

the recording of pension and OPEB costs. Accordingly, the Company is submitting its proposal to utilize an alternative accounting approach for the recording of pension and OPEB costs in accordance with Accounting Instruction 5 of the USOA (adopted by the Commission pursuant to 83 Ill. Adm. Code Section 605.10). That Instruction states that a utility may submit questions of accounting interpretation to the Commission for a decision.

2. In accord with the accounting and rate-making treatment of pension and OPEB costs approved by the Commission in past proceedings (*see, e.g., Illinois-American Water Company*, Docket 07-0507), IAWC presently records in the accrued amount of each respective cost as determined under the applicable accounting standard in USOA Account 604 (for both pension and OPEB cost). The applicable accounting standards are Financial Accounting Board Statement No. 87 (“FAS 87”) in the case of pension cost and Financial Accounting Board Statement No. 106 (“FAS 106”) in the case of OPEB cost. The accrued amounts of each respective cost is based on an actuarial study. The Commission has determined in prior orders that the amounts of pension and OPEB costs accrued for a given year under FAS 87 and FAS 106, respectively, should be recorded (and for a rate case test year recovered in rates) because the FAS 87 and FAS 106 amounts appropriately reflect the amounts of pension and OPEB expense that are associated with utility service provided during the year. *See Illinois-American Water Co.*, Docket 02-0690, Final Order, pp. 24-25.

3. Attachment “A” to this Petition shows the levels of pension and OPEB expense determined in accordance with FAS 87 and FAS 106, respectively, for the years 2000-2008, and on a projected basis for the years 2009-2014. The Attachment shows that pension and OPEB costs are each a recurring cost that exhibits a pattern of fluctuation. In particular, there is a significant increase in each expense in 2009 over the prior level. Also, in each case, the expense

is expected to trend downward subsequent to 2009 through the year 2014.

4. Because pension and OPEB costs recur annually but fluctuate from year to year, each such cost is similar to costs, such as tank painting expense and well and pump maintenance expense, which also recur but fluctuate in amount annually. For these types of fluctuating expenses, the Commission has approved amortization of the expense over a certain period and deferral of the unamortized amount, with the unamortized balance included in rate base. *See Illinois-American Water Co., Docket 07-0507 (tank painting); Illinois-American Water Co., Docket 02-0690 (tank painting); Illinois-American Water Co., Docket 95-0076 (well and pump maintenance); Illinois-American Water Co., Docket No. 90-0100 (deferred maintenance and tank painting).* The Commission has expressly found that such deferrals are properly made under Account 186. *Illinois-American Water Co., Docket 95-0076, Final Order, pp. 11-12.*

5. Due to the pattern of pension and OPEB costs, IAWC proposes reconsideration of the approach used to record pension and OPEB costs for accounting purposes. Specifically, IAWC proposes to account for pension and OPEB costs in a manner similar to that used for other costs that fluctuate in amount from year to year. Commencing with the year 2009, IAWC proposes that the respective annual amount of pension and OPEB currently reflected in rates as approved by the Commission in Docket No. 07-0507 (the “Docket 07-0507 Amount”) would continue to be recorded in Account 604 (pension and OPEB cost). For each respective cost, the amount determined for the year under the applicable accounting standard that is above the Docket 07-0507 Amount of the cost (the “Amortization Amount”) would be amortized over a five year period, and deferred in USOA Account 186. This approach would continue in succeeding years until such time as the Commission approves a return to the prior or other accounting methodology for use in recording these expenses.

6. In the event that the Commission approves the modified accounting methodology proposed by IAWC for pension and OPEB costs, IAWC would propose for rate-making purposes in its pending rate case, Docket 09-0319 (in which IAWC proposes use of a 2010 future test year), to recover for each respective cost: (i) the Docket 07-0507 Amount; (ii) one fifth of each of the 2009 and 2010 Amortization Amounts (with amortization of each cost commencing when the rates approved in Docket 09-0319 take effect); and (iii) a return on the unamortized portion of the 2009 and 2010 Amortization Amounts.¹ As compared to the presently proposed rate-making approach in Docket 09-0319 (to recover the amount of each expense as determined respectively under FAS 87 and FAS 106), use of the alternate rate-making approach proposed by IAWC would reduce the revenue requirement for these costs by \$1,061,543 (pension cost) and \$313,241 (OPEB cost), respectively. In the event that the Commission elects not to approve the revised accounting methodology proposed by IAWC for pension and OPEB costs, IAWC would continue to propose in Docket 09-0319 that rates reflect the respective 2010 amounts of pension and OPEB costs, as is determined under the applicable accounting standard.

7. As discussed above, the Company's proposal to amortize a portion of its pension and OPEB expenses while deferring the unamortized balance is consistent with the Commission's treatment of other expenses that fluctuate in amount, such as tank-painting expense. The Commission has stated that "[f]or ratemaking purposes, the Commission has allowed the deferral and amortization of fluctuating expenses." *Illinois-American Water Co.*, Docket 95-0076, Final Order, p. 22 (granting deferral and amortization of well and pump maintenance costs where, "The evidence indicates that the pattern of expenditures made by the

¹ In the event that this alternative approach is approved by the Commission, it would not cause IAWC to earn more than its allowed rate of return in 2009. The Company's projected earned rate of return on common equity for 2009 is 1.63%. Under the proposed alternative approach, the Company's projected earned rate of return on common equity for 2009 would be 2.25%. The Company's authorized rates of return in 2009, as determined in Docket 07-0507, for common equity is 10.35%.

Company for tank painting is very similar to its pattern of expenditures for well and pump maintenance”). In making this determination, the Commission looks to the “pattern of expenditures made by the Company” for a particular expense category, and allows amortization and deferral where these costs “fluctuate significantly from year to year.” *Id.* The Commission has explained that where there are wide annual fluctuations in an expense, “the amount projected to be expended in any given test year may not be representative of a normal year.” Therefore, “for ratemaking purposes, other methods of calculating such expenses may be used.” *Illinois-American Water Co.*, Docket 02-0690, Final Order, p. 16 (finding that tank-painting expense should be deferred and amortized). In keeping with this principle, the Commission has allowed deferral and amortization of fluctuating expenses. *See, for instance, Illinois-American Water Co.* Dockets 85-0202, 90-0100, 95-0076, 02-0690, and 07-0507.

8. Under the proposed approach, the respective Amortization Amounts of pension and OPEB cost each year would be based on the actual level of expense for the year as determined under the applicable accounting standard. As the forecast data through 2014 on Attachment A shows, there is an expected decline in pension and OPEB cost in future years from the 2010 level. If the proposed approach is adopted for accounting (and in Docket 09-0319 for rate-making) purposes, ratepayers would benefit in the event that the expected decline in cost occurs. Ratepayers would also benefit because, under the proposed approach, the revenue requirement related to pension and OPEB costs in IAWC’s pending rate case would be reduced as shown on Attachment “B”.

WHEREFORE, for all of the reasons set forth above, IAWC respectfully requests that the Commission approve IAWC’s request to modify its method of accounting for pension and OPEB

costs in the manner described above.

September 1, 2009

Respectfully submitted,

ILLINOIS-AMERICAN WATER
COMPANY

By: /s/ Albert D. Sturtevant

One of their attorneys

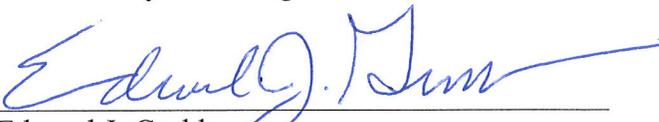
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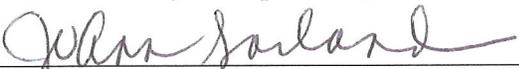
CHI-1718565

VERIFICATION

I, Edward J. Grubb, certify that: (i) I am Assistant Treasurer of Illinois-American Water Company; (ii) I have read the foregoing PETITION; (iii) I am familiar with the facts stated therein; and (iv) the facts are true and correct to the best of my knowledge.


Edward J. Grubb

SUBSCRIBED and SWORN to before
me this 1st day of September, 2009.


Notary Public



My commission expires: April 18, 2011