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**Citizens Utilities Company of Illinois** )  
**d/b/a Citizens Water Resources** )  
)  
**Petition for a Certificate of Public** )  
**Convenience and Necessity to provide** )  
**water and sanitary sewer service to** )  
**parcels in McHenry County, pursuant** )  
**to Section 8-406 of the Public Utilities** )  
**Act; and for approval of contract** )

**CHIEF CLERK'S OFFICE**

**Docket No. 00-0194**

**APPLICATION FOR REHEARING OF CITIZENS UTILITIES COMPANY OF ILLINOIS d/b/a CITIZENS WATER RESOURCES**

**INTRODUCTION**

On February 25, 2000, Citizens Utilities Company of Illinois d/b/a Citizens Water Resources ("Citizens") filed a Petition, pursuant to Section 8-406 of the Public Utilities Act ("PUA"), 220 ILCS 5/8-406, requesting that the Illinois Commerce Commission ("Commission") grant a Certificate of Public Convenience and Necessity authorizing Citizens to provide water and sanitary sewer services to various parcels located in McHenry County, Illinois. The area for which Citizens sought certification comprises approximately 1,444 acres and is located within the corporate limits of the Village of Prairie Grove. Citizens Ex. 2.0 at 4 (Khan). Ancillary to Citizens' request for a certificate, Citizens further requested, to the extent necessary, approval of a related Agreement with Terra Cotta Realty Co. ("Terra Cotta"). This Agreement, in relevant part, provides for refunds to Terra Cotta for the cost of water backbone plant based on new customer connections, in accordance with 83 Ill. Admin. Code Part 600 and Citizens' tariffs on file with the Commission. The Agreement does not contemplate or provide

for refunds of costs incurred by Terra Cotta for construction and installation of sewer supply plant. It is undisputed that the Agreement is the result of an arms' length transaction between Terra Cotta and Citizens, and reflects mutually satisfactory terms and conditions.

The Commission entered its Order in this case on April 25, 2001, granting the requested certificate, but disapproving, in part, the Agreement, because the Commission suddenly and unilaterally decided that it would require Citizens to pay to Terra Cotta "sewer supply plant" refunds.<sup>1</sup> Order at 7. Citizens seeks rehearing of this aspect of the Commission's decision, because it unlawfully purports to extend the water "main extension rule" contained in 83 Ill. Admin. Code § 600.370(a) to sewer facilities,<sup>2</sup> without following the mandatory procedures set forth in the Administrative Procedure Act ("APA") and the PUA. Specifically, the Commission's decision deviates from its prior interpretation of Section 600.370(a) and, for all practical purposes, amends that rule so that it applies to both Citizens in this case and sewer utilities generally, thereby affecting *all* sewer utilities, without giving interested parties notice or the opportunity to respond to the Commission's proposed action. The Commission's decision to unilaterally extend the requirements of Section 600.370(a) to sewer facilities also is contrary to

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<sup>1</sup> In its Findings and Ordering Paragraphs, the Commission states, "the portion of the Petition requesting approval of the Asset Purchase Agreement should be denied." Order at 7. While this statement appears to literally disapprove the Asset Purchase Agreement in its entirety, the decision as a whole appears to reject *only* the sewer supply plant provisions. For example, the body of the Order states, "the Commission concludes that the Agreement with Developer is unreasonable *to the extent* that it fails to require a refund of expenses advanced by Developer for the acquisition of sewer supply plant." Order at 6. In fact, the water provisions of the Agreement were not contested in this case, as Staff urged the Commission to approve those provisions. Staff Init. Br. at 3. In Section IV of this Application for Rehearing, Citizens seeks clarification of this issue.

<sup>2</sup> The phrase "water main extension rule" is being used generically to refer to 83 Ill. Admin. Code § 600.370 as a whole. That section consists of three parts. Subsection (a) addresses water supply (backbone) plant such as wells and storage reservoirs, subsection (b) addresses water mains, and subsection (c) addresses individual water service connections between the main and the property line.

sound policy, because the extension would unnecessarily exert upward pressure on sewer rates. By improperly interfering with a voluntary Agreement between a utility and a developer, the Commission would essentially take money away from consumers (in the form of higher rates) and give it to a developer, even though the developer voluntarily negotiated an agreement (which was in compliance with Citizens' tariffs and standard operating procedures) that expressly provided it would *not* receive that money. In addition to being unlawful, this result is directly contrary to the public interest, prior Commission policy, and the interests of ratepayers.

For these reasons and as further explained below, the Commission should grant rehearing on this issue and revise its decision to approve the Agreement between Terra Cotta and Citizens in its entirety or, in the alternative, to approve the Agreement to the extent it relates to water facilities, while disclaiming jurisdiction to the extent it relates to sewer facilities.

### ARGUMENT

#### **I. THE COMMISSION'S DECISION TO APPLY THE WATER MAIN EXTENSION RULE TO SEWER FACILITIES IN THIS CASE IS PATENTLY UNLAWFUL.**

##### **A. APPLYING THE WATER MAIN EXTENSION RULE TO SEWER FACILITIES IN THIS CASE AMENDS THE COMMISSION'S RULES WITHOUT FOLLOWING THE MANDATORY PROCEDURES OF THE APA.**

The Commission's decision to disapprove, in part, the Agreement between Terra Cotta and Citizens appears to rest on the erroneous conclusion that the Commission's current rules require utilities to provide refunds to developers for sewer investment. Without explanation, the Order summarily states that the Commission "has no difficulty interpreting Section 600.370(a) as also pertaining to sewer supply plant." Order at 6. Even a cursory review of the rule at issue, however, demonstrates that the Order's interpretation is wrong, as it squarely conflicts with the plain language of Section 600.370(a).

As the Commission is aware, rules are to be construed using the same standard that is applied to statutes.<sup>3</sup> "Under the well established rules of statutory construction, the words used in the statute must be given their ordinary and popularly understood meaning, and the relevant language must be read within the context of the entire provision of which it forms an integral part."<sup>4</sup> The plain language of Part 600 and, in particular, Section 600.370, makes it absolutely clear that the water main extension rule applies only to water plant, *not* sewer plant. Specifically, nowhere in the Part 600 rules, let alone Section 600.370 itself, are *sewer* mains, *sewer* utilities or *sewer* facilities ever mentioned. In fact, Part 600 of the Commission's rules is entitled "Standards of Service for *Water Utilities*." Section 600.370 makes numerous references to "water mains," "contracts for . . . water service," "water service line[s]," and "water furnished" by the utility, but it does *not* mention sewer mains or sewer service. Even more specifically, Section 600.370(b) states that "the utility shall extend its *water mains*" under the terms and conditions set forth in that rule. Similarly, Section 600.370(c) states that the utility shall "furnish, install and maintain at its expense the permanent service connection, meter and any other appliance necessary to deliver and measure the *water furnished*." Thus, it is clear beyond question that the express terms of Part 600, including Section 600.370, apply *only* to water utilities, *not* sewer utilities.

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<sup>3</sup> *Villalobos v. F.D.L. Food, Inc.*, 298 Ill.App.3d 132, 138, 698 N.E.2d 243, 247 (2<sup>nd</sup> Dist. 1998).

<sup>4</sup> *Garner v. City of Chicago*, 744 N.E.2d 867, 872 (1<sup>st</sup> Dist. 2001) (citing *Illinois Wood Energy Partners, L.P. v. County of Cook*, 281 Ill.App.3d 841, 850, (1995)).

Given that Section 600.370 addresses only the extension of *water* mains and service, not *sewer* mains and service, it cannot logically or lawfully be interpreted in any other way.<sup>5</sup> As explained above, the rule must be read according to its plain language and in the “context of the entire provision of which it forms an integral part,” which is Part 600. If Section 600.370(a) were intended to apply to the extension of both water *and* sewer mains, the rule obviously would have said so. Indeed, Commission rules that *are* intended to apply to sewer facilities, such as Part 650, expressly use the word “sewer” as opposed to “water.” Similarly, Sections 3-105 and 9-220.2 of the PUA clearly distinguish between sanitary sewer service and water service. It simply is not reasonable to interpret Section 600.370’s references to “water utilities” and “water mains” as somehow encompassing sewer utilities and sewer mains. This conclusion is bolstered by the fact that the Commission traditionally has held that the water main extension rule does *not* apply to sewer facilities, as is discussed in more detail in Part I.B below. *Citizens Util. Co. of Illinois*, Ill.C.C. Docket No. 94-0481, 1995 WL 612576, \*14 (1995) (“The Commission is not prepared to extend the main extension rule to sewer service as proposed by Staff.”).

By ignoring the plain language of Section 600.370 and purporting to extend applicability of that rule to sewer facilities in this case, the Commission has amended its rules without following the proper statutory procedure pertaining to rulemakings as set forth in the APA. Indeed, Section 5-35(a) of the APA expressly provides: “Before the adoption, amendment, or repeal of any rule, each agency *shall* accomplish the actions required by Section 5-40, 5-45, or 5-

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<sup>5</sup> *Central Illinois Public Service Co. v. Pollution Control Bd.*, 165 Ill.App.3d 354, 363, 518 N.E.2d 1354, 1359 (4<sup>th</sup> Dist. 1988) (“Where the language of a regulation is clear and certain, an administrative agency’s interpretation of the regulation which runs counter to the regulation’s plain language is entitled to little, if any, weight in determining the effect to be accorded the regulation.”); *Chicago Transit Authority v. The Industrial Commission*, 144 Ill.App.3d 930, 933, 491 N.E.2d 58, 60 (1<sup>st</sup> Dist. 1986) (“courts will not be bound by an agency’s interpretation of its rules where that interpretation is clearly erroneous, arbitrary, or unreasonable.”).

50, whichever is applicable.” 5 ILCS 100/5-35(a) (emphasis added). Section 5-40, which sets forth the procedures for general rulemaking, provides, *inter alia*: that each agency shall provide notice of the intended action to the general public, including the text of the proposed rule; a description of the subjects and issues involved; an initial regulatory flexibility analysis; and the “time, place, and manner in which interested persons may present their views and comments concerning the proposed rulemaking.” 5 ILCS 100/5-40.

The Commission has done none of the things required by the APA in this case—and it is obvious that the Commission’s decision to extend applicability of Section 600.370(a) will affect all sewer utilities, not just Citizens. Yet, neither Citizens nor these “interested persons” were given proper notice of the “time, place, and manner” in which they could “present their views and comments.” While the Commission certainly has the right to initiate a rulemaking to consider whether Section 600.370(a) should be amended to apply to sewer facilities, it must give affected sewer utilities notice and the opportunity to respond to the Commission’s proposed action for any decision it reaches to be lawful. Ironically, the Commission itself has previously (and correctly) acknowledged that a “generic docket *is* the appropriate venue to examine whether the main extension rule should apply not only to [Citizens], but also to other sewer utilities.” *Citizens Util. Co. of Illinois*, Ill.C.C. Docket No. 94-0481, 1995 WL 612576, \*14 (emphasis added). Inexplicably, however, the Commission now disregards the proper procedures for amending its rules and purports to change Section 600.370 in this certificate case. The Commission, however, is not free to disregard the mandatory procedures of the APA in this manner and, accordingly, should grant rehearing and correct its error.

**B. APPLYING THE WATER MAIN EXTENSION RULE TO SEWER FACILITIES UNLAWFULLY DEVIATES FROM THE COMMISSION'S PAST PRACTICE AND INTERPRETATION OF SECTION 600.370.**

The Commission traditionally has interpreted Section 600.370 as applying only to water, *not sewer* facilities. In *Citizens Util. Co. of Illinois*, the Staff of the Illinois Commerce Commission ("Staff") similarly proposed that the Commission broaden the scope of Section 600.370 by applying the water main extension rule to sewer service. The Commission expressly and correctly rejected that proposal, finding:

[T]he Company has convinced the Commission that the proposed sewer main extension rule need not be applied to the Company. The Commission is not prepared to extend the main extension rule to sewer service as proposed by Staff. A generic docket is the appropriate venue to examine whether the main extension rule should apply not only to the Company, but also to other sewer utilities.

*Id.* at \*14. It cannot credibly be denied that the Commission traditionally has applied Section 600.370 only to water facilities and *not* sewer facilities. In fact, Staff's own testimony confirms that the Commission has traditionally treated sewer utilities differently from other utilities with respect to refunds, and has done so precisely because of the high level of investment per customer needed to provide sewer service. Staff. Ex. 2.0 at 12.

The Commission's decision to deviate from its prior interpretation of Section 600.370 and apply the water main extension rule to sewer facilities is unlawful because it alters the Commission's past practice without following the mandatory procedures set forth in Section 10-101 of the PUA.<sup>6</sup> That Section provides, in relevant part:

Any proceeding intended to lead to the establishment of policies, practices, rules or programs applicable to more than one utility may, in the Commission's

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<sup>6</sup> The rulemaking procedures required by Section 10-101 and the APA are generally designed to protect the due process and equal protection interests of all potentially affected persons or entities under the Illinois and United States Constitutions. Because the Commission has failed to follow these procedures, it should also grant rehearing and revise its Order to avoid violating the constitutional rights of Citizens and/or other sewer utilities.

discretion, be conducted pursuant to either the rulemaking or contested case provisions, *provided such choice is clearly indicated at the beginning of such proceeding and subsequently adhered to.* (emphasis added).

220 ILCS 5-10-101; *See Business and Prof'l People for the Pub. Interest v. Commerce Comm'n*, 136 Ill.2d 192, 226; 555 N.E.2d 693 (1989). As discussed above, the Commission's decision to apply the water main extension rule to sewer utilities will obviously apply to Citizens as well as other sewer utilities and, therefore, compliance with Section 10-101 is mandatory. *Id.* (“[t]he Commission may alter or amend its past practice, but it must follow the procedures set forth in its rules and the Act.”) (citing 220 ILCS 5/10-101).

Under Section 10-101, whenever the Commission intends to establish new policy or rules that are applicable to more than one utility, it must do so pursuant to either a rulemaking or contested case proceeding.<sup>7</sup> With respect to the latter approach, the Commission must make its intention to establish a new policy or rule known *upfront*. 220 ILCS 5/10-101. In this case, the Commission's intention to establish a new policy with respect to Section 600.370 was not apparent at the outset of this case and, in fact, no other sewer utilities participated or had any reason to even be aware of the proceeding. This clearly violates Section 10-101 of the PUA. Notably, the Illinois Supreme Court held that the Commission violated Section 10-101 when it altered its past practice concerning test-years in ratemaking proceedings by establishing and immediately applying a new test-year standard in a contested case, without following the procedures of Section 10-101 or amending its rules pursuant to the APA procedures discussed in Part I.A above. *Business and Prof'l People for the Pub. Interest*, 136 Ill.2d at 226, 555 N.E.2d at

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<sup>7</sup> *People v. Commerce Commission*, 239 Ill.App.3d 368, 390, 606 N.E.2d 1283, 1298 (2<sup>nd</sup> Dist. 1993) (“We further agree that policies applicable to more than one utility must be set in accord with Section 10-101 of the Act.”).

708-709. The Commission's decision in this case to apply the water main extension rule to sewer facilities similarly violates Section 10-101 of the PUA.

Even putting aside the requirements of Section 10-101 of the PUA, Illinois common law provides that "[a]n agency may be bound by its own established custom and practice as well as by its formal regulations," and "may not deviate from such prior rules of decision on the applicability of a fundamental directive without announcing *in advance* its change in policy." *Illinois Bell Tel. Co. v. Allphin*, 95 Ill.App.3d 115, 125, 419 N.E.2d 1188, 1198 (1<sup>st</sup> Dist, 1981) (emphasis added); *Gatica v. Dept. of Public Aid*, 98 Ill.App.3d 101, 107, 423 N.E.2d 1292, 1296 (1<sup>st</sup> Dist. 1981). An administrative agency simply cannot *arbitrarily or capriciously* disregard its prior customs and practices, including its *prior interpretation of rules*, as the Commission has done here. *Alton Packaging Corp. v. Pollution Control Bd.*,<sup>8</sup> 146 Ill.App.3d 1090, 1094, 497 N.E.2d 864, 866 (5<sup>th</sup> Dist. 1986) ("administrative bodies are bound by prior custom and practice in interpreting their rules and may not arbitrarily disregard them.")<sup>9</sup> In fact, in *Central Illinois*

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<sup>8</sup> In *Alton Packaging Corp.*, the court reversed the Pollution Control Board's dismissal of a petition for failure to prosecute with diligence, holding that the Board had improperly departed from its past precedent of first ordering a matter to hearing whenever it perceived delay in prosecution of a case.

<sup>9</sup> See also *United Cities Gas Co. v. Commerce Comm'n*, 163 Ill.2d 1, 27-28, 643 N.E.2d 719, 732 (1994) (While the Commission it not prohibited from changing its policies, it may not do so in an arbitrary or capricious manner); *United Cities Gas Co.*, 225 Ill.App.3d at 782, 587 N.E.2d at 588 (Commerce Commission may not depart from prior practices and customs in interpreting their procedural rules, especially where there may have been detrimental reliance on the agency's prior interpretation of its rules.); *Chicago Transit Authority v. The Industrial Commission*, 491 Ill.App.3d at 933, 491 N.E.2d at 60 ("An agency's interpretation of its own rules also binds the agency as its policy and must be followed by the agency."); *Gatica v. Dept. of Public Aid* 98 Ill.App.3d 101, 423 N.E.2d 1292 (1981) ("An agency which has changed a previously existing construction, or application of a rule, or an informal practice, may be bound thereby as a result of the previous custom."); *Holland v. Quinn*, 67 Ill.App.3d 571 (1978) ("An administrative agency's custom and practice in interpreting its rules may bind the agency."); *Harris-Hub Co., Inc. v. Pollution Control Bd.*, 50 Ill. App.3d 608, 613, 365 N.E.2d 1071, 1075 (1<sup>st</sup> Dist. 1977) (An agency is bound to follow its own procedures and practices. "This principle is applicable to rules, practices, procedures and interpretations by administrative agencies.").

*Public Service Co.*, the court held that an administrative agency could not lawfully depart from long-established constructions of regulations, absent significant changes in circumstances. 165 Ill.App.3d at 363, 518 N.E.2d at 1359.<sup>10</sup>

As explained above, the Commission's decision to apply Section 600.370(a) to sewer utilities in this case is a drastic deviation from its prior practices and interpretation of that rule as articulated in *Citizens Util. Co. of Illinois* (at \*14). As a matter of law, the Commission is not free to arbitrarily change that interpretation without, at a minimum, giving affected parties *advance* notice of its intention to do so. The Commission's conclusory assertion that its decision in Docket No. 94-0481 is somehow not controlling in this case is a red herring, and we urge the Commission to carefully review that decision. If it does so, we have no doubt that the Commission will recognize that its decision in Docket No. 94-0481 unequivocally reflects the Commission's past practice and interpretation of Section 600.370—that it does *not* apply to sewer utilities or facilities—and that past practice and interpretation cannot be arbitrarily changed. This is particularly true where, as here, there has been no change in circumstances since the Commission's 1995 decision in Docket No. 94-0481. The Commission's sudden departure from its past practice and interpretation of Section 600.370 is arbitrary, capricious and unlawful, and it should be reversed on rehearing.

It is also significant that, if an administrative agency seeks to depart from past practices, it is required "to articulate a reasoned basis for its sudden departure" from past precedent.

*Citizens Util. Bd. v. Commerce Comm'n*, 166 Ill.2d 111, 132; 652 N.E.2d 1089 (1995), *reh'g*

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<sup>10</sup> In *Central Illinois Public Service Co.*, the court stated, "[i]n view of the lack of changed circumstances which would support the Agency's unprecedented decision to include the 6.0 pounds/mbtu sulfur dioxide emission limitation in CIPS' August 1986 operating permit for its Meredosia generating unit, we hold that the Agency is bound by its prior policy of *not* subjecting that facility to a 6.0 pounds/mbtu sulfur dioxide emission limitation."

denied; *Reich v. Interstate Brands Corp.*, 849 F.Supp. 1261, 1263 (C.D. Ill. 1994) (“[W]hen an agency changes its interpretation of an established regulation, it must provide a reasoned analysis for the change.”) Any decision by an administrative agency that fails to articulate a reasoned basis for departing from past practices cannot be upheld. *United Cities Gas Co. v. Commerce Comm’n*, 225 Ill.App.3d 771, 782-783, 587 N.E.2d at 581, 588-589 (4<sup>th</sup> Dist. 1992).

For example, in *United Cities Gas Co.*, the court recognized that the Commission is not precluded from “changing its rate-making policy by excluding flotation costs attributable to unissued securities from the expenses utilities may recover from their customers,” “provided the ICC stated a basis for such a holding.” In that case, however, the court overturned the Commission’s decision, because “the ICC provided no findings to support its departure” and “did not state any reasons which support its decision to depart” from its prior rate-making policy. Similarly, in *Chemetco, Inc. v. Pollution Control Bd.*, 140 Ill.App.3d 283, 288-289, 488 N.E.2d 639, 643 (5<sup>th</sup> Dist. 1986), the court stated, “although we find that an administrative agency may alter its past interpretation and overturn past administrative rulings and practice . . . such abrupt shifts constitute ‘danger signals’ that the Board may be acting inconsistently with its statutory mandate. Thus, at the very least, a reasoned analysis is required, indicating that prior policies and standards are being deliberately changed, not casually ignored.” In *Chemetco*, the court ultimately held that the administrative order failed to provide an “adequate analysis necessary to justify such a shift.” *Id.*

Like the administrative decisions overturned in *United Cities Gas Co.* and *Chemetco*, the Commission’s decision here falls far short of articulating any basis, let alone a reasoned basis, for its departure from its prior interpretation of Section 600.370. Indeed, the Commission’s Order provides *no* findings or reasons that could support its departure from its prior

interpretation of Section 600.370. Rather, the Order makes conclusory, unsupported assertions that consumers somehow will be harmed, and Citizens unjustly enriched, unless the water main extension rule is applied to sewer facilities. However, the Commission's conclusory statements have no record support, are factually wrong and fail to articulate a reasoned basis for its decision. *See Citizens Util. Bd.*, 166 Ill.2d at 126, 131-32 (rejecting arguments that sharing of coal tar remediation expenses should be imposed "simply as a matter of 'public policy'" or due to the Commission's need to make a "blunt policy decision."). In fact, as explained below, the Commission's decision will *harm*, rather than benefit, consumers.

In sum, the Commission's decision to apply the water main extension rule to sewer facilities is an arbitrary, capricious and unreasonable deviation from the Commission's past practice and interpretation of that rule. Accordingly, the Commission should grant rehearing on this issue and correct its error.

**C. ANY CHANGE IN THE COMMISSION'S RULES, POLICIES OR PRACTICES CAN BE APPLIED ONLY PROSPECTIVELY, AND NOT APPLIED TO CITIZENS IN THIS CASE.**

Even assuming that the Commission could properly amend Section 600.370 without following the procedures set forth in the APA and the PUA (which it cannot), its new rule could lawfully apply only on a *prospective* basis and, therefore, could have no effect on the Agreement between Citizens and Terra Cotta in this case. *Heckler v. Community Health Services of Crawford County, Inc.* 467 U.S. 51, 61, 104 S.Ct. 2218, 2224 (1984). This is because "an administrative agency may not apply a new rule retroactively when to do so would unduly intrude upon reasonable reliance interests." *Id.* See also *Gonzales-Blanco, M.D. v. Clayton*, 110 Ill.App.3d 197, 204, 441 N.E.2d 1308, 1314 (1<sup>st</sup> Dist. 1982) ("Although an administrative agency may change its rules and practices, it may apply its rules retroactively only in the proper cases.") Factors to consider in determining whether a newly adopted regulation can be applied

retroactively include: (1) whether the agency action results in injury or substantial prejudice; (2) whether the case is one of first impression; (3) whether the regulation represents an abrupt departure from well-established practice; (4) the extent to which the party against whom the new regulation is applied relied on the former regulation; and (5) the degree of burden imposed upon that party. *Gonzales-Blanco, M.D.*, 110 Ill.App.3d at 204, 441 N.E.2d at 1314; *Shapiro v. Regional Board of School Trustees*, 166 Ill.App.3d 397, 409, 451 N.E.2d 1282, 1290 (1<sup>st</sup> Dist. 1983).

Applying these factors to the case at bar clearly establishes that this is a proceeding in which retroactive application of the Commission's new interpretation of Section 600.370 is *not* appropriate. With respect to the first factor, the Commission's newly-adopted interpretation of Section 600.370 will unquestionably result in "injury or substantial prejudice." As explained further in Part II below, the Commission's decision interferes with a voluntarily negotiated Agreement between Terra Cotta and Citizens, to the detriment of Citizens and its sewer customers. As a matter of logic, all of the agreed-upon terms in a negotiated agreement are dependent upon each other and are the result of the normal give and take of negotiation. An individual term or condition may be a "give" based on a "take" on another term. The Commission's decision ultimately disregards this process, and the fact that the terms of the final agreement were mutually satisfactory. Instead, the Order grants Terra Cotta additional benefits that it did not bargain for, while taking away from Citizens and its customers rights that Citizens negotiated. Furthermore, unless the Commission's decision is changed on rehearing, *ratepayers* will ultimately pay the price for this regulatory interference, in the form of increased rates. Citizens Ex. 1.1 (Scheppmann) at 4.

With respect to the remaining factors, the Commission, as recently as 1995, *in a proceeding involving Citizens*, addressed the issue of whether Section 600.370 should apply to sewer utilities and held that it should not. In that case, the Commission rejected a proposal made by Staff similar to the one made here, holding that Citizens should *not* be required to adopt sewer main extension rules which mirror those applicable to water utilities. *Citizens Util. Co of Illinois*, at \*14. The Commission's decision to apply Section 600.370(a) to sewer facilities in this case is obviously a drastic departure from its decision in Docket No. 94-0481, and will place a substantial burden on Citizens and its ratepayers if applied retroactively. Citizens unquestionably negotiated the Terra Cotta Agreement with the Commission's past practices and interpretation of Section 600.370 in mind. This reliance was fully justified in light of the Commission's decision in Docket No. 94-0481.

In sum, evaluation of the above factors demonstrates that, even if the Commission's new interpretation of Section 600.370 were lawful (which it is not), retroactive application of that new interpretation to Citizens in this case would be improper. Therefore, the Commission should grant rehearing on this issue and revise its Order accordingly.

**D. THE COMMISSION'S DECISION IS NOT SUPPORTED BY RECORD EVIDENCE.**

The Commission's decision on the sewer refund issue is also unlawful because it is not supported by record evidence. *See Citizens Util. Bd.* 166 Ill.2d at 132-133; 652 N.E.2d at 1100. Among other things, the Commission's assertion that Citizens will somehow be unjustly enriched by "gain[ing] \$1,439,350 in sewer plant value without any corresponding investment" (Order at 6) has no record support and ignores the evidence demonstrating the significant investment Citizens makes in sewer facilities.

More specifically, the Commission's "unjust enrichment" theory erroneously rests on the unsupported assumption that the \$1,439,350 figure represents *sewer treatment facilities* being acquired from Terra Cotta. To the contrary, the unrefuted evidence establishes that the \$1,439,350 figure represents *gross sewer plant* (collection and treatment) being acquired (Citizens Ex. 1.1 (Scheppmann) at 5), not just sewer treatment facilities, as the Commission's decision suggests. Order at 5-6. Further, as explained by Mr. Scheppmann, Citizens does not earn a return on the *gross* utility plant, but only on *net* plant (Tr. at 34). Thus, Citizens will *not* earn a return on the \$1,439,350 of contributed plant and will *not* be "unjustly enriched."

Perhaps more importantly, the unrefuted evidence also establishes that Citizens invests a substantial amount of money in additions, rehabilitation and improvement of the facilities that it acquires. Tr. at 34. For example, using the 1999 data in the record, the \$1,439,350 figure cited in the Order (which, as stated above, constitutes gross sewer plant) only represents approximately 1.5% of Citizens' \$94,018,482 in Gross Sewer Utility Plant In Service. Citizens Ex. 1.1 (Scheppmann) at 5. Citizens' 1999 Annual Report on file with the Commission also reflects \$45,895,665 in Net book *cost* of sewer facilities. Citizens Ex. 1.1 (Scheppmann) at 5. Thus, the record clearly establishes that Citizens *is* making a significant continuing investment in sewer facilities, and *will not* be "unjustly enriched" if the Agreement with Terra Cotta is approved as filed. The Commission's conclusion to the contrary has absolutely no record support and, therefore, cannot withstand legal scrutiny.

It is worth noting again that the Order ignores Staff's *own* evidence that sewer utilities have traditionally been treated differently from other utilities with respect to refunds precisely because of the high level of investment per customer needed to provide sewer service. Staff. Ex. 2.0 at 13. The Order also ignores Citizens' undisputed testimony that its regular practice is to

receive contributions of sewer facilities from developers and not to include sewer refund provisions in the contracts it negotiates. Citizens Ex. 1.1 at 5. Simply put, Citizens' Agreement with Terra Cotta is consistent with Citizens' own past practices and agreements with other developers that have contributed sewer facilities for many years. Because there is nothing in this case to justify a different result, the Commission should approve the Agreement in its entirety.

In sum, because the Commission's decision is not supported by substantial evidence in the record, it is legally indefensible. *Citizens Utilities Bd.*, 166 Ill.2d at 126, 132-133, 651 N.E.2d at 1097, 1100 (Commission's decision reversed by Illinois Supreme Court where it was "not supported by substantial evidence based on the entire record of evidence."); *People v. Commerce Comm'n*, 239 Ill.App.3d 368, 376, 606 N.E.2d 1283, 1289 (2<sup>nd</sup> Dist. 1993) (The reviewing court should reverse the Commission's order where its findings are not supported by substantial evidence in the record); *Moncada v. Commerce Comm'n*, 212 Ill.App.3d 1046, 1051, 571 N.E.2d 1004, 1008 (1<sup>st</sup> Dist. 1991) (Reviewing court can reverse if the ICC's decision is not based on substantial evidence). This is yet another compelling reason why the Commission should grant rehearing and revise the Order.

## **II. THE ORDER IS UNSOUND AS A MATTER OF POLICY.**

In addition to having no basis in the law or the record, the Order is misdirected from a policy perspective, because it will adversely affect Citizens, sewer utilities throughout the state and, most importantly, their ratepayers.

As the record demonstrates, increased investment in sewer facilities will unavoidably exert upward pressure on sewer rates charged to customers. Citizens Ex. 1.1 (Scheppmann) at 4. The attached affidavit of Reed T. Scheppmann illustrates the magnitude of the rate increase that can be expected if the Commission's decision is not changed. Specifically, in order to ultimately provide sewer service to the customers located in the area for which Citizens has received

certification in this case, 1.00 mgd of sewage treatment capacity will have to be constructed at a cost of approximately \$8,000,000.<sup>11</sup> Under the Order as written, Citizens would be required to incur the cost of building this additional plant. As explained in Mr. Scheppmann's affidavit, this added expense likely would increase the monthly charge for all of Citizens' sewage treatment customers by 66%. In fact, if the cost of this additional plant were not spread across all of Citizens' sewage treatment customers and were recovered only from Terra Cotta customers, the rate increase likely would be 240%.

Significantly, these figures do not even include the impact on rates caused by any additional investment Citizens may be required to make in sewer mains or sewer service connections. Neither do they illustrate the cumulative effect the Commission's newly-adopted policy would have on sewer rates throughout the state. Indeed, if Citizens and other sewer utilities are required to incur the cost of sewer plant investment each time expansion is necessary or a new housing development is built, sewer rates will continually rise. And, even putting aside the increase in rates, as a practical matter every sewer utility would be forced to seriously consider filing a request for a rate increase every time it incurred costs to expand sewer plant, thereby adding numerous rate case filings to the Commission's workload.

The unreasonable negative impact of the Commission's Order becomes even more apparent upon examination of the effect it would have on Citizens' investment per customer. As explained in the Affidavit of Mr. Scheppmann, Citizens' Year 2000 Annual Report to the Commission indicates that the Company's Net Book Cost for all sanitary sewer facilities (collection and treatment) was \$41,651,659. The total number of sewer customers (collection and treatment) was 35,141. Accordingly, the average Net Book Investment per customer was

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<sup>11</sup> Based on its experience, Citizens believes that it is likely that a 1.00 mgd plant will have a

\$1,185 (\$41,651,659 divided by 35,141). Under the Commission's decision, the investment per customer would drastically increase. Specifically, requiring Citizens to incur the cost of the \$8,000,000 investment in 1.0 mgd of plant capacity for an estimated 2,857 Terra Cotta customers would result in an average investment per customer of \$2,800 (\$8,000,000 divided by 2,857). This \$2,800 average investment per customer is 236% greater than the average investment per customer of \$1,185 for all sewer customers reported in Citizens' Year 2000 Annual Report. The unreasonableness of the Commission's Order forcing this drastic increase in investment per customer should be self-evident.

In contrast with the financial arrangement the Order would force upon Citizens and Terra Cotta, the negotiated Agreement with Terra Cotta would not put upward pressure on sewer rates and would not drastically increase the average investment per customer. Citizens Ex. 1.1 at 4. Indeed, the negotiated Agreement would allow Citizens to operate in a manner consistent with its past practice of having developers regularly contribute sewer treatment facilities, which would insure reasonable and stable sewer rates. As a matter of policy, the Commission should refrain from burdening sewer customers with the cost of constructing and installing sewer supply plant, as the Order does. This is particularly true where, as here, the developer is both willing to incur those costs, and has voluntarily agreed to do so.

Additionally, the costs at issue here benefit only new development and therefore should be borne by the developer, not sewer customers as a group. As noted above, Terra Cotta voluntarily entered into an Agreement that requires *it* to bear the cost of constructing and installing sewer plant—not Citizens or Citizens' sewer customers. Section 1-102(d)(iii) of the PUA declares one goal of regulation to be that “the cost of supplying public utility services is

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total project cost of approximately \$8,000,000.

allocated to those who cause the costs to be incurred.” Citizens’ agreement with Terra Cotta is consistent with this goal. By way of contrast, the Order, which inevitably would require higher rates for customers, plainly is not.

Equally significant, the Commission’s decision improperly alters an Agreement that was entered into by willing parties under mutually agreeable terms. The Agreement between Terra Cotta and Citizens was the result of arms’ length negotiations between two experienced parties. Citizens Ex. 1.0 at 8. Terra Cotta and Citizens negotiated these terms over a period of time, and each party was represented by experienced business persons and legal counsel. Citizens Ex. 1.1 at 5-6. If the terms of the Agreement were not satisfactory to Terra Cotta, or would somehow “unjustly enrich” Citizens, Terra Cotta could have chosen to provide the services itself or negotiate with another utility. Citizens Ex. 1.0 at 8. Tellingly, Terra Cotta chose not to do so.

Moreover, as stated above, Citizens’ Agreement with Terra Cotta is consistent with its past practices—that is, other developers have regularly contributed similar facilities. The Commission’s decision nevertheless attempts to substitute its judgment for that of Terra Cotta’s experienced management. As a matter of policy, the Commission should be wary of such an approach, since it should not be in the business of protecting the theoretical interests of developers at the expense of customers. By unilaterally altering the Agreement, the Commission “unjustly enriches” Terra Cotta, deprives Citizens of the benefits of its negotiated contract with Terra Cotta, and ultimately places these additional costs (costs that Terra Cotta is willing to incur) on sewer treatment customers. The Order is also inconsistent with the record evidence, which demonstrates that municipally-owned utilities generally require developers to contribute sewer facilities and an additional amount toward backbone plant. Staff Ex. 2.0 at 12.

In sum, the record clearly demonstrates that the Agreement is in the best interest of ratepayers, and Staff has presented no evidence to the contrary. Citizens Ex. 1.0 at 10-11. Therefore, the Commission should grant rehearing of this issue and revise its Order to approve the Agreement between Terra Cotta and Citizens in its entirety.

**III. APPROVAL OF THE SEWER-RELATED PORTIONS OF THE AGREEMENT IS NOT REQUIRED UNDER THE PUA.**

Putting aside the legal infirmities and negative policy implications of the Commission's decision, approval of the sewer-related portions of the Terra Cotta Agreement is not required under the PUA. For that reason, the Commission's decision purporting to disapprove that portion of the Agreement is wholly unnecessary.

In its petition, Citizens requested, as a matter of administrative efficiency, Commission approval of the Agreement only "to the extent necessary." Petition ¶ 1. Citizens' request for approval of the Agreement was limited to approval of the provisions relating to water facilities, which Staff agrees should be approved (Staff Init. Br. at 3). This request was limited because approval of the Agreement's provisions concerning sewer facilities is not required under the PUA or existing Commission rules. Specifically, Section 600.370(a) provides:

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

While under certain circumstances Section 600.370 requires approval of contracts concerning water facilities, Commission approval of provisions concerning sewer facilities is not necessary.

As discussed above, Section 600.370 does not, either by its express terms or under the Commission's traditional interpretation, apply to sewer facilities or sewer utilities.

The primary purpose of Citizens' Petition was to seek a Certificate of Public Convenience and Necessity to enable it to serve certain parcels in McHenry County, and Citizens' request for approval of the Agreement, to the extent necessary, was ancillary. Citizens' request described the Agreement with Terra Cotta as "an Asset Purchase Agreement . . . with the property owner, Terra Cotta, to acquire existing water and sewer facilities to serve the parcels for which certification is requested." Petition, ¶ 2. The Commission's statutory authority to approve a public utility's transactions does not extend to asset acquisitions in general, or to asset acquisitions from real estate developers such as Terra Cotta, in particular. *See* 220 ILCS 5/7-102. The primary purpose of requiring Commission approval of certain public utility transactions, especially those involving a public utility's transfer or encumbrance of its assets, is to protect the customers' quality of service. In this case, Citizens seeks merely to acquire sewer facilities so that customers located in the areas for which Citizens has received certification will, in fact, be able to receive such service. This point, however, is lost in the Order. Rather, the Order chooses unnecessarily to assert jurisdiction and disapprove the Agreement based upon assertions made by Staff that have no factual or legal basis. In doing so, the Order ignores the unrefuted evidence that Terra Cotta is a sophisticated real estate developer and that the Agreement will benefit Citizens' customers.

Because there is no statutory mandate that the Commission review, approve or disapprove the Agreement's provisions relating to sewer plant costs, the Commission should grant rehearing on this issue and decline to assert jurisdiction over the provisions of the Agreement insofar as it relates to sewer facilities.

**IV. AT A MINIMUM, THE COMMISSION SHOULD CLARIFY THAT THE ORDER APPROVES THE WATER PROVISIONS OF THE AGREEMENT.**

Even if the Commission does not grant rehearing on the sewer refund-related issue, it should, at a minimum, clarify the fact that all other provisions of the Agreement between Terra Cotta and Citizens are approved. The only contested issue in this case relates to the sewer provisions of the Agreement, as Staff supports approval of the Agreement regarding the water supply facilities and distribution system. Staff. Init. Br. at 3. The Findings and Ordering Paragraphs, however, read literally, appear to disapprove the Asset Purchase Agreement in its entirety. That Section of the Order states, “the portion of the Petition requesting approval of the Asset Purchase Agreement should be denied.” Order at 7. In contrast to the Findings and Ordering Paragraphs, the body of the Order clearly indicates the Commission’s intent to disapprove *only* the sewer provisions of the Agreement, as it states that “the Commission concludes that the Agreement with Developer is unreasonable *to the extent* that it fails to require a refund of expenses advanced by Developer for the acquisition of sewer supply plant.” Order at 6. Accordingly, the Commission, at an absolute minimum, should clarify that it approves the water provisions of the Agreement.

**CONCLUSION**

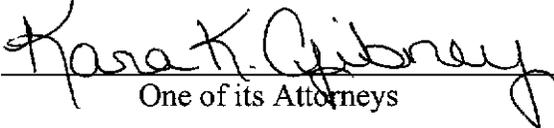
The Commission’s Order unlawfully purports to extend 83 Ill. Admin. Code 600.370(a) to sewer supply facilities, without following the mandatory procedures set forth in the APA and PUA. Specifically, the Commission’s decision deviates from its prior interpretation of Section 600.370(a) and, for all intents and purposes, amends that rule to apply to Citizens and all other sewer utilities without giving interested parties notice or the opportunity to respond to the Commission’s proposed action. Extending the requirements of Section 600.370(a) to sewer utilities also is contrary to sound policy, because it interferes with a voluntarily negotiated

agreement between Terra Cotta and Citizens that requires Terra Cotta to contribute the sewer plant. Perhaps most importantly, ratepayers ultimately will pay the price of the Order's unlawful new approach to sewer supply plant refunds. Unless revised in accordance with Citizens' Application for Rehearing, the Commission's Order will require drastically increased sewer treatment rates for customers, handing over the revenue generated to developers.

For these reasons, the Commission should grant rehearing in this case and revise its Order to approve the Agreement between Terra Cotta and Citizens in its entirety, or to approve the provisions relating to water service and disclaim jurisdiction over the mutually agreed provisions related to sewer plant.

Respectfully submitted,

CITIZENS COMMUNICATIONS COMPANY

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Dated: May 24, 2001.

**CERTIFICATE OF SERVICE**

I, Kara K. Gibney, hereby certify that on this 23rd day of May, 2001, I caused the foregoing Application for Rehearing and Affidavit of Reed Scheppmann to be served on all parties listed below by either facsimile, messenger or U.S. mail.



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