

DIRECT TESTIMONY

of

BONITA A. PEARCE

Accountant

Accounting Department

Financial Analysis Division

Illinois Commerce Commission

Illinois-American Water Company Petition for Issuance of Certificate of Public
Convenience and Necessity, and for Approval
of Rates and Accounting Entries to Record the Acquisition
of the Village of Pesotum Water System

Docket No. 06-0564

January 4, 2007

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Attachment B – IAWC Response to WD 1.18, Schedule 3.5 of the Asset Purchase Agreement, Spare Parts on Hand

1 **WITNESS IDENTIFICATION**

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

3 A. My name is Bonita A. Pearce. My business address is 527 East Capitol
4 Avenue, Springfield, Illinois 62701.

5

6 **Q. By whom are you employed and in what capacity?**

7 A. I am an Accountant in the Accounting Department of the Financial
8 Analysis Division of the Illinois Commerce Commission ("ICC" or
9 "Commission").

10

11 **Q. Please describe your background and professional affiliations.**

12 A. I am a licensed Certified Public Accountant with a Bachelor of Science in
13 Accountancy from Illinois State University. Prior to joining the
14 Commission Staff ("Staff") in March 2001, I was engaged in the practice of
15 public accounting for sixteen years. I returned to the practice of public
16 accounting for a brief period in 2005, but returned to the Commission in
17 2006. I am a member of the American Institute of Certified Public
18 Accountants.

19

20 **Q. Have you previously testified before any regulatory bodies?**

21 A. Yes, I have testified on several occasions before the Commission.

22

23 **PURPOSE OF TESTIMONY**

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

25 A. The purpose of my testimony is:

- 26 1) to present Staff's recommendation regarding Illinois-American
27 Water Company's ("Company" or "Illinois-American") request for
28 the approval of accounting entries, as detailed on Illinois-
29 American's Exhibit MJH 1.7 (Revised), attached to the
30 Supplemental Direct Testimony of Illinois-American witness Michael
31 J. Hoffman; and
32 2) to present Staff's recommendation regarding Illinois-American's
33 filing of final accounting entries with the ICC.

34

35 **SCHEDULES AND ATTACHMENTS**

36 **Q. Are you sponsoring any schedules or attachments with your**
37 **testimony?**

38 A. Yes, I am sponsoring the following schedules and attachments as part of
39 this testimony:

40 Schedule 2.1 – Staff Proposed Accounting Entries,

41 Schedule 2.2 – Estimated Total Contributions in Aid of Construction

42 Received,

43 Attachment A – Company's Response to Data Request WD 1.20

44 (Revised), and

45 Attachment B – Company’s Response to Data Request WD 1.18,
46 Schedule 3.5 of the Asset Purchase Agreement, Spare
47 Parts on Hand
48

49 **STAFF PROPOSED ACCOUNTING ENTRIES**

50 **Q. Please describe ICC Staff Exhibit 2.0, Schedule 2.1, Staff Proposed**
51 **Accounting Entries.**

52 A. Schedule 2.1 reflects my proposed accounting entries for this transaction.
53 There are three differences between my proposed accounting entries and
54 the Company’s proposed accounting entries:

- 55 1) The recognition of tap-on fees paid by customers in the Village of
56 Pesotum (“Pesotum” or the “Village”);
- 57 2) The recognition of \$4,762 of spare parts that were received,
58 according to Schedule 3.5 of the Asset Purchase Agreement –
59 Spare Parts on Hand (Attachment B hereto); and
- 60 3) The reflection of the one-time amortization of the acquisition
61 adjustment proposed by the Company to record amortization
62 expense in Account 426, Miscellaneous Non-utility Expenses,
63 “below-the-line”.

64

65 **Recognition of Tap-on Fees**

66 **Q. Please explain why the journal entries to record the transaction**
67 **should recognize tap-on fees paid by customers in Pesotum.**

68 A. The Uniform System of Accounts for Water Utilities Operating in Illinois
69 (“USOA”) for Account 271, Contributions in Aid of Construction (“CIAC”),
70 states that this account shall include any amount of money received by a
71 utility from any person, any portion of which is provided at no cost to the
72 utility, which represents an addition to the capital of the utility, and which is
73 utilized to offset the acquisition, improvement, or construction costs of the
74 utility’s property, facilities, or equipment used to provide utility services to
75 the public.

76
77 According to the Company’s response to Staff Data Request WD 1.20
78 (Revised) (Attachment A hereto) the Village of Pesotum does charge
79 customers a tap-on fee when they are connected to the water system.
80 The known tap-on fees that were recorded by the Village amount to
81 \$8,076.73, according to the response, and the Village acknowledges that
82 tap-on fees may have been collected for the remaining 213 homes within
83 the Village. Based on this response, I estimated the amount of additional
84 tap-on fees that would have been collected from the 213 additional
85 customers, assuming each customer paid \$295, the lowest known amount
86 of tap-on fees that was charged by the Village. That amount, calculated
87 on ICC Staff Exhibit 2.0, Schedule 2.2, along with the known amount of
88 tap-on fees collected from customers, \$8077, should be recognized as
89 CIAC in Account 271, according to the USOA.

90

91 A corresponding entry is also necessary to reflect the accumulated
92 amortization of the CIAC related to these tap-on fees. Using the ratio of
93 accumulated depreciation to the total water plant purchased (excluding
94 land and land rights), I estimated the amount of accumulated amortization
95 related to CIAC that should be recorded in Account 272, Accumulated
96 Amortization of Contributions in Aid of Construction (ICC Staff Exhibit 2.0,
97 Schedule 2.2).

98
99 Accordingly, my proposed journal entries to record the acquisition of the
100 Village of Pesotum's water system as indicated on ICC Staff Exhibit 2.0,
101 Schedule 2.1 reflects the CIAC and corresponding accumulated
102 amortization of the CIAC, and the impact on the acquisition adjustment.

103

104 **Recognition of Spare Parts**

105 **Q. Please explain why the journal entries to record the transaction**
106 **should recognize the spare parts that were received, according to**
107 **Schedule 3.5 of the Asset Purchase Agreement – Spare Parts on**
108 **Hand (Attachment B).**

109 A. According to the Asset Purchase Agreement between the Village and
110 Illinois-American (Exhibit A to the Application for Certificate of
111 Convenience and Necessity), Schedule 3.5 (Attachment B hereto),
112 describes the tangible property that will be conveyed to Illinois-American in
113 return for the purchase price. Schedule 3.5 lists \$4,762 in spare parts that

114 will be transferred to Illinois-American that the Company has not reflected
115 in its proposed journal entries (Exhibit MJH 1.7 (Revised)) attached to the
116 Supplemental Direct Testimony of Company witness Michael J. Hoffman
117 (IAWC Exhibit No. MJH-1.0S). In addition, the calculation of the
118 acquisition adjustment should be impacted by the cost of the spare parts
119 received by Illinois-American. Accordingly, my proposed journal entries to
120 record the acquisition of the Village of Pesotum's water system as
121 indicated on ICC Staff Exhibit 2.0, Schedule 2.1 reflects the cost of the
122 spare parts received by Illinois-American and the impact on the acquisition
123 adjustment.

124

125 **Reflection of One-time Amortization of Acquisition Adjustment**

126 **Q. Please explain why the journal entries to record the transaction**
127 **should reflect the one-time amortization of the acquisition**
128 **adjustment proposed by the Company to record amortization**
129 **expense in account 426, Miscellaneous Non-utility Expenses,**
130 **“below-the-line”.**

131 A. The Direct Testimony of Illinois-American witness Michael J. Hoffman
132 (IAWC Exhibit No. MJH-1.0) presents the Company's proposed journal
133 entries but does not reflect the proposed ratemaking treatment of the
134 acquisition adjustment. However, at page 9, lines 199 – 203 of his
135 testimony, he indicates that the Company proposes to dispose of the
136 acquisition adjustment through a one-time charge to Account 426,

137 Miscellaneous Non-utility Expenses, at the time final journal entries are
138 recorded.

139

140 My proposed journal entries reflect the disposition of the balance of
141 Account 114 to record the acquisition of the Pesotum water system. In
142 that way, the Commission may address the disposition of the balance of
143 Account 114, either through approval of the proposed entries reflected on
144 Schedule 2.1 attached hereto, or by modification of the proposed journal
145 entries in the final Order for this proceeding. Section C of the USOA's
146 instructions for Account 114, Utility Plant Acquisition Adjustments, states
147 that the amounts recorded in this account with respect to each property
148 acquisition shall be amortized, or otherwise disposed of, as the
149 Commission may approve or direct.

150

151 **Q. Do you object to this proposal?**

152 A. No, I do not object to the one-time charge to Account 426 because there
153 will be no increased cost to ratepayers due to the treatment of the
154 acquisition adjustment. The amount of the debit acquisition adjustment is
155 minimal. The Company's proposed acquisition adjustment to be recorded
156 in Account 114, Utility Plant Acquisition Adjustment, approximates \$9,000.
157 My proposed amount is more than \$9,000 due to the recognition of CIAC
158 from tap-on fees, partially offset by the recognition of the spare parts
159 inventory on hand. In addition, Account 426 is a "below-the-line" account

160 and would not impact the revenue requirement in a rate proceeding.
161 Thus, the treatment proposed by Illinois-American will not increase costs
162 to ratepayers.

163

164 **RECOMMENDATIONS REGARDING ACCOUNTING ENTRIES**

165 **Q. Do you have any recommendations regarding the accounting entries**
166 **to be used by the Company in recording the acquisition of the**
167 **Pesotum water system?**

168 A. Yes, in accordance with the instructions for Account 104 of the USOA,
169 Utility Plant Purchased or Sold, I recommend that the Company file with
170 the Chief Clerk of the Commission and provide a copy to the Manager of
171 Accounting copies of the actual accounting entries used to record the
172 purchase of the Pesotum water system within six months of finalizing the
173 acquisition.

174

175 **SUMMARY**

176 **Q. Please summarize your recommendations.**

177 A. I recommend the following:

178 1. The Commission should approve my proposed accounting entries
179 to record the estimated purchase costs of the water system from
180 the Village of Pesotum as reflected on my Schedule 2.1; and

181 2. The Commission should order the Company to provide actual
182 accounting entries to record the purchase of the water system
183 within six months of finalizing the acquisition.

184

185 **CONCLUSION**

186 **Q. Does this conclude your prepared direct testimony?**

187 A. Yes, it does.

Illinois-American Water Company
 Village of Pesotum
 Proposed Accounting Entries

Line No.	Account Number	Description	Debit	Credit
	(a)	(b)	(c)	(d)
1		Journal Entry #2 To clear the balances recorded in Utility Plant Purchased and transfer to the appropriate accounts.		
2	(a) 104	Utility Plant Purchased or Sold		(\$161,549)
3	(a) 114	Utility Plant Acquisition Adjustment		
4	(a) 303	Land & Land Rights - SS	\$4,877	
5	(a) 303	Land & Land Rights - Water Tower	2,027	
6	(a) 304	Structures & Improvements - SS	17,465	
7	(a) 304	Structures & Improvements - SS	2,437	
8	(a) 331	Transmission & Distribution Mains	195,060	
9	(a) 333	Services	42,028	
10	(a) 334	Meters	8,768	
11	(a) 334	Meter Installations	9,709	
12	(a) 335	Hydrants	29,497	
13	(a) 108	Accum. Depr. - Structures & Improvements - SS		(19,426)
14	(a) 108	Accum. Depr. - Structures & Improvements - Water Tower		(294)
15	(a) 108	Accum. Depr. - Transmission & Distribution Mains		(72,394)
16	(a) 108	Accum. Depr. - Services		(32,202)
17	(a) 108	Accum. Depr. - Meters		(10,048)
18	(a) 108	Accum. Depr. - Meter Installations		(4,887)
19	(a) 108	Accum. Depr. - Hydrants		(19,998)
20	(c) 271	Contributions in Aid of Construction - Tap-on fees		(21,922)
21	(c) 272	Accumulated Amortization of CIAC - Tap-on fees	11,399	
22	(e) 620	Materials and Supplies	4,762	
23	(d) 114	Utility Plant Acquisition Adjustment	14,691	
		TOTAL	<u>\$342,720</u>	<u>(\$342,720)</u>
24		Journal Entry #3 Annual entry to record the one-time amortization of acquisition adjustment.		
25	(b) 115	Accum. Amort. Of Utility Plant Acquisition Adjustment		\$14,691
26	(b) 426	Miscellaneous Non-utility Expenses	<u>\$14,691</u>	<u>\$14,691</u>

- Source:
- (a) Illinois-American Exhibit MJH 1.7 (Revised)
 - (b) To eliminate the balance of Account 114, shown in Journal Entry # 2.
 - (c) ICC Staff Exhibit 2.0, Schedule 2.2.
 - (d) Calculated by difference between purchase price, \$161,549 and original cost of plant, net of depreciation and CIAC (See Note1).
 - (e) Response to Staff Data Request WD 1.18, Schedule 3.5 of the Asset Purchase Agreement, Spare Parts on Hand.

Note 1: Calculation of Account 114, Acquisition Adjustment:

	Debit/(Credit)
Purchase price	(\$161,549)
Debit:	
Utility plant in service	311,868
Materials and supplies	4,762
Accumulated Amortization of CIAC	11,399
Credit:	
Accumulated depreciation	(159,249)
CIAC	(21,922)
Balance of Account 114, Acquisition Adjustment	<u>\$14,691</u>

**Illinois-American Water Company
 Village of Pesotum
 Estimated Total Contributions In Aid of Construction Received**

<u>Line No.</u> (a)	<u>Description</u> (b)	<u>Amount</u> (c)	<u>Source</u> (d)
1	ICC Staff Estimated Additional Tap-On Fees	\$21,921.73	ICC Staff Exhibit 2.0, Schedule 2.2, Page 2.
2	ICC Staff Estimated Accumulated Amortization on CIAC	(11,399.30)	Line 1, col. (c) times 52% (see Note 1 below).
3	ICC Staff Estimated Total CIAC, net of Accumulated Amortization	<u>\$10,522.43</u>	Line 1, col. (c) minus line 3, col. (c).

Note 1 Estimated Accumulated Amortization on CIAC estimated as 52% of CIAC balance is based on relative accumulated depreciation to underlying plant, as calculated below:

4	Account 304, Structures & Improvements	\$19,902	Exhibit MJH 1.7 (Revised)
5	Account 331, Transmission & Distribution Mains	195,060	Exhibit MJH 1.7 (Revised)
6	Account 333, Services	42,028	Exhibit MJH 1.7 (Revised)
7	Account 334, Meters & Meter Installations	18,477	Exhibit MJH 1.7 (Revised)
8	Account 335, Hydrants	<u>29,497</u>	Exhibit MJH 1.7 (Revised)
9	Water Plant Purchased, excluding Land and Land Rights	304,964	Subtotal
10	Account 108, Reserve for Depreciation	(\$159,249)	Exhibit MJH 1.7 (Revised)
11	Estimated Accumulated Amortization on CIAC	-52.22%	Line 10, col. (c) divided by line 9, col. (c)

**Illinois-American Water Company
 Village of Pesotum
 Estimated Total Tap-On Fees**

<u>Line No.</u> (a)	<u>Description</u> (b)	(c)	<u>Amount</u> (d)	<u>Source</u> (e)
1	Homes in Pesotum without records of tap-on fees	213		Response to WD 1.20 (Revised), b.(ii.) - (iii).
2	Estimated tap-on fee (minimum)	\$65		Response to WD 1.20 (Revised), b.(i.) lowest fee
3	ICC Staff Estimated Additional Tap-On Fees	<hr/>	\$13,845.00	Col. (c) line 1 times Col. (c) line 2.
4	Recorded and Discoverable Tap-On Fees		\$8,076.73	Response to WD 1.20 (Revised), b.(ii.) - (iii).
5	ICC Staff Estimated Total Tap-On Fees		<u><u>\$21,921.73</u></u>	Col. (d) line 3 plus Col. (d) line 4.

ILLINOIS-AMERICAN WATER COMPANY

RESPONSE TO ILLINOIS COMMERCE COMMISSION

REQUEST NUMBER WD 1.20

Person Responsible: Barry L. Suits
Title: Network Operations Manager
Phone No.: 217-373-3255
Date Received: September 12, 2006
Docket No.: 06-0564

REVISED
WD 1.20

- a. Did the Village of Pesotum charge the customers a tap-on-fee when connecting to the water system for water service?
- b. If yes, please provide the following information:
 - (i) the dollar amount of the tap-on-fee the Village of Pesotum charged its customers when connecting to the water system for water service,
 - (ii) the number of customers charged this tap-on-fee, and
 - (iii) the total dollar amount of tap-on-fees collected from the customers over the life of the water system.

Response

- a. The Village of Pesotum does charge customers a tap-on-fee when connecting to the system.
- b.
 - (i.) The Village of Pesotum records are incomplete due to the age of the water system. Records indicate the following fees were charged, in these approximate time periods:

1956-June 1978	\$65.00
July 1978-May 1986	\$150.00
1987-Nov. 2002	\$175.00
May 2006-Present	Actual cost

Village of Pesotum Ordinances are provided as to the tap-on-fees charged during the 1956-1978, 1987-2002, and current time-periods. The decision to increase the tap-on-fee charged from July 1978 through May of 1986, was made by a decision of the Board of Trustees.

(ii)-(iii)

<u>Years</u>	<u>#of Customers</u>	<u>Tap-on-Fees</u>
1956-1977		Unknown
1977-1978	2	\$295.00
1978-1979	6	\$825.00
1979-1980	2	\$300.00
1980-1981	0	\$0.00
1981-1982	0	\$0.00
1982-1983	0	\$0.00
1983-1984	2	\$400.00
1984-1985	1	\$200.00
1985-1986	0	\$0.00
1986-1987	0	\$0.00
1987-1988	3	\$500.00
1988-1989	5	\$1,181.73
1989-1990	0	\$0.00
1990-1991	3	\$525.00
1991-1992	1	\$175.00
1992-Present	<u>21</u>	<u>\$3,675.00</u>
	46	\$8,076.73

*These numbers reflect the tap-on-fees that were recorded, and discoverable, by the Village of Pesotum. Upon information and belief, additional tap-on-fees may have been collected for the remaining 213 homes within the Village of Pesotum.

Please see additional attached documents.

ILLINOIS-AMERICAN WATER COMPANY

RESPONSE TO ILLINOIS COMMERCE COMMISSION

REQUEST NUMBER WD 1.18

Person Responsible: Barry L. Suits
Title: Network Operations Manager
Phone No.: 217-373-3255
Date Received: September 12, 2006
Docket No.: 06-0564

WD 1.18

Please provide a copy of Schedules 3.4, 3.5, 2.2, 3.8, 2.1(f), 2.2(f), 2.5, 3.6, 3.7(a), 3.9, and 3.14 of the Asset Purchase Agreement (Exhibit A of the Application for a Certificate of Public Convenience and Necessity).

Response

Please see attachment. In addition, IAWC notes the following:
Section 3.4 and 3.9 are amended pursuant to the "ADDENDUM" to the Asset Purchase Agreement attached. Pursuant to the same addendum, Section 3.14 is no longer a schedule to the Asset Purchase Agreement.

