IIWC Exhibit 6.0

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

ILLINOIS-AMERICAN WATER COMPANY	**:**	
	:	**Docket No. 07-0507**
Proposed General Increase In Water Rates	**:**	

Rebuttal Testimony of

Brian Janous

On Behalf of

Illinois Industrial Water Consumers
Fosterburg Water District
Jersey County Rural Water Co., Inc.
Bond-Madison Water Company

March 4, 2008
Project 8888

BRUBAKER & ASSOCIATES, INC.
ST. LOUIS, MO 63141-2000

STATE OF ILLINOIS

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ILLINOIS-AMERICAN WATER COMPANY	**:**	
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Direct Testimony of Brian Janous

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A My name is Brian Janous and my business address is 1215 Fern Ridge Parkway, Suite 208, St. Louis, MO 63141-2000.

Q WHAT IS YOUR OCCUPATION?

A I am an energy advisor and a consultant in the field of public utility regulation in the firm of BAI (Brubaker & Associates, Inc.).

Q ARE YOU THE SAME BRIAN JANOUS WHO PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?

A Yes.

Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A I am appearing on behalf of the Illinois Industrial Water Consumers (IIWC). IIWC consists of large water users taking service from Illinois-American Water Company (Illinois-American or Company). I am also appearing on behalf of three water districts: Fosterburg Water District, Jersey County Rural Water Co., Inc., and

Bond-Madison Water Company, who are also large water users taking water service from the Company.

Q WHAT IS THE SUBJECT OF YOUR REBUTTAL TESTIMONY?

A I will respond to Company witness Ms. Pauline M. Ahern's comments, contained in her rebuttal testimony (IAWC Exhibit 12.10), regarding: (i) my assertion that IIllinois-American's return on common equity (ROE) and overall rate of return (ROR) should reflect current market costs; (ii) the comparability of my proxy water and gas company groups to Illinois-American; and (iii) my two-stage DCF model.

Q AT PAGE 26 OF HER REBUTTAL TESTIMONY MS. AHERN RESPONDS TO YOUR POSITION THAT THE COMMISSION SHOULD CONSIDER OBSERVABLE AND VERIFIABLE ACTUAL CURRENT COSTS BY SUGGESTING THAT YOUR "COMMENTS REGARDING PROJECTED INTEREST RATES ARE MISLEADING." WERE YOUR COMMENTS MISLEADING?

A I do not believe my comments were misleading. Ms. Ahern has not provided any support for her claim that my analysis, which is based upon empirical evidence demonstrating the inaccuracy of interest rate projections over the last several years (IIWC Exhibit 3.2), is "misleading." Those projections have, in fact, been inaccurate.

It is important to note that I did, in fact, use projected interest rates in my CAPM analysis. However, the projections I used differ materially from those utilized by Ms. Ahern, as I will explain below. As I demonstrated in my direct testimony, over the last several years these projections have been consistently high and current interest rates, at the time of the projection, have been a more accurate predictor of future interest rates.

Further, in the event uncertain future projections of increased interest rates actually materialize, Illinois-American can file for rate relief to mitigate any higher capital costs associated with those increases. Therefore, given the uncertainty of projected increases to future interest rates, it would be detrimental to ratepayers to reflect these uncertain projected capital costs in rates at times when projected interest rates are substantially higher than current observable interest rates.

The important distinction between the interest rate projections used in my analysis and those used in Ms. Ahern's is the date of the projection and the spread between actual and projected rates at the time of the projection. Ms. Ahern used an interest rate projection of 5.33% from July 2007, when there was a fairly large spread between the then current and projected interest rates. The projection used in my analysis, 4.8%, is from December 2007. At that time, there was a negligible difference between projected and then current interest rates. Further, as Ms. Ahern noted in her rebuttal testimony (IAWC Exhibit 12.10 at 24, lines 663-667), the latest projections, from February 2008, maintain this relatively flat relationship between current and projected interest rates and are significantly below the rates used in either Ms. Ahern's or my testimony (the current rate is approximately 4.3%).

Q PLEASE COMMENT ON MS. AHERN'S CLAIM THAT YOUR REFERENCES TO THE FINANCIAL RISK OF ILLINOIS-AMERICAN RELATIVE TO BOTH YOUR WATER PROXY GROUP AND YOUR GAS PROXY GROUP ARE INCONSISTENT SINCE, WITH RESPECT TO THE FORMER, YOU REFERRED TO THE FINANCIAL RISK AS BEING "SLIGHTLY HIGHER" WHILE, WITH RESPECT TO THE LATTER, YOU REFERRED TO IT AS "REASONABLY COMPARABLE."

A Ms Ahern makes this claim at pages 26-27 of her rebuttal testimony. As I indicated in response to IAWC-IIWC 1.82, both statements are true. That is, the financial risk of my water group is slightly higher than that of Illinois-American and the financial risk of my gas group is reasonably comparable to Illinois-American. I did not intend to imply that the relative financial risks of the two groups are meaningfully different. In any event, I consider both groups to be comparable to Illinois-American for the reasons stated in my direct testimony. Ms. Ahern's critique is one of grammatical interpretation and has no impact on the analysis or conclusions contained in my testimony.

Q PLEASE COMMENT ON MS. AHERN'S CLAIM THAT YOUR PROXY GROUPS ARE NOT COMPARABLE TO ILLINOIS-AMERICAN IN TERMS OF TOTAL RISK.

A Ms. Ahern claims that my proxy group analysis is based upon outdated S&P guidelines that have been superseded by new guidelines. She claims that my conclusions regarding my proxy groups are invalidated by these new guidelines.

Q DO YOU AGREE WITH MS. AHERN THAT YOUR CONCLUSIONS BASED UPON YOUR PROXY GROUPS ARE NO LONGER VALID?

A No, I do not. S&P's new methodology, as revealed in Ms. Ahern's testimony, in no way invalidates the comparability of my proxy groups. As I demonstrated in my testimony, S&P's assessment of my proxy groups' business risk was, on average, higher than that of Illinois-American's (using American Water Capital as a proxy) on a scale of 1 to 10 (10 being the highest risk). My proxy groups were given an average score of "3" compared to Illinois-American's score of "2." I accepted this higher business risk since the business risk scores were relatively comparable. I also noted that the financial risk of Illinois-American was slightly higher than that of the proxy groups. Thus, the total risk (a combination of business and financial risk) was reasonably comparable.

Ms. Ahern indicates that under S&P's new methodology, which I would note is less granular with only five levels of business risk ("excellent," "strong," "satisfactory," weak," or "vulnerable"), my proxy groups and Illinois-American are now both rated as "excellent" in the context of business risk; whereas, the financial risk of Illinois-American is still slightly higher than the financial risk of the proxy groups.

As I indicated above, I still stand by my proxy groups as S&P's assessments of their business risks are, even under the new methodology, reasonably comparable to that of Illinois-American. Further, I am not inclined to completely discount S&P's very recent previous assessment (Illinois-American's business profile score of "2" was reiterated by S&P as recently as November 17, 2007) in favor of their current, less granular assessment published two weeks later on November 30, 2007.

Nor am I inclined to assume, as Ms. Ahern does, that less granularity equates to identical assessments of business risk. If one is grading students on a numerical scale, a student who scores a 99% is clearly differentiated from the student who scores a 90%. However, assessing them with a less granular letter-grade, each student would receive an ‘A’. In this example, the only factor that has changed is the scale, not the student’s relative abilities. I would argue that the same reasoning applies to S&P’s new methodology. A change in the scale that S&P uses to evaluate business risk does not change the fact that S&P has considered Illinois-American’s business risk to be lower than that of its peers in my proxy groups.

Q PLEASE COMMENT ON MS. AHERN’S CLAIM, WITH RESPECT TO YOUR TWO-STAGE DCF ANALYSIS, THAT THERE IS NO EMPIRICAL EVIDENCE TO SUPPORT THE USE OF GDP GROWTH AS A PROXY FOR THE LONG-TERM, SUSTAINABLE GROWTH RATE OF A UTILITY COMPANY.

A Ms. Ahern falsely claims there is no empirical evidence that any company, especially utility companies, would grow at the average rate of the U.S. economy (i.e., GDP). I find this statement puzzling since empirical data supporting utility company growth rates in line with GDP was provided to Ms. Ahern in response to IIWC-IAWC 1.91 and is contained in the Ibbotson 2007 Yearbook-Valuation Edition (p. 92), which Ms. Ahern, herself, cites in her direct testimony. Growth in earnings and dividends have historically been in tandem with the growth in the overall economy (i.e., per capita GDP). Further, it defies logic to suggest that a utility, whose growth is dependent upon service territory growth, could sustain, indefinitely, a growth rate that is greater than that of the overall economy since it is the growth in the economy that feeds a utility’s plant investment and related earnings.

It is not surprising to see current three- to five-year growth rates for water companies in excess of GDP growth in light of the current need for major capital improvement projects. However, this major investment in capital projects is a temporary phenomenon. To rely on these unsustainable growth rates as a proxy for the constant growth rate required by the standard DCF model is to clearly overstate the ROE required by the Company to support its operations.

Q PLEASE COMMENT ON MS. AHEARN'S REJECTION OF YOUR USE OF THE FIVE- TO TEN-YEAR PROJECTED GROWTH RATE IN THE GDP IN YOUR TWO-STAGE DCF MODEL.

A Ms. Ahern states, "There is no evidence that a five- to ten-years growth rate in GDP accurately represents the in perpetuity growth rate in GDP" (IAWC Exhibit 12.10 at 33, lines 892-894). I find Ms. Ahern's line of reasoning here curious as she has advocated strongly for the use of three- to five-year growth rate projections as a proxy for the in perpetuity growth rate of utility companies in her DCF model. Yet, here she calls into question my use of five- to ten-year projections as a proxy for the in perpetuity growth rate in GDP. Not only is this inconsistent, her position is surprising given the stability of GDP growth over time, relative to the instability of a utility's three- to five-year earnings growth outlooks, that are significantly impacted by construction cycles. Once again, I would cite Ibbotson (p. 70) which states "Growth in real GDP (with only a few exceptions) has been reasonably stable over time…" Consequently, the five- to ten-year projected GDP growth rate is a perfectly reasonable proxy for the in perpetuity GDP growth rate.

Q DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A Yes.