

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Aqua Illinois, Inc.)	
)	
Proposed General Increase for Water and Sewer Rates for the Woodhaven Division)	Docket No. 05-0071
)	
Proposed General Increase for Water Rates For the Oak Run Division)	Docket No. 05-0072
)	

**INITIAL BRIEF OF
AQUA ILLINOIS, INC.**

Dated: August 24, 2005

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BACKGROUND

Aqua Illinois, Inc. (“Aqua” or the “Company”) simultaneously filed proposed new rates for three service areas (“Divisions”)—the Oak Run Water Division (“OR”), the Woodhaven Water Division (“WW”) and the Woodhaven Wastewater or Sewer Division (“WS”). It has not sought rate relief for Oak run and Woodhaven Sewer since the 1998 rates approved by the Commission in Docket No. 97-0351, and for Woodhaven Water since the rates approved in Docket No. 00-0338. Rate relief is necessary now because, at previously approved rates, each of these Divisions is significantly under-earning. In 2004, Aqua suffered *losses* in each of the Divisions as follows:

Oak Run	\$ (29,021)
Woodhaven Water	\$(100,428)
Woodhaven Wastewater	\$ (12,519)

(Aqua Ex. 5.0A2, p. 14; Aqua Ex. 7.0RR, p. 12). Aqua requests revenue increases of \$190,701, \$482,598 and \$403,099, respectively, to earn the return Staff has deemed is appropriate herein.¹ Aqua’s Surrebuttal Statements of Operating Income are attached hereto as Appendix A.

Aqua’s proposed rates are based on a 2005 future test year. The independent accounting firm London Witte Group, Inc. (“London Witte”) reviewed Aqua’s budget. It concluded that the budget is in full conformity with the American Institute of Certified Public Accountants’ guidelines and that the assumptions underlying the budget are reasonable bases for future test year projections. (Aqua Filings (OR), (WW) & (WS) at Intro., pp. 4-17).

The Commission’s Staff (“Staff”) concurs that it is appropriate to increase rates in each of the Divisions. However, Staff proposes several substantial adjustments that are unreasonable. If adopted, Aqua would be unable to earn a reasonable rate of return for the Divisions.

¹ Aqua has accepted Staff’s proposed rate of return for purposes of these cases.

The Woodhaven Association (“WH Association”) and Oak Run Property Owners Association (“ORPA”) (jointly the “Associations”) also participated in these proceedings and raised limited challenges. None of their proposals are supported by compelling evidence. As discussed herein, the Commission should not adopt their proposals

Accordingly, Aqua respectfully requests that the Commission approve proposed rates based on its test year Surrebuttal Statements of Operating Income for each of the three Divisions, Aqua Schedule 8.1 (OR), (WW) and (WS),² respectively, attached hereto as Appendix A.

ARGUMENT

I. RATE BASE

A. Introduction

There are no Rate Base issues between Aqua and Staff. The Associations, however, each seek to disallow Aqua’s recovery of legitimately incurred capital investment. They raise three unfounded issues: (1) Aqua’s recovery of \$35,222 in capital costs to complete a pilot study for the Reverse Osmosis (“RO”) Plant (Oak Run), (2) whether Aqua appropriately excluded the WH Association’s contribution to a 1998 Sewer Main Extension and Lift Station from Plant in Service (Woodhaven Sewer), and (3) whether Aqua appropriately excludes sewer customers’ contributions to new sewer extension from Plant in Service (Woodhaven Sewer).³ The Commission should not adopt any of the Association’s adjustments on these issues.

² Schedules will be denoted with an (OR), (WW) or (WS) to designate Oak Run, Woodhaven Water or Woodhaven Sewer, respectively.

³ The Administrative Law Judge’s (“ALJ’s”) Outline for Rate Case Briefs lists these as Operating Expense issues; but, the issues actually relate to Rate Base rather than Operating Expense.

B. Summary of Uncontested Issues

Staff accepted a known and measurable change to Aqua's Pension Expense for all Divisions.⁴ (Staff Ex. 7.0R, p. 7). Also, the Company and Staff agree in principle that Cash Working Capital is the result of multiplying 12.5% times Operations and Maintenance ("O&M") Expense. (Aqua Ex. 6.0R, p. 6). Thus, the final amount of Cash Working Capital will be based on the Commission's final O&M Expense.

C. Contested Issues

1. RO Plant Pilot Study – Oak Run

ORPA witness Mr. Michael Davison asserts Aqua should not recover its capital costs to complete the pilot study because, in his opinion, consumers are not likely to vote in favor of the RO Plant. (ORPA Ex. 1.0, pp. 6, 11). However, Aqua witness Mr. Bunosky conducted a cost-benefit analysis and assessed the significant benefits the RO Plant would produce. In his opinion, the water quality benefits will far outweigh the cost of building the RO Plant. Thus, he believes that consumers are likely to vote in favor of the RO Plant. (Aqua Ex. 5.0A2, pp. 2-5).

Moreover, based on a consumer survey Aqua already has conducted, the majority of customers have expressed opinions in favor of the RO Plant. Consumers favored the water quality produced by the RO Plant and asked for further information. (Tr., pp. 131-32). This is strong evidence that Mr. Davison's opinion is not representative of the majority of consumers.

Irrespective of whether consumers ultimately vote in favor of the plant, however, Aqua acted prudently and reasonably in conducting the pilot study, which is a critical and unavoidable component of the final RO Plant construction. An RO Plant would significantly improve water

⁴ As noted below, Pension Expense also impacts Operating Expense.

quality by bringing it into compliance with the Illinois Environmental Protection Agency's ("IEPA's") secondary and the health industry's standards on Fluoride, Total Dissolved Solids, Sodium and Chlorides. (Aqua Ex. 5.0A2, pp. 3-4). The current heightened levels of these minerals increase risks for elderly persons and those on sodium restricted diets, cause tooth decay, reduce appliance life and produce an objectionable taste. (*Id.*) The RO Plant would eliminate all of these traits. (*Id.*) A pilot study for a RO Plant that would produce such substantial benefits was a prudent exercise. Moreover, the Company has demonstrated the costs to be reasonable.

2. Sewer Installation Costs – Woodhaven Sewer

a. 1998 Sewer Main Extension And Lift Station Project

The WH Association claims that Aqua included the Association's payments toward a 1998 sewer main extension and lift station project in Rate Base. (WA Ex. 1.00, p. 15). The Association is not correct. Aqua properly accounted for the Association's payments as Customer Advances and deducted them from Rate Base. In particular, the Association paid a total of \$184,207 toward the project. (Aqua Cross Ex. 1). On Aqua's Schedule B-15 (WS), pages 1 and 2, that amount is correctly reflected as Customer Advances; and on Aqua's Schedule B-1 (WS), the amount is shown as a Customer Advance deduction from Rate Base. (Aqua Sch. B-1, B-15 (WS)). Aqua witness Mr. Bunosky confirmed that Aqua did not account for the Association's payments as the Company's capital investment, but rather deducted them from Rate Base by accounting for them as Customer Advances. (Aqua Ex. 5.0A2, p. 28). There is no merit to the Association's claim and it should be rejected.

b. Sewer Service Extensions

The WH Association also claims that Aqua included customers’ payments toward sewer service extensions in Rate Base. (WA Ex. 1.00, p. 15). Once again, the Association is incorrect. Aqua pays costs toward sewer service extensions *in addition to* the amounts paid by customers. (Aqua Ex. 5.0A2, p. 29; Aqua Ex. 7.0R, pp. 24-27). Only the costs that Aqua paid were included in capital additions and, therefore, Rate Base. (Aqua Ex. 5.0A2, p. 29; Aqua Ex. 7.0R, pp. 26-27). Aqua treats as contributions and reductions from Rate Base those amounts paid for by customers. (*Id.*) Staff witness Mr. Marr testified that Aqua properly accounted for the customer payments related to sewer service extensions. (Tr., p. 210).

D. Recommended Rate Bases

As noted, Staff and Aqua are in agreement on Rate Base; but, the final amount will depend on the Commission’s O&M Expense and, in turn, Cash Working Capital determinations. As such, Aqua’s Surrebuttal and Staff’s Rebuttal Rate Base numbers are the same except for different Cash Working Capital amounts. Aqua’s Surrebuttal position is that the following Cash Working Capital and Rate Base amounts are appropriate:

<u>Division</u>	<u>Cash Working Capital</u>	<u>Rate Base</u>
Oak Run	\$24,905	\$1,589,806
Woodhaven Water	\$82,631	\$2,831,454
Woodhaven Sewer	\$60,075	\$2,918,721

(Aqua Ex. 8.0, Sch. 8.1 (OR), (WW) and (WS)).

II. OPERATING REVENUES AND EXPENSES

A. Introduction

Staff is the primary party that seeks adjustments to Operating Revenues and Expenses. Those adjustments are largely based on inadequate analyses that fail to account for all of the relevant evidence and, thus, lack support. Staff also advances recommendations for Aqua's future rate filings that are discriminatory, would constitute poor public policy and are premature. Finally, Staff makes errors in its Income Tax and Revenue Requirement increase calculations that should be corrected.

B. Summary of Uncontested Issues

Staff accepted known and measurable changes to Aqua's Pension Expense⁵ for all Divisions and Radium Removal Expense for Woodhaven Water. (Staff Ex. 7.0R, pp. 7-8). In addition, Interest Synchronization and the Gross Revenue Conversion Factor are agreed-to in principle.

The final Interest Synchronization will depend on final Rate Base and Weighted Cost of Debt. (Aqua Ex. 6.0R, p. 5). Aqua has accepted Staff's proposed Weighted Cost of Debt. But, the Commission should use Aqua's Rate Base for purposes of this calculation, as discussed *supra*.

The final Gross Revenue Conversion Factor will depend on the final Uncollectibles Expense⁶ for each Division. As discussed *infra*, Staff's proposed adjustments would cause Bad Debt Expense to be significantly understated for all Divisions. The Commission should utilize Aqua's Bad Debt Expense to calculate the Gross Revenue Conversion Factor.

⁵ As noted above, the Pension Expense update also has a Rate Base related aspect.

⁶ The parties have referenced this Expense interchangeably as Uncollectibles and Bad Debt Expense.

C. Contested Issues

1. RO Plant – Oak Run

Staff proposes to transfer \$68,180 in capital expenditures for the RO Plant incurred thus far from Plant in Service to Account 183, Preliminary Survey and Investigation.⁷ (Staff Ex. 2.0, p. 6). Aqua agrees with this transfer because the likelihood that the RO Plant will be built is reasonably certain.⁸ However, if the Commission disagrees that the RO Plant will likely be built, it is more appropriate to amortize the \$68,180 over a ten year period to Account 675, Miscellaneous Expense. (Aqua Ex. 6.0R, p. 42). Indeed, the Section of the Uniform System of Accounts to which Staff witness Ms. Jones cites provides that, in the case a project is abandoned, the expenses should be charged to Miscellaneous Expense or another operating expense account. 83 Ill. Adm. Code 605.10.

2. Uncollectible Expense

a. Oak Run Division

Staff proposes an unadjusted Uncollectible Expense of \$1,620 or .49%, which amount would be increased \$936 based on Aqua's proposed surrebuttal revenue increase. However, Aqua is incurring substantially higher Bad Debt Expense. For Aqua to adequately recover its Bad Debt Expense the unadjusted amount Staff proposes needs to be increased by \$4,829 to \$6,449, which equates to Aqua's pro forma proposed amount of \$7,385 less the pro forma proposed adjustment of \$936. (Aqua Ex. 8.0, pp. 7-9).

Staff's position considers only a single, misleading factor—Aqua's write-offs for the past five years. (Staff Ex. 6.0, p. 7; Tr., p. 333). This factor is misleading because Aqua cannot

⁷ As this was agreed, both Aqua and Staff have removed this amount from Plant in Service in their Schedules.

⁸ In turn, a three year amortization period for Oak Run rate case expense is reasonable, as discussed *infra*, because the capital investment in the RO Plant in 2007 will necessitate a rate filing.

write-off Bad Debt Expense that is caused by the Division's availability customers.⁹ (Aqua Ex. 8.0, pp. 8-9). Because availability customers are not connected to the system but rather pay for the opportunity to take service, Aqua cannot terminate or shut-off their service. (*Id.*) As a result, availability customers who are delinquent remain customers. (*Id.*) It would constitute a forgiveness of debt to write-off of existing customers' delinquent accounts, so those amounts cannot be written-off. (*Id.*) Consequently, historical write-offs only identify the amount of Bad Debt Expense Aqua is able to write-off, *i.e.*, the amount consumption customers cause in Oak Run; historical write-offs do not account for the amount of Bad Debt caused by availability customers.

Aged receivables greater than 91 days are not likely to be collected and, therefore, demonstrate the amount of Bad Debt Expense Oak Run availability customers are causing. (*Id.*, p. 9). Oak Run's aged receivables greater than 91 days for availability customers is \$14,487. (*Id.*, pp. 8-9; Aqua Ex. 6.0R, p. 6). This equates to \$4,829 annually over a three year period, against which Aqua reserves. (*Id.*) Accordingly, while Oak Run's historical write-offs support the \$1,620 in Bad Debt Expense caused by consumption customers, Oak Run's availability customers are causing an additional \$4,829 in Bad Debt Expense.

This evidence was not disputed. Staff witness Ms. Pearce acknowledged this fact but then failed to account for it in her analysis. (Staff Ex. 6.0, pp. 6-7). Her resultant analysis, therefore, is flawed because it does not account for the Bad Debt Expense caused by availability customers. The amount she proposes for recovery is substantially less than the *actual* Bad Debt Expense Aqua is incurring.

⁹ An availability customer is one that is not connected to the system now but pays for the opportunity to connect in the future if and when desired. (Tr., p. 116).

Aqua is entitled to recover its total Bad Debt Expense in rates. *Citizens Util. Bd. v. ICC*, 116 Ill.2d 111, 121 (1995)(holding the Commission “must allow the utility to recover costs prudently and reasonably incurred”); *Illinois Cent. R. Co. v. ICC*, 387 Ill. 256, 275 (1944) (holding utility constitutional rights are infringed on by the Commission fixing rates that are insufficient to pay operating expenses); *In re Commonwealth Edison Co.*, Dkt. 87-0043, 84 PUR 4th 469, 1987 WL 257840 (1987)(holding “a utility is entitled to recover its reasonable expenses incurred in providing service to its customers”). The evidence establishes that Aqua’s adjusted test year Bad Debt Expense for the Division is \$6,449 (the \$1,620 historical write-offs that consumption customers cause plus the \$4,829 aged receivables that availability customers cause). The Commission should conclude that Aqua is entitled to recover all of its Bad Debt Expense, which includes the Bad Debt of both consumption and availability customers. Accordingly, the Commission should find that Aqua’s proposed Bad Debt Expense for its Oak Run Division is reasonable.

b. Woodhaven Divisions

Aqua filed test year Bad Debt Expense of \$53,148 and \$53,724. (Aqua Sch. C-16 (WW), (WS)). Staff proposes to decrease Aqua’s test year amounts to \$31,187 and \$28,195, respectively. (Staff Ex. 6.0, Sch. 6.09 (WW), (WS)). Staff’s proposal would cause a gross under-recovery of Bad Debt Expense.

Once again, Staff’s position is based solely on historical write-offs. (Staff Ex. 6.0, Sch. 6.10 (WW), (WS)). Staff’s proposed adjustment fails to consider the entire picture concerning the Woodhaven Divisions’ Bad Debt Expense. As with Oak Run, sole reliance on historical write-offs produces a seriously misleading result because there is a substantial amount of Bad Debt Expense that Aqua cannot write-off, albeit for a different reason than in Oak Run.

With very limited exceptions, the water and sewer systems were constructed without meters or shut-off valves. (Aqua Ex. 8.0, p. 10). It would be cost prohibitive for Aqua to install the valves on the water system now,¹⁰ and Aqua can never install them on the sewer system because of health and sanitation concerns. (Tr., p. 133). This means that delinquent customers, as with Oak Run availability customers, continue to be customers; and it would be a forgiveness of their debt to write-off their past due amounts.¹¹ (*Id.*) Historical write-offs for the Woodhaven Divisions, therefore, only account for the portion of Bad Debt Expense caused by individuals who cease being customers; historical write-offs do not account for Bad Debt Expense caused by individuals who remain customers despite delinquent accounts.

At Aqua's originally proposed rates, it anticipated annual Bad Debt Expense of \$103,394 and \$112,174, against which it reserves, for Woodhaven Water and Sewer, respectively.¹² (Aqua Ex. 6.0R, p. 7; Aqua Ex. 8.0, p. 10, Ex. A and B (Aqua responses to Staff data requests BAP 5.04 and 6.04)). The calculations are based on the 536 accounts across both Divisions that were delinquent more than 91 days as of April 22, 2005, when Aqua prepared its data request responses. (*Id.*) As of May 31, 2005, the number of delinquent accounts had increased to 552 with a total amount in delinquency of \$451,991. (Aqua Ex. 8.0, p. 10, Ex. C). By the time of Aqua's Surrebuttal Filing, an additional 250 accounts, with an estimated additional \$192,480 in delinquencies prior to the add-on of monthly late fees, were on the verge of becoming more than 91 days past due. (*Id.*, p. 11).

¹⁰ It would cost Aqua approximately \$400 per customer to install shut-off valves on the water system. (Aqua Ex. 5.0, p. 16). It would be cost-prohibitive, at \$2,440,000, for Aqua to install valves for every customer. (*Id.*) As a result, Aqua has to be selective of when such a significant expense is incurred. (*Id.*) It does, however, install the valves when the circumstances indicate the action may motivate the customers to pay their past due amounts, such as when customers pay their Association Dues and real estate taxes and use their lots regularly. (*Id.*)

¹¹ Aqua can only write-off these past due amounts in those limited situations where the individuals will no longer be customers. For example, the properties of approximately 49 individuals with past due accounts (out of a total of 552) were sold at a tax auction on July 15, 2005, for non-payment of taxes. Those individuals will no longer be Aqua's customers, and Aqua will write-off their past due amounts. (Aqua Ex. 8.0, p. 11).

¹² This is prior to the addition of late payment fees.

Accordingly, the test year Bad Debt Expense of \$53,148 and \$53,724, respectively, that Aqua filed is fully supported. It is, moreover, extremely conservative in favor of Woodhaven customers. Although Aqua's Bad Debt Expense is steadily increasing and anticipated to be \$103,394 and \$112,174, respectively, at Aqua's originally proposed rates, Aqua only seeks to recovery \$53,148 and \$53,724 in the test year and \$85,279 and \$82,576 at surrebuttal proposed rates, respectively. The Commission should view this as a significant compromise between Aqua's actual Bad Debt Expense and Staff's recommendation.

Once again, this evidence was not disputed. Rather, as with Oak Run, Staff witness Ms. Pearce acknowledged the situation but then disregarded it in her analysis. (Staff Ex. 6.0, p. 7). Her analysis, therefore, is fatally flawed because it fails to account for Bad Debt Expense that Aqua actually incurs but cannot write-off.

The fact Staff proposes recovery of only a limited subset of actual Bad Debt Expense is plainly set forth in Ms. Pearce's Rebuttal Schedules. In her Schedule 6.10, she calculates "Bad Debt Expense" for both of the Divisions in total and for each Division separately. (Staff Ex. 6.0, Sch. 6.10, pp. 1-3, col. (d)). She then calculates "Actual Write-Offs," which are significantly smaller amounts. (*Id.*, Sch. 6.10, pp. 1-3, col. (e)). The basis for her proposed recoveries is not her "Bad Debt Expense" calculations in column (d) but rather the significantly smaller "Actual Write-Offs" calculations. (*Id.*, Sch. 6.10, pp. 1-3, ln. 9 (calculating 5-year average percentage of actual write-offs); *Id.*, Sch. 6.09, p. 2 (deriving Staff's proposed Bad Debt Expense based on the 5-year average percentage of actual write-offs calculated in Sch. 6.10)). Due to the unique collection circumstances of Oak Run and Woodhaven, Bad Debt Expense, which includes uncollectibles reserved against, should be the basis for Aqua's Bad Debt Expense recovery, not write-offs.

The unreasonableness of Staff's position is further demonstrated by the fact it seeks to lower Aqua's recovery when the Woodhaven Divisions' uncollectibles problem is worsening. The Commission allowed a combined recovery of \$92,165 in the Divisions' last rate cases. (Aqua Ex. 8.0, pp. 11-12). Staff would lower this combined recovery by \$32,783 to \$59,382. Based on the evidence, Aqua's recovery needs to be increased, not reduced.

Aqua is entitled to recover its *total* test year Bad Debt Expense in rates. *See supra*, p. 8. The evidence establishes that Aqua's total, annual Bad Debt Expense for Woodhaven Water and Sewer is \$103,394 and \$112,174, respectively, at original proposed rates. Staff's proposal to substantially lower Aqua's already conservative test year requests from \$53,148 and \$53,724 to \$31,187 and \$28,195, respectively, is unreasonable and unfair in its disregard of substantial evidence and its own calculations of actual Bad Debt Expense. It would cause Aqua to unfairly and improperly under-recover this expense. The Commission should reject Staff's proposal to substantially lower Aqua's requested Bad Debt Expenses, which, as noted, already reflect significant compromises.

3. Bulk Billing – Woodhaven Divisions

The WH Association has raised the question of implementing a bulk billing option pursuant to which Aqua would issue a single bill to the WH Association for all non-metered properties and the WH Association would be responsible for payment irrespective of its ability to collect from the ultimate end users. (WH Assoc. Issues List, p. 2). The WH Association, however, has not said it will implement the option. (Aqua Ex. 5.0A2, pp. 21-22). It has only said that it is interested, (WH Ex. 1.00, pp. 6-7), but that its interest requires further study. (Aqua Ex. 5.0A2, p. 22 (citing WH Association response to Aqua data request 1.11)).

Aqua believes a bulk billing option could be a good resolution to the Woodhaven Divisions' uncollectibles problem. (Aqua Ex. 5.0A2, p. 24). In fact, it is an option Aqua first raised with the WH Association. It was the very first item on Aqua's May 15th 2003 meeting agenda with the WH Association. (WA Ex. 1.00, Ex. WA 1.02, p. 4). Aqua attempted to pursue the option with the WH Association in early 2004. (Aqua Ex. 5.0A2, p. 22; WA Ex. 1.02).

Irrespective, the Public Utilities Act does not grant the Commission legal authority to implement a bulk billing option. *Bus. & Prof. People for the Public Interest v. ICC*, 136 Ill.2d 192, 243 (1989)(holding the Commission is a creature of statute that only has the authority granted it by the legislature); *City of Chicago v. Fair Employ. Prac. Comm'n.*, 65 Ill.2d 108-112-13 (1976)(holding administrative agencies cannot take action unless enabling legislation specifically confers the requisite authority). Nowhere in the Act is the Commission given authority to require a property owners association to assume legal responsibility for third party customers' utility bills, nor can it (a) impose on an association the costs associated with billing and collecting from end users, or (b) regulate the manner in which an association bills and collects for utility service. Aqua's customers are those individuals that take service, not the WH Association that operates the campsite facilities. Unless the WH Association voluntarily agrees to assume these responsibilities, it is the customers themselves that are responsible to pay the bills.

There is no evidence as to what a bulk billing option would specifically entail. For example, the WH Association alleges generally that some of Aqua's administrative costs would be reduced (WA Ex. 1.00, p. 13); but, it does not identify those costs specifically. As such, the Association has not presented even a minimal evidentiary foundation from which a bulk billing option could be constructed and implemented. Consequently, the Commission has no

evidentiary record to adjust Aqua's expenses in the event a bulk billing option is somehow adopted.

Further, even in the WH Association's *general* discussion of costs that its proposal would allegedly reduce, it identifies costs that are entirely unrelated to the uncollectibles problem. It alleges the option would reduce the management expenses related to the customer count allocation issue. (*See e.g.*, WH Assoc. Issues List, p. 2). However, as discussed *infra*, the expenses that are the subject of the customer count allocation issue are common costs incurred at Aqua's corporate parent and Illinois corporate levels to operate all divisions. (Tr., pp. 64, 122-23). The Division-specific costs Aqua incurs in relation to the Woodhaven Divisions' uncollectibles problem are not common costs that are allocated among all divisions by customer count. (Tr., p. 123 (Mr. Bunosky testifying that division specific costs are allocated directly)).

In conclusion, the Commission does not have the legal authority to impose the bulk billing option. Moreover, there is no evidence demonstrate which expense items would be reduced if the option was adopted. The Commission should reject the bulk billing proposal.

4. Allocation of Management Expense – Woodhaven Divisions

The Management Expenses at issue are those included in Account 634, Contractual Services - Management Expense. These are *common* costs incurred at Aqua's Illinois corporate and Aqua America, Inc. parent corporate levels to operate the entire state, *i.e.*, manage *all* Illinois divisions.¹³ (Tr., pp. 64, 122-23). Examples are the costs to prepare an overall state budget, and the salaries and wages of the Company's President and Chief Financial Officer. (Tr., pp. 122-23,

¹³ That these two types of costs make up Account 634, Contractual Services – Management expense is clearly set forth in Staff Ex. 7.0R, Att. A. The second to last column to the right is “Contractual – Parent [*i.e.*, Aqua America, Inc.] Account 634” and the last column to the right is “Illinois Corporate Account 634.”

125-26). Specific divisions do not cause these costs to be incurred. (Tr., p. 126 (Mr. Bunosky explaining that Aqua cannot assign the costs to specific divisions)).

Because common costs cannot be assigned to specific divisions, Aqua has to use an allocation methodology to assign such costs across customers in all divisions. (Tr., pp. 125-26). The method Aqua uses is customer count. (Tr., p. 126). This method is fair because it results in every single customer bearing an equal amount of the costs.¹⁴ (Tr., p. 128).

The Commission has approved the use of this allocation method. In Aqua's most recent rate cases for its Kankakee and Vermilion Divisions, Aqua allocated Management Expenses on a per customer basis. (See Sch. A-5, WP-A5 in Dkts. 03-0403 and 04-0442). Staff did not object to use of the customer count allocation method, and the Commission approved the Management Expenses based on the customer count allocation method as set forth in Aqua's filings.

a. Reduced Allocations Would Cause Inequalities

Allocation methodologies distribute 100% of common costs among all customers. (Tr., pp. 127-28; see also Staff Ex. 7.0R, Sch. 7.0R2, p. 2). If there is a reduction in the allocation to any set of customers, the allocations to all other customers necessarily increase such that 100% of the costs are still allocated in total.¹⁵ (Tr., pp. 127-28). The result would be an unequal distribution of common costs—Aqua would recover more common costs from some customers than from others even though all customers are equal causers of common costs. Aqua's common

¹⁴ Mr. Bunosky gave a hypothetical example. Assume Management Expenses of \$100 to be allocated over 100 total customers in Illinois using the customer count method. The \$100 is divided between divisions equal to the number of customers in each division, so that a division with 10 customers is allocated \$10 and one with 6 customers is allocated \$6. In turn, the division that is allocated \$10 divides that amount among each of its 10 customers so each customer is allocated \$1, and the division that is allocated \$6 divides that amount among its 6 customers so that, again, each customer is allocated \$1. (Tr., p. 130).

¹⁵ Using the same hypothetical, if the division with 10 customers were allocated half its share, *i.e.*, only \$5 instead of \$10, then each customer in the division would only bear .50¢ rather than \$1 of the common costs. The remaining \$5 would be reallocated to the division with 6 customers, with the result being that the 6 customer division would be allocated \$11 in total and each customer in the division would bear \$1.83 of the common costs.

cost allocation method seeks to avoid the imposition of such cross-customer “subsidies.”

Instead, under Aqua’s allocation method, each customer pays its fair share.

b. The Reasons Advanced For Reduced Allocations Are Red Herrings

Staff and the WH Association propose to reduce the Woodhaven Divisions’ allocations of Management Expense. Both parties allege reductions would be appropriate because customers in the Division do not use their properties on a year around basis. (Staff Ex. 7.0R, pp. 13-14; WH Ex. 1.00, p. 14). The WA Association also alleges that Aqua treats customers who take both water and sewer service as a single customer and asserts, therefore, that a customer who is a customer of both Divisions should be counted only one time.¹⁶ (WH Ex. 1.00, p. 14). Neither is a valid basis to reduce the Woodhaven Divisions’ allocations of common costs.

i. There Is No Evidence Of Common Cost Savings

Staff and the WA Association have identified service variables that produce *direct* cost savings. Direct costs are those incurred to provide service to specific divisions and, therefore, can be directly assigned to (or recovered from) those divisions. (Tr., pp. 115-16, 123). The recovery of direct costs is not at issue. The issue is how *common* costs should be recovered.

Usage is a direct cost variable. The only costs Aqua avoids if a customer does not use its service are the variable costs directly related to usage, such as the cost of the water consumed.¹⁷ Aqua still has to be prepared to provide service 24 hours a day, 365 days a year. It still incurs all common costs accounted for as Contractual Services – Management Expense. (Tr., p. 124).

¹⁶ Aqua has 11,575 customers across both Divisions (6,169 water customers and 5,406 wastewater customers. (See Staff Ex. 7.0R, Att. A).

¹⁷ The WH Association incorrectly claims that Woodhaven customers are like availability customers. However, availability customers are very different from Woodhaven customers who simply choose not to use service during certain times. Availability customers do not take service at all. They pay a bi-monthly fee for the *opportunity* to become a customer in the future. (Tr., p. 116). Because availability customers are only paying for the opportunity to take service at some future time, it is Staff’s current position that those customers should not bear as great a responsibility for the viability of the system. (Staff Ex. 9.0, p. 3).

Similarly, the manner in which Aqua “treats” customers who take both water and sewer service only affects direct costs. The WA Association notes that (a) Aqua sends a single bi-monthly bill with both service charges to people who are customers of both service divisions, and (b) Aqua provided the Association with uncollectibles information based on a per lot rather than customer-by-division basis. (WA Ex. 1.00, p. 14). The only costs Aqua avoids by issuing a single bill are the variable costs directly related to billing, *i.e.*, the cost of paper and postage to send a second bill when customers take both services.¹⁸ (Tr., p. 108). The services are still separate. Aqua has a water plant and distribution system through which it provides water service, and a sewer plant and distribution system through which it provides wastewater service. (Tr., p. 108). It still incurs all common costs irrespective of whether it issues a single bill.¹⁹

Accordingly, the assertion that Woodhaven customers should receive reduced allocations of *common* costs because of *direct* cost savings mixes apples with oranges. Management Expense only includes those common costs incurred at the Illinois corporate and parent corporate levels to operate all Illinois divisions. The avoidance of direct costs does not impact, in any way, whether Aqua incurs common costs.

ii. Reduced Allocations Would Double Count Savings

As discussed, direct costs are directly assigned and recovered from those customers that cause the costs. (Tr., pp. 115-16, 123). To the extent any factor reduces direct costs, the amount of direct costs assigned and recovered are smaller—*i.e.*, savings result. In other words, if direct

¹⁸ Aqua still incurs the cost of deriving the bill amounts and applying payments for both services. Aqua did not save any costs by the mere fact that it reported uncollectibles to the Association on a per lot basis.

¹⁹ At the hearing, Mr. Bunosky also explained that Aqua is able to share some operating costs between the Water and Sewer Divisions. For example, Aqua uses the same employees and some of the same equipment to operate both systems. (Tr., p. 108). Once again, however, these types of operating costs are directly associated with providing service to the two Divisions and, therefore, are directly assigned and recovered. (Tr., p. 115). They are not common costs included in Contractual Services - Management Expense.

costs are not incurred, they are neither assigned nor recovered. Passing on additional savings via common cost reductions on the grounds that direct cost savings exist would double count the direct cost savings that already are being passed on to customers.

To take one example, Mr. Bunosky explained at hearing that, to the extent Aqua is able to share its direct operating costs between the Woodhaven Water and Sewer Divisions, it divides the costs between them. (Tr., pp. 110, 115). As such, the employees who operate in both Divisions track their work and activities, and Aqua assigns the proportionate share of their salaries directly between the two Divisions via the Labor Expense account. (Tr., p. 115). If an employee spends 60% of the time on the Water system and 40% on the Sewer system, Aqua assigns 60% and 40% of the employee's salary to the Water and Sewer Division, respectively. (*Id.*) Each Woodhaven Division saves the portion of the employee's salary that is directly proportionate to the amount of time and work the employee performs for the other Woodhaven Division.

Accordingly, customers in the Division already receive the full savings that result from the direct cost savings that have been identified. Any reduction in those Divisions' share of common costs would double count the savings. The customers would reap significantly greater savings than they actually produce. The Commission should not approve such a windfall for Woodhaven customers.

iii. Reduced Allocations Would Be Discriminatory

Neither Staff nor the WH Association has identified a reasonable basis to treat customers in the Woodhaven Divisions differently when it comes to the allocation of common costs. Because the factors those parties identified relate to direct costs, they are not reasonable bases to

distinguish or differentiate the allocation of common costs. In the absence of such a reasonable basis founded in the record, any reduced allocation would amount to preferential treatment.

The factors Staff and the WH Association identified are not even unique to Woodhaven. Customers in other divisions do not take usage at all times. In fact, ORPA witness Mr. Davison testified that half of the Oak Run Division’s 600 consumption customers are “weekend or part-time owners who use very little water.” (ORPA Ex. 1.0, p. 8). Yet, based on the proposal of Staff and the WH Association, the allocations to customers in the Oak Run Division would *increase* while the allocations to customers in the Woodhaven Divisions *decrease*.²⁰

Furthermore, Aqua provides both water and sewer service in the majority of its service areas. Aqua has fifteen operating systems in Illinois:²¹

- | | | | |
|----|------------------------------|-----|---|
| 1. | Kankakee | 8. | Candlewick Water |
| 2. | Willowbrook Water | 9. | Candlewick Sewer |
| 3. | Willowbrook Sewer | 10. | Oak Run |
| 4. | University Park Water | 11. | Ivanhoe Water |
| 5. | University Park Sewer | 12. | Ivanhoe Sewer |
| 6. | Woodhaven Water | 13. | Vermilion |
| 7. | Woodhaven Sewer | 14. | Hawthorn Woods Water ²² |
| | | 15. | Hawthorn Woods Sewer |

(Staff Ex. 7.0R, Att. A). As is readily seen, twelve of Aqua’s systems are in areas where Aqua provides both water and sewer service. Aqua operates those systems in all relevant respects the

²⁰ As explained *supra*, any reduction in the allocations to the Woodhaven Divisions would be transferred to customers in the other Divisions for recovery.

²¹ It provides contract services at two systems, Sublette Water and Tower Lakes Water, (tr., pp. 143-44), which leaves thirteen traditional operating systems in Illinois.

²² Aqua also provides service to Hawthorn Woods Water and Sewer, which service areas it included in Ivanhoe Water and Sewer in its data request response that is Staff’s Ex. 7.0R, Att. A.

same way it operates its Woodhaven Divisions—*i.e.*, it sends a single bi-monthly bill to the customers who take both services. (Tr., p. 118). It allocates direct operating costs directly to the divisions, including the salaries of the employees who operate the divisions. (Tr., pp. 108-10, 115-16). Yet, again, based on Staff’s and the WH Association’s proposal, customers in the Willowbrook, University Park, Candlewick, Ivanhoe and Hawthorn Woods Water and Sewer Divisions would receive *increased* common cost allocations at the same time that customers in the Woodhaven Divisions’ received *reduced* allocations.

Accordingly, neither Staff nor the WH Association has identified a legitimate basis to distinguish the Woodhaven Divisions from Aqua’s other divisions on the issue of common costs. The reduced allocation proposed, therefore, would treat Woodhaven customers preferentially to the disadvantage of Aqua’s customers in other divisions. There is no basis to subsidize the customers in the Woodhaven Divisions at the expense of customers in Aqua’s other divisions. It would not be appropriate to engage in such preferential treatment.

Indeed, quite contrary to the position of Staff and the Association, the evidence is replete with reasons that customers in the Woodhaven Divisions should not be treated to a windfall in common cost savings. For example, the Divisions have caused a great amount of management time to be spent addressing the uncollectibles problem, yet they are not allocated a greater share of costs as a result. (Tr., p. 120). In addition, the radical variances in the customers’ usage, *i.e.*, from low week-day usage to “tremendous peak loading on the weekends,” make the systems very difficult to operate. (Tr., pp. 120-21). Aqua, nonetheless, operates the systems with only three employees when systems of the same size are typically operated with an average of twelve employees. (Tr., pp. 121-22). The Woodhaven Divisions, therefore, already are treated very favorably in terms of the costs they are required to bear.

c. No Evidence Supports The WH Association’s Claim That The Customer Count Method Is Unfair

The WH Association asserts that Woodhaven customers are somehow treated unfairly by Aqua’s customer count allocation method. (WA Ex. 2.0, pp. 8-9). The only basis it advances for its position, however, is that Woodhaven customers would be allocated less common costs under an average plant or rate base method. (*Id.*) It does not present any evidence that a rate base method is more reasonable than using a customer count method. (*Id.*)

The WH Association’s position is inherently unreasonable. It clearly favors the method that will allocate less common costs to Woodhaven customers irrespective of the resultant effect on customers in Aqua’s other divisions. It disregards the fact that customers in other divisions will pay more than their equal shares of common costs so that Woodhaven customers can pay less.

In fact, allocating less than equal shares to Woodhaven customers would cause increased allocations to customers in mostly smaller divisions. The two Woodhaven Divisions are the third and fourth largest in customer size.²³

Kankakee	23,093	Candlewick Water	1,908
Willowbrook Water	1,038	Candlewick Sewer	1,907
Willowbrook Sewer	1,083	Oak Run	1,266
University Park Water	2,044	Ivanhoe Water	280
University Park Sewer	1,968	Ivanhoe Sewer	237
Woodhaven Water	6,169	Vermilion	17,255
Woodhaven Sewer	5,406		

²³ Again, Hawthorn Woods Water and Sewer are included within Ivanhoe Water and Sewer in Staff Ex. 7.0R, Att. A.

(Staff Ex. 7.0R, Att. A). Customers in these other divisions should not bear more than their equal shares of common costs just so Woodhaven customers can bear less.²⁴

Again, the WH Association did not present any evidence that rate base allocations would be more equitable; but, there is substantial evidence that customer count allocations are. First, as explained *supra*, the customer count method produces equal allocations, which is inherently fair for common costs that are driven equally by all customers. The rate base method, on the other hand, would allocate unequal customer shares. Second, customer counts better reflect the fact that the more customers a water or sewer system has the more issues arise that require customer support, engineering, accounting, operations, maintenance, planning, forecasts, budgets, etc. (Aqua Ex. 5.0A2, pp. 27-28). Third, customer count is consistent with the manner in which Aqua's parent company allocates common costs and, therefore, the simplest for Aqua to administrate.²⁵ (*Id.*, p. 28). In contrast, the rate base method has none of these benefits.

Further, the evidence demonstrates that the rate base method is flawed. It will be skewed by Customer Advances and/or Contributions in Aid of Construction. (Aqua Ex. 8.0, p. 19). A utility still has to expend resources to manage contributed plant; but, because the plant is not included in Rate Base, it would not serve as a basis to allocate Management Expense.

The WH Association overlooks all these factors that demonstrate that allocation of common costs using customer count is the more appropriate method to utilize. The Commission should not ignore these factors, but instead should consider the impact on all customers, not just

²⁴ While Kankakee and Vermilion are larger, the customer count method allocates a proportionately larger share of common costs to those Divisions. In particular, Kankakee and Vermilion customers bear \$984,474 out of a total of \$1,568,014 in Illinois corporate and \$864,347 out of a total of \$1,376,683 in Aqua America, Inc. parent costs allocated via account 634. (Staff Ex. 7.0R, Att. A).

²⁵ The common costs Aqua's parent company incurs to operate its divisions across all states are allocated based on the customer counts in each state.

those in the Woodhaven Divisions. Because the customer count method allocates common costs fairly to all customers, the Commission should approve its use.

d. Any Prior Windfall To The Woodhaven Divisions Should Not Dictate The Use Of A Less Equitable Allocation Method

As noted, the Commission approved Management Expense allocations based on customer count in Aqua's two most recent rate cases in 2003 and 2004. *See supra*, p. 15. Yet, both Staff and the WH Association seek to fall back on the fact that for a period of time *before 2003* Aqua used rate base to allocate the Illinois corporate portion of Contractual Services – Management Expense.²⁶ (*See e.g.*, Tr., pp. 63-64). The Commission should not require Aqua's use of the rate base method, which produces less equitable allocations of common costs, for this reason.

Aqua is currently using the customer counts to allocate all Management Expenses because it is the fairer method for allocating common costs, as discussed *supra*. The WH Association prefers the rate base method simply because it allocates to Woodhaven customers less than their equal shares of common costs. But, the rate base method causes Aqua's other customers to pay more than their fair shares. It would be unreasonable to require Aqua's use of the less equitable rate base method simply because, for some period prior to 2003, Woodhaven customers received *unearned* common cost reductions via Aqua's use of the rate base method for the Illinois corporate portion of Management Expense.

Nor are customers in the Woodhaven Division in any way penalized by Aqua's use of the customer count method. To the contrary, those customers clearly received unearned benefits to the extent Aqua previously used the rate base method. The fact that they have historically reaped

²⁶ As noted above, there are two type of common costs included in Account 634, Contractual Services – Management Expense, namely Illinois corporate and Aqua America, Inc. parent. Prior to 2003, Aqua only allocated the Illinois corporate portion of Management Expense pursuant to rate base. (Tr., pp. 63-64).

such a windfall does not mean it should continue to the detriment of customers in other divisions. The customer count method allocates an equal amount of common costs to all customers. The allocation of Management Expense to Woodhaven Customers based on this method should be approved.

5. Rate Case Expense

Staff advances several unreasonable positions on Rate Case Expense. First, it proposes to disallow Aqua's expense to present a Return on Equity ("ROE") witness. Second, Staff disregards the reasonableness of Aqua's original Rate Case Expense projections in total and, instead, proposes the adoption of one-sided adjustments to underlying components. Third, it proposes the application of unreasonable and discriminatory rules to Aqua's future rate case filings. The Commission should reject Staff's proposals in their entirety.

a. Expense for Aqua's ROE Witness Ms. Ahern

Aqua is entitled to seek what it believes is a reasonable ROE. Indeed, it has the burden of presenting evidence on each aspect of its rate request, including ROE. Aqua could not rely upon the Commission's prior ROE findings for other rate divisions because capital costs change over time. (Aqua Ex. 6.0R, p. 18). It had to support its position in these cases or it would have had no recourse if it found Staff's position unacceptable.²⁷ Aqua's ROE witness expense, therefore, is a legitimate expense that needs to be recovered.

Staff, nonetheless, advances two unreasonable grounds to disallow Ms. Ahern's expense. First, it asserts that Aqua could have avoided the expense if Aqua had filed these three cases earlier with either Vermilion in May 2004 (seven months) or with Kankakee in May 2003 (nineteen months). (*See* Staff Ex. 6.0, p. 9). Second, Staff claims Ms. Ahern's expert opinion is

²⁷ As discussed below, Aqua was able to accept Staff's position on ROE in these cases.

not in “good faith” because the Commission did not adopt it previously. (*Id.*) It is imperative that Staff’s adjustment, based on these grounds, be rejected by the Commission.

i. The Commission Has Already Rejected Staff’s Position

In Docket No. 99-0288, which was a filing for Aqua’s Candlewick Division, Staff argued to disallow certain Rate Case Expense because Aqua filed the “rate case for only the Candlewick Water Division instead of simultaneously filing rate cases for several divisions and thereby realizing the economies of scale.” *Consumers Ill. Water Co.*, Dkt. 99-0288, 2000 WL 34446603, slip op. at 14 (2000). The Commission unequivocally held: “We determine that there is no legal basis on which to penalize [Aqua] and disallow a portion of the proposed rate case expense, as Staff suggests, for not combining this rate filing with rate filings for other divisions.” *Id.*, slip op. at 16. The Commission should rule consistently in these pending cases.

ii. It Would Have Cost Ratepayers *More* If Aqua Had Filed These Cases With Kankakee Or Vermilion

Staff’s assertion that Aqua could have avoided Ms. Ahern’s expense if it had filed these cases with Kankakee or Vermilion misses the forest for the trees. All other aspects of these rate cases would have occurred earlier, *including the rate increases*, if Aqua had done so. While Staff presumes ratepayers would have received a net benefit, they would have seen a *net detriment*:

Seven Month Acceleration to file with Vermilion in May 2004

- **Oak Run:** Oak Run’s cost of service reflects \$3,250 annually for ROE witness expense. This equates to savings of only \$1,896 had Oak Run been accelerated seven months. However, Aqua requested an annual revenue increase of \$213,209. This amount less the \$3,250 annual ROE savings results in a net increase of \$209,959 annually. Accelerating this net increase seven months equates to \$122,476 more in revenues for Oak Run customers to pay.

- **Woodhaven Water:** Cost of service reflects \$3,875 annually for ROE witness expense. This equates to savings of only \$2,260 had Woodhaven Water been accelerated seven months. Aqua requested an annual revenue increase request of \$500,284. This amount less the \$3,875 annual ROE savings results in a net increase of \$496,409 annually. Accelerating this net increase seven months equates to \$289,572 more in revenues for customers to pay.
- **Woodhaven Sewer:** Cost of service also reflects \$3,875 annually for ROE witness costs. This equates to savings of only \$2,260 had Woodhaven Sewer been accelerated seven months. Aqua requested an annual revenue increase of \$459,314. This amount less the \$3,875 annual ROE savings results in a net increase of \$455,439 annually. Accelerating this net amount seven months equates to \$265,673 more in revenues for Woodhaven Sewer customers to pay.

Nineteen Month Acceleration to file with Kankakee in May 2003

- **Oak Run:** As noted, the Oak Run cost of service reflects \$3,250 annually for ROE witness expense. This equates to \$5,146 in savings had Oak Run been accelerated nineteen months. However, the \$213,209 annual revenue request less the \$3,250 ROE savings results in an annual net increase of \$209,959 that, accelerated nineteen months, equates to \$332,435 more in revenues for Oak Run customers to pay.
- **Woodhaven Water:** As also noted, the Woodhaven Water cost of service reflects \$3,875 annually for ROE witness expense. This equates to \$6,135 in savings had Woodhaven Water been accelerated nineteen months. The \$500,284 annual revenue request less the \$3,875 ROE savings results in a net increase of \$496,409 that, accelerated nineteen months, equates to \$785,981 more in revenues for Woodhaven Water customers to pay.
- **Woodhaven Sewer:** Lastly, the Woodhaven Sewer cost of service also reflects \$3,875 annually for ROE witness expense. This equates to \$6,135 in savings had Woodhaven Sewer been accelerated nineteen months. The \$459,314 annual revenue request less the \$3,875 ROE savings results in a net increase of \$455,439 that, accelerated nineteen months, equates to \$721,112 more in revenues for Woodhaven Sewer customers to pay.

(Aqua Ex. 6.0R, pp. 12-14). In total, ratepayers would have paid \$677,721 or \$1,839,528 more in revenues had Aqua filed these three cases with Vermilion or Kankakee, respectively. (*Id.*, p. 15).

Staff witness Ms. Pearce weakly acknowledged that the ROE witness savings would have been “mitigated.” (Staff Ex. 6.0, p. 10). She asserted, however, that other savings are inherent

in combined filings such that, presumably, ratepayers would have received a net benefit if Aqua had filed these cases with Kankakee or Vermilion. The areas where she alleged other savings would arise are (a) outside legal costs because only one hearing and one set of briefs would be required, (*id.*, pp. 10-11), and (b) expenses related to the preparation of “*total company* schedules, common expenses and accounting issues....” (Tr., p. 334)(emphasis added).

Ms. Pearce’s assumption that a single evidentiary hearing and set of briefs would reduce outside legal expense is not correct. With the single exception of ROE, which Aqua settled after Direct Testimony in these pending cases, *none* of the issues in these cases are the same as those in either Vermilion or Kankakee. The same amount of legal work would have needed to be done to address all the issues. The single hearing and set of briefs simply would have been longer.²⁸

Indeed, when Ms. Pearce was asked how attorney time would have been saved, Staff counsel objected on the grounds that Ms. Pearce is not “in a position to know” what goes on “with respect to lawyer time and other time that goes into each issue.” (Tr., p. 331). When allowed to respond whether it would take additional lawyer time to address the additional issues in a combined case, Ms. Pearce responded with “I can’t say” and “It might.” (Tr., p. 332). Such testimony does not support a finding that outside counsel expense would have been reduced by a single hearing and set of briefs if these cases had been filed with Kankakee or Vermilion.

As to savings related to the preparation of total company schedules, expenses and accountings, Aqua is recognizing those savings in these cases already. (Aqua Ex. 6.0R, p. 35). Aqua developed total company information for a 2005 test year for the Vermilion filing in May,

²⁸ Travel expense to Springfield for the hearings may have been saved but, as noted, the number of issues that would have been addressed during the hearings would have increased so the hotel stays and related expense would most likely have increased. The savings, *i.e.*, mileage and airline tickets, would have been very small.

2004, and used the same information in its filings for these pending cases. (*Id.*) The filings did not need to be combined with Kankakee or Vermilion for these savings to be realized.²⁹

Ultimately, Ms. Pearce took the position that “[a]bsent a complete analysis of the incremental costs and savings ... it is difficult to quantify the full impact on ratepayers.” (Staff Ex. 6.0, p. 11). But, when asked if she conducted an analysis, Ms. Pearce said “No.” (Tr., p. 335). Indeed, it is not difficult to determine that the impact on ratepayers would have been negative. To support Staff’s position that Aqua should have filed these cases with Vermilion or Kankakee, the savings would have to exceed \$667,721 and \$1,839,528 in increased revenues, respectively. It would not be possible for savings to exceed those amounts because it is not even costing Aqua that much to process these three cases now.

Accordingly, the evidence clearly demonstrates the unreasonableness of Staff’s position. In order to avoid ROE witness expense, between \$677,721 and \$1,829,528 more in revenues would have been imposed on ratepayers. The Commission should not adopt this position.

iii. It Would Be Illegal To Condition Legitimate Expense Recovery On Postponing Rate Case Filings

The WH Association asserts Aqua could have avoided its ROE witness expense if it had postponed these cases from December, 2004 until early 2006 when it intends to file its next rate case for Kankakee.³⁰ (WA Ex. 2.0, p. 12). Once again, however, the quantitative analysis would necessarily show that a postponed filing would impose greater costs than ROE witness savings, this time on Aqua rather than ratepayers. Aqua would incur significant costs in foregone revenue

²⁹ Ironically, Staff proposes to prohibit Aqua from realizing these savings in future rate cases. *Infra*, pp. 36-39.

³⁰ The WH Association misrepresents that Aqua intended to file Kankakee in 2005, and cites an Earnings Conference Call in support. (WA Ex. 2.0, p. 12). The statement made during the Call, however, was that Aqua intended to file Kankakee either *late* in 2005 or early 2006. (*Id.*) Aqua currently does not intend to file Kankakee until sometime in 2006. Irrespective, the same analysis applies—it would be equally inappropriate to condition Aqua’s recovery of a legitimate expense on postponing its filings from December 2004 to either late 2005 or 2006.

during the postponement. (Aqua Ex. 8.0, p. 23). Further, because rates from the anticipated Kankakee filing would not be in effect until 2007, if Aqua had delayed these cases it also would have forgone at least a year's recovery of the significant carrying costs and expenses associated with the Radium Removal project for Woodhaven Water. (*Id.*) The fact that Aqua would bear these costs rather than ratepayers does not make it reasonable.

Nor would it be legal. Aqua is entitled to a fair return on its investment. *Candlewick Lake Util. Co. v. ICC*, 122 Ill. App. 3d 219, 222 (1983); *Cerro Copper Prod. v. ICC*, 83 Ill.2d 364, 369 (1980); *Union Elec. Co. v. ICC*, 77 Ill.2d 364, 379 (1979); *Illinois Cent. R. Co.*, 387 Ill. at 275. The evidence demonstrates that Aqua lost money in each of these three Divisions during 2004. Under-earning cannot be legally imposed *for any period of time* as a condition to the recovery of legitimate ROE witness expense.

Accordingly, the WH Association's suggestion that Aqua should have under-earned its allowed return (and, in fact, provided service at a loss) for more than an additional year in order to save ratepayers ROE witness expense is unfair and illegal. Staff has not even supported the position. The Commission should reject it.

iv. Ms. Ahern Testified To Her Expert Opinion In Good Faith

Ms. Ahern is, without question, a recognized expert in her field. (Aqua Ex. 3.0, pp. 1-2). There can be no doubt that she possesses the relevant expertise to form a good faith opinion on ROE. Staff's assertion that she did not have a good faith basis for her opinion on ROE is entirely unfounded and unreasonable.

Staff witness Ms. Freetly claims, nonetheless, that Ms. Ahern's opinion is not in good faith because the Commission did not adopt it in earlier rate cases. (Staff Ex. 8.0, pp. 8-10).

Such a position would require Ms. Ahern misrepresent her expert opinion under oath (in order to be consistent with the Commission's prior orders) to be considered in "good faith." Such a position is not reasonable. Ms. Ahern's expert opinion is based on her education and experience. It is not dependent on whether it is adopted by the Commission or any other third party.

Further, the Commission's decisions are not res judicata. *Citizens Util. Bd. v. ICC*, 225 Ill. Dec. 435, 440 (1997); *Peoples Gas, Light & Coke Co. v. ICC*, 175 Ill. App. 3d 39, 51 (1988). Parties always have the opportunity to argue for the Commission to change its position on an issue, including ROE. There is no prohibition in the Public Utilities Act or the Commission's rules on what positions parties may advance. The Commission can change its position on any issue provided it has a reasonable basis for doing so. *Citizens Util. Bd. v. ICC*, 166 Ill.2d at 132. Ms. Ahern's expert opinion would be a reasonable basis for the Commission to adopt a new position on ROE.

Indeed, Staff's proposal is contrary to its own actions. It argues Ms. Ahern's expert opinion is not in good faith because it is not consistent with past Commission decisions; but, Staff testifies to positions that contrary to Commission decisions all the time. In fact, Staff is doing so in these pending cases, it did so in the 2004 Vermilion rate case, and Staff witness Ms. Freetly testified there is no guarantee it will not do so again.

In these pending cases, Staff is testifying that Aqua should not recover its ROE witness expense because Aqua did not file these cases with either Vermilion or Kankakee. As discussed *supra*, however, the Commission unequivocally rejected the same position in *Candlewick*. Similarly, in the 2003 Kankakee case, the Commission held that 30 basis points ("bps") should be added to ROE to account for Aqua's NAIC-2 rating. (Order, Dkt. 03-0403, p. 43). Yet, in the 2004 Vermilion case, Staff testified against the Commission's decision. (See e.g., Dkt. 04-0442,

Staff Ex. 7.0R, pp. 14-15). When asked if Staff would testify against the Commission's decision in future cases, Ms. Freetly testified she could not guarantee that Staff would not. (Tr., p. 388).

Staff, therefore, freely advances positions that are contrary to prior Commission orders but argues that when other parties do so that it is somehow in bad faith. This is an unreasonable and discriminatory position.

It is, furthermore, one that Staff is attempting to retroactively apply. Aqua is unaware of any instance when a party's recovery of witness expense has been disallowed on the grounds Staff proposes. It had no notice of Staff's proposed rule when Ms. Ahern prepared her Direct Testimony for filing in these cases and Aqua incurred the expense. There would be no way for Aqua to go back in time to account for Staff's new position.

b. Rate Case Expense Recovery

Because Rate Case Expense is incurred over the course of rate proceedings, the final amounts are not known until case completion. (Aqua Ex. 8.0, p. 16). Accordingly, the Commission allows recovery as a function of actual costs incurred plus a reasonable estimate of the costs that will be incurred through the conclusion of the case. *Consumers Ill. Water Co.*, Dkt. 99-0288, 2000 WL 34446603, slip op. at 16 (2000). The Commission has accepted actual costs to complete similar cases as a reasonable basis to estimate costs through case completion. *Id.* at 12, 16 (the Commission accepted Aqua's Rate Case Expense where the costs through case completion was based on Aqua's actual costs in a similar rate case).

i. Aqua's Original Projections, In Total, Are Supported³¹

In this case, Aqua original projections of \$129,875, \$160,950 and \$160,950 to process the Oak Run, Woodhaven Water and Sewer cases, respectively, are supported. (Aqua Ex. 8.0, p. 16). Aqua has incurred more than \$89,156, \$85,133 and \$80,665, in turn, through the time of its Surrebuttal Filing.³² (Aqua Ex. 8.0, p. 14). Its invoices prove that these amounts have actually been incurred. (*Id.*, Ex. D).

Aqua reasonably anticipates that it will incur its total original projections to complete these cases. From the week before hearings through case completion in the Vermilion rate case, Aqua incurred \$97,819.36 in outside legal expense. (*Id.*, p. 15). The amount incurred through case completion in Vermilion, assuming each Division in the pending cases drives approximately 1/3 of the costs, supports an additional \$32,606.45 per Division in outside legal expense through case completion. (*Id.*)

Vermilion is a reasonable case from which to estimate additional outside legal expense because it was Aqua's most recent rate case. It is the most reflective of the degree of work necessary to process a rate case before the Commission's current Staff, which, as discussed *infra*, is conducting more extensive reviews. While the Vermilion case addressed one of Aqua's larger divisions, the three Divisions at issue in these consolidated cases should drive a similar amount of work. In fact, the number of issues raised has been relatively equal. (*Id.*)

Indeed, the Vermilion case is most likely a conservative estimate of the work necessary to process the three pending cases. There are two active intervenors in these cases where there

³¹ The ALJ's Outline breaks total Rate Case Expense into components. Aqua's position, however, is that its original projections are supported in total. Staff's attempt to make one-sided adjustments to underlying components of the Expense is addressed in the subsequent sub-section of the Brief.

³² These are not the total amounts Aqua had incurred because they do not include July time for Aqua's counsel Mr. Rooney, witness Mr. Schreyer or any other individual in the rate department of Aqua's parent company. (*Id.*)

were none in Vermilion. Aqua has to respond to three sets of briefs whereas, in Vermilion, Aqua only had to respond to Staff. In addition, Staff has conducted a significantly heightened review in these pending cases. In the 2003 Kankakee case, Staff issued a total of 177 data requests. (Aqua Ex. 6.0R, p. 29). In Vermilion it issued 358 including subparts, which was very significant. In these consolidated cases, however, Staff has issued almost 700.³³ (*Id.*, p. 30). This evidences an overall heightened review process that has increased even more since Vermilion and that, in turn, drives more legal work and expense. (*Id.*, p. 29). The legal work necessary to process these cases, therefore, will likely be more than in Vermilion such that the additional \$32,606.45 per Division in Outside Legal Expense that Vermilion supports is likely conservative.

In addition to a projection of Outside Legal Expense, it is also necessary to account for additional witness and rate department expense through case completion, and it is appropriate to include a margin of error to account for unanticipated events that may arise. (*Id.*, p. 16). Indeed, the need for a margin of error has been demonstrated in these cases. Unanticipated events during the evidentiary hearings necessitated an expedited Petition for Interlocutory Review.

Accordingly, Aqua reasonably anticipates it will incur its overall Rate Case Expense projections of \$129,875, \$160,950 and \$160,950 to process the Oak Run, Woodhaven Water and Woodhaven Sewer cases, respectively. In turn, this equates to \$43,292, \$40,238 and \$40,238 as amortized annually based on Aqua's proposed amortization periods. The Commission should grant Aqua's full recovery.

³³ At the time of Mr. Schreyer's Rebuttal Testimony that includes this information, Staff had issued 626 data requests. By the end of the evidentiary phase of the cases, the number had risen to almost 700. Staff has claimed that the number is the sheer result of it issuing duplicate data requests for each of the three Divisions; but, only 76 have actually called for the same answers. Staff has also alleged it was necessary to issue such an extreme number of data requests because Aqua's filings were somehow incomplete. But, Aqua complied with the ALJ's Deficiency Notice, and Staff never asserted the ALJ's Notice was insufficient.

ii. Staff's One-Sided Approach Is Unreasonable

Staff proposes downward adjustments to two underlying Rate Case Expense components because it alleges Aqua's invoices show it will not incur its original projections for those two components, namely in-house Rate Department and Miscellaneous Expenses. (Staff Ex. 6.0, pp. 15-17). This approach is unreasonable because it is entirely one-sided.

Because Rate Case Expense is incurred during the case, it is never possible to project with certainty the degree to which each component will need to be relied upon. (Aqua Ex. 8.0, p. 16). Actual events will drive more costs for some components and less for others. (*Id.*) As a result, the original projections for some components will be exceeded and others will not. (*Id.*)

In these cases, actual events drove costs away from in-house Rate Department and Miscellaneous to Outside Legal Counsel and Witness Expense. Aqua had to rely upon outside counsel to a much greater extent than anticipated because Staff conducted a more heightened review, issuing almost 700 data requests,³⁴ two active intervenors participated, and both Staff and the intervenors raised a large number of issues that have serious implications. Aqua also used its outside counsel for miscellaneous-type activities, such as copying, postage, transcript fees and filings rather than handling those activities in-house. In addition, Aqua had to rely on its outside witness Mr. David Monie to a greater degree than anticipated to respond to very time consuming rate design data requests and handle issues raised by Staff's Schedule 9.01. (*Id.*, pp. 14-18).

As a result of these changes, Aqua may not reach its original projections for the in-house Rate Department and Miscellaneous components of Rate Case Expense but it will exceed its original projections for Outside Legal and Witness Expenses. Aqua originally projected it would

³⁴ See *Supra*, pp. 32-33 and fn. 33.

incur \$50,400 per Division in Outside Legal Expense. But, as of its Surrebuttal Filing, it had already incurred \$46,760, \$45,069 and \$44,427 for Oak Run, Woodhaven Water and Sewer, respectively. (*Id.*, p. 15). Based on the conservative amount of \$32,606.45 that the Vermilion case supports, it will clearly go over its original Outside Legal Expense projections for all of the Divisions. In addition, at the time of its Surrebuttal Filing, Aqua had already incurred fees for Mr. Monie in excess of original projections by \$5,251, \$6,378 and \$6,506, respectively, for the Divisions. It estimates that it will incur an additional \$1,500 per Division for Mr. Monie's testimony during the hearings and assistance on the briefs. (*Id.*, p. 15).

Staff's approach is unreasonable because, based on the actual costs Aqua's invoices show it is incurring, it adjusts Aqua's Rate Department and Miscellaneous Expense components down but does not adjust Rate Case Expense components upward where Aqua's invoices show it is exceeding its original projections. Such a unilateral, piece-meal approach is inherently biased to produce an under-recovery of legitimately incurred Rate Case Expense. Aqua is penalized for being unable to predict in advance of actually incurring Rate Case Expense that the events in the case would drive more costs to Outside Legal and Witness Expense and away from in-house Rate Department and Miscellaneous. Such a result is completely unfair.

Accordingly, the Commission should grant Aqua's recovery of its original Rate Case Expense projections because they are supported by actual costs incurred during the evidentiary phase of the cases plus a reasonable estimate of costs to be incurred through case completion. But, if the Commission follows a component approach, which it should not, it should take a more balanced approach than Staff. Rather than only making down-ward adjustments, it should also

adjust upward the components of Outside Legal and Witness Expenses that the evidence shows are being exceeded.³⁵

c. Staff Recommendations Regarding Future Rate Case Filings

Staff makes three proposals: (1) Aqua should consolidate future rate filings for several divisions; (2) Aqua should file rate cases for small divisions simultaneously with at least one of the larger divisions; and (3) back-to-back rate cases should not be for the same test year. (Staff Ex. 1.0, pp. 23-24). The Commission should not adopt any of these recommendations.

Initially, there is no legal requirement as to when a utility must file a rate case. The proper process for promulgating administrative rules to govern rate filings is a rulemaking proceeding, the result of which would apply to all utilities equally. 5 ILCS 100/5-5; *Riverboat Devel. Corp. v. Illinois Gaming Bd.*, 268 Ill. App. 3d 257, 259 (1994). Staff has not presented any basis to justify promulgating rules via a rate proceeding or applying the rules to Aqua alone. Its proposal is a clear example of discriminatory rulemaking.

Further, Staff's proposal for mandated, simultaneous filings would conflict with the Commission's holding in the 1999 Candlewick rate case discussed *supra*. The Commission did not address the issue of future rate case filings; but, the rationale of its holding was clear. The legitimacy of Rate Case Expense is not dependent on whether divisions are filed together.

Moreover, Staff witness Ms. Pearce admits that divisional-specific factors drive the need to file rate cases for different divisions at different times. (Tr., pp. 326-27). These include divisional specific capital investment, revenues and expenses. (*Id.*) Aqua is in the position to

³⁵ Staff has erroneously claimed that Aqua is attempting to "update" its rate filing in violation of the Commission's regulations. However, Aqua has simply presented evidence and arguments to demonstrate that Staff's one-sided, component-based approach is unreasonable. It continues to request recovery of its original Rate Case Expense projections in total.

know how these factors evolve over time and, therefore, is able to make appropriate decisions as to when they indicate rate cases should be filed. This is a proper management function. Staff's proposed rules would amount to improper micromanagement of the Aqua's operations.

Indeed, Ms. Pearce explained at hearing that one cannot predict the future and, therefore, cannot know when the factors will indicate a filing is appropriate for any division.³⁶ (Tr., p. 323). Accordingly, not only is Staff attempting to micromanage Aqua's operations, but it is attempting to set strict rules in advance of knowing the relevant information. It is not reasonable to require Aqua to file its different divisions at the same time when there is no basis to conclude that divisional-specific factors will indicate different divisions should be filed at the same time.

If Aqua is to file its divisions at the same time, then its divisions should be consolidated into a single rate area.³⁷ In the absence thereof, requiring Aqua to file its different divisions at the same time would require it to ignore the divisional-specific factors. It would necessitate the acceleration or postponement of filings *solely* to enable different divisions to be filed together. If cases are accelerated, ratepayers will be harmed whereas if postponed Aqua will be subject to an illegal condition to its right to earn a reasonable return. *See supra*, pp. 25-29.

The incentive would clearly be to accelerate the filings in order to avoid an illegally mandated delay and resultant cost to the Company. (Aqua Ex. 6.0R, p. 34). Such hasty action would run the added risk that cases would be filed before the best information is available. (*Id.*) The result would likely be rates that do not reflect operating conditions and, hence, would drive follow-up rate cases and even more costs. (*Id.*, pp. 11-12).

³⁶ Ms. Pearce made these comments when discussing the basis for her proposed Rate Case Expense amortization periods but they apply equally here.

³⁷ If Aqua's multiple divisions comprised a single rate area then the same factors would drive the need for rate cases across the entire area. It would be necessary, however, for the same rates to apply across the entire area as well.

Staff's third proposal is equally problematic. Use of the same test year is one area where economies of scale can be realized when divisional-specific factors determine that filings should be made at different times. (*Id.*, p. 35). Aqua has been able to recognize this type of savings in these pending cases by utilizing the total company portion of the rate template from Vermilion. (*Id.*) Staff's proposal would require these savings be foregone.

Staff's intended objective is clearly to lower rate case expense. But, the only savings Staff has been able to identify as necessarily flowing from simultaneous case filings is the cost of the ROE witness.³⁸ *See supra*, pp. 25-28. This is a very small savings compared to the costs of accelerating or delaying filings. Staff's future rate case proposals are not reasonably designed to meet its objective.

Nor does Aqua need artificial incentives in the form of more regulations to maintain Rate Case Expense. Rate Case Expense is amortized over a period of time. The deferred amount is not included in Rate Base and, therefore, is un-earning and reducing Aqua's ability to achieve its allowed return even though it is capital Aqua has already expended. (Aqua Ex. 6.0R, p. 33). The more Rate Case Expense Aqua incurs the greater the unfavorable gap between actual and allowed return becomes. (*Id.*) While divisional-specific factors will not, as rule, indicate that simultaneous filings should be made, to the extent it is appropriate to do so Staff's proposed rules simply are not needed. Indeed, Aqua filed these three pending cases together and utilized the total company portion of the Vermilion rate template without the need for the rules.

That there are not any limitations on Staff's proposals is also troubling. There are no exceptions on when Aqua would have to accelerate or postpone a filing to coincide with when

³⁸ The only other saving Staff alleged would flow from simultaneous filings is reduced outside legal cost from a single hearing and single set of briefs. However, outside legal costs would not be reduced because each division's issues would still need to be addressed—the single hearing and briefs would just be longer. And the savings from using the same test year can already be realized when cases are filed separately.

the divisional-specific factors for Kankakee or Vermilion indicate those divisions should be filed. Will Aqua have to accelerate or hold cases 6 months, a year, two years? Similarly, if Aqua files Kankakee and a small division in January 2006 using a 2007 future test year will it be prohibited from using the same test year if it files Vermilion and another small division in December 2006? The slippery slope implications are endless.

Accordingly, it is very clear that Staff's proposals would amount to poor public policy and should not be adopted. The Commission rejected Staff's challenge to the timing of Aqua's Candlewick case in 1999 and it should do so again here.

6. Amortization Period Of Rate Case Expense

Aqua proposes a three year amortization period for Oak Run and four year periods for the Woodhaven Divisions. These are reasonable projections of when Aqua is likely to file its next rate cases. (Aqua Ex. 6.0R, p. 39). In particular, Aqua anticipates it will file cases within these periods to capture the effects of inflation and capital projections that are routinely incurred and, thereby, avoid any degree of rate shock that would result from longer intervals. (*Id.*) Staff agrees that Rate Case Expense "should be recovered over the period of time that the subject tariffs are reasonably anticipated to be in effect." (Staff Ex. 6.0, p. 24).

In addition, for Oak Run, Aqua anticipates it will build the RO Plant in 2007. (Aqua Ex. 5.0A2, pp. 1-5). It is asking consumers to vote on whether to install the Plant; but, there is a reasonable likelihood they will vote in favor of doing so. (*Id.*, pp. 3-5). The RO Plant would produce substantial water quality benefits by bringing it into compliance with IEPA secondary and health industry standards for Fluoride, Total Dissolved Solids, Sodium and Chlorides. (*Id.*, pp. 3-4). Based on a cost benefit analysis, Mr. Bunosky concluded these benefits far outweigh the additional rate increase that would be necessary to pay for the Plant. (*Id.*, p. 3). Aqua

performed a customer survey when it conducted the pilot study for the Plant, and the majority of consumers reported in favor of the Plant's benefits at that time. (Tr., p. 131). The capital expenditure for the RO Plant will necessitate a rate filing in 2007. (Aqua Ex. 6.0R, p. 39).

7. State and Federal Income Tax Calculation Errors

An error occurs in Staff's Income Tax calculations that causes Staff's proposed revenue requirements to be misstated for all Divisions. In particular, the following well-established calculation is used to identify Taxable Income: pro forma proposed revenue requirement less operating expenses before income taxes less synchronized interest. (Aqua Ex. 8.0, p. 4). This amount is then multiplied by the State tax rate of 7.30% to produce the State Income Tax. (*Id.*, pp. 4-5). On Staff Ex. 6.0, Sch. 6.01 (OR), (WW) and (WS), however, each Division's Taxable Income multiplied by the State tax rate of 7.30% produces State Income Tax amounts different than those shown by Staff in column (i). (*Id.*) In turn, using either the correct or Staff erroneous State Income Tax as to the State deduction for Federal purposes does not result in the Federal Income Tax amounts Staff identifies in its Schedules 6.01. (*Id.*, p. 5).

That an error exists in Staff's Income Tax calculations is further apparent because, with regard to the two Woodhaven Divisions, Staff increases its Rate Base amount in Rebuttal versus its Direct case. (*Id.*, p. 6). This fact, plus Staff's higher allowed rate of return on Rate Base and slightly higher equity percentage of capitalization in its Rebuttal case should lead to increased State and Federal Income Tax amounts. (*Id.*) Yet, Staff's Rebuttal Income Tax amounts are lower than in its Direct case. (*Id.*) This is a clear indication of a calculation problem. (*Id.*)

Applying the correct Income Tax calculations to Staff's Rebuttal position shows the following impact on Staff's proposed Revenue Requirement between the correct calculations and those reflected in Staff's Schedules 6.01 for each Division:

	<u>Oak Run</u>	<u>Woodhaven Water</u>	<u>Woodhaven Sewer</u>
Staff Shown Revenue Requirement	\$486,994	\$1,100,525	\$980,181
Staff Actual Revenue Requirement	<u>\$484,816</u>	<u>\$1,108,683</u>	<u>\$986,440</u>
Required Rev. Adjustment	(\$2,178)	\$8,158	\$6,259

(*Id.*, pp. 5-6). To the extent the Commission adopts Staff’s position and/or works from Staff’s Schedules 6.01, it should incorporate these adjustments to the Revenue Requirements for each of the Divisions.

8. Staff Revenue Requirement Calculation Error

There are no Revenue Requirement adjustments *per se* associated with this issue. Rather, the manner in which Staff presents its recommended Revenue Requirement increases overstates the increases. Aqua believes the manner in which the Revenue Requirement increases are presented in the Commission’s Order should not overstate the increases it actually authorizes.

The overstatement occurs because Staff applied to Aqua’s pro forma *present* revenues the reductions Aqua proposed in its Rebuttal case to its *proposed* revenues. (Aqua Ex. 8.0, p. 2). Aqua’s pro forma present revenues are the revenues its present, or current, rates produce. Those revenues are not changing. Aqua’s present revenues are what they are. It is not appropriate to reduce them by Aqua’s adjustments to its proposed future revenues because doing so incorrectly shows Aqua’s present revenues as being less than they actually are.

Because Staff does so and, thereby, shows Aqua’s present revenues to be less than they actually are, it calculates the revenue change from an erroneously low starting point for present

revenues. As a result, the revenue increases, *i.e.*, difference between Aqua’s present and proposed revenues, that Staff shows in its Schedules 6.01 are overstated as follows:

	<u>Oak Run</u>	<u>Woodhaven Water</u>	<u>Woodhaven Sewer</u>
Staff Actual Revenue Change	\$157,104	\$302,255	\$229,596
Staff Shown Revenue Change	<u>\$179,716</u>	<u>\$321,058</u>	<u>\$284,730</u>
Revenue Overstatement	\$22,612	\$18,803	\$55,134
Staff Actual % Revenue Change	47.62%	37.86%	30.59%
Staff Shown % Revenue Change	<u>58.49%</u>	<u>41.19%</u>	<u>40.94%</u>
% Rev. Change Overstatement	10.87%	3.33%	10.35%

(*Id.*, pp. 2-3).

In Aqua’s prior cases, the Commission’s Orders have not overstated the revenue changes as Staff does in its Schedules 6.01. Attached as Appendix B hereto are copies of the Appendixes to the Commission’s Orders in Aqua’s three most recent rate cases, Docket Nos. 04-0442, 03-0403 and 00-0337/00-0338/00-0339, *consol.* In each and every one of them, the Commission calculates the revenue increases from Aqua’s pro forma *present* revenues without recognizing within those present revenues any reductions to Aqua’s *proposed* revenues.³⁹ The Commission should do the same in these cases.

D. Recommended Operating Revenues and Expenses

For the reasons discussed, the Commission should not adopt any of the proposed adjustments to Aqua’s operating expenses. Further, it should approve Interest Synchronizations based on Aqua’s proposed Rate Bases and Gross Revenue Conversion Factors based on Aqua’s

³⁹ In the 2000 and 2003 cases, the Commission did adjust Aqua’s pro forma present revenues by adjustments to *present* revenues in the cases but not by adjustments to *proposed* revenues.

proposed Bad Debt Expenses for each of the Divisions. Accordingly, Aqua's recommends the Commission approve Operating Incomes and Revenue Requirements as set forth in its Schedules 8.01 (OR), (WW) and (WS) attached hereto as Appendix A.

Should the Commission for some reason adopt Staff's proposals, which it should not, then the Commission should correct the Income Tax and Revenue Requirement increase calculation errors contained within Staff's Schedules and proposed amounts.

III. COST OF CAPITAL/RATE OF RETURN

For purposes of this case, the Company is accepting Staff's proposals on these issues.

IV. RATE DESIGN

Aqua has accepted Staff's rate design proposals set forth in Ms. Harden's Rebuttal Testimony as amended by Ms. Harden during the evidentiary hearings. (Tr., pp. 36-39).

CONCLUSION

WHEREFORE, for each of the reasons set forth herein, Aqua Illinois, Inc. respectfully requests that the Commission approve proposed rates based on its test year Surrebuttal Statements of Operating Income for each of the three Divisions, Aqua Schedule 8.1 (OR), (WW) and (WS), respectively, attached hereto as Appendix A, and grant any and all other appropriate relief.

Dated: August 24, 2005

Respectfully submitted,

Aqua Illinois, Inc.

By: _____
One of its attorneys

CERTIFICATE OF SERVICE

I, Sarah N. Galioto, hereby certify that I served a copy of the Initial Brief of Aqua Illinois, Inc upon the service list in consolidated Docket Nos. 05-0071 and 05-0072 by electronic mail on August 24, 2005.

Sarah N. Galioto