

ILLINOIS-AMERICAN WATER COMPANY

IAWC EXHIBIT 1.0

DIRECT TESTIMONY

OF

FREDERICK L. RUCKMAN

(Docket 06-0782)

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1
2 **DIRECT TESTIMONY**

3 **OF**

4 **FREDERICK L. RUCKMAN**

5 **I. WITNESS IDENTIFICATION AND BACKGROUND**

6 **Q1. Please state your name and business address.**

7 A. My name is Frederick L. Ruckman. My business address is Illinois-American Water
8 Company, 100 N. Water Works Drive, P.O. Box 24040, Belleville, Illinois 62223-9040.

9 **Q2. By whom are you employed?**

10 A. Illinois-American Water Company ("IAWC" or the "Company").

11 **Q3. What is your position with IAWC?**

12 A. General Manager-Network.

13 **Q4. Please discuss your educational and business background.**

14 A. I earned a Bachelor of Science degree, with a major in accounting, from Eastern Illinois
15 University in 1971. I was employed by Northern Illinois Water Corporation ("NIWC")
16 beginning April 1972 as a staff accountant. In April 1980, I was promoted to
17 Comptroller and elected Secretary. In 1994, I was elected to NIWC's Board of Directors
18 and, in 1996, I was promoted to Vice President. On January 1, 2000, I became Vice
19 President and Treasurer of IAWC. I assumed my current position on July 1, 2004.

20 **II. PURPOSE OF TESTIMONY**

21 **Q5. What is the purpose of your testimony?**

22 A. My testimony explains certain aspects of the Petition filed in this case and the reasons
23 why the Company believes it is reasonable and should be approved. In particular, I offer
24 testimony in support of the following: (1) an order issuing a Certificate of Public

25 Convenience and Necessity (“Certificate”) for IAWC to construct, operate and maintain a
26 water supply and distribution system and a wastewater treatment and collection system in
27 an area of McHenry County, Illinois, which I describe later in my testimony as the
28 “Expanded Area;” (2) approval of certain provisions of an Amended and Restated Asset
29 Purchase Agreement between IAWC and Terra Cotta Realty Co. (“Terra Cotta”) dated
30 November 4, 2005 (“Agreement”); (3) a variance from IAWC’s Metro Division’s Rule
31 16, which can be found in the Company’s tariffs as Ill. C.C. No. 5, Sheet Nos. 53-57
32 (“Rule 16”), with regard to the amount of the required construction deposit for additional
33 wastewater treatment plant capacity; and (4) approval of certain provisions of an
34 agreement (“Westminster Agreement”) between IAWC and WS Land Partners - Prairie
35 Grove II, LLC (“Westminster”), an entity which serves as the agent of the entities which
36 have purchased portions of the land located in the Expanded Area (the “Westminster
37 Land”). In this proceeding, IAWC also seeks approval of accounting entries to record the
38 net original cost of facilities that will be used to provide service in the Expanded Area,
39 approval of applicable depreciation rates and approval to apply the Metro Division rates
40 for water and wastewater service in the Expanded Area. Those issues will be addressed
41 by IAWC witness Michael Hoffman in his direct testimony.

42 **III. BACKGROUND**

43 **Q6. Please provide background information that will help the Commission understand**
44 **what the Company is requesting in this proceeding.**

45 A. The Company’s Petition expands on earlier agreements between IAWC or its
46 predecessor, Citizens Utilities Company of Illinois, Inc. (“Citizens”), and various entities.
47 In 1999, Terra Cotta requested that Citizens provide water and wastewater service to an

48 area near the Village of Prairie Grove, McHenry County, Illinois, known as the “Original
49 Terra Cotta Area.” Terra Cotta and Citizens entered into an Asset Purchase Agreement,
50 dated February 16, 2000 (the “Original Agreement”) whereby Citizens agreed to
51 purchase from Terra Cotta certain water backbone facilities (“TC Water Backbone
52 Plant”), water distribution mains (“TC Original Area Water Mains”), sewer backbone
53 facilities (“TC Sewer Backbone Plant”), and sewer collection mains (“TC Original Area
54 Sewer Mains”). The TC Sewer Backbone Plant included a wastewater treatment plant
55 (the “Original Wastewater Plant”) with a treatment capacity of 100,000 gallons per day. I
56 will refer to the TC Water Backbone Plant and TC Original Area Water Mains as
57 “Existing TC Water Facilities” and the TC Sewer Backbone Plant and TC Original Area
58 Sewer Mains as “Existing TC Sewer Facilities.” Certain water and wastewater mains
59 now serving the Original Terra Cotta Area were constructed by other developers pursuant
60 under Citizens’ Rules, Regulations and Conditions of Service and were not acquired by
61 Citizens under the Original Agreement.

62 **Q7. What were the general terms of the Original Agreement?**

63 A. The major provisions of the Original Agreement relate to Existing TC Water Facilities,
64 Existing TC Sewer Plant and Future Water and Sewer Facilities. These provisions are
65 summarized below:

66 1. Existing TC Water Facilities. The Original Agreement required that Terra Cotta
67 transfer ownership of the TC Water Backbone Plant, subject to required refunds
68 on a per population equivalent, or “P.E.” basis, as customers attach. The Original
69 Agreement further required Terra Cotta’s consent for use of the TC Water
70 Backbone Plant outside the Original Terra Cotta Area. For the TC Original Area

71 Water Mains, the Original Agreement called for refunds of the cost of service
72 connections constructed by Terra Cotta, between the main and the curb stop, and
73 one and one half times estimated annual revenue from customers that attach to
74 water mains constructed by Terra Cotta over a ten year period.

75 2. Existing TC Sewer Plant. The Original Agreement provided for transfer to
76 Citizens of the Original Wastewater Plant, which had been constructed by Terra
77 Cotta in 1973 and used by Terra Cotta since that time, with an upgrade in 1996-
78 97, with no refund of costs related to the Original Wastewater Plant as customer
79 attach. The Original Agreement provided for transfer to Citizens of the TC
80 Original Area Sewer Mains, with no requirement for a refund of the associated
81 cost.

82 3. Future Water and Sewer Facilities: The Original Agreement contemplated that
83 Citizens would finance construction of future water backbone facilities in the
84 Original Terra Cotta Area. For Future Sewer Backbone Facilities, under the
85 Original Agreement, Terra Cotta was to pay the full cost of constructing future
86 sewer backbone facilities with no refund obligation for Citizens. The Original
87 Agreement did not address the construction of future water distribution or sewer
88 collection mains.

89 **Q8. Was the Original Agreement submitted to the Commission for approval?**

90 A. Yes. Citizens filed the Original Agreement for approval by the Commission, to the
91 extent required, in Commission Docket 00-0194. In the Docket 00-0194 Order, the
92 Commission did not approve the Original Agreement, but did grant a Certificate to serve

93 the Original Terra Cotta Area, or “Original Certificate,” and indicated that certain
94 provisions of the Original Agreement which relate to the water facilities were reasonable.

95 **Q9. Why did the Commission not approve certain provisions of the Original**
96 **Agreement?**

97 A. In the Docket 00-0194 Order, the Commission determined that the Original Agreement
98 was unreasonable in that it did not provide for a refund to Terra Cotta of the cost
99 advanced for the TC Sewer Backbone Plant. The Commission concluded that, for the
100 purposes of Docket 00-0194, the principles of 83 Illinois Administrative Code Section
101 600.370(a), which applies by its terms to water backbone plant, would also apply in
102 evaluating proposed levels of developer contribution for the TC Sewer Backbone Plant.
103 At page 7, Finding Number 6 of its Order, the Commission found specifically that
104 Citizens should refund to Terra Cotta the cost advanced for the TC Sewer Backbone
105 Plant. The Commission’s decision was affirmed on appeal in the case of *Illinois-*
106 *American Water Co. v. Commerce Comm.*, 331 Ill. App. 3d 1030 (3rd Dist. 2002), which
107 I will refer to simply as the “Appellate Decision.”

108 **Q10. What happened following the Docket 00-0194 Order?**

109 A. Per the Original Agreement and a subsequent agreement between Terra Cotta and
110 Citizens, dated June 13, 2001 (“June 13 Agreement”), Terra Cotta transferred to Citizens
111 title to the Existing TC Water Facilities, Existing TC Sewer Facilities and related
112 property rights. In the June 13 Agreement, Terra Cotta and Citizens agreed not to rescind
113 or restructure the Original Agreement, except as required to comply with the Docket 00-
114 0194 Order. On January 15, 2002, pursuant to an order in Docket 00-0476, the Company
115 assumed Citizens’ rights and obligations under the Original Certificate and acquired

116 certain water and wastewater assets of Citizens, including, among other things, Citizens’
117 rights and obligations under the Original Agreement and the June 13 Agreement. The
118 areas served by Citizens, with certain other areas, now comprise the Metro Division.

119 **Q11. Please describe the area encompassed by the Original Certificate granted in the**
120 **Docket 00-0194 Order.**

121 A. The Original Certificate encompasses the Original Terra Cotta Area, which is comprised
122 of approximately 1440 acres. To date, a total of approximately 241 residential units have
123 been constructed in this area, in the Cobblestone Woods and Oak Grove subdivisions.
124 These residences receive water and wastewater service from IAWC through the TC
125 Water Facilities and Existing TC Sewer Facilities described previously.

126 **Q12. Has Terra Cotta acquired additional land or sold any land that is included in the**
127 **Original Certificate?**

128 A. Yes. Terra Cotta has acquired, or is under contract to acquire, an additional 110 acres of
129 land. The Original Terra Cotta Area and newly-acquired areas comprise approximately
130 1,550 acres known as the “TC Land.” Terra Cotta sold 1,077 acres of the TC Land,
131 known as “TC Acres,” to Prairie Grove 1078 SPE. Furthermore, an entity known as Tall
132 Grass Prairie Grove, LLC acquired from another entity approximately 322 acres of land,
133 known as the “WS Acres.” WS Acres is part of an area of approximately 368 acres
134 known as “Tall Grass.” TC Acres and WS Acres are known collectively as the
135 “Westminster Land.” The “Expanded Area” for which IAWC seeks a Certificate in this
136 proceeding encompasses both the TC Land and Tall Grass, and therefore includes both
137 the Westminster Land and other land that Terra Cotta will retain and/or sell to other
138 developers.

139 **Q13. Please describe the agreements for which the Company seeks Commission approval**
140 **in this proceeding.**

141 A. In this proceeding, IAWC seeks approval of the Agreement and the Westminster
142 Agreement, to the extent discussed in my testimony. The purpose of the Agreement is
143 threefold. First, to establish arrangements for the provision of public water and sanitary
144 sewer service in the Expanded Area, and for the construction of additional and/or
145 expanded water and wastewater facilities needed to serve expected customer growth in
146 the Expanded Area. Second, to comply with the terms of the June 13 Agreement. And
147 third, to address matters covered by the Original Agreement in a manner consistent with
148 the Docket 00-0194 Order and the applicable rules, regulations and policies of the
149 Commission. A copy of the Agreement is provided in IAWC Exhibit FLR 1.1. IAWC
150 also seeks approval of provisions of the Westminster Agreement that relate to
151 construction and financing of water backbone plant for Tall Grass and construction and
152 financing of water and wastewater collection mains for the Westminster Land. IAWC
153 and Westminster are in the processing of finalizing the Westminster Agreement. IAWC
154 will provide an executed copy of the Westminster Agreement in supplemental testimony
155 in this proceeding and/or during the course of discovery.

156 **IV. CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY**

157 **Q14. Please describe the Expanded Area for which the Company is seeking a Certificate.**

158 A. As I discussed above, the Original Certificate presently authorizes IAWC to serve the
159 Original Terra Cotta Area. IAWC seeks to expand the Original Certificate to encompass,
160 in addition to the Original Terra Cotta Area, the approximately 110 additional acres that
161 Terra Cotta has now acquired, or is under contract to acquire, and Tall Grass. The

162 Expanded Area is shown in IAWC Exhibit FLR 1.2, and legally described in IAWC
163 Exhibit FLR 1.3. IAWC Exhibits FLR 1.2 and 1.3 designate separately the Original
164 Terra Cotta Area, the additional 110 acres acquired by Terra Cotta and Tall Grass.

165 **Q15. Has the Company been requested to provide service in the Expanded Area?**

166 A. Yes. Westminster and Terra Cotta have requested that IAWC extend service to their
167 developments. At present, except for service provided by IAWC in the Original Terra
168 Cotta Area, there is no public water or sewer service provided in the Expanded Area.

169 **Q16. Are there other entities besides IAWC that could provide the necessary water and
170 sewer service?**

171 A. No. Other than service provided currently by IAWC in the Original Terra Cotta Area,
172 there is no municipal corporation or other entity willing or able to provide water or sewer
173 service to the Expanded Area. IAWC has served a copy of the Petition on each
174 municipality located partly or wholly within the Expanded Area, or with a corporate
175 boundary that is within one and one half miles of the Expanded Area. IAWC's notice of
176 service of the Petition is on file with the Commission.

177 **Q17. Will occupants of the Expanded Area require water and sewer service?**

178 A. Yes. In the Expanded Area, which includes all of the TC Land and Tall Grass, the
179 Company anticipates that approximately 2,449 additional residential units will be
180 constructed, approximately 400 of which are to be constructed by Terra Cotta, and
181 approximately 2,049 of which are to be constructed by Westminster, including 1,405
182 units in the TC Acres and 644 units in the WS Acres. These occupants will require
183 public water and wastewater service, and Terra Cotta and Westminster have contracted
184 with IAWC to provide that service pursuant to the Agreement and Westminster

185 Agreement. Including the existing units in Oak Grove and Cobblestone, the Expanded
186 Area is presently expected to include a total of approximately 2,680 residential units.
187 IAWC also anticipates that governmental (schools), retail and other commercial entities
188 will be developed within the Expanded Area, as residential development occurs.
189 However, the Company presently has no basis to project a precise level of future
190 governmental, retail and commercial development.

191 **Q18. Please discuss the Company's ability to provide the necessary water and sewer**
192 **service.**

193 A. IAWC currently provides public water and/or wastewater service in portions of the State
194 of Illinois through twelve Districts: Alton, Cairo, Champaign, Chicago Metro, Interurban,
195 Lincoln, Peoria, Pekin, Pontiac, South Beloit, Sterling and Streator. The Chicago Metro
196 District serves incorporated and unincorporated areas in portions of Cook, DuPage, Will,
197 Kendall, Grundy, Kane and McHenry Counties. IAWC has the technical, financial and
198 managerial ability to construct, operate and maintain a public water supply and
199 distribution system, and a sewage treatment and collection system for the Expanded Area,
200 without adverse financial consequences for existing customers. The provision of public
201 water and sewer service in the Expanded Area will impose no financial burden on either
202 the Company or its existing customers. Also, existing customers would experience
203 benefits from growth of the IAWC system as common costs are spread over a larger
204 customer base. The Company has taken steps to assure that any construction processes
205 and supervision will be adequate and efficient, and that the cost it will incur for
206 constructed facilities is the least cost means of providing the required water/wastewater
207 service.

208 **V. WATER AND WASTEWATER FACILITIES**

209 **Q19. Are water and wastewater facilities available to serve the Expanded Area?**

210 A. Yes. Pursuant to the Original Agreement, the June 13 Agreement and other documents,
211 Terra Cotta transferred to Citizens title to the Existing TC Water Facilities and Existing
212 TC Sewer Facilities. On January 15, 2002, IAWC acquired title to the Existing TC Water
213 Facilities and Existing TC Sewer Facilities from Citizens, as approved by the
214 Commission in Docket 00-0476. In addition, as successor to Citizens, IAWC is the
215 lessee of property on which the Original Wastewater Plant is located. Under a lease
216 agreement between Terra Cotta and Citizens, dated June 13, 2001, IAWC, as successor to
217 Citizens, is permitted use of this property for wastewater treatment plant purposes,
218 including use for additions and expansions of the Original Wastewater Plant.

219 **Q20. What is the capacity of the existing TC Water Backbone Facilities?**

220 A. The TC Water Backbone Facilities have a projected capacity of 4,950 P.E. This capacity
221 is sufficient to accommodate the existing developments of Oak Grove and Cobblestone,
222 and anticipated development in the TC Land over the next several years.

223 **Q21. Do the Agreement and the Westminster Agreement address construction of**
224 **additional water backbone facilities?**

225 A. Yes. Under Section IV of the Agreement, IAWC will provide future water backbone
226 plant for the TC Land, including the TC Acres, as required to provide water service that
227 is adequate, reliable, efficient and environmentally safe, and in accordance with the
228 Agreement and requirements of the Illinois Public Utilities Act. Under the Westminster
229 Agreement, water backbone facilities for the TC Acres will include a portion of the
230 capacity of the Existing TC Water Facilities and such new wells, storage and other

231 facilities as IAWC constructs in accordance with the terms of the Agreement. For Tall
232 Grass, construction of a separate water supply plant is the least-cost approach. Under the
233 Westminster Agreement, Westminster will construct the Tall Grass Water Backbone
234 Plant, subject to approval by IAWC of the plans and specifications. IAWC will monitor
235 and inspect the construction. Upon its successful completion, Westminster will transfer
236 title to the Tall Grass Water Backbone Plant to IAWC. The Tall Grass Water Backbone
237 Plant will include two wells, a pumping station and a 650,000 gallon ground storage
238 reservoir.

239 **Q22. Does the Agreement also address construction of additional wastewater backbone**
240 **facilities?**

241 A. Yes. Under Sections V through IX of the Agreement, Terra Cotta, by itself or together
242 with Westminster, will construct an “Initial Plant Expansion” of the Original Wastewater
243 Plant to increase the design average flow from 100,000 gallons per day to 1.0 million
244 g.p.d. Terra Cotta has entered into a “Design/Build Agreement” with Lintech
245 Engineering, LLC and Joseph J. Henderson & Son for construction of the Initial Plant
246 Expansion. The Design/Build Agreement updates an agreement initially signed by Terra
247 Cotta in 2003. Construction of the Initial Plant Expansion will be subject to inspection
248 and monitoring by IAWC. The Company has approved the engineering specifications for
249 the Initial Plant Expansion, and, under the Agreement, has the right to approve any future
250 changes to such specifications. Under Section VII of the Agreement, after completion of
251 the Initial Plant Expansion, and subject to approval of the Commission, Terra Cotta and
252 IAWC will conduct a closing to confirm that ownership and control of the Initial Plant
253 Expansion is held by IAWC. In addition, the Agreement provides that, if Terra Cotta

254 fails to complete the Initial Plant Expansion within twelve months after the date on which
255 the Commission's Order in this proceeding becomes final and no longer subject to appeal,
256 the Company may elect to assume control of the construction before its completion.
257 Funding for the Initial Plant Expansion will be provided by Terra Cotta, by itself or
258 together with Westminster, through establishment of a cash construction escrow or a
259 letter of credit in a form and from an institution satisfactory to IAWC. The Company
260 will provide an investment in the Initial Plant Expansion in an amount discussed below.

261 **Q23. Does the Company anticipate that additional wastewater facilities may be needed in**
262 **the future, in addition to the Initial Plant Expansion?**

263 A. Yes. To accommodate expected growth in the Expanded Area, IAWC intends to
264 construct a "Second Plant Expansion" to provide an additional 600,000 g.p.d. of
265 wastewater treatment plant capacity, in addition to the 1,000,000 g.p.d capacity of the
266 Initial Plant Expansion. IAWC will commence construction of the Second Plant
267 Expansion either upon Terra Cotta's consent or, if Terra Cotta does not consent, after
268 transfer of the Initial Plant Expansion to IAWC under the terms of the Agreement.
269 Construction of the Second Phase Plant Expansion will be designed and managed in a
270 manner that will not delay or disrupt completion of the Initial Plant Expansion.

271 **Q24. Have the Company and Terra Cotta addressed whether certain capacity from the**
272 **Initial Plant Expansion should be reserved?**

273 A. Yes. Under Section V of the Agreement, IAWC will reserve 1.0 m.g.d. of wastewater
274 treatment capacity from the Initial Plant Expansion exclusively for the TC Land and Tall
275 Grass, which includes the Westminster Land, and is referred to in the Agreement as the
276 "Reserved Area." Also, under Section II.B of the Agreement, certain other land

277 purchased by Terra Cotta and/or Westminster within two miles of the boundary of the
278 Expanded Area can, subject to the terms of the Agreement, be included in the Reserved
279 Area, provided that IAWC concludes that such land can reasonably be served based on an
280 engineering review, and that all applicable governmental approvals are obtained,
281 including approval of the Commission. The 1.0 m.g.d. of reserved capacity is intended to
282 provide 10,000 P.E. of capacity for the Reserved Area. Under the Agreement, there is no
283 requirement for Terra Cotta, Westminster for Tall Grass nor the “TC Land Entities,”
284 meaning any entities that purchase land from Terra Cotta or Westminster, to pay IAWC a
285 connection or other capacity fee for use of the reserved 1.0 m.g.d. of capacity within the
286 Reserved Area. Terra Cotta has agreed that development of the Reserved Area may only
287 utilize a combined level of up to 10,000 P.E. of capacity from the 1.0 m.g.d. of reserved
288 capacity. If development of the Reserved Area requires a level of capacity above 10,000
289 P.E., arrangements for additional capacity will be made under Rule 16, or on such other
290 terms as the Commission may approve.

291 **Q25. Do the Agreement and Westminster Agreement address water main extensions?**

292 A. Yes. Under Section III.B(2) and (3) of the Agreement, water mains may be extended by
293 Terra Cotta in the Original Terra Cotta Area pursuant to terms substantially similar to
294 those of the Original Agreement, as approved in the Docket 00-0194 Order, and also
295 substantially similar to the terms set forth in the Metro Division’s Rules, Regulations and
296 Conditions of Service, or “Standard Water Rules.” Aside from minor language changes
297 made for clarification of the provisions; for example, substituting IAWC as the utility in
298 place of Citizens, these provisions are the same as the comparable provisions of the
299 Original Agreement. To the extent that the provisions of Section III.B (2) and (3) of the

300 Agreement, applicable to the Original Terra Cotta Area, differ in minor respects from the
301 comparable provisions of the Original Agreement, IAWC seeks approval of those
302 provisions in this proceeding. Under the Westminster Agreement, Westminster will
303 construct water and wastewater mains for the Westminster Land, in accordance with
304 provisions consistent with terms of the Standard Water Rules and Rule 11 of the Metro
305 Division's Rules, Regulations and Conditions of Service, or "Standard Sewer Rules."
306 The applicable provisions of the Westminster Agreement will be discussed below.
307 Except as otherwise provided in the Agreement or the Westminster Agreement, water and
308 wastewater mains will be extended in the Expanded Area in accordance with the
309 Standard Water Rules and Standard Sewer Rules, respectively. All construction
310 performed by Terra Cotta under the Agreement, or by Westminster under the
311 Westminster Agreement, will comply with plans and specifications approved by IAWC.
312 In addition, the Company will monitor and inspect all construction.

313 **Q26. Does the Company expect to have to acquire rights-of-way from landowners for the**
314 **construction of water or wastewater mains?**

315 A. No. Terra Cotta and Westminster will provide property rights and/or rights-of-way for
316 water and wastewater facilities. At present, IAWC is not aware of a need to acquire
317 additional rights-of-way from private landowners. If it becomes necessary for the
318 Company to acquire additional rights-of-way, IAWC will follow the requirements of 83
319 Illinois Administrative Code, Part 300.

320 **VI. FUNDING OF FACILITIES**

321 **Water Backbone Plant**

322 **Q27. Will the Company continue to provide reimbursements for contributions for**
323 **existing water backbone plant in the TC Land?**

324 A. Yes. Under Section III of the Agreement, IAWC's refunds for the TC Water Backbone
325 Plant would continue to be made pursuant to the methodology approved by the
326 Commission in the Docket 00-0194 Order. The amount of reimbursement payments is
327 determined by dividing the actual cost of the TC Water Backbone Facilities, which is
328 approximately \$5.9 million, by the number of population equivalents that can be served
329 by the backbone facilities. Under the Agreement, the actual number of P.E.s that could
330 be served by the backbone facilities is 4,950 P.E. Under Section 6 of the Original
331 Agreement, the per P.E. refund is made as customers attach to the TC Water Backbone
332 Plant in the Original Terra Cotta Area. Under the Agreement, subject to the approval of
333 the Commission, the per P.E. refund would be paid as customers attach to the TC Water
334 Backbone Plant in the TC Land. IAWC seeks approval for this change.

335 **Q28. Will the Company require payment from developers for future water backbone**
336 **facilities needed to serve the TC Land?**

337 A. No. As expanded water supply facilities are needed for the TC Land, IAWC would,
338 under Section IV of the Agreement, construct any additional water backbone plant
339 without any requirement that Terra Cotta or any TC Land Entities provide a construction
340 deposit or any other funding or collateral.

341 **Q29. Does the Agreement permit the Company to use the TC Water Backbone Plant**
342 **outside of the Original Terra Cotta Area?**

343 A. Yes. The Original Agreement provides that IAWC will construct expanded water
344 backbone in the Original Terra Cotta Area, and this approach was approved by the
345 Commission in the Docket 00-0194 Order. The Original Agreement, however, requires
346 Terra Cotta's consent for use of the TC Water Backbone Plant outside the Original Terra
347 Cotta Area. In return for IAWC's agreement to provide additional water backbone plant
348 for the TC Land without investment by Terra Cotta or TC Land Entities, Terra Cotta has
349 consented in the Agreement to use of the TC Water Backbone Facilities to serve any
350 portion of the Expanded Area outside the Original Terra Cotta Area, to the extent that the
351 capacity of such facilities is adequate. The Company believes that the resulting
352 flexibility in the use of the TC Water Backbone Plant will allow it to more efficiently
353 serve customers.

354 **Q30. How will construction of the Tall Grass Water Backbone Plant be funded?**

355 A. Under Section IV.A of the Agreement, for those portions of the Expanded Area that are
356 not a part of the TC Land; in other words, Tall Grass, IAWC will provide additional
357 water backbone in accordance with Section 600.370(a). Consistent with this approach,
358 the Westminster Agreement requires that, subject to the approval of the Commission,
359 Westminster will construct the Tall Grass Water Backbone Plant at its expense and
360 transfer it to IAWC. Because there will be only a few customers in Tall Grass when
361 water service is first provided and extensive supply plant additions are required to serve
362 the Tall Grass area, receipt of this contribution is necessary to avoid undue risk for the
363 Company and its customers and is appropriate under 83 Illinois Administrative Code

364 Section 600.370(a). IAWC will provide to Westminster a refund of the cost of the Tall
365 Grass Water Backbone Plant of \$1,082 for each new customer connection, as defined in
366 the Westminster Agreement. This amount is approximately equivalent to the average per
367 customer investment in the Metro Division for “wells and springs.” As a result, the
368 Company’s investment in “wells and springs” backbone plant for Tall Grass will be
369 consistent with the level of investment in such plant for the Metro Division.

370 **Q31. What factors do you believe make it reasonable for the Commission to approve the**
371 **contribution/refund proposal described for Tall Grass?**

372 A. In the case of extensive plant additions, Section 600.370(a) allows a utility to seek
373 contributions from developers in appropriate circumstances. The rule provides that:

374 The utility will provide all supply plant (backbone plant) at its cost
375 and expense without requiring contributions or tap-on-fees from
376 customers, developers or promoters, except in those unusual cases
377 where extensive plant additions are required before customers can
378 be attached. In such instances the utility may require the customer,
379 developer and/or promoter to advance funds, subject to refund as
380 customers are attached, or require a revenue guarantee in lieu of
381 customers being attached. Each contract for such an advance or
382 revenue guarantee shall be filed with the Commission for approval.

383 In applying this section in orders in Dockets 00-0591, 01-0606, 03-0455 and 03-0550
384 (consolidated) and 05-0253, among others, the Commission has determined that the
385 utility’s investment in new plant should be at a level under which the investment in rate
386 base per customer for the area affected is comparable to that of other areas served by the
387 utility. As the Commission has recognized, a significantly higher level of investment
388 would increase revenue requirement per customer to an unreasonably high level. In the
389 case of the Tall Grass area, extensive plant additions are needed, and without an
390 investment by Westminster, the level of rate base per customer, and corresponding
391 revenue requirement per customer, would increase, causing existing customers to

392 subsidize service to new customers in the Expanded Area. Also, Westminster's funding
393 of the Tall Grass Water Backbone Plant places the risk that the area may not develop as
394 planned on Westminster, not on IAWC or existing customers, making a gradual
395 investment by IAWC in the form of refunds reasonable. IAWC's proposed level of
396 investment is consistent with the principles of Section 600.370(a) and comparable to the
397 approach approved in Docket 00-0194 for the TC Water Backbone Plant in the Original
398 Terra Cotta.

399 **Q32. To summarize, which specific portions of the Agreement and the Westminster**
400 **Agreement relating to funding of facilities is the Company seeking approval?**

401 A. The Company seeks approval of Section III.B.1 of the Agreement, which modifies the
402 water refund methodology approved in the Docket 00-0194 Order for the TC Water
403 Backbone Plant to permit per P.E. refunds as customers attach throughout the TC Land
404 rather than in only the Original Terra Cotta Area. The Company further seeks approval
405 of the above-described provisions of Section IV of the Agreement, which describe the
406 agreed arrangements for the funding of future water backbone plant. The Company also
407 seeks approval of the provisions of the Westminster Agreement that provide for a
408 contribution of the Tall Grass Water Backbone Plant, with related refunds.

409 **Wastewater Backbone Plant**

410 **Q33. How will the investments for wastewater backbone plant be funded?**

411 A. Under Section VIII of the Agreement, IAWC would provide an investment in the amount
412 of \$322,202 for the Existing TC Sewer Backbone Facilities and Initial Plant Expansion.
413 This amount is intended to cover the obligation that IAWC, as successor to Citizens, has
414 to refund the cost advanced to Citizens for the TC Sewer Backbone Plant under the terms
415 of the Docket 00-0194 Order and related Appellate Decision, and provide a reasonable

416 level of investment in the Initial Plant Expansion. Terra Cotta constructed the Original
417 Wastewater Plant in 1973 and upgraded it in 1996-97 at a cost of approximately
418 \$449,221. Over the years that these facilities were in use, Terra Cotta recorded
419 depreciation in the approximate amount of \$362,912. Accordingly, under the Uniform
420 System of Accounts for Wastewater Utilities, 83 Illinois Administrative Code Part 650,
421 the amount of the cost advanced for sewer backbone plant that is part of the Existing TC
422 Sewer Facilities is \$86,309, as shown in accounting entries submitted by Illinois-
423 American Water in Docket 00-0194. The \$322,202 investment amount specified in the
424 Agreement consists of the \$86,309 refund of the cost advanced for the TC Sewer
425 Backbone Plant, and a \$235,893 investment in the Initial Plant Expansion.

426 **Q34. How would the wastewater backbone plant investments be funded under the**
427 **Company's Standard Rules?**

428 A. Unless other terms are approved by the Commission, the financing of wastewater
429 backbone plant is subject to Rule 16. Under Rule 16.04(c), Terra Cotta and/or
430 Westminster, as developer of Reserved Area, would be required to pay a deposit in an
431 amount equal to the cost of the Initial Plant Expansion. Under Rule 16.04(c)(ii), IAWC
432 would pay a refund to the Reserved Area developer(s) as customers connect to the
433 expanded wastewater plant capacity inside the development area. The per customer
434 refund amount is equivalent to the estimated amount of annual treatment revenue to be
435 received from each customer, estimated to be \$327.48 in the case of each residential
436 customer. Assuming that there are approximately 2,449 new residential customers in the
437 Reserved Area, the potential amount of the refund that Terra Cotta could receive under

438 Rule 16, if the anticipated development were to occur as expected, would be
439 approximately \$802,000. This amount would be paid under Rule 16 as customers attach.

440 **Q35. Why is the Company proposing a different approach?**

441 A. As an alternative to this approach, IAWC and Terra Cotta agreed to the fixed payment
442 discussed above, which includes a fixed component of \$235,893 for the Initial Plant
443 Expansion. Under the agreed approach, IAWC is able to provide a fixed investment in
444 the Initial Plant Expansion at a reasonable level, which is below the level of amount of
445 investment that Metro Division customers might otherwise be required to support in rates
446 if full build-out were to occur. Terra Cotta, on the other hand, receives a fixed certain
447 investment now rather than the uncertainty that would exist under Rule 16. The
448 Company believes that either the approach under Rule 16 or the agreed refund terms
449 would be consistent with the finding in the Docket 00-0194 Order that the utility should
450 provide an investment in sewer backbone plant. Under the circumstances of this
451 transaction, however, the Company believes that the agreed approach is reasonable and
452 should be approved.

453 **Q36. If the Company proceeds with the Second Plant Expansion, how will those facilities
454 be funded?**

455 A. The Second Plant Expansion would be constructed in accordance with Rule 16, or on
456 such other terms as the Commission may approve.

457 **Q37. To summarize, what specifically is the Company asking the Commission to approve
458 with respect to wastewater backbone plant?**

459 A. IAWC seeks approval of the above-described provisions of the Agreement which relate
460 to construction of the Initial Plant Expansion and the funding approach for the TC Sewer

461 Backbone Facilities and the Initial Plant Expansion, which varies from the provisions of
462 Rule 16.

463 **Water and Wastewater Mains**

464 **Q38. How will water main extensions be funded?**

465 A. Under the Westminster Agreement, Westminster will construct, at its expense, water
466 distribution mains within the Westminster Land (“WM Water Mains”) and transfer those
467 WM Water Mains to IAWC. The Company will refund to Westminster, for each new
468 customer that connects to a WM Water Mains and taking water service within the
469 Westminster Land, during the first ten-year period following construction of WM Water
470 Mains, an amount equal to one and one-half times the average annual water revenue paid
471 to IAWC by other similarly situated customers. These refunds would be paid to
472 Westminster during the first ten year period following transfer of WM Water Mains. The
473 total amount refunded will not exceed the total cost to Westminster the constructing the
474 WM Mains. IAWC also will refund to Westminster the cost of the Company service line
475 for each new customer.

476 **Q39. How will wastewater main extensions be funded?**

477 A. Under the Westminster Agreement, Westminster will construct, at its expense,
478 wastewater collection mains within the Westminster Land (“WM Wastewater Mains”)
479 and transfer those WM Wastewater Mains to IAWC. The Westminster Agreement will
480 provide that IAWC will refund to Westminster an amount determined in accordance with
481 the “Sewer Refund Methodology” approved in Docket 01-0645. In accord with the
482 Sewer Refund Methodology, IAWC will refund to the Developer one and one-half times
483 the amount of estimated per customer annual sewer collection service revenue from a
484 customer similarly situated to each “Original Prospective Customer,” as defined in

485 Docket 01-0645, and contracts for at least one year of sewer service, commencing within
486 30 days after the date that service is first available. In no event would the total amount of
487 sewer main refunds paid to Westminster exceed the total cost of constructing the WM
488 Wastewater Mains.

489 **Q40. What is the Company asking the Commission to approve?**

490 A. The provisions of the Westminster Agreement that relate to sewer mains are a “special
491 contract” under Rule 11.01(m) of the Standard Sewer Rules and thus require Commission
492 approval. Also, as noted above, certain provisions of the Agreement regarding Terra
493 Cotta’s construction of water mains for the Original Terra Cotta Area differ in minor
494 respects from the comparable provisions of the Original Agreement. Except as provided
495 in the Agreement and Westminster Agreement, the contribution/refund provisions of the
496 Standard Water Rules and Standard Sewer Rules will apply in connection with the
497 construction of water and sewer mains, respectively, for the Expanded Area.

498 **Q41. Are the various contributions and refunds you have discussed in your testimony
499 necessary to establish reasonable rate levels in the Expanded Area?**

500 A. Yes. As shown in IAWC Exhibit MJH 2.2, sponsored by Mr. Hoffman, the combined
501 rate of return of 7.48% on water and sewer rate base in the Expanded Area, on an average
502 basis after the 5th year of initiation of service, is comparable to the rate of return allowed
503 in the Company’s last case, Docket 02-0690. The rate base used in developing this rate
504 of return is based on approval of the contributions and refunds I have discussed in my
505 testimony. In particular, IAWC is seeking approval to (i) modify the water refund
506 methodology approved in Docket 00-0194 for the TC Water Backbone Plant to permit
507 per P.E. refunds as customers attach throughout the Expanded Area, rather than only in

508 the Original Terra Cotta Area, (ii) approval of the provisions of the Westminster
509 Agreement that provide for a contribution of the Tall Grass Water Backbone Plant, with
510 related refunds, (iii) approval to provide a fixed level of investment of \$322,202 for the
511 Existing TC Sewer Facilities and Initial Plant Expansion, and (iv) approval of the funding
512 proposal for the WM Wastewater Mains. If the Company were to receive lower levels of
513 contributions, or provided higher levels of refunds, the Company's investment in water
514 and sewer rate base would increase, reducing the rate of return and requiring other
515 customers in the Metro Division to subsidize new customers in the Expanded Area. With
516 the proposed level of investment by IAWC, Terra Cotta and Westminster, existing Metro
517 Division customers will not be required to subsidize the water or wastewater service
518 provided to new customers within the Expanded Area.

519 **Q42. Does this conclude your direct testimony?**

520 A. Yes.

521