

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

ILLINOIS-AMERICAN WATER COMPANY)
Petition for re-approval of an Agreement with)
American Lake Water Company, an "Affiliated) Docket No. 05-0504
Interest" under Section 7-101 of the Illinois Public)
Utilities Act, as amended pursuant to Docket No.)
02-0690)

DRAFT ORDER

I. INTRODUCTION

On August 9, 2005, Illinois-American Water Company ("Illinois-American" or the "Company") submitted a Petition to the Illinois Commerce Commission ("Commission") for re-approval of a services agreement (the "Agreement") with American Lake Water Company ("ALWC"), an affiliated interest, under Section 7-101 of the Illinois Public Utilities Act, 220 ILCS 5/7-101, and pursuant to the Commission's Order in Docket 02-0690, in which Illinois-American was directed to re-file all of its affiliated interest agreements. On October 19, 2005, Illinois-American filed the Direct Testimony of Stephen J. Phillips, the Production Superintendent for Illinois-American. On November 16, 2005, Ms. Mary H. Everson, an Accountant in the Accounting Department of the Financial Analysis Division of the Commission, submitted Direct Testimony on behalf of Commission Staff. Illinois-American filed the Rebuttal Testimony of Mr. Phillips on December 2, 2005. An evidentiary hearing was held on December 13, 2005. At the hearing, Illinois-American was represented by counsel. Staff also appeared at the hearing. At the conclusion of the hearing on December 13, 2005, the record was marked "Heard and Taken."

II. POSITION OF THE COMPANY

Mr. Phillips testified that the Company is engaged in the business of furnishing potable water service and/or sanitary sewer service to the public in portions of Alexander, Champaign, Cook, Douglas, DuPage, Grundy, Jersey, Kane, Kendall, LaSalle, Livingston, Logan, Madison, McHenry, Monroe, Peoria, St. Clair, Tazewell, Whiteside, and Will Counties, Illinois, as it is duly authorized to do, and is a public utility within the meaning of Section 3-105 of the Act.

Mr. Phillips further stated that ALWC is a corporation organized and existing under the laws of the State of Illinois and that ALWC sells Lake Michigan water at wholesale to Illinois-American. The wholesale water agreements between Illinois-American and ALWC were re-approved in Commission Docket No. 04-0594. Mr. Phillips testified that ALWC was formerly known as Citizens Lake Water Company ("CLWC"), and that American Water Works Company, Inc. ("AW") acquired the stock of CLWC at the same time as Illinois-American acquired the water and wastewater assets

of Citizens Utilities Company of Illinois ("CUCI"), as approved in Docket No. 00-0476. AW then changed the name of CLWC to ALWC. Mr. Phillips noted that, since Illinois-American and ALWC are both subsidiaries of AW, they are affiliated interests pursuant to Section 7-101 of the Act, 220 ILCS 5/7-101.

Mr. Phillips described how CUCI and CLWC had, prior to their acquisition, negotiated the Agreement, whereby CUCI provided services to CLWC. He then stated that the Agreement was approved, as between CUCI and CLWC's predecessor in interest, Citizens Water Resources Company, in Docket Nos. 96-0200 and 96-0240 (consolidated). Subsequently, in Docket No. 00-0476, the Commission approved the assumption by Illinois-American of the Agreement as a part of Illinois-American's acquisition of CUCI's water and wastewater assets.

Mr. Phillips testified that in Docket No. 02-0690, Illinois-American was instructed to file for re-approval all of its affiliated agreements. Mr. Phillips noted that Illinois-American filed all of its other affiliated agreements for re-approval in 2004, but re-approval of the Agreement was not sought at that time because the Company believed it would be terminating the Agreement and that all employees performing services for ALWC would become employees of American Water Works Service Company, which has a service agreement with Illinois-American for which re-approval was granted in Docket No. 04-0595. Mr. Phillips stated that, upon further review of applicable collective bargaining requirements, it was determined that the contemplated transfer of employees or work was not feasible and the Agreement would continue in effect, thereby requiring re-approval pursuant to the Commission's Order in Docket No. 02-0690.

With respect to the Agreement, Mr. Phillips explained that, pursuant to the Agreement as approved in Docket Nos. 96-0200 and 96-0240 (consolidated), CUCI provided CLWC with certain services at cost, including general management, general operation support, maintenance, customer billing, engineering, data processing, general administrative, purchasing and other general services. Mr. Phillips further explained that, after Illinois-American assumed CUCI's position under the Agreement, as approved in Docket No. 00-0476, and CLWC was re-named ALWC, the Agreement was revised to change the parties from CUCI and CLWC to Illinois-American and ALWC, respectively, and re-executed as of August 8, 2005. Mr. Phillips stated that no other changes were made to the Agreement. Mr. Phillips concluded that he believed that the terms and provisions of the Agreement are fair and reasonable and in the best interest of Illinois-American and its customers, and otherwise in the public interest.

III. STAFF'S POSITION

Staff Witness Everson testified that the Agreement provides for Illinois-American employees to provide ALWC with "general management, general operation support, maintenance, customer billing, engineering, data processing, general administrative purchasing and such other services as may be required by or beneficial to ALWC." Ms. Everson further stated that, in response to data request MHE 1.01, the Company stated that the Agreement contains a complete list of the services that will be provided. She also explained that the Agreement contained provisions for determining cost of these services. Ms. Everson also confirmed that the Agreement allows Staff to review appropriate documentation and verify the amounts of the charges for services, citing the Company response to data requests which said that payroll records and the general ledger will be

available for Staff to review in determining that the correct charges are assessed to ALWC. Ms. Everson also noted that, according to the Company, the charges represent Illinois-American's fully distributed cost which will be charged to ALWC for work performed under the Agreement by Illinois-American employees, and, in addition, the fully distributed cost is the amount that would be charged by Illinois-American if it were to perform those same services for unaffiliated entities.

Ms. Everson proposed two changes to the Agreement. The first proposal was to modify the Agreement by removing the language on page 2, paragraph number 1, which stated that the listed services include "other such services as may be required by or beneficial to ALWC." Ms. Everson testified that, under Section 7-101(3) of the Act, 220 ILCS 7-103(3), the Commission is charged with the responsibility of approving only those agreements that are in the public interest. Ms. Everson stated that, absent a complete listing of the services to be offered under the Agreement, the Commission could unknowingly approve a service that is not in the public interest, and the Commission should not approve agreements that contain a general list of services that can be modified or changed without Commission approval. Ms. Everson further testified that conditions in the industry may change over time such that what was once thought to be in the public interest can turn out to be something the Commission would have rejected. She concluded that it is not possible for the Commission to find a services agreement in the public interest without knowing all of the intended uses of the agreements and the details of the services provided.

The second change Ms. Everson proposed was the addition of a new section (paragraph number 5) that includes the provision that, notwithstanding the previous paragraph numbers 3 and 4 that specify the cost elements that are to be used to determine charges to ALWC, Illinois-American shall perform the services at no less than the fully distributed cost of providing those services.

Ms. Everson then recommended that, if the Company agreed to her proposed language changes, she would recommend the Commission approve the Agreement.

IV. ILLINOIS-AMERICAN RESPONSE

Mr. Phillips responded, in his Rebuttal Testimony, that he had reviewed Ms. Everson's proposed changes, and, for the purpose of this case only, that the Company will accept those suggested changes. However, Mr. Phillips also stated that the changes should not be construed as setting a precedent for future proceedings. Mr. Phillips provided with his Rebuttal Testimony IAWC Exhibit 2.1, an Amended and Restated Agreement, dated November 28, 2005, between Illinois-American Water Company and American Lake Water Company ("Amended Agreement"), incorporating the changes recommended by Ms. Everson.

V. COMMISSION CONCLUSION

Having reviewed the record, the Commission finds that the Amended and Restated Agreement is in the public interest within the meaning of Section 7-101 of the Act, and should be approved. The Amended and Restated Agreement allows IAWC to provide certain services to its affiliate, ALWC. The arrangement appears to provide potential economies in the use of resources, while at the same time ensuring fairness to

ratepayers by setting forth appropriate cost allocation methodologies for the transactions covered by it.

VI. FINDINGS AND ORDERING PARAGRAPHS

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

- (1) Illinois-American Water Company ("Illinois-American") provides water and sewer public utility services to the public in certain areas of the State of Illinois and is a public utility within the meaning of the Act. 220 ILCS 5/3-105;
- (2) the Commission has jurisdiction over Illinois-American and of the subject matter of this proceeding;
- (3) the conclusions and statements of fact set forth in the prefatory portion of this Order are supported by the evidence and the record, and are hereby adopted as findings of fact;
- (4) the Amended and Restated Agreement between Illinois-American Water Company and American Lake Water Company is reasonable and should be approved.

IT IS THEREFORE ORDERED that that consent to and approval of the Amended and Restated Agreement between Illinois-American Water Company and American Lake Water Company is hereby granted;

IT IS FURTHER ORDERED that any motions or objections or petitions in this proceeding that have not specifically been ruled on shall be disposed of in a manner consistent with the findings and conclusions herein;

IT IS FURTHER ORDERED that, subject to the provisions of Section 10-113 of the Illinois Public Utilities Act and 83 Illinois Administrative Code, Section 200.800, this Order is final; it is not subject to the Administrative Review Law.

By Order of the Commission this ____ day of _____, 2006.