

**STATE OF ILLINOIS**  
**ILLINOIS COMMERCE COMMISSION**

AQUA ILLINOIS, INC.	)	
f/n/a Consumers Illinois Water Company	)	
	)	Docket No. 04-0362
	)	
Petition for the Issuance of a Certificate of	)	
Public Convenience and Necessity to Operate	)	
A Water Supply and Distribution System in	)	
Champaign County, Illinois; and for the	)	
Issuance of an Order Approving Rates,	)	
Accounting Entries and Tariff Language.	)	

Rebuttal Testimony of

**GERARD P. CONNOLLY**

Vice President and Division Manager

On Behalf of  
Aqua Illinois, Inc.

January 7, 2005

1 **I. INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. Gerard P. Connolly, Jr., 322 North Gilbert Street, Danville, Illinois 61834.

4 **Q. Have you previously submitted testimony in this proceeding?**

5 A. Yes.

6 **Q. What is the purpose of your rebuttal testimony in this proceeding?**

7 A. I will comment initially on Staff’s overall findings that Aqua’s Petition satisfies the  
8 requirements of Section 8-406 of the Public Utilities Act (“Act”) and should be approved.  
9 Then, I will comment on and rebut certain portions of Staff witness Mr. William D.  
10 Marr’s Direct Testimony (Staff Exhibit 1.0), Staff witness Ms. Mary H. Everson’s Direct  
11 Testimony (Staff Exhibit 2.0) and Staff witness Mr. Mike Luth’s Direct Testimony (Staff  
12 Exhibit 3.0). Specifically, I will address the following:

- 13 a. Proposed Capital Improvements
- 14 b. Utility Plant in Service
- 15 c. Rates
- 16 d. Franchise and Fire District Fees
- 17 e. Filing Requirements proposed by Staff

18 **II. STAFF’S OVERALL FINDINGS**

19 **Q. Has Staff determined that Aqua Illinois’ (“Aqua’s” or the “Company’s”)**  
20 **acquisition of the Village of Philo’s water system satisfies the public convenience**  
21 **and necessity standard set forth in Section 8-406 of the Act?**

22 A. Yes. Staff witness Mr. Marr concludes that the proposed acquisition is necessary to  
23 provide adequate, reliable and efficient service to customers in the Village. (Staff

24 Ex. 1.0, pp. 4-5). He explains that the Village “no longer wishes to provide water service  
25 and has accepted the Company’s bid to purchase the water system.” (*Id.*, p. 5). He also  
26 concludes that Aqua “will provide a cost efficient means of providing water service to the  
27 Village of Philo” and “has the necessary technical and managerial ability to own, operate,  
28 and maintain a public water supply and distribution system within the Village of Philo.”  
29 (*Id.*, pp. 8-9). Staff witness Ms. Phipps also concludes that Aqua has the financial ability  
30 to construct, operate and maintain the Philo water system. (Staff Ex. 4.0, pp. 2-5).

31 **Q. Does Staff also agree with Aqua’s proposed service area for certification?**

32 A. Yes. Staff witness Mr. Marr recommends “the Commission approve the Company’s  
33 proposed certificated service area consisting of the area within the corporate limits of the  
34 Village of Philo, which is legally described on Exhibit C of the Petition.” (Staff Ex. 1.0,  
35 p. 10).

36 **Q. What is Staff’s conclusion on Aqua’s proposed capital improvements?**

37 A. Staff determines that Aqua’s proposed improvements are prudent. (Staff Ex. 1.0, p. 12).  
38 There is one clarification that I make with regard to Staff’s analysis on this issue in  
39 Section III below.

40 **Q. Does Staff conclude that Philo customers should be added to Aqua’s tariffs for the  
41 Vermilion area?**

42 A. Yes. Staff recommends that Aqua revise its current Rates, Rules, Regulations, and  
43 Conditions to include the Village of Philo within 10 days of closing on the acquisition.  
44 (Staff Ex. 1.0, pp. 14-15). I address this issue further in Sections V and VII below.

45 **Q. Did Staff consider the fact that Illinois American Water Company (“IAWC”) also**  
46 **submitted a bid to purchase the Village’s system in arriving at these conclusions?**

47 A. Yes. Staff witness Mr. Marr compared the costs of providing service to the Village  
48 between Aqua and IAWC, Staff witness Ms. Everson prepared forecasted revenue  
49 requirement schedules for both companies, Staff witness Mr. Luth compared rate  
50 implications under both Aqua and IAWC ownership, and Staff witness Ms. Phipps  
51 evaluated both companies’ financial ability to construct, operate and maintain the water  
52 system. However, Staff correctly noted a significant consideration, namely that the  
53 Village of Philo chose to accept Aqua’s bid to purchase its water system. The Village  
54 officials are charged with the responsibility to take action in the best interest of the  
55 Village’s citizens. Mr. Marr concluded that “[t]he officials of the Village of Philo have  
56 apparently decided that Aqua Illinois’s offer is the best alternative for its residents when  
57 it evaluated the total bid package.” (Staff Ex. 1.0, p. 7).

58 **Q. In your opinion, is Staff correct to have relied upon the Village’s determination in**  
59 **assessing Aqua’s satisfaction of Section 8-406 of the Act?**

60 A. As I am not an attorney, I am not responding to this question on a legal basis as to  
61 whether it is appropriate for the Commission to engage in the type of comparative  
62 analysis Staff conducted under the applicable standard of Section 8-406, nor do I opine  
63 on whether the Commission can override the Village’s decision to accept Aqua’s rather  
64 than IAWC’s bid. However, from a non-legal perspective, I believe it is appropriate for  
65 the Village’s determination to be given considerable weight. It is the Village’s system  
66 that is being sold and the Village should be given the discretion to determine to whom it  
67 sells its system, provided, of course, that the purchaser satisfies Section 8-406

68 requirements as Aqua does. Because Staff does defer to the Village's decision in this  
69 regard, Aqua agrees that Staff's overall conclusion to recommend approval of Aqua's  
70 Petition, given Aqua's satisfaction of Section 8-406 requirements, is correct.

71 **Q. Despite Staff's overall conclusion that Aqua's Petition should be granted, does Staff**  
72 **raise any issues that are concerning?**

73 A. Yes. First, Staff witness Ms. Everson makes several adjustments to Utility Plant in  
74 Service that are not correct and should not be adopted. I address these adjustments in  
75 Section IV below. One of these adjustments pertaining to Contributions in Aid of  
76 Construction ("CIAC") is also addressed by Aqua witness Mr. Monie. These adjustments  
77 as well as other accounting adjustments proposed by Ms. Everson are addressed from an  
78 accounting perspective by Aqua witness Mr. Bratetic. Second, it appears that Staff may  
79 be proposing to re-evaluate Philo's inclusion in Vermilion rates at the time of Aqua's  
80 next rate case for the Vermilion Division, and I respond to that suggestion in Section V  
81 below. Third, Staff proposes to disallow entirely the Franchise Fees and Fire District  
82 Fees imposed by the Village. I respond to Staff on this issue in Section VI below.

83 **III. PROPOSED CAPITAL IMPROVEMENTS**

84 **Q. Do you have any comments on Mr. Marr's direct testimony regarding proposed**  
85 **capital improvements?**

86 A. Yes. As noted above, Mr. Marr has found all of Aqua's proposed capital improvements  
87 to be prudent. (Staff Ex. 1.0, p. 12). However, there is an assumption Mr. Marr makes in  
88 his analysis that I would like to clarify.

89 **Q. What is your clarification?**

90 A. Mr. Marr correctly notes that Aqua has proposed to replace the existing 50,000 gallon  
91 elevated tank in Philo with a new or reconditioned tank. One of the options being  
92 investigated is to relocate an existing 300,000 gallon elevated steel spheroid tank from  
93 Danville to Philo. In my reading of Mr. Marr's testimony, it appears he assumes Aqua  
94 has made a final decision to relocate the Danville tank to Philo. (Staff Ex. 1.0, pp. 12-  
95 13). However, until a complete structural engineering evaluation of the 300,000 gallon  
96 elevated water storage tank in Danville has been completed, a final decision will not be  
97 made.

98 **Q. What was the purpose of the engineering evaluation report by Tank Industry**  
99 **Consultants, Inc.?**

100 A. The engineering evaluation report by Tank Industry Consultants, Inc. was provided in  
101 order to prove to the Village of Philo that the existing 300,000 gallon elevated spheroid  
102 water tank currently located in Danville was in good shape. Tank Industry Consultants'  
103 report addresses the condition of the tank, but Tank Industry did not conduct a structural  
104 analysis to determine if the tank could withstand being relocated and re-erected.

105 **Q. Will Aqua Illinois conduct a complete structural analysis of the existing 300,000**  
106 **gallon elevated tank to determine if the tank can be relocated?**

107 A. Yes. If the Commission approves the acquisition of the water system to Aqua, then Aqua  
108 will retain the services of a consulting engineering firm who specializes in tank  
109 relocations to determine if the 300,000 gallon elevated spheroid can be relocated and still  
110 meet the structural requirements of new tank construction as set by the American Water  
111 Works Association.

112 **Q. Are there any other considerations in relocating the existing 300,000 gallon elevated**  
113 **tank to Philo?**

114 A. Yes. There are several antennas on the top of the 300,000 gallon elevated tank currently  
115 located in Danville that would need to be relocated and re-erected. These antennas are  
116 used by the City of Danville, Aqua Illinois and Nextel Communications. If the 300,000  
117 gallon elevated tank were to be located to Philo, these antennas would need to be  
118 relocated as well.

119 In addition, it may determined that the purchase of a new elevated water storage tank,  
120 while having a higher initial cost, is the better alternative because a new tank would have  
121 a longer life and less maintenance expense.

122 **Q. What will be the impact on rate base if the existing 300,000 gallon elevated tank**  
123 **currently located in Danville is not relocated to Philo?**

124 A. Per the Assets Purchase Agreement, Aqua Illinois would still replace the existing 50,000  
125 gallon elevated water tank currently in Philo. This would require Aqua Illinois to  
126 purchase a new elevated water storage tank. Therefore, the amount of investment  
127 required to replace the tank would increase by approximately \$290,000, thus causing rate  
128 base to increase.

129 **IV. UTILITY PLANT IN SERVICE**

130 **Q. Please describe generally Ms. Everson's adjustments that you are addressing.**

131 A. Ms. Everson proposes three adjustments that I will address herein: namely: (1) to  
132 incorrectly re-characterize \$491,538 of the plant included in Aqua witness Mr. Monie's  
133 Original Cost Study as CIAC; (2) to reduce the amount of Account 330 – Distribution

134 Reservoirs & Standpipes by a total of \$48,054.58 for costs the Village summarily  
135 referenced as “tank painting” that Ms. Everson erroneously asserts should be fully  
136 amortized; and (3) to recognize the West Water Tank, which is no longer in use, as  
137 retired and adjust the depreciation expense associated with its retirement.

138 **Q. Do you agree with Ms. Everson’s adjustments to Utility Plant in Service?**

139 A. I agree with Ms. Everson’s third adjustment to recognize the West Water Tank as retired;  
140 but, I do not agree with Ms. Everson’s first and second adjustments described above.

141 **Q. Please comment on Ms. Everson’s proposed adjustment to re-characterize \$491,538**  
142 **of the plant included in Aqua’s Original Cost Study as CIAC.**

143 A. As Mr. David Monie explains in more detail in his Rebuttal Testimony, CIAC was not  
144 included in Aqua’s Original Cost Study. In particular, Ms. Everson’s adjustment is based  
145 on an amount of contributed property Aqua identified in response to data request WD  
146 1.07. However, the contributed property set forth in response to WD 1.07 was not  
147 included in Aqua’s Original Cost Study and, therefore, the adjustment proposed by Ms.  
148 Everson should not be allowed.

149 **Q. What is the basis Ms. Everson asserts for her proposal to fully amortize the costs the**  
150 **Village summarily referenced as “tank painting?”**

151 A. In response to WD 1.15, Aqua informed Staff that the Village had not kept detailed  
152 records of the improvements made to its 50,000 gallon elevated storage tank over the  
153 years. However, the Village did reference three expenses totaling \$48,054.58 in the years  
154 1977, 1982 and 1989 as various tank painting projects. Based solely on these references,

155 Ms. Everson assumes the various projects consisted entirely of tank painting in each of  
156 the three years and should be fully amortized as tank painting expenses.

157 **Q. Why do you disagree with Ms. Everson's assumption?**

158 A. I disagree because the expense amounts are not reasonable for tank painting. Based on  
159 Aqua's experience, it costs substantially more than even the largest of the three expenses  
160 (\$18,793 in 1989) to paint a tank.

161 **Q. What is your opinion as to why the expenses were incurred?**

162 A. It is my opinion that the Village's references to tank painting were generic titles or  
163 summary references for various improvements made to the water tank that were then  
164 painted to blend the repair or improvement in with the original color of the tank. In other  
165 words, it is my belief these entries were not for the repainting of the elevated tank in each  
166 of the three years but rather were for other improvements made to the tank.

167 **Q. Is there any other basis for your opinion?**

168 A. The Village Engineer, Mr. David Phillippe of HDC Engineering, has records that confirm  
169 at least two of the three projects were not painting projects. The expense incurred in  
170 1997 in the amount of \$13,459 was for maintenance and improvements to the tank. The  
171 expense incurred in 1982 in the amount of \$15,820, while the exact nature of the work is  
172 unknown, was performed by Caldwell Tanks and, therefore, would also have been for  
173 maintenance and repairs.

174 **Q. What were HDC Engineering's records as to the nature of the third expense in**  
175 **1989?**

176 A. HDC Engineering’s records indicate tank repainting for the third expense in 1989.  
177 However, as I discussed above, the amount of the expense \$18,793 is substantially less  
178 than it costs to paint a tank. Therefore, similar to the expenses in 1982 and 1997, it is my  
179 opinion that this expense was also summarily referenced as tank painting when the actual  
180 expense was most likely for tank improvements that were then repainted to blend with the  
181 rest of the tank.

182 **Q. What is your overall recommendation with regard to the expenses referenced as**  
183 **“tank painting?”**

184 A. My opinion is that the expenses Ms. Everson seeks to adjust were not incurred to paint  
185 the tank and should not be amortized as tank painting expenses. As my opinion is  
186 supported by the information discussed above, the Commission should not reduce Utility  
187 Plant in Service by Staff’s proposed \$48,054.58.

## 188 V. RATES

189 **Q. Has Staff agreed that Philo customers should be added to Aqua’s rates for the**  
190 **Vermilion Division at this time?**

191 A. Yes. As I noted above, Staff does not object to Philo customers receiving service as part  
192 of Aqua’s Vermilion Division at this time. However, Staff witness Mr. Luth suggests  
193 that “[t]he inclusion of Philo in the overall customer base for revenue recovery from the  
194 Vermilion service area could be addressed in the next Vermilion rate docket.” (Staff Ex.  
195 3.0, p. 8).

196 **Q. Do you have any concern with Mr. Luth’s suggestion that Philo customers’ inclusion**  
197 **in the Vermilion Division be addressed during the next rate case?**

198 A. Yes. I have a very serious concern with that proposal. Philo customers' inclusion in the  
199 Vermilion Division is a specific condition to Aqua's Asset Purchase Agreement with the  
200 Village. (Petition, Ex. A, p. 6, §6(c)). Both Aqua and the Village have certain rights that  
201 flow should the Commission impose any conditions upon its approval of the Agreement.  
202 (*Id.* at Ex. A, p. 5, §3(d), p. 6, §6(c)). Accordingly, Aqua and the Village need to know  
203 within the context of this Docket whether the Commission is going to condition any  
204 aspect of the Agreement. Issues, the resolution of which could result in ICC imposed  
205 conditions to the Agreement, simply cannot be deferred to future proceedings.

206 **Q. Is the cost of serving Philo customers sufficiently similar to that of serving**  
207 **Vermilion customers for Philo customers to be included in the Vermilion Division?**

208 A. Yes. As I explained in my Direct Testimony, Aqua will serve Philo customers in an  
209 identical manner to Vermilion customers with the single exception of source of supply.  
210 This means that all remaining aspects of water service including water quality, pumping,  
211 customer service, metering, meter reading, bill preparation and mailing, bill remittance,  
212 system maintenance, engineering and improvements will be the same.

213 **Q. How do you respond to Staff's revenue forecast analysis?**

214 A. Initially, it is appropriate to address Staff's presentation of an analysis based on two  
215 different revenue forecasts, one prepared by Aqua and a second prepared by Staff witness  
216 Ms. Everson. Based on Aqua's analysis, Staff notes that Aqua would have been expected  
217 to earn a return of approximately 6.11% from serving Philo customers during 2004,  
218 which, as I explained in my Direct Testimony, is not excessive given it is less than the  
219 Commission has authorized in Aqua's recent rate cases. In contrast, based on Ms.

220 Everson's forecast, Staff witness Mr. Luth asserts that Aqua would have experienced a  
221 return of 25.85%. (Staff Ex. 3.0, p. 4).

222 **Q. Which revenue forecast is the appropriate one to utilize?**

223 A. The forecast based on Aqua's statement of rate base is the appropriate one for the  
224 Commission to utilize. The discrepancy between Aqua's and Staff's forecasts is the  
225 result of Staff erroneously adjusting Utility Plant in Service for, most significantly, CIAC  
226 as well as the expenses summarily referenced as tank painting, that I discuss in Section  
227 IV above. As Staff's underlying adjustments are erroneous, Staff's resultant forecast  
228 analysis is also erroneous for the exact same reasons. Given the amount of plant Staff  
229 seeks to incorrectly re-characterize as CIAC is \$491,538, the amount of Staff's revenue  
230 forecast is also off by this considerable amount. The Commission, therefore, should base  
231 its analysis of the issue on Aqua's statement of rate base and revenue forecast.

232 **Q. Please comment on the revenue forecast analysis based on Aqua's stated rate base.**

233 A. As Staff witness Mr. Luth correctly notes, if Philo customers were charged Vermilion  
234 rates along with Aqua's public fire protection rate of \$4.05 per month for the City of  
235 Danville, then Aqua would under-recover its costs for serving Philo by approximately  
236 \$21,188 per year. (Staff Ex. 3.0, p. 7). Mr. Luth concludes that this would equate to only  
237 an approximate 2/10<sup>th</sup> of 1% potential under-recovery based on the revenue requirement  
238 Staff has proposed for Vermilion in Docket 04-0442, which Mr. Luth further concludes is  
239 not significant. (Id.) Therefore, the evidence demonstrates that Aqua would only under-  
240 recover by the slightest amount, only 2/10<sup>th</sup> of 1%.

241 **Q. How do you respond to Mr. Luth’s point that Aqua has not requested to recover the**  
242 **\$4.05 public fire protection charge from Philo customers?**

243 A. Aqua would like to recover the \$4.05 public fire protection charge currently assessed for  
244 the City of Danville from Philo customers. Accordingly, to the extent such a request has  
245 not clearly been stated, Aqua hereby states its request for the Commission to approve  
246 Aqua’s recovery of this charge from Philo customers.

247 **Q. Is there any other factor the Commission should consider with respect to the**  
248 **inclusion of Philo customers in the Vermilion Division?**

249 A. Yes. The Commission should consider the cost-benefit of treating Philo customers as a  
250 stand-alone division. The cost to Aqua, the Commission and ratepayers of performing  
251 rate cases for Philo would be substantial given that only 547 customers are within Philo.  
252 The incursion of such costs would not be prudent simply to avoid the potential of an  
253 insignificant flow of less than 2/10<sup>th</sup> of 1 % between Philo customers and those in the  
254 current Vermilion Division.

255 **Q. What is your recommendation?**

256 A. I recommend that the Commission make a definitive decision to include Philo in the  
257 Vermilion Division within the context of this Docket and avoid the cost of conducting  
258 stand-alone studies for the small number of customers in Philo during future cases.

259 **VI. FRANCHISE AND FIRE DISTRICT FEES**

260 **Q. Would you please summarize Staff’s position on the Village’s 6% Franchise Fee and**  
261 **3% Fire District Fee?**

262 A. Yes. Staff has proposed to disallow both of the Village's Fees because they total 9% and  
263 Section 9-221 of the Act only allows customers to be assessed utility taxes imposed under  
264 Section 8-11-2 of the Illinois Municipality Code of up to 5.15% (equal to a 5% tax plus a  
265 3% administrative fee based on the total taxes collected). Further, with respect to the Fire  
266 District Fee, Staff states that it does not satisfy the requirements of a utility's fire  
267 protection charge allowed under Section 9-223 of the Act because: (i) it is not a fixed  
268 amount, and (ii) it is a municipality charge that does not cover Aqua's costs to meet fire  
269 protection needs. (Staff Ex. 3.0, pp. 8-11).

270 **Q. How do you respond?**

271 A. The Village has informed Aqua that the Village's intent was not to impose a utility tax  
272 under Section 8-11-2 or a fire protection charge under Section 9-223 of the Act. Rather,  
273 the Village's intent is to impose franchise fees, which Section 8-11-2 of the Illinois  
274 Municipal Code allows in addition to any utility tax of 5%.

275 **VII. FILING REQUIREMENTS PROPOSED BY STAFF**

276 **Q. Does the Company agree with Mr. Marr's Direct Testimony that would require**  
277 **Aqua Illinois to file revised Rates, Rules, Regulations and Conditions of Service**  
278 **Tariffs for water service that would include the Village of Philo and the Village of**  
279 **Indianola?**

280 A. Yes, the Company agrees with Mr. Marr's recommendation.

281 **Q. Does the Company agree with Mr. Marr's Direct Testimony that would require**  
282 **Aqua Illinois to file a report stating the date of the closing of the transaction with**

