expected to be incurred, and transition costs will be eligible for rate recovery at about the same time that the proposed freeze would end. See JA Ex. 9.0 at 25.

City/CUB urge the Commission to extend the Joint Applicants' commitment to freeze rates from two years to five years, in order to assure rate stability and to prevent adverse rate impacts over the period of the freeze.

5. Commission Analysis and Conclusion

Section 7-204(b)(7) requires the Commission to determine if the proposed reorganization is not likely to result in any adverse rate impacts on retail customers. Staff recommended that certain conditions be required of the Joint Applicants to guard against possible credit downgrades of the Gas Companies as well as the impact on the

cost of capital. The Joint Applicants have agreed to these conditions imposed by Staff and if a possible downgrade occurs, the Joint Applicants have agreed to mitigate against higher rates if a downgrade should occur post-merger. There is a dispute between the Joint Applicants, Staff and City/CUB as to what effect the negative outlook placed on the Gas Companies by S&P means. Whether the downgrade is "likely" versus merely possible, if the credit rating is downgraded, it would lead to a higher capital cost, which would have an impact on rates. The Joint Applicants have agreed with Staff to present a detailed study within 6 months showing the benefits of the Gas Companies registering with the U.S. Securities and Exchange Commission showing the costs and savings. (Appendix A, Condition # 32). The Commission finds that this agreed upon condition between Staff and the Joint Applicants will alleviate the concerns of a downgrade. The fact that the Joint Applicants have agreed to a two year rate freeze and not seek an increase in base rates (Appendix A, Condition # 1) should help mitigate the possibility of a downgrade.

Both the AG and City/CUB argue that the Joint Applicants should be required to revisit the commitments of the AMRP. Otherwise, this will have a major impact on customer's rates. The capital expenditures of this program would be made whether or not the merger took place. Peoples Gas will have to continue on with this program and this cannot be considered as an adverse rate impact under this Section of the Act. This is not an increase related to the Reorganization.

City/CUB have requested that additional reporting requirements and performance metrics be established and that penalties be imposed based on the AMRP. We decline to adopt this system because as we have stated elsewhere in this Order, a Section 7-204 proceeding is not the proper place for attempting to determine and implement improvements or enhancements to a utility's operations or performance, given that the standard we are to apply under the statute is to determine whether the reorganization will negatively impact - not improve - a utility. The Commission has determined that no additional requirements will be placed on the AMRP, so there are no conflicts with Liberty's Final Report.

The Commission must determine that the Joint Applicants' transition costs and savings resulting from the Reorganization will not likely result in adverse rate impacts. The Joint Applicants bear the burden of establishing the accuracy of their tracking mechanism to the Commission's satisfaction in subsequent rate cases before there will be any rate impact because, as a result of conditions agreed to by Staff and the Joint Applicants, transition costs can only be recovered up to the amount of any savings those costs generate. The Joint Applicants must also demonstrate that any cost they seek to recover is just and reasonable and that the transition costs have generated savings equal to or greater than the costs being recovered. The Joint Applicants will not seek the recovery of any transition costs incurred before the test year to be used in the Gas Companies' next rate cases, so there will be no adverse impacts by approving the Reorganization without having an opportunity to review a detailed tracking mechanism in this proceeding. Moreover, with respect to forecasts of transition costs and related savings, in future test year rate cases, City/CUB have failed to establish any difference

between the use of forecasting for these figures from any of the other financial forecasts that must, of necessity, be used in a future test year rate case.

Further, the Commission declines to impose a longer "rate freeze" on the Joint Applicants than the two year period voluntarily committed to by Wisconsin Energy in its Application. The Commission has determined that there is no basis for such an extension, while a lengthier extension would create problems with respect to the fact that North Shore has no means, such as Rider QIP, to recover its capital expenses in between rate cases. Peoples Gas would also have a problem with a longer freeze because of the cap on the operation of Rider QIP.

For all of the reasons stated above, the Commission adopts the conditions proposed by Staff and agreed to by the Joint Applicants, along with the additional commitments made by the Joint Applicants. Subject to these conditions, the Commission finds that the proposed Reorganization satisfies the requirements of Section 7-204(b)(7) of the Act.

V. SECTION 7-204(c): TREATMENT OF COSTS AND SAVINGS

Section 7-204(c) of the Act states that:

> The Commission shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated.

220 ILCS 5/7-204(c).

A. Joint Applicants' Position

The Joint Applicants argue that the record evidence supports the required findings by allocating any net savings realized from the Reorganization to the Gas Companies' customers, and establishing conditions that provide for no recovery of transaction costs and recovery of transition costs only to the extent they have generated savings.

With respect to savings, the Joint Applicants assert that the evidence demonstrates that there are no immediate cost savings that will result from the Reorganization. JA Ex. 2.0 Rev. at 12; JA Ex. 3.0 at 33-34. The Joint Applicants state that net savings in non-fuel O&M are not expected to occur until five to ten years after the Reorganization. Net savings achieved in the future will flow through to ratepayers in future rate cases. JA Ex. 2.0 Rev. at 12-13; JA Ex. 7.0 at 19; JA Ex. 3.0 at 46.

With respect to the costs of the reorganization, the Joint Applicants note that they committed that they will not seek recovery of costs incurred to accomplish the reorganization – i.e., transaction costs – from customers, and that they will not seek recovery in base rates of the acquisition premium paid as part of the Reorganization, nor the amortization of the premium in future cost of service determinations. Further, the Joint Applicants agreed that they may recover transition costs only to the extent that they produce savings, and then only those transition costs that are incurred in a rate case test year. Transition costs are costs incurred after the close of the reorganization to achieve long-term efficiencies and savings, and which may be recoverable to the extent they produce savings. JA Ex. 7.0 at 19. The Joint Applicants state that any transition costs incurred prior to the first rate cases after the reorganization is closed, therefore, will not be recoverable from customers.

Additionally, the Joint Applicants note that they agreed to be bound by conditions and findings recommended by Staff to be imposed by the Commission in order to find that the Reorganization meets the requirements of Section 7-204(c). Staff Ex. 11.0 at 5-6; JA Ex. 16.0 at 9; JA Ex. 15.1 Rev. at Nos. 16-21. The Joint Applicants rely upon the fact that with the adoption of these conditions, Staff recommended that the Commission find that the proposed Reorganization complies with Section 7-204(c) of the Act.

The Joint Applicants state that they will use a spreadsheet model operating in parallel with their existing accounting systems similar to what has been used in other utility mergers to track and monitor transition costs and savings. JA Ex. 17.0 at 6-7. As used with other mergers, the model to be used will be multi-layered allowing granular as well as higher-level tracking to occur. The Joint Applicants assert that they will bear the burden of proof to establish that any transition cost they seek to recover is just and reasonable, and has produced savings equal to or greater than the cost for which recovery is sought in a rate case. Thus, the Gas Companies will bear the burden of establishing the appropriate amount of such costs to be recovered, just as they must do for every other element of their revenue requirement to be recovered in a rate case.

The Joint Applicants state that based upon the testimony of a City/CUB witness, the AG has requested that approval of the Reorganization be conditioned on exclusion of all transaction costs including severance packages. The Joint Applicants assert that they have agreed to the conditions which address the AG's concerns.

B. Staff's Position

Staff states that the proposed Reorganization complies with the requirements of Section 7-204(c). Staff notes that the Joint Applicants do not expect the savings to occur until five to ten years after the Reorganization and assert that savings to be achieved in the future will flow through to ratepayers in future rate cases. Staff Ex. 5.0 at 3. The Joint Applicants also state that they will not seek recovery of costs incurred to accomplish the Reorganization from customers and also commit to not seek recovery from customers of the acquisition premium paid as part of the Reorganization in rate base, nor the amortization of the premium in future cost of service determinations. *Id*. at 3-4.

Staff notes that the Joint Applicants have agreed that the allocation of any savings resulting from the proposed Reorganization will flow through to ratepayers. Staff Ex. 11.0 at 3. The Joint Applicants have further agreed that they will not seek recovery of costs incurred to accomplish the proposed Reorganization. *Id*. Transaction costs are costs incurred to accomplish the proposed Reorganization and are not recoverable. *Id*.; JA Ex. 8.0 at 18. Examples of transaction costs include costs associated with executing the transaction such as banker's fees, legal fees, severance package costs (i.e., executive change-in-control payments as identified in an SEC Form S-4). JA Ex. 8.0 at 18. Transition costs are costs incurred to achieve long-term efficiencies and savings and may be recoverable to the extent the transition costs do not exceed the savings the transition costs produce. *Id*.

Staff argues that the Gas Companies should be directed to separately identify and track transaction costs and transition costs. Staff Ex. 11.0 at 3. The Joint Applicants agree that, in future rate cases, all costs included in the test period resulting from accomplishing the Reorganization (transaction costs) would be identified and such costs would be shown to not be included in the rate case for recovery. *Id*. at 4. Given the above, Staff proposed several conditions which the Joint Applicants accepted. JA Ex. 15.1 REV. #19; Staff IB, Appendix A, #9; JA Ex. 15.1 REV. #20; Staff IB, Appendix A, #10; JA Ex. 15.1 REV. #16; Staff IB, Appendix A, #6; JA Ex. 15.1 REV. #17; Staff IB, Appendix A, #7; and JA Ex. 15.1 REV. #21; Staff IB, Appendix A, #11.

C. City/CUB's Position

City/CUB argue that despite the enticing possibility or promise of future savings, nothing in this record assures the sharing of cost savings as required by 7-204(c). The Joint Applicants' proposal in this case is distinguishable from other cases where the Commission has accepted a mere promise that future savings would flow to ratepayers.

According to City/CUB, in past cases, the reorganization applicants did not project savings as substantial as those in this case. In fact, in some past reorganization cases, there were minimal or no savings forecast. *See, e.g.,* Docket No. 04-0299*,* Final Order at 8*.* City/CUB note that the Joint Applicants asserted in their Initial Brief that "Indeed, the evidence shows that the Reorganization is likely to have the long-term positive rate impacts of net savings in non-fuel O&M and reduced debt costs due to enhanced access to capital." JA IB at 28; Tr. 369 ("tens of millions" in costs); JA Ex. 3.0 at 34 (approximately 5% of non-fuel expenditures in savings). Interestingly, the Joint Applicants, which have the burden of proof, have presented no evidence on utilities' or ratepayers' actual experience with the ratemaking approach they propose in this case.

City/CUB state that whatever such an analysis might show (had the Joint Applicants presented one), it would not be determinative for the proposal at issue. In this case, the determination and allocation of savings is further complicated by the Joint Applicants' proposal to delay transition planning and activity, with a similar effect on costs and net savings, and by the uncertainty surrounding their lack of any defined

protocols to accurately identify and account for millions in transition costs and net savings.

City/CUB claim that the combination of purposeful delay, no savings estimate, a net savings cap that must be determined using undefined protocols, caps determined over a period of years and overlaid by test year cost analyses that possibly using projected savings (which may not be achieved) and the irrevocability of rate recovery based on projections, all make this proposal unique. City/CUB conclude that the uncertainty caused by these unique characteristics demands more than the promise that savings will flow though to ratepayers.

D. The AG's Position

The AG asserts that the Joint Applicants' promise of future net savings as a result of the Reorganization is so vague and unsupported as to be worthless. JA witness Reed claimed the Reorganization "is likely to generate net savings in the range of three to five percent of non-fuel O&M of the combined company after a five to ten year ramp up period relative to what non-fuel O&M for the Companies would have been absent the transaction." JA Ex. 3.0 at 34. The AG points out, however, that the Joint Applicants conducted no specific WEC/Integrys synergy savings analysis.

In the instant case, WEC is seeking a merger with a company (Integrys) that has already consolidated operations with another holding company, Peoples Energy Corporation, the former corporate parent of the Gas Companies, in 2007. Docket 06-0540. The AG points out that this suggests any synergies that typically result from a merger of two holding companies will not necessarily occur with this merger. The Joint Applicants further claim, generally, that the increased scale and scope of the Reorganization will "create a financially stronger company with both greater financial liquidity and improved access to capital markets." JA Ex. 3.0 at 28. But here again, the Joint Applicants did not describe any improved access to capital that does not already exist for the Gas Companies with their current parent, Integrys, the AG contends.

The AG argues that while the Joint Applicants state that they will not seek recovery of costs incurred to accomplish the Reorganization, including transaction, change in control, financing and "legal/other professional" costs, City/CUB witness Gorman notes that it is not clear whether all costs associated with the Reorganization transaction will not be recovered from ratepayers. He recommended that the Commission condition any merger approval by specifically prohibiting recovery in rates of any executive, Board of Director or senior employee severance costs or early termination fees, i.e. severance packages. City/CUB Ex. 4.0 at 11. Mr. Gorman explained costs incurred in order to produce savings should be permitted in rate recovery up to the level of savings created. City/CUB Ex. 8.0 at 5. He noted that if transition costs are included in a future rate case test year, then the JA have the burden of proving that there are savings within the test year and over the life of the project that fully offset the level of transition costs. *Id*. at 6. This condition should be attached to any Commission merger approval as well, according to the AG.

E. Commission Analysis and Conclusion

The Commission must determine the allocation of any savings and what costs the Joint Applicants are allowed to recover from the proposed Reorganization, as well as the amount of the costs eligible for recovery and how the costs will be allocated. While the Joint Applicants do not expect the savings to occur right away, any savings will flow to ratepayers in future rate cases. The Joint Applicants and Staff have agreed to conditions that properly allocate all net savings generated by the Reorganization to the Gas Companies' customers. The Joint Applicants also agree not to seek recovery of any costs incurred to accomplish the Reorganization or any acquisition premium will be in rate base or future cost of service determinations. The conditions also state that no transaction costs will be recovered and that the transition costs will only be recovered to the extent that they produced or will produce savings equal to or greater than the transition costs to be recovered. As stated herein, the Gas Companies in their next rate case will have the burden of showing that the transition costs are just and reasonable, before any recovery will be approved. Based on the conditions agreed to by the Joint Applicants and Staff, the Commission finds that the Reorganization meets the requirements of Section 7-204(c). (Listed as conditions 16, 17, 19, 20, 21 & 41 in Appendix A).

The argument of the AG concerning exclusion of all transaction costs including all severance packages will be addressed in condition 20 and 41 of Appendix A. With respect to the argument of City/CUB concerning not producing a specific mechanism or tracking for costs and savings, the Commission has determined under this section it is not necessary. As stated above, the burden will be on the Joint Applicants to provide the necessary information before any of these costs or saving are approved in the next rate case.

The Commission finds that the Reorganization, along with the agreed upon conditions, meets the requirements under this section.

VI. SECTION 7-204(f)

> In approving any proposed reorganization pursuant to this Section the Commission may impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers.

220 ILCS 5/7-204(f).

A. Conditions Proposed by Staff

1. Pipeline Safety Management System

a. Staff's Position

Staff states that the record in this proceeding demonstrates that Peoples Gas has, over an extended period, been the subject of a number of Notices of Probable

Violations ("NOPVs") issued by the Commission's Gas Pipeline Safety Program Staff, alleging apparent violations of federal regulations governing gas pipeline safety. Staff Ex. 3.0 at 10. Pipeline Safety Staff issued NOPVs for apparent violations of pipeline safety regulations governing corrosion control procedures, leak survey procedures, improperly abandoning facilities, inadequate record keeping, failure to follow procedures for numerous requirements, pressure testing, emergency procedures, customer notification, qualifying employees to fabricate pipe joints, public awareness, reporting safety-related conditions, hazardous leak repairs, resolving unsafe conditions, operator qualifications and plastic pipe overexposure to ultraviolet light. *Id*. Staff explains that these NOPVs demonstrate a pattern of failure at Peoples Gas - more specifically, failure to properly identify regulatory requirements, failure to adequately follow procedures, failure to provide adequate supervision, and failure to provide adequate quality assurance. *Id*. at 11. These failures can be attributed at least in part to the fact that Peoples Gas has had continual issues communicating areas of concern within its own organization. *Id*.

Staff notes that the record in this proceeding further identifies three particularly serious violations of pipeline safety requirements by Peoples Gas. Staff Ex. 3.0 at 6-10. Two of these violations resulted in injuries to persons, and one in a fatality. *Id*. at 8-9. Peoples Gas paid fines totaling $1.3 million to resolve these violations, and in each case was ordered to revise its pipeline safety policies and procedures. *Id*. at 7-9. Peoples Gas was also required to retain a consultant to investigate Peoples Gas' compliance with pipeline safety regulations, including evaluation of Peoples Gas' record-keeping procedures, substantiation of Peoples Gas' pipeline safety inspection records, and verification of recorded pipeline safety conditions in the Peoples Gas system, followed by an audit of Peoples Gas' continuing actions to implement recommended improvements to its pipeline safety program. *Id*. at 7-8.

Given this history, Staff contends that it is vital that the Commission condition approval of the transaction upon Peoples Gas being required to take positive steps to improve its pipeline safety performance, in order to protect the interests of Peoples Gas and its customers consistent with Section 7-204(f) of the Act. More specifically, the Commission should require Peoples Gas to implement a Pipeline Safety Management System ("PSMS") in accordance with American Petroleum Institute ("API") Recommended Practice 1173 ("RP 1173"). Staff Ex. 3.0 at 15-16.

Staff explains that RP 1173 provides guidance to pipeline operators for developing and maintaining a PSMS. Staff Ex. 3.0 at 16. It is anticipated that RP 1173 will be available in its final form this spring. Staff Ex. 3.0 at 19. The elements of RP 1173 are structured to minimize nonconformity with other pipeline safety processes and procedures. *Id*. While RP 1173 may include some elements of other management systems (such as those specific to environmental management, occupational health, personnel safety management, financial management, or insurance risk management), it does not include all requirements specific to those systems. *Id*. RP 1173 may be used either in conjunction with or independent of other industry-specified documents. *Id*. Finally, RP 1173 builds upon and augments existing requirements and is not intended to duplicate requirements of any other consensus standards or regulations. *Id*.

According to Staff, managing the safety of a complex process requires a system of efforts to address multiple, dynamic activities and circumstances. Staff Ex. 3.0 at 16. Pursuing the industry-wide goal of zero pipeline safety incidents requires a comprehensive, systemic effort. *Id*. Some efforts within a PSMS are directed to a specific need or activity. *Id*. For example, non-punitive reporting of near misses is one element that can be used to identify potential risks and initiate proactive measures. *Id*. Though many process incidents are relatively infrequent, they can still lead to serious consequences; indeed, they can lead to fatalities. *Id*. at 18-19. Accordingly, other elements of a safety management system address the need to continuously operate safely and improve safety performance. *Id*. at 19. Effective communication between various departments to identify potential and interactive threats can produce effective risk reduction. *Id*. Staff outlined items that it states should be included in indirect broader-based efforts. *See*, Staff Ex. 3.0 at 17.

Also, Staff outlined principles that a PSMS should be based on. *See*, Staff Ex. 3.0 at 17-18. Staff asserts that implementation of a PSMS at Peoples Gas would improve Peoples Gas' pipeline safety performance. *Id*. at 18. A PSMS would improve Peoples Gas' internal lines of communication and would require all facets of the organization to better understand their roles and what is required of them. *Id*. Given the record evidence regarding Peoples Gas' pipeline safety performance, implementation of such a system as a condition of approval of the transaction is clearly necessary to protect the interests of the Gas Companies and their customers, within the meaning of Section 7-204(f) of the Public Utilities Act. *Id*.

Staff argues that Peoples Gas' concerns regarding implementing a PSMS lack merit. While initial implementation of a PSMS will not resolve the various deficiencies at Peoples Gas, as Peoples Gas encounters issues not currently resolved by the PSMS, steps can be taken to strengthen the program and thus implement a stronger PSMS. Staff Ex. 10.0 at 2. Accordingly, Peoples Gas' concern that it has no other PSMS to emulate is ill-taken, since Peoples Gas will, over the course of time, have its own experience to draw on. It is likely that the program will be markedly different in 10 years from the PSMS originally adopted. *Id*. As to costs and burdens, it seems likely that the successful operation of a PSMS is likely to result in a substantial reduction in the fines that Peoples Gas is required to pay for violations of the Illinois Gas Pipeline Safety Act; the record reflects that Peoples Gas was fined $1.3 million to resolve only three violations. Such savings are likely to offset at least some of the costs of implementing a PSMS. Likewise, as noted above, Peoples Gas has in the past been required to retain consultants to identify defects in its pipeline safety policies, procedures and practices. To the extent that a PSMS improves Peoples Gas' pipeline safety performance without requiring the retention of consultants, Peoples Gas can realize significant offsetting savings there as well. Further, arguing that implementing a PSMS will be burdensome; Peoples Gas' pipeline safety record is such that it must be required to undertake certain burdens to improve it.

The main disagreement between Staff and the Joint Applicants is the time frame for a draft plan to be prepared by the Gas Companies. The Joint Applicants propose two years, while Staff proposes one year. Staff's condition also makes clear that the plan is subject to Commission approval. Staff is encouraged by the Joint Applicants' agreement to develop a PSMS, and while in Staff's opinion a draft plan could be developed within one year from the close of the transaction, if the Gas Companies in fact need two years to develop such a draft plan, then Staff will defer to the Gas Companies on that issue provided that the plan is fully subject to Commission approval.

b. Joint Applicants' Position

The Joint Applicants emphasize that there is no dispute between the Joint Applicants and Staff as to whether a PSMS based upon the API RP 1173 should be developed and implemented by the Gas Companies. The only difference in positions is how much time should be allotted for the Gas Companies and Staff to work together to develop a PSMS to be implemented by the Gas Companies – one year (Staff's position) or two years (the Joint Applicants' position). The Joint Applicants state that they do not agree that the adoption of a PSMS is necessary to protect the interests of the Gas Companies and their customers, and state that adopting a PSMS would be an "enhancement" of public interest rather than a measure designed to protect the status quo as authorized under Section 7-204(f). *See* Docket No. 11-0046, Order at 77. Nevertheless, in an effort to narrow the issues and seek compromise with Staff, the Joint Applicants note that they have agreed to a condition requiring the development of a PSMS with Staff that would be implemented by the Gas Companies when completed and approved by the Commission.

The Joint Applicants believe that based on the evidence it would be more appropriate for the Commission to allow two years for a PSMS to be developed for implementation by the Gas Companies.

The Joint Applicants point out that the document upon which a PSMS would be based, API RP 1173, is not yet finalized and has not been issued in final form. Consequently, at this time, the Joint Applicants assert that the Commission, Staff and the Gas Companies can only speculate as to what exactly may be required to develop and establish a PSMS. In any event, what is known for a certainty is that no model exists for a PSMS that has been developed for or adopted by a natural gas distribution company. JA Ex 11.0 at 4; Staff Ex. 10.0 at 2.

Further, the Joint Applicants point out that the proposed development of the PSMS by the Gas Companies and Staff will coincide with the implementation of recommendations from Liberty's Final Report of its investigation of the AMRP. Consequently, the Joint Applicants assert that the Gas Companies and Staff will need to ensure that the PSMS being developed is consistent with and causes no conflict with any processes that are implemented in response to Liberty's final recommendations.

c. Commission Analysis and Conclusion

It is undisputed between Staff and the Joint Applicants that a PSMS based upon the API RP 1173 should be developed and implemented by the Gas Companies. The problem is that the document has not been released by the API. The main issue between the parties was how much time it should take for the Gas Companies to provide Staff their draft proposal. Staff indicated that they would like to see the draft in one year, but if the Gas Companies need two years to develop the system, Staff would defer to the two years. Therefore, the compromise language as proposed by Staff will be approved as a condition (set forth in Appendix A as condition 14) by the Commission.

2. Requiring Movement of Inside Meters

a. Staff's Position

According to Staff, federal regulations enforced under the Illinois Gas Pipeline Safety Act require operators of gas distribution systems, such as Peoples Gas, to conduct periodic leakage surveys and periodically monitor facilities for atmospheric corrosion. *See, generally*, 49 C.F.R. §§192.481; 192.723. More specifically, Peoples Gas is required to conduct leakage surveys in business districts "at intervals not exceeding 15 months, but at least once each calendar year" and outside of business districts "at least once every 5 calendar years at intervals not exceeding 63 months." 49 C.F.R. §723(b)(1), (b)(2). Further, Peoples Gas must inspect exposed pipelines for evidence of atmospheric corrosion "[a]t least once every 3 calendar years, but with intervals not exceeding 39 months[.]" 49 C.F.R. §192.481(a). Each of these regulations applies to gas meter locations, including insider meters. Staff Ex. 3.0 at 11. Staff states that it has taken Peoples Gas approximately fourteen years to accomplish compliance. Staff Ex. 3.0 at 14. Staff avers that this is clearly well in excess of what is permitted by federal regulations.

Staff notes that this problem may be attributable to any of several causes, but the main cause has been Peoples Gas' difficulty in gaining access to locations where the inside meters are located. Staff Ex. 3.0 at 14. Staff proposes to require that all inside meters be moved outside. The Joint Applicants assert that it is not feasible to move all meters outside. JA Ex. 11.0 at 7. According to Staff, the objective of meter placement is to provide Peoples Gas with unencumbered access to meters of any kind, so that it can conduct required safety inspections. Staff Ex. 10.0 at 4

Peoples Gas contends that inside meters are not per se inaccessible. JA Ex. 11.0 at 9. Peoples Gas argues that inside meters are accessible in multi-unit buildings where there is staffing 24 hours per day, commercial buildings staffed during business hours, and multi-unit buildings that have a landlord or property manager who can provide access. *Id*. While it is reasonable to conclude that inside meters in these specific, discrete classes of buildings may be accessible for inspection and need not be moved outside, (Staff Ex. 10.0 at 5) this does not by any means resolve the entire problem. Staff states that the record reflects that Peoples Gas has gone so far as to at least consider disconnecting customers' gas service due to its inability to obtain access to conduct Inside Safety Inspection ("ISI") of customers' premises. *Id*. It is apparent that

Peoples Gas has difficulties obtaining access to its own gas meters located inside customer's residences and/ perhaps commercial or business locations. *Id*.

Peoples Gas next contends that moving meters supplied by the low pressure cast iron main system outside will result in reduced reliability of services, because cast iron main systems are susceptible to water infiltration. JA Ex. 11.0 at 9-10. Staff agrees that this concern is not unreasonable. Accordingly, in order to protect the interests of Peoples Gas and its customers and consistent with Section 7-204(f) of the Act, Peoples Gas should be required as a condition of approval of the transaction to move all meters from inside to the outside when accessibility is, or may become a concern when Peoples Gas is replacing cast iron or ductile iron pipelines as part of AMRP. Staff Ex. 10.0 at 6. These meters must be moved as part of AMRP, but no later than 2030. *Id*. Such a requirement should also assuage Peoples Gas' concerns regarding cost, potential inefficiency, and conflict with AMRP. *See* JA Ex. 11.0 at 9-10.

Peoples Gas has encountered meter accessibility issues for at least the past 14 years in attempting to meet its ISI obligations relating to 49 C.F.R. §§192.481 and 192.723. Staff Ex. 10.0 at 7. Not only has it taken Peoples Gas 14 years to complete the ISIs, there is no reason to suppose this will not be a continuing problem. *Id*. If Peoples Gas remains unable to complete the ISIs in a timely manner going forward, then monetary penalties should imposed. *Id*. In an effort to alleviate the issue with accessibility of indoor meters where access is not guaranteed; the Commission should direct Peoples Gas to move indoor meters to the outside. *Id*. If the indoor meters are associated with pipe to be replaced as part of AMRP, then those meters can be moved in the course of associated AMRP work, but no later than 2030. *Id*. If there are inside meters that are not associated with pipe to be replaced as part of AMRP, and accessibility is an issue, then those meters should be moved outside, or to a location indoors where access by Peoples Gas is guaranteed, within 10 years of the date of the Commission Order in this proceeding. *Id*. at 7-8. In addition, with respect to large multi-unit buildings with 24-hour staff, multi-unit buildings with landlords or property managers on the premises who have a right to access the units, and commercial buildings that are staffed during normal business hours, those meters need not be moved to the outdoors and may be allowed to remain in the current location, provided those meters remain accessible to Peoples Gas personnel. *Id*. at 8.

With respect to the Joint Applicants proposed condition regarding the relocation of inside meters, Staff states that it appears that Peoples Gas proposes to prepare a plan, without input from Staff, providing the bases pursuant to which Peoples Gas will or will not move a meter. In essence, Staff argues that the Joint Applicants' language would give Peoples Gas a unilateral basis for never moving certain meters.

Staff asserts that its language, on the other hand, requires that inside meters will either be moved outside, or to an accessible location, within certain time frames. Staff's condition language is the only condition which guarantees that all inside meters, after a certain point in time (2030 for meters associated with AMRP and within 10 years for non-AMRP), will be accessible to Peoples Gas. *See*, Staff IB, Appendix B, #4.

In the alternative, if the Commission believes that there may be some instances where some inside meters should not be moved, Staff proposes modifications to the Joint Applicants' proposed condition #15. Staff's modifications address the situation where Staff and Peoples Gas are unable to reach a common agreement on the process for determining whether certain meters remain inside, or are not relocated to an accessible inside location. The Joint Applicants' proposed condition #15 assumes that Staff and Peoples Gas will be able to reach complete agreement on the process for determining whether certain meters remain inside, or are not relocated to an accessible inside location. While Staff is hopeful that such a process can be worked out between it and Peoples Gas, it is possible that such agreement may not be reached. In the event Staff and Peoples Gas are not able to reach agreement, Staff recommends that Peoples Gas be required to file a petition with the Commission initiating a new docket seeking the approval of its process. In that proceeding, Staff and Peoples Gas would have the opportunity to provide testimony and argument supporting its proposed process, with the Commission ultimately deciding the issue.

b. Joint Applicants' Position

The Joint Applicants state that they agree with the goal of moving as many meters currently located inside customers' premises to the outside or accessible indoor locations. The Joint Applicants highlight that the first sentence of Staff's proposed condition is consistent with Peoples Gas' existing AMRP plan, and, to support this goal the Joint Applicants have proposed an additional condition that would require the development of a new standardized process, to be reviewed by Staff, for determining when to leave a meter inside or in a decentralized location. With respect to the second sentence of Staff's proposed condition, however, the Joint Applicants argue that Staff's request for the Commission to impose a requirement on the Joint Applicants to move all inside meters that are not part of the AMRP outside or to an accessible location within 10 years should be rejected, as it is problematic for several reasons.

As an initial matter, the Joint Applicants state that this proposed condition does not comply with the Commission's permissive authority to impose a condition on a reorganization when, in its judgment, such condition is "necessary to protect the interests of the public utility and its customers" because it is not consistent with any interest set forth in Section 7-204(b), and instead seeks to enhance or improve Peoples Gas' performance. The Joint Applicants assert that there has been no showing that imposing this additional requirement which would require the creation of a new capital program in addition to AMRP is necessary to protect the interests of Peoples Gas or its customers. While having meters moved to the outside would make it easier and more convenient for Peoples Gas to conduct required federal safety inspections, the Joint Applicants maintain that Staff has failed to show that it is necessary to do so. The federal regulations at issue assume that there will be inside meters to be inspected and, although difficult, Peoples Gas has demonstrated that it can comply with the inspection requirements even with meters being located inside customers' premises. Indeed, the Joint Applicants aver that it should become easier for compliance to be achieved as the universe of existing inside meters shrinks due to the movement of meters as part of the AMRP. The Joint Applicants contend that the existence of inside meters that need to be

inspected is a long-standing condition of Peoples Gas' service territory, and Staff has not argued that the Reorganization threatens the existing ability of Peoples Gas to comply with its required inside safety inspections. Requiring the movement of non-AMRP meters, therefore, would be a potential enhancement, not protection, of utility and its customers' interests. Thus, it is the Joint Applicants' position that the second sentence of Staff's proposed condition is not an appropriate condition for the Commission to impose on the Reorganization pursuant to Section 7-204(f).

Furthermore, the Joint Applicants argue that the evidence demonstrates there are practical problems with imposing such a requirement. The Joint Applicants point out that they submitted evidence demonstrating that it is not reasonably feasible to move all meters outdoors in light of there being physical and legal constraints on the ability of Peoples Gas to place meters outside in all situations. Further, the Joint Applicants emphasize that while Staff dismisses this testimony as an assertion that "bears little scrutiny", Staff recently agreed in a stipulation made part of a Commission Order (*Illinois Commerce Comm'n v. The Peoples Gas Light and Coke Company*, Docket No. 13-0460, Order at 4 (Jan. 28, 2015)) that, "[i]t will not be feasible to move 100% of [Peoples Gas'] meters outdoors or to a central, accessible location." Docket No. 13-0460, Order at 4.

Furthermore, the Joint Applicants also argue that a requirement to start a new program to move all meters outside of the AMRP in 10 years in addition to what also is being done to move meters as part of the AMRP would greatly increase costs for Peoples Gas' customers. The Joint Applicants note that they introduced evidence that such a program would increase the current workload being done to move meters as part of the AMRP by over 14%. Not only would this add significant capital costs to be recovered from customers in addition to AMRP costs, but the strain on Peoples Gas' resources to conduct this additional capital program could delay the current AMRP schedule. Thus, the Joint Applicants state that it is unlikely that this portion of Staff's proposed condition would be beneficial to the interests of Peoples Gas or its customers.

c. Commission Analysis and Conclusion

The Commission notes that Peoples Gas has had a long standing problem with meter inspection. As pointed out by Staff there are concerns about the meters that have remained inside or in inaccessible locations. Federal regulations enforced under the Illinois Gas Pipeline Safety Act require operators of gas distribution systems, such as Peoples Gas, to conduct periodic leakage surveys and periodically monitor facilities for atmospheric corrosion. Thus, Peoples Gas is required to inspect the pipelines and meters for leaks and corrosion. This includes meters located inside of residences and buildings. The Joint Applicants argue that the conditions requested by Staff would require Peoples Gas to initiate an additional capital program. While the Commission understands the Joint Applicants' argument, there is concern that the pipes and meters that are not inspected in a reasonable time could lead to catastrophic problems. Staff has recommended a compromise proposal in an effort to address this problem. This proposal would have Peoples Gas develop a new process for Staff's review. If they cannot agree on a process for leaving some meters inside or not relocating all meters to

an accessible location, Peoples Gas would be required to file a petition for review of the proposed process by the Commission. The Commission finds that the compromise as recommended by Staff is hereby adopted as condition 15 of Appendix A.

3. Docket No. 15-0186

a. Staff's Position

On March 11, 2015, the Commission initiated a docket to investigate allegations made in two anonymous letters concerning mismanagement of the AMRP and alleged criminal and fraudulent activity by employees and other parties associated with several of the Joint Applicants. In its Initial Brief, Staff recommended that the Commission impose two conditions on its approval of the Reorganization. First, Staff proposed that the Commission impose a condition to ensure that Peoples Gas' ratepayers are not responsible for any expenses that arise out of misconduct, illegal or criminal activity should the allegations be true, while allowing Wisconsin Energy and Integrys to contractually assign between themselves any such costs arising out of the investigation. Second, Staff proposed a condition that would require Wisconsin Energy to terminate the employment or contract of any officer, employee, agent or representative of the Joint Applicant if, through the investigation, that person is found to have committed wrongdoing.

b. Joint Applicants' Position

The Joint Applicants do not have any objection to the Commission imposing conditions to address these concerns, but suggest modifying the language of the conditions to address certain issues. The Joint Applicants request modifications to clarify that it would be the Commission making the determination that any conduct had occurred that requires action by the Joint Applicants under the conditions, and to define the term misconduct for purposes of the proposed conditions. Additionally, with respect to the second condition, the Joint Applicants suggest that language was needed to address the potential scenario where an employee at issue is a union member whose termination could be subject to grievance or arbitration proceedings. The Joint Applicants assert that they were able to reach agreement with Staff on the conditions to be imposed by the Commission with respect to the investigation that will occur in Docket No. 15-0186.

c. Commission Analysis and Conclusion

The Commission initiated an investigation of two anonymous letters concerning mismanagement of the Peoples Gas' AMRP in Docket No. 15-0186. The anonymous letters allege mismanagement of the AMRP and criminal and fraudulent activity by several of the Joint Applicants. Staff proposed implementing conditions on the Joint Applicants in the event that as a result of the ongoing investigation the Commission determines that there has been misconduct, or unlawful or criminal activity. The Commission agrees with Staff that conditions should be imposed to protect Peoples Gas' ratepayers from incurring any expenses related to any misconduct related to the

AMRP. Staff's Motion to Request Administrative Notice of the Corrected Initiating Order in Docket No. 15-0186 was granted in this Docket. The Commission finds that a condition requiring Wisconsin Energy to take action to terminate the employment or contractual relationship of any officer, employee, agent or representative of the Joint Applicants found by the Commission to have committed such wrongful conduct is required to protect the interests of Peoples Gas and its customers. The language of the two conditions agreed to by Staff and the Joint Applicants is reasonable and is adopted as conditions to the Reorganization. The conditions are included as conditions 46 and 47 of Appendix A.

B. Conditions Proposed by AG and/or City/CUB

1. Construction Fines and Penalties

a. The AG's Position

As a condition of the approval of the Reorganization, the AG has proposed the following language.

> Peoples Gas shall credit customers for all construction fines and penalties paid from the beginning of 2011 to date to the City of Chicago, plus any fines and penalties incurred through the close of the merger, that were recovered in base rates or infrastructure riders. The credits could be flowed through PGL's Rider QIP during a single month or alternatively contributed by PGL to its "Share the Warmth" fund.

This is a proposal from AG witness Coppola based on the information received from City/CUB witness Cheaks who indicated that Peoples Gas has paid degradation fees concerning the AMRP.

b. Joint Applicants' Position

The Joint Applicants argue that the unrebutted evidence in the record establishes that Peoples Gas excludes construction fines and penalties from base rate recovery requests and it does not include fines and penalties in any rider recovery mechanism. The Joint Applicants assert that the conditions requested by the AG, therefore, would be superfluous and unnecessary for the protection of the utility or its customers. Accordingly, the Joint Applicants contend that the request for this condition should be denied.

c. Commission Analysis and Conclusion

The AG listed this item as a proposed condition for the Reorganization without any details or argument to support this provision. There was very limited information contained in the record to indicate that Peoples Gas was recovering construction fines

and penalties as part of its rate base or through any rider mechanism. Mr. Cheaks indicated that Peoples Gas had paid significant degradation fees, but there was no information in the record to indicate that any fines or penalties were recovered in rates or rider. The Joint Applicants specifically state that the degradation fees are charges from CDOT for opening within a moratorium street. JA Resp. to AG DR 11.01, AG Ex. 4.5. There was no information that Peoples Gas included penalties and fines in base rates or in any rider mechanism. Therefore, this condition proposed by the AG is denied.

2. Cap on Fixed Charges for Residential Revenue Recovery

a. The AG's Position

The AG claims that it is no secret that in addition to experiencing the financial pains of five rate increases over the last seven years, the Gas Companies' customers have seen their fixed monthly customer charges grow to 63% of the bill for Peoples Gas customers and 73% for North Shore customers. The AG points out that Peoples Gas and North Shore customers now pay the highest fixed monthly customer charges and overall rates in Illinois, with customer charges at $30.84 and $23.94 for Peoples Gas and North Shore heating customers, and $16.37 and $15.70 for Peoples and North Shore non-heating customers, respectively.

Including a merger condition that lowers the customer charge portion of the bill such that no more than 40% of revenues is collected through the residential heating class customer charge is in the public interest and fully justified if customers are to see value from the Reorganization beyond any rate freeze commitment, according to the AG. Adding the customer charge cap to the merger condition list is particularly appropriate in view of facts arising since the filing of testimony in this case and the Commission's January 21, 2015 rate case Order in Docket Nos. 14-0224/14-0225 (Consol.) - specifically, the January 23, 2015 Supreme Court Decoupling Opinion, which affirmed the Commission's approval of Rider VBA. Rider VBA uncouples the Companies' revenues from their sales such that utilities that have "decoupling" riders have recovery of the full amount of their Commission-approved revenue requirement guaranteed, through an annual reconciliation process that accounts for under-recovery or over-recovery of approved revenues and authorizes customer bill surcharges or credits, respectively. Since the Supreme Court's decision now guarantees that Peoples Gas and North Shore will continue to recover their entire Commission-approved revenue requirement each year, the AG argues that the Commission should add the customer charge reduction commitment to the list of merger conditions in light of the increased value this reduction in shareholder risk brings to WEC.

The Supreme Court's decision just two days after entry of the Commission's Final Order in Docket Nos. 14-0224/14-0225 (Consol.) provides added value to WEC shareholders because it effectively settled any uncertainty as to whether the Gas Companies would be permitted to retain their decoupling riders going forward, according to the AG. A WEC commitment to lower the customer charge to a level that caps recovery of revenues through the fixed charge portion of monthly customer bills

would acknowledge this reduction in risk and provide a tangible value to Peoples Gas/North Shore customers. Doing so, too, would provide Peoples Gas and North Shore customers more control over their natural gas bills, enabling the General Assembly's public policy goal of reducing the usage of natural gas and achieving least cost utility service, consistent with Sections 8-104 and 1-102 of the Act, the AG states.

In view of these new facts and circumstances regarding Rider VBA and the revenue protections it now offers the Joint Applicants on a permanent basis, and in light of the fact that ratepayers have seen their monthly customer charges rise by almost 200% (Peoples Gas) and 179% (North Shore) since the inception of Rider VBA, the AG urges the Commission to condition merger approval on a (revenue-neutral) lowering of the customer charge that would provide additional, tangible value to the Gas Companies' customers outside of any rate freeze condition, and is consistent with the public interest.

b. Staff's Position

In response to the AG's proposal, Staff states that if the Commission wanted the fixed charge recovery of the revenue requirement to be set even lower than what it set in the most recent rates cases for the Gas Companies, it would have so ordered. The Commission should base its decisions about rate design on the evidence in each rate case and not impose an overall cap on the percentage of fixed cost recovery independent of cases-specific evidence. Staff recommends the Commission reject the AG's proposed condition.

c. Joint Applicants' Position

The Joint Applicants state that the AG proposes, for the first time in its Initial Brief, a condition requiring that the customer charge portion of the Gas Companies' bills for residential heating class customers be lowered so that it is no more than 40% of their bills. It is the Joint Applicants' position that the AG's proposal would disrupt and change the rate design recently established for the Gas Companies in Docket Nos. 14-0224/14-0225 (Consol.). Moreover, there is no evidence in the record to support the AG's request. The Joint Applicants argue that the only basis for this request, other than the AG's standard opposition to higher customer charges generally, is the AG's argument that two days after the final Order was issued, the Supreme Court of Illinois issued its opinion affirming the Commission's permanent authorization of the Gas Companies' decoupling rider, Rider VBA. The problem with this argument, the Joint Applicants assert, is that the Commission set the Gas Companies' rate design in Docket Nos. 12-0511/12-0512 (Consol.) based upon the assumption that Rider VBA would be in effect.

d. Commission Analysis and Conclusion

The AG proposes a condition that would lower the customer charge for the Gas Companies residential heating class to 40% of their bill. The Commission made the determination of the customer charge portion based on the evidence that was presented

in Docket Nos. 14-0224/14-0225 (Consol.). There has been no record evidence in this docket as to this proposal and the Commission is reluctant to impose this cap outside of a rate case. It is noted that the first time the AG proposed this condition was in its initial post hearing brief. The Commission will not make changes to the rate design from the recent rate case and this proposal by the AG is denied.

3. ICE Costs

a. The AG's Position

The AG asserts that merger approval should be conditioned on the Joint Applicants' agreement to provide an additional rate benefit to Peoples Gas and North Shore customers based on new information in the record in this docket that demonstrates that the Gas Companies will be experiencing significant savings post-merger related to ratepayer financing of the Integrys Customer Experience ("ICE") project. The ICE project will unify Cfirst, which is the customer information system that Peoples Gas and North Shore currently uses, and the various customer information systems currently in use across Integrys. It will provide significant benefits to Peoples Gas and North Shore and the other Integrys regulated utilities such as improved efficiency and productivity and standardization of internal delivery which will improve customer satisfaction. In addition to unifying systems, the ICE project will improve and enhance billing, collections, call center, and self-service related offerings by ensuring that these functions are staffed appropriately to continue to leverage the opportunities of a large corporation, while maintaining the high level of service of a local utility. AG Ex. 1.0 at 12 (citing Docket Nos. 14-0224/14-0225 (Consol.); PGL Ex. 13.0 at 10.

According to the AG, the Gas Companies have taken contradictory positions in Docket Nos. 14-0224/14-0225 (Consol.) and this proceeding as to whether savings associated with the ICE project will be realized sooner than forecasted in the rate case. In particular, the Gas Companies included $9.2 million in expenses associated with the ICE project in their revenue requirements in Docket Nos. 14-0224/14-0225 (Consol.) and asserted that the ICE system would result in significant efficiencies that will produce cost reductions. The Gas Companies did not reflect savings associated with the project in the 2015 test year. But then, in discovery responses in this docket from the Joint Applicants, they provided updated information that show the ICE project with estimated net benefits beginning in 2015. AG Ex. 1.0 at 14-16. In fact, Mr. Effron testified, it is expected that ICE will produce a "'net benefit (a credit to expense, i.e. pre-tax reduction in O&M),'" which is "'derived from forecasted system savings greater than forecasted system costs'" *Id*. at 13-14, citing Joint Applicants' response to Data Request AG 2.13, attached as AG Ex. 1.3. This new information provided in this case contradicts the Gas Companies' position in Docket Nos. 14-0224/14-0225 (Consol.) that ICE savings would not be achieved until 2016, with no reductions in the 2015 Test Year. *Id*. at 14. Response to AG Data Request PGL 11.08, Docket Nos. 14-0224/14-0225 (Consol.), attached as AG Ex. 1.4.

Accordingly, the AG maintains that the evidence in this case shows that if there is no adjustment to the ICE costs forecasted by the Gas Companies in those cases, the

Gas Companies will be recovering $19.2 million in non-existent expenses when the ICE project goes into service. *Id*. at 18-19. In effect, during the term of the proposed rate freeze, the customers would be charged for all of the annual costs of the ICE project, while 100% of the benefits of the ICE project would be retained for shareholders. *Id*. at 19. The AG points out that the Joint Applicants have stated that they are "prepared to provide immediate benefits to customers and the Illinois communities the Gas Companies serve by making commitments that it would accept as conditions on the Commission's approval of the Reorganization." JA Ex. 1.0 at 15. Adoption of a mechanism that properly credits customers for the ICE savings is a reasonable condition for approval of the merger.

In reply to the Joint Applicants, the AG argues that both interpretations of the proposal are incorrect. First, the AG points out, Mr. Effron's proposed condition is offered as an attempt to ensure that new information about the ICE project provided by the JA in this merger proceeding is reflected in customer rates going forward, not, as the JA suggest, to cure some past rate infraction. In no way does it seek any kind of retroactive adjustment of rates. It would not be implemented pursuant to any refund provision of the Act, but rather as a condition of the merger pursuant to Section 7-204(f) of the Act.

In reply to Staff, the AG states that the Commission has specifically rejected the argument that rate adjustment proposals in the context of merger proceedings trigger single-issue and retroactive ratemaking concerns under Article IX principles. *See* Docket No. 11-0046, Order at 29-30. In that case, the AG points out, the Commission rejected claims by AGL/Nicor that the "adverse rate impacts" prohibited by the statute cannot occur unless the "totality" of a merger, rather than a limited number of cost elements, will likely affect the utility's retail rates. *Id*. at 29. The Commission stated, "Absolutely nothing in the subsection states or implies that only the 'totality' of a proposed merger can have the precluded adverse impact. Subsection (b)(7) bars 'any' likely adverse rate impact, of whatever cause associated with reorganization. Indeed, the Commission cannot perceive what would constitute the 'totality' of merger, why the legislature would not protect retail customers from adverse rate impacts resulting from less than a 'totality,' or why resources should be expended debating or implementing a 'totality' standard." *Id*.

In the instant case, according to the AG, the evidence makes clear that unless action is taken under Section 7-204(f), ratepayers will be adversely impacted by rates that reflect all of the costs but none of the savings associated with the ICE project. Moreover, contrary to Staff's unlawful rider argument, the proposal by Mr. Effron is not intended to be a permanent rider mechanism. Rather it is intended to provide the benefit that the Joint Applicants' discovery responses indicate will occur in 2015 and beyond. If the Commission is uncomfortable in recognizing this benefit through a rider refund mechanism, it should calculate the value of the ICE-related benefit for the period of any rate freeze and provide a one-time refund to Peoples Gas/North Shore customers at the close of the merger.

For all of these reasons, the AG states that Mr. Effron's proposal (or a modification of that proposal that captures this revenue difference) should be adopted as a condition of any Commission merger approval, pursuant to Section 7-204(f).

b. Staff's Position

Staff recommends that the Commission reject the AG's proposal that the Joint Applicants' merger be conditioned on the Commission ordering that a rider be imposed on the Gas Companies. *See* Staff Ex. 12.0 at 6-7. Staff states that approving the AG's rider would be contrary to the law. While "the Commission has the power to authorize a rider in a proper case and such authorization will not be reversed absent an abuse of discretion" (*Commonwealth Edison Co. v. Illinois Commerce Comm'n*, 405 Ill. App. 3d 389, 411 (2nd Dist. 2010)), the proposed AG rider ICE satisfies neither requirement. The AG rider is intended to address the difference in costs of the ICE project reflected in the rate cases versus the ICE costs incurred if the Reorganization is approved. Under the law, the Commission only has the discretion to approve a rider mechanism if: (1) the cost is imposed upon the utility by external circumstances over which the utility has no control; and (2) the cost does not affect the utility's revenue requirement. *Id.* at 414. That is, a rider is only appropriate, if the utility cannot influence the cost and the expense is a pass through item that does not change other expenses or increase income. *Id*. With respect to the first element of the Commonwealth Edison test, the AG has failed to show that the costs related to the ICE project are costs imposed by external circumstances over which North Shore/Peoples Gas has no control. With respect to the second element, the ICE project costs would have an impact People Gas/North Shore's revenue requirement, given that the base for determining the costs to be recovered through the rider are the costs approved in the recent People Gas/North Shore rate cases.

Finally, in rebuttal, AG witness Effron, testified that, "[c]onditioning approval of the merger of the adoption of the described rider[s] is not the same as ordering Peoples Gas and North Shore to adopt such a rider." AG Ex. 3.0 at 2. If by this testimony, the AG is suggesting that as long as the Joint Applicants do not object to the AG's proposed rider conditions, the Commission can include the riders as part of its order, this assertion is contrary to law, for either of two reasons. First, under the law, a Commission order must be consistent with and not violate the Act. *See*, *Business and Professional People v. Illinois Commerce Comm'n*, 136 Ill. 2d 192, 217 (1989) ("Absent statutory law to the contrary, we have no quarrel with the Commission's ability to consider a settlement proposal not agreed to by all of the parties and the intervenors as a decision on the merits, as long as the provisions of such a proposal are within the Commission's power to impose, the provisions do not violate the Act, and the provisions are independently supported by substantial evidence in the whole record. Such was not the situation in the case at bar"). Staff states that because the AG's rider proposal would violate the Act, the Commission cannot impose it even if it is agreed to by Joint Applicants.

Also, if the AG's argument is indeed that a voluntary commitment to, or acquiescence in, a rider makes it lawful, this simply does not survive the Commonwealth Edison test. Staff states that to be properly recoverable under a rider, costs must be imposed by external circumstances over which a utility has no control. Yet, a utility has absolute control over whether it will accept a voluntary commitment, or not object to the imposition of one. Accordingly, the AG's logic is fatally flawed, and its

arguments must be rejected. For these reasons, Staff recommends that the Commission reject the AG's proposed rider ICE project costs.

c. Joint Applicants' Position

The Joint Applicants observe that the AG requests that the Commission impose a rider mechanism for costs for the ICE project (Integrys' customer information system). This rider would require the Gas Companies to refund to customers the difference between cost recovery that was approved in Docket Nos. 14-0224/14-0225 (Consol.) and what the AG argues are the lower, actual costs for these items. The Joint Applicants argue that the Commission addressed and rejected the AG's arguments concerning the appropriate level of cost recovery for this item in its January 21, 2015 final Order in those rate cases. The Joint Applicants believe the AG's position in this proceeding is an effort to re-litigate this issue, which the Commission previously denied. The Joint Applicants assert that singling out ICE costs (and savings) for such treatment, while ignoring other specific cost items that have increased, such as City paving, restoration and permitting costs, is unsound and unfair. Moreover, imposing this rider mechanism would be a violation of the legal rule prohibiting retroactive ratemaking.

d. Commission Analysis and Conclusion

The AG requests that the Commission impose a rider mechanism concerning the ICE project. We agree with Staff and the Joint Applicants with respect to this condition requested by the AG. This issue was addressed in the most recent rate case for the Gas Companies. A rider is only appropriate if the cost is imposed upon the utility by external circumstances over which the company has no control and the cost does not affect a utility's revenue requirement. The Commission finds that it would be a violation of the Act for the Commission to go back to adjust a single item from a utility's revenue requirement after a rate case has concluded if the Commission determined that it had set rates too high or too low. As stated by Staff, even if the Joint Applicants agreed to this proposal, the Commission cannot include such an action in its order issued in this case. Therefore, the Commission rejects the AG's requests for a rider with respect to ICE costs.

4. Illinois Board Member

a. City/CUB's Position

City/CUB argue that the Joint Applicants have given no reason for refusing to require that the Illinois Board member be a customer of one of the Illinois utilities. The Joint Applicants state that their guidance for Commitment 36, requiring an Illinois resident on the reorganized entity's board of directors, was the Commission's decision in Docket 11-0046. Docket No. 11-0046, Order at 30.

City/CUB assert that the Joint Applicants have missed the point of that Commission-imposed condition. The Commission explained its reasons for imposing the condition -- ownership of an Illinois utility by a foreign corporation, the clear legislative policy of protecting utility and customer interests, and ensuring the presence

of a board member with "first-hand knowledge of the issues and concerns unique to [the foreign company's] Illinois utilities and their customers." *Id*. at 15.

City/CUB further assert that only a customer of one of the affected Illinois utilities can provide that first-hand knowledge of the concerns of the utilities' customers. Moreover, since the utilities serve a major portion of Illinois residents and its chief business center, finding a qualified Peoples Gas or North Shore customer should not be difficult. Accordingly, City/CUB conclude that the Joint Applicants' Commitment 36 should be modified to add a requirement that the Illinois board member be a customer of one of the Illinois utilities involved in the proposed Reorganization.

b. Joint Applicants' Position

The Joint Applicants argue that while City/CUB rely upon language in Docket No. 11-0046 to support this request, City/CUB fail to acknowledge that the Commission did not require that the Illinois board member in the AGL-Nicor merger be a Nicor customer. The Joint Applicants further argue that unlike the AGL-Nicor merger, the proposed holding company in this docket will be located closer to the Gas Companies' service territories and it will be responsible for fewer utilities in fewer states. The Joint Applicants also maintain that City/CUB fail to explain or present evidence to show why the condition imposed in the AGL-Nicor merger would not be sufficient in this proceeding. Therefore, the Joint Applicants contend that the Commission should reject this additional condition and impose a condition on the WEC Energy Group Board that is similar to the condition imposed in the AGL-Nicor merger.

Moreover, the Joint Applicants note that they presented evidence that it is not uncommon for the parent company of a utility to be located in a different state. The Joint Applicants note that they also presented evidence that demonstrated that the residency of its board members or location of its headquarters has no impact on the company's focus on making sure each of its utilities provide high-quality service in their service territories. The Joint Applicants opine that the residency of a utility holding company's board members is not predictive of whether or not the interests of the utility's customers will be protected, and this is especially true in a situation like the present case where the Gas Companies will maintain local headquarters and have local management running the day-to-day operations of the utilities.

c. Commission Analysis and Conclusion

The Commission agrees that as a condition of this Reorganization one of WEC Energy Group's board members should be from Illinois. It important to the Commission that the local interests of the Gas Companies be protected. City/CUB has requested an additional requirement be placed on the Joint Applicant, that the WEC board member be a customer of one of the Gas Companies. The record does not support imposing an additional condition here for the Joint Applicants. Accordingly, the Commission adopts the condition proposed by the Joint Applicants in this proceeding with respect to at least one of WEC Energy Group's board members being a resident of Illinois (condition 36 of Appendix A).

VII. SECTION 7-204A OF THE ACT

Subsection 7-204A(a) of the Act describes the information that must be provided in connection with a reorganization application.

Subsection 7-204A(b) establishes contract requirements for the use of utility employee services by, and the supply of utility property to, utility affiliates.

A. Joint Applicants' Position

The Joint Applicants state that they have satisfied all the minimum filing requirements under Section 7-204A(a), including submission of copies of any proposed affiliated interest agreements in accordance with Section 7-204A(a)(5). The Joint Applicants seek approval on an interim basis of the WEC Energy Group AIA as recommended by Staff witness Hathhorn.

The Joint Applicants contend that they have satisfied all the information filing requirements in the statute. No party challenges the Joint Applicants' contention.

B. Commission Analysis and Conclusion

The Commission finds that the Joint Applicants have met the minimum information requirements set out in Subsection 7-204A(a). Regarding Subsection 7-204A(b), the evidence presented by the Joint Applicants and Staff supports approval of the WEC Energy Group AIA on an interim basis, subject to the conditions discussed above in connection with subsections 7-204(b)(2) and (b)(3) of the Act.

VIII. SECTION 7-102 OF THE ACT

A. Joint Applicants' Position

The Joint Applicants state that they referenced Section 7-102 in their Application, which requires Commission approval whenever a "public utility may by any means, direct or indirect, merge or consolidate its franchises, licenses, permits, plants, equipment, business or other property with that of any other public utility." The same section also requires Commission approval for a public utility to "assign, transfer, lease, mortgage, sell (by option or otherwise), or otherwise dispose of or encumber the whole

or any part of its franchises, licenses, permits, plant, equipment, business, or other property…." 220 ILCS 5/7-102(A)(c).

The Joint Applicants assert that neither of the above-referenced provisions of Section 7-102 applies to the Reorganization because the Reorganization does not involve a direct or indirect merger or consolidation of two utilities' businesses or property and is not a sale or disposition of a utility's business or property, but rather is a change in control transaction subject to Sections 7-204 and Section 7-204A. Accordingly, the Joint Applicants contend that Section 7-204(e) of the Act applies, which expressly provides that "[n]o other Commission approvals shall be required for mergers that are subject to this Section." 220 ILCS 5/7-204(e).

Further, the Joint Applicants assert that if the Commission determines that the Reorganization is also subject to the requirements of Section 7-102, the information submitted by the Joint Applicants in this proceeding is sufficient to meet the requirements of that section. No party other than the Joint Applicants presented evidence regarding Section 7-102. The Joint Applicants argue that because the evidence supports Commission approval under Section 7-204, it also supports approval of the Reorganization pursuant to Section 7-102 of the Act, should such approval be necessary.

B. Commission Analysis and Conclusion

As part of the application process, the Joint Applicants included Section 7-102 for Commission consideration. No other party in this proceeding commented on whether or not this section applies to the proposed Reorganization. The Commission agrees with the Joint Applicants that this transaction does not involve a direct or indirect merger or consolidation of two utilities' businesses or property and is not a sale or disposition of a utility's business or property, but rather is a change in control transaction. Therefore, the Commission does not consider it necessary to rule on the applicability of Section 7-102.

IX. SECTION 6-103 AND SECTION 9-230

A. Staff's Position

Staff asserts that Section 6-103 of the Act requires that in any reorganization, the Commission shall authorize the amount of capitalization of a public utility formed by a reorganization, which shall not exceed the fair value of the property involved. Staff Ex. 7.0 at 12. Staff also asserts that in prior merger/acquisition proceedings involving Illinois utilities, the Commission has preemptively addressed concerns regarding potential violations of Section 9-230, which prohibits the Commission from reflecting in a utility's rates any incremental risk or increased cost of capital which is the result of a public utility's affiliation with non-utility companies. Staff also notes that, in a recent discussion of this proceeding, as it relates to the Gas Companies' ongoing rate setting proceeding, the Commission cited the influence that WEC Energy Group's capital structure might have on the Gas Companies' financial condition and capital structures. Staff further asserts that WEC has chosen to fund the proposed transaction by

significantly increasing its debt obligations at the corporate level, which creates higher financial leverage at the parent than at the operating companies and increases the risk to the operating companies, potentially necessitating a rate of return adjustment pursuant to Section 9-230.

With respect to Section 6-103, Staff asserted that based on this information, as a condition of any approval of the proposed Reorganization, the Commission should require the Gas Companies to file a compliance report with a copy to the Manager of the Commission's Finance Department following the proposed Reorganization that describes the Gas Companies' post-merger capital structures and identifies capital structure adjustments that result from the proposed Reorganization. Staff states that no further action would be required with regard to this recommendation if the Gas Companies' post-merger capital structures do not involve any push down accounting adjustments. On the other hand, if there are push down accounting adjustments to the Gas Companies' balance sheets, then it is Staff's position that the Commission should also require the Gas Companies to file a petition seeking Commission approval of the fair value studies and resulting capital structures for the Gas Companies' pursuant to Section 6-103 of the Act.

Staff further asserts that it is unlikely that the Merger, as proposed, will comply with Section 9-230 of the Act. Staff relies upon the fact that S&P has assigned Peoples Gas and North Shore a negative rating outlook which indicates that the Gas Companies' credit rating could be downgraded as a result of the proposed Reorganization. Staff asserts that such a downgrade would likely increase the Gas Companies' cost of capital, which would necessitate an adjustment to the authorized rate of return pursuant to Section 9-230 if not properly addressed beforehand. Staff further asserts that a credit rating downgrade notwithstanding, a Section 9-230 adjustment would be necessary because there is a limited debt capacity at the consolidated level, which means that the Gas Companies cannot take full advantage of their debt capacities without jeopardizing WEC Energy Group's current credit ratings and their own S&P credit ratings due to S&P's practice of aligning subsidiary credit ratings with those of the parent company. Adjusting the Gas Companies' capital structures is a reasonable method for addressing this issue, Staff argues, particularly in light of the greater financial leverage expected at WEC Energy Group (56% debt) compared to Peoples Gas (49.52% debt) and North Shore (49.67% debt). As such, Staff initially recommended that the Commission require a study of appropriate post-merger capital structures for Peoples Gas and North Shore, similar to those ordered in Docket Nos. 11-0721 and 12-0001. The study, to be performed by the Gas Companies under the guidance of the Commission's Finance Department Manager, was proposed to commence no later than six months prior to, and be presented to the Commission in final form at the time of or before, the filing of the Gas Companies' next rate case.

Staff proposes two conditions, which were agreed to by the Joint Applicants. With these two conditions, Staff states that the Reorganization would satisfy the requirements of Sections 6-103 and 9-230 of the Act.

B. Joint Applicants' Position

The Joint Applicants state that they do not agree with Staff that Section 6-103 and 9-230 apply to this proceeding, relying in large part on the language of Section 7-204(e) which provides that no other Commission approvals shall be required for mergers subject to Section 7-204. Further, the Joint Applicants assert that by its very terms, Section 9-230 applies only in a proceeding in which the Commission is determining a utility's rate of return, and thus it does not apply to the present Section 7-204 proceeding. The Joint Applicants argue that these issues could be addressed in the Gas Companies subsequent rate cases, which will not occur in the immediate future in light of the Joint Applicants' commitment not to seek an increase in base rates that would be effective any earlier than two years from the closing of the Reorganization.

Nevertheless, in an effort to compromise and narrow the disputed issues in this proceeding, the Joint Applicants state that they agreed with Staff on the language for the two conditions to address Staff's Section 6-103 and Section 9-230 concerns.

C. Commission Analysis and Conclusion

Staff's compliance reporting recommendations and requested study will enable the Commission to better monitor post-merger events, both predictable and unforeseen. The Joint Applicants disagreed with Staff as to whether these sections applied in this proposed Reorganization. However, the Joint Applicants agreed to the conditions as proposed by Staff. Both of the foregoing Staff recommendations, which the Joint Applicants accept for purposes of securing merger approval, are adopted. The Commission agrees with Staff that the inclusion of these conditions would satisfy the requirements of Section 6-103 and 9-230 of the Act. (Condition # 31 and Condition # 33, Appendix A).

X. APPROVAL OF REORGANIZATION WITH RESPECT TO ATC

A. Joint Applicants' Position

The Joint Applicants state that ATCLLC is a Wisconsin limited liability company managed by a corporate manager, ATCM, a Wisconsin corporation, and together, they operate as a single entity, "ATC", which owns and operates a high-voltage electric transmission system in an area from the Upper Peninsula of Michigan, throughout the eastern half of Wisconsin and small portions of Minnesota and Illinois. As a result of the Reorganization, WEC Energy Group will own a majority – 60.31% – of the outstanding shares of ATCM. The Joint Applicants assert that because ATC is certificated as an Illinois transmission-only utility and the Reorganization will result in a change in ownership of a majority of its voting capital stock, the Commission arguably needs to approve this change in ownership of ATC pursuant to Section 7-204 of the Act, as well. The Joint Applicants note that they provided all of the information for ATC required by Section 7-204A(a) and submitted testimony to demonstrate that the Reorganization meets each of the required Section 7-204(b) findings with respect to the change in ATC's ownership. The Joint Applicants assert that ATC charges no retail rates to any

Illinois end-user and that ATC's transmission service rates are regulated exclusively by the FERC, and that except for fundamental corporate matters, Wisconsin Energy will not exercise control over ATC on matters requiring shareholder approval. The Joint Applicants argue that for these reasons, Wisconsin Energy's acquisition of a majority ownership interest in ATC will have no material impact on end-use customers, competition or the Commission's regulatory authority.

No other party presented evidence with respect to the change in ownership in ATC that will result from the Reorganization or addressed the Joint Applicants evidence on this issue. Neither Staff nor any other party to this proceeding has opposed the Joint Applicants' position and arguments in favor of the Commission approving the Reorganization with respect to the partial change in ATC's ownership that will result from the Reorganization.

B. Commission Analysis and Conclusion

ATC is certificated as a public utility in Illinois and the Reorganization will result in a change in the majority ownership of the voting capital stock of ATC. The Commission must review the Reorganization to determine whether the requirements of Section 7-204 are met with respect to ATC. The Commission notes that ATC charges no retail rates to any Illinois end-user and that ATC's transmission service rates are regulated exclusively by the FERC. The Joint Applicants state that except for fundamental corporate matters, Wisconsin Energy will not exercise control over ATC on matters requiring shareholder approval. No other party commented on the issues concerning ATC. Therefore, the Commission finds that the evidence in the record establishes that the Reorganization meets the requirements of Section 7-204 with respect to the change in the majority ownership of ATC and the Commission approves the Reorganization with respect to ATC.

XI. FINDINGS AND ORDERING PARAGRAPHS

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

(1) Peoples Gas and North Shore are Illinois corporations that are engaged in the distribution of natural gas to the public at retail in this State; ATC consists of a Wisconsin limited liability company managed by a Wisconsin corporation that is engaged in the operation of a high-voltage transmission system in this State; Peoples Gas, North Shore, and ATC are each a "public utility" as that term is defined in Section 3-105 of the Act;

(2) the Commission has jurisdiction over the parties hereto and the subject matter herein;

(3) the recitals of fact set forth in the prefatory portion of this Order are supported by the record and are hereby adopted as findings of fact;

(4) Appendix A is attached and fully incorporated into this Order; it contains the Required Conditions of Approval established by this Commission in this Order, which are indispensable conditions for approval of the proposed Reorganization and for approval of all other relief sought or granted in this Order;

(5) for the reasons set forth in this Order, and subject to the conditions established in this Order (enumerated in Appendix A), the proposed Reorganization will not adversely affect either Peoples Gas', North Shore's or ATC's ability to perform its duties under the Act, within the meaning of Section 7-204 of the Act; this finding is dependent upon the conditions established in this Order and would not be rendered in the absence of those conditions;

(6) pursuant to Section 7-204 of the Act, and subject to the conditions established in this Order (enumerated in Appendix A), the Commission finds that:

a) the proposed Reorganization will not diminish either Peoples Gas' or North Shore's or ATC's ability to provide adequate, reliable, efficient, safe and least-cost public utility service;

b) subject to the condition imposed in finding (7) of this Order (in addition to the conditions enumerated in Appendix A), the proposed Reorganization will not result in the unjustified subsidization of non-utility activities by the utilities or their customers;

c) under the proposed Reorganization, costs and facilities will be fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utilities for ratemaking purposes;

d) the proposed Reorganization will not significantly impair the ability of either Peoples Gas or North Shore or ATC to raise necessary capital on reasonable terms or to maintain a reasonable capital structure;

e) after approval of the proposed Reorganization, Peoples Gas, North Shore, and ATC will remain subject to all applicable laws, regulations, rules, decisions, and policies governing the regulation of Illinois public utilities;

f) the proposed Reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction; and

g) the proposed Reorganization is not likely to result in any adverse rate impact on retail customers;

(7) the WEC Energy Group AIA shall be approved on an interim basis until the Commission has approved a new affiliated interest agreement in an order in the pending Docket Nos. 12-0273/13-0612 (Consol.) and the resulting affiliated interest agreement approved by the Commission in Docket Nos. 12-0273/13-0612 (Consol.) shall replace the existing 10-0408 AIA as the governing document of affiliated transactions between the Joint Applicants;

(8) subject to the Commission's conclusions in Docket Nos. 12-0273/13-0612 (Consol.), the Commission finds that the Joint Applicants are in compliance with Section 7-204(b)(2) of the Act, such that the proposed Reorganization will not result in the unjustified subsidization of non-utility activities by the utility or its customers;

(9) subject to the Commission's conclusions in Docket Nos. 12-0273/13-0612 (Consol.), the Commission finds that the Joint Applicants are in compliance with Section 7-204(b)(3) of the Act, such that costs and facilities are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities that are properly included by the utility for ratemaking purposes;

(10) subject to the conditions established in this Order (enumerated in Appendix A), the Joint Applicants comply with the minimum information requirements set out in subsection 7-204A(a) of the Act for an application for approval of reorganization;

(11) subject to the conditions established in this Order (enumerated in Appendix A), and in the manner described in those conditions, any savings resulting from the proposed Reorganization shall be allocated to Peoples Gas' and North Shore's ratepayers and no transaction costs incurred in accomplishing the proposed Reorganization shall be recovered by the Joint Applicants, or by either Peoples Gas or North Shore individually, through Illinois jurisdictional regulated rates:

a) The allocation of any savings resulting from the proposed Reorganization shall flow through to ratepayers;

b) The Gas Companies shall not be allowed to recover any transaction costs;

c) The Gas Companies must demonstrate that transaction costs are not included in the revenue requirement in future rate cases;

d) The Gas Companies are required to separately identify and track transaction costs and transition costs; and

e) In future rate cases, transition costs may be recoverable to the extent the transition costs produce savings;

(12) It is unnecessary for the Commission to rule on the applicability of Section 7-102 of the Act insofar as this proceeding concerns the Joint Applicants' Reorganization application; and

(13) subject to compliance with the conditions set out in this Order (enumerated in Appendix A), the proposed Reorganization will not be inconsistent with Section 6-103 and Section 9-230 of the Act, insofar as that statute applies to the subject matter of this proceeding.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that, subject to each and all of the required conditions of approval set forth in this Order and enumerated in Appendix A, the Joint Applicants' request to engage in the Reorganization, through which Peoples Gas and North Shore will become subsidiaries of WEC Energy Group, Inc., is hereby approved.

IT IS FURTHER ORDERED that, subject to each and all of the required conditions of approval set forth in this Order and enumerated in Appendix A, as applicable, Peoples Gas' and North Shore's request to enter into the proposed WEC Energy Group AIA shall be approved on an interim basis until the Commission has approved a new affiliated interest agreement in an order in the pending Docket Nos. 12-0273/13-0612 (Consol.); and the resulting affiliated interest agreement approved by the Commission in Docket Nos. 12-0273/13-0612 (Consol.) shall replace the existing 10-0408 AIA as the governing document of affiliated transactions between the Joint Applicants.

IT IS FURTHER ORDERED that, subject to each and all of the required conditions of approval set forth in this Order (enumerated in Appendix A), as applicable, the proposed accounting entries associated with the Reorganization are approved, on the condition that any effect on such entries resulting from our resolution of disputed issues or our imposition of merger conditions must be reflected in such entries, in a manner consistent with the rationale, determinative principles, findings and conclusions of this Order.

IT IS FURTHER ORDERED that, in carrying out and completing the Reorganization, and in all subsequent Peoples Gas and North Shore activities and operations subject to the jurisdiction of this Commission, the Joint Applicants shall comply with each and all of the required conditions of approval set forth in this Order and enumerated in Appendix A, unless expressly relieved of such obligation, in whole or in part, by directive of this Commission.

IT IS FURTHER ORDERED that subject to the conditions established in this Order (enumerated in Appendix A), and in the manner described in those conditions, any savings resulting from the proposed Reorganization shall be allocated to People Gas' and North Shore's ratepayers and no transaction costs incurred in accomplishing the proposed Reorganization shall be recovered by the Joint Applicants, or by either Peoples Gas or North Shore individually, through Illinois jurisdictional regulated rates.

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 Act and 83 Illinois Administrative Code 200.880, this Order is final, it is not subject to the Administrative Review Law.

DATED: May 14, 2015
BRIEFS ON EXCEPTIONS: May 26, 2015
REPLY BRIEFS ON EXCEPTIONS: June 1, 2015

Glennon Dolan,
Administrative Law Judge