

ILLINOIS COMMERCE COMMISSION

IAWC EXHIBIT 1.00

DIRECT TESTIMONY OF

KARLA O. TEASLEY

ILLINOIS-AMERICAN WATER COMPANY

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**DIRECT TESTIMONY
OF
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1 **I. WITNESS IDENTIFICATION AND BACKGROUND**

2 **Q1. Please state your name.**

3 A. Karla O. Teasley.

4 **Q2. Please state your business address.**

5 A. 100 North Water Works Drive, Belleville, Illinois 62223.

6 **Q3. By whom are you employed and in what capacity?**

7 A. I am employed by Illinois-American Water Company (“IAWC” or “Company”), and
8 serve as President of the Company.

9 **Q4. Please summarize your education and employment history.**

10 A. I hold a bachelor’s degree from the University of Wisconsin (Eau Claire) and a
11 Juris Doctor from the University of Minnesota Law School. I am a member of the
12 bar in Minnesota and Florida, currently on inactive status in both states. I have
13 been President of the Company since January 2007. Since graduating from law
14 school in 1983, I have held increasingly responsible positions in the public utility
15 industry. Between 1983 and 1989, I was a staff attorney for Minnesota Power
16 based in Duluth, Minnesota. From 1989 through 1997, I was Vice President,
17 General Counsel and Director of Florida Water Services, a privately owned water
18 and wastewater utility based in Orlando, Florida. In addition to my duties as
19 Secretary for the Board of Directors, I provided all in-house legal services for the
20 utility including contracts, regulatory affairs (including rate and environmental
21 regulation), human resources, bond issues, eminent domain and real property.
22 From 1997 through 2007, I was a Vice President of Louisville Water Company in
23 Louisville, Kentucky. When I left that position, I had Board Officer responsibility in

24 the customer contact area and business development. I was also responsible for
25 extending the distribution system to make water available to customers, capital
26 budgeting and infrastructure planning and pipeline design and construction.

27 **Q5. Are you a member of any industry or professional organizations?**

28 A. Yes. I serve on the board of the Leadership Council of Southwestern Illinois and
29 the Illinois Chamber of Commerce. I am also a member of the Illinois Business
30 Roundtable, the American Water Works Association (Illinois Section) and the
31 American Bar Association.

32 **Q6. Please summarize your responsibilities as President of the Company.**

33 A. I have overall responsibility for the day-to-day operation of the Company. In that
34 endeavor, I am in regular contact with the General Manager and each Division
35 Manager and provide guidance to them in carrying out their duties. I also assist
36 other officers in developing strategic and annual goals and objectives for the
37 Company and in administering policies and procedures as approved by the
38 Board of Directors of the Company. It is my responsibility to ensure that these
39 goals and objectives are achieved. I, along with other Company officers,
40 represent the Company before governmental and regulatory agencies. I, along
41 with others, formulate financial objectives and budgets and provide the direction
42 necessary to meet those objectives while remaining within budgetary guidelines.
43 I am part of the management team that establishes employee levels, working
44 conditions, and safety requirements within guidelines established by law and the
45 Board of Directors. I have the responsibilities associated with developing and
46 controlling the Company's operating and maintenance and capital budgets, as

47 well as providing direction in the areas of construction, purchases or other
48 acquisitions, operation, maintenance and protection of all property, facilities and
49 equipment required to maintain water quality standards and continuity of service.

50 **II. PURPOSE OF TESTIMONY**

51 **Q7. What is the purpose of your testimony?**

52 A. My testimony provides a description of the Company and its operations and
53 discusses the factors related to the application for an increase in rates. I also
54 discuss the order issued by the Commission in Docket 05-0681/06-0094/06-0095
55 (consol.) (“Docket 05-0681 Order”).

56 **III. COMPANY BACKGROUND**

57 **Q8. As President of the Company, are you generally familiar with the business,
58 facilities, and operations of the Company in each of its divisions?**

59 A. Yes.

60 **Q9. Are you also generally familiar with the books and records of the
61 Company?**

62 A. Yes.

63 **Q10. Please summarize the history of IAWC.**

64 A. The five Districts of IAWC (prior to acquisition of the properties of United Water-
65 Illinois, Northern Illinois Water Corporation and Citizens Utilities Company of
66 Illinois) began operating between 1875 and 1889. The earliest water system was
67 established in the Alton District in 1875, followed by water systems in the Cairo
68 and Interurban Districts in 1885. The Pekin District began operation in 1886; and
69 the Peoria District in 1889. Prior to June 1, 1978, American Water Works

70 Company, Inc. (“American Water”) had four operating subsidiaries in the State of
71 Illinois. These were Alton Water Company, The Cairo Water Company, East St.
72 Louis and Interurban Water Company, and Peoria Water Company. The initial
73 step in the creation of the current Illinois-American Water Company came on
74 June 1, 1978, when the name of East St. Louis and Interurban Water Company
75 was changed to Illinois-American Water Company. On February 1, 1981,
76 American acquired Pekin Water Works Company. In Docket No. 81-0727, the
77 Commission approved the merger of The Cairo Water Company and Pekin
78 Water Works Company into Illinois-American Water Company, effective July 1,
79 1982. On January 1, 1985, with Commission approval in Docket No. 84-0204,
80 the merger of all American subsidiaries in Illinois became complete when Alton
81 Water Company and Illinois-American Water Company were merged into Peoria
82 Water Company, the name of which was then changed to Illinois-American Water
83 Company. Effective during 1987, for organizational and management purposes,
84 the Company further consolidated its operations by forming two Divisions within
85 the Company. The Northern Division consisted of the Peoria and Pekin Districts
86 and the Southern Division consisted of Alton, Cairo and Interurban Districts.

87 On June 25, 1999, American Water acquired all of the common stock of
88 National Enterprises Inc. (“NEI”), and NEI was merged into American. One of the
89 operating water utilities owned by Continental Water Company, a subsidiary of
90 NEI, was Northern Illinois Water Corporation (“NIWC”). On March 29, 2000, in
91 Docket No. 99-0418, the Commission approved the merger of NIWC into IAWC.
92 The merger was completed on March 31, 2000. As a result, the four former

93 Divisions of NIWC – Champaign, Sterling, Streator, and Pontiac – each became
94 Districts of IAWC’s Eastern Division.

95 On May 31, 2000, IAWC acquired United Water Illinois, Inc. (“UWIL”),
96 which provided public utility water service in the City of Lincoln and vicinity.
97 UWIL was merged with and into IAWC. The acquisition and merger were
98 approved by the Commission in Docket No. 99-0457, on May 10, 2000.

99 In January 2002, IAWC acquired the Illinois water and wastewater assets
100 of Citizens Utilities Company of Illinois. The Commission approved the
101 transaction in Docket No. 00-0476, on May 15, 2001.

102 In January, 2003, a German multinational company, RWE AG (“RWE”),
103 acquired American Water, the direct parent of IAWC. The Commission approved
104 the transaction in Docket No. 01-0832 on November 20, 2002, and that order
105 was affirmed on appeal in *City of Pekin v. Illinois Commerce Comm’n*, Case No.
106 3-03-0113 (3rd Dist. Oct. 29, 2003).

107 **Q11. Have there been recent developments regarding the ownership of IAWC?**

108 A. Yes. In November, 2005, RWE announced that it had revised its core business
109 focus to be on the European power and energy markets, where historically its
110 roots lie. In order to maintain its position among Europe’s leading integrated
111 electricity and gas companies in response to fierce competition, growing
112 customer needs, and rising costs both for energy production facilities and many
113 other energy production inputs, RWE determined that it must concentrate on its
114 power and energy markets. As a result of these developments, RWE’s ability to
115 maintain its competitiveness in its core European businesses is expected to be

116 far more capital intensive than RWE could have predicted when it acquired
117 American Water. Consequently, RWE decided to sell the water operations of
118 Thames Water in the U.K. and to return American Water to its status as a U.S.
119 publicly-traded company. The contemplated transaction (the "Proposed
120 Transaction") consists of (i) the sale by RWE's subsidiary Thames Water Aqua
121 Holdings GmbH ("Thames GmbH") of up to 100% of the shares of common stock
122 of American Water in one or more public offerings, and (ii) prior to the closing of
123 the initial public offering, the merger of Thames Water Aqua U.S. Holdings
124 ("TWAUSHI") with and into American Water, with American Water being the
125 surviving corporation. On April 21, 2006, IAWC, along with American Water,
126 TWAUSHI and Thames GmbH ("Joint Applicants") filed a Petition with the
127 Commission seeking approval of the Proposed Transaction pursuant to Section
128 7-204 of the PUA, 220 ILCS 5/7-204. The Commission docketed the proceeding
129 as Docket No. 06-0336. The Commission issued a final order approving the
130 Proposed Transaction, subject to certain conditions, on June 27, 2007. The
131 primary benefit of the Proposed Transaction will be to return American Water to
132 its status as a United States publicly-traded company. Closing of the proposed
133 transaction is expected to occur during the fourth quarter of 2007. After the
134 proposed transaction, IAWC will remain a wholly-owned subsidiary of American
135 Water.

136 **Q12. Please describe the relationship between IAWC and American Water.**

137 A. American Water owns all of the outstanding stock of IAWC.

138 **Q13. Please describe the relationship between IAWC and American Water Works**
139 **Service Company, Inc. (“Service Company”).**

140 A. IAWC contracts for services to be supplied at cost by the Service Company,
141 which also is a subsidiary of American Water. The Service Company office in
142 Voorhees, New Jersey provides support to the IAWC staff in the areas of
143 accounting, engineering, operations, regulatory practices, finance, water quality,
144 information systems, personnel information and training, purchasing, insurance,
145 safety, and community relations. The Service Company also operates facilities
146 for water quality analyses and Central Region field support in Belleville, Illinois.
147 As Mr. Grubb discusses, in recent years IAWC has secured an increased level of
148 service through the Service Company, thus providing enhanced customer service
149 and cost efficiencies.

150 **Q14. Has the contractual relationship between the Service Company and IAWC**
151 **been approved by this Commission?**

152 A. Yes. The current contract between the Company and the Service Company was
153 initially approved by the Commission on July 19, 1989, in Docket No. 88-0303.
154 Pursuant to the Commission's order in the Company's last rate case, Docket No.
155 02-0690, the agreement between the Company and the Service Company was
156 reapproved in Docket 04-0595 on October 20, 2005.

157 **IV. THE PROPOSED RATE INCREASE**

158 **Q15. Why has the Company proposed a rate increase?**

159 A. The proposed rates are designed to produce additional revenues needed to
160 provide the revenue requirements of the Company's service areas. Since the

161 last rate case, Docket No. 02-0690, the Company has experienced increased
162 operating expenses, and in some cases, substantially increased rate base. The
163 proposed rates are intended to yield revenues sufficient to recover test year
164 operating expenses and to produce a reasonable return on rate base. In
165 particular, the Company seeks an increase in rates to earn a return of and on
166 capital expenditures and recover the increase in operating expenses required to
167 allow the Company to maintain a high level of service to its customers, and,
168 where warranted, address service concerns that have been raised.

169 The test year in this proceeding is the twelve month period ended June 30,
170 2009. For the test year, the Company's operating expenses, since the test year
171 in the last rate case, have increased by approximately \$17.7 million. Schedule
172 A-4, sponsored by Mr. Kerckhove, shows that rate base has increased by over
173 \$113 million. As also shown on Schedule A-4, additional annual revenue of
174 approximately \$35.4 million is needed to afford the Company the opportunity to
175 earn a reasonable rate of return.

176 **Q16. Please discuss major projects included in rate base.**

177 A. Schedule B-5, sponsored by Mr. Kerckhove, shows that gross plant additions for
178 water and wastewater totaled \$50,328,973 for the prior year ending June 30,
179 2006. For the prior period ending June 2007, gross additions totaled
180 \$54,907,691, and for the period ending June 2008, forecasted gross additions
181 total \$90,283,976. The forecasted gross plant additions for the test year exceed
182 \$ 109 million. Mr. DeBoy's testimony includes a discussion of major capital
183 projects completed or planned for completion between 2004 and the end of the

184 test year. The test year plant additions include a new ground water treatment
185 facility planned for the Champaign District (the "Champaign Plant"), which will
186 help provide high quality water to a growing customer base in Champaign when
187 the plant is in service in December 2008. Mr. Suits's testimony provides
188 additional information about this project.

189 **Q17. Please comment on major programs that have affected operating income.**

190 A. The Company is engaged in several ongoing programs that have led to
191 increased operating expenses. Mr. Ruckman's testimony explains an ongoing
192 program to replace meters in the Chicago Metro area with automated meter
193 reading technology. He also explains the hiring of additional personnel to
194 perform hydrant and valve inspection and maintenance and related activities. In
195 addition, Mr. Ruckman discusses the Company's efforts to reduce levels of
196 unaccounted-for water ("UFW") where economically justified. Also, as mentioned
197 previously, Mr. Grubb explains the increased level of services provided by the
198 Service Company which benefit IAWC customers.

199 **Q18. What is the Company's cost of equity?**

200 A. The Company's cost of equity is at least 11.25%, as determined by the
201 Company's witness Pauline Ahern. Her presentation is contained in Exhibit No.
202 12.00.

203 **Q19. What is the Company's cost of capital for the test year?**

204 A. As shown on Schedule D-1, page 1, the Company's cost of capital and required
205 rate of return is at least 8.29%.

206 **Q20. What are the financing requirements for 2007 through the test year ending**
207 **June 30, 2009?**

208 A. As Mr. Jenkins explains, IAWC's financing program for 2007 through June of
209 2009 includes the issuance of up to \$28,500,000 in long-term debt (IAWC is
210 currently seeking Commission approval for this issuance in Docket 07-0371),
211 primarily to finance a portion of the capital costs of the Champaign Plant. The
212 balance of the approximately \$51,000,000 total cost of the Champaign Plant, and
213 additional equity as needed, will be funded through receipt of additional paid-in
214 capital from the Company's parent, American Water. To the extent internally
215 generated funds are available to finance the capital costs associated with the
216 Champaign Plant and other capital projects, IAWC will use those funds to offset
217 the amount of debt and additional paid-in capital that would otherwise have been
218 required.

219 **Q21. Are the Company's current revenues sufficient to earn a reasonable rate of**
220 **return?**

221 A. No. Schedule A-2, sponsored by Mr. Kerckhove, shows a test year revenue
222 deficiency of approximately \$35.4 million.

223 **Q22. Please describe generally the nature and extent of the changes proposed in**
224 **operating revenues for water and wastewater service.**

225 A. The proposed changes for each district of the Company are as follows:

226	Southern/Peoria/Pontiac/Streator:	20.00%
227		
228	Champaign:	59.83%
229		
230	Lincoln:	-.76%
231		

232	Pekin:	26.70%
233		
234	Sterling:	31.00%
235		
236	Chicago-Metro Water:	5.80%
237		
238	Chicago-Metro Sewer:	-3.18%
239		
240	South Beloit:	20.00%
241		

242 Specific changes in rates for each operating district are discussed in the
243 testimony of Mr. Grubb.

244 **Q23. Has the Company obtained a waiver in connection with the standard rate**
245 **case filing requirements?**

246 A. Yes. In Docket No. 07-0370, the Commission granted the Company's request for
247 a waiver of 83 Ill. Adm. Code Part 285.7010(a), to use the most current version
248 of the American Institute of Certified Public Accountants Guide for Prospective
249 Financial Information.

250 **Q24. Has the Company caused notice of the filing of the proposed rates to be**
251 **published in a newspaper of general circulation within each District for**
252 **which revised rates are proposed?**

253 A. Yes. Exhibit No. 1.1 is a copy of the Certificates of Publication.

254 **Q25. Did the Company also cause notice of the filing to be posted in its business**
255 **offices for the various subject Districts?**

256 A. Yes.

257 **Q26. Did the Company also cause notice of the filing to be sent to its customers**
258 **in the subject Districts with the first billing after filing?**

259 A. Yes. A copy of the notice sent to each customer is Exhibit No 1.2.

260 V. DOCKET 05-0681 ORDER

261 **Q27. Please discuss the Docket 05-0681 Order.**

262 A. In Docket 05-0681, IAWC committed to, and the Commission ordered, a number
263 of actions designed to improve customer service. In Docket 05-0681, a
264 customer, Mr. Grens, the Village of Homer Glen ("Homer Glen") and the Office of
265 the Illinois Attorney General ("Attorney General"), brought complaints against the
266 Company. On February 23, 2007, the Company entered into a stipulation with
267 the Attorney General in which the Company agreed to undertake a number of
268 steps, including increased monitoring and reporting of high bills, estimates and
269 zero-use bills, improved bill format, and enhanced customer service. The
270 Company also agreed to undertake valve and hydrant inspections in its
271 Champaign and Chicago-Metro service areas and perform fire flow tests for
272 those areas. The Commission issued a final order in this proceeding on April 18,
273 2007 which ordered the Company to undertake the commitments agreed to in the
274 stipulation. The Commission also ordered IAWC to take certain steps with
275 regard to recordkeeping and reporting, customer service and communication,
276 hydrant inspection, and billing. IAWC is in the process of complying with all
277 requirements established by the Commission pursuant to this order.

278 **Q28. Q29. Has IAWC taken other action in response to the Docket 05-0681**
279 **Order?**

280 A. Yes. In the Docket 05-0681 Order, the Commission found that "the evidence in
281 this case suggests that the rates charged by IAWC in the Chicago Metro service
282 [area] may not be just and reasonable because they are disproportionately high

283 relative to the rates charged in other nearby communities." In this proceeding,
284 Mr. Uffelman of Deloitte & Touche LLP ("Deloitte") and Ms. Kane of Stifel
285 Nicolaus ("Stifel") present an analysis of the cost structures and rates of IAWC
286 and certain neighboring municipalities in the vicinity of IAWC's Chicago Metro
287 District. As the evidence presented by these witnesses demonstrates, the cost
288 structures and rate-making practices of municipally-owned entities in the vicinity
289 of the Chicago Metro District differ significantly from those of IAWC. As a result, a
290 comparison of IAWCs rates to those of the municipalities does not support the
291 conclusion that IAWC's rates are unreasonable.

292 **Q29. The Report prepared by Stifel and Deloitte references certain cost**
293 **advantages realized by IAWC as a result of its participation in the American**
294 **Water system. Would you discuss these advantages?**

295 A. Yes. IAWC benefits from its participation in the American Water system. IAWC
296 utilizes the expertise in accounting and finance, legal, human resources, water
297 quality, engineering, safety and loss control areas that the professional
298 management and administrative staff employed by the Service Company offer.
299 Through the Service Company, IAWC is able to obtain expert capabilities without
300 the expense of contracting with outside service providers. The cost of
301 maintaining this management and administrative staff through the Service
302 Company is allocated among all of American Water's operating subsidiaries, and
303 the services of these personnel can therefore be accessed by IAWC at a lower
304 cost than if IAWC maintained such staffing itself. Similarly, American Water's
305 consolidation of separate customer service centers into a national customer

306 service center, located in Alton, Illinois, has produced efficiencies that benefit all
307 American Water customers, including customers in Illinois. The national call
308 center is available to customers in all IAWC districts to make account or service
309 inquiries 24 hours a day. The national call center is staffed by dedicated, full-
310 time customer service representatives who are supported by full- time trainers.
311 IAWC is also able to take advantage of statewide and national contracts through
312 the Service Company for mass purchase of a variety of goods, including office
313 supplies, pipe, chemicals and meters, at a lower cost. IAWC can also take
314 advantage of the Service Company's national laboratory for processing water
315 quality samples, which is located in Belleville, Illinois. Finally, the Service
316 Company can provide highly specialized expertise in such areas as security,
317 environmental management, and planning that would not be cost effective for
318 IAWC to provide for itself.

319 **Q30. Does this conclude your testimony?**

320 A. Yes.