REBUTTAL TESTIMONY
ON REHEARING

of

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Camelot Utilities, Inc.
Great Northern Utilities, Inc.
Lake Holiday Utilities Corporation

Proposed General Increase in Water and Sewer Rates

Docket Nos. 11-0059/11-0141/0142 (Cons.) on Rehearing

February 23, 2012

Table of Contents

INTRODUCTION

Q. Please state your name and business address.

A. My name is Philip Rukosuev. My business address is 527 East Capitol Avenue, Springfield, Illinois 62701.

Q. Are you the same Philip Rukosuev who provided direct testimony on rehearing in this case?

A. Yes.

Q. What is the purpose of your rebuttal testimony on rehearing?

A. I am responding to the direct testimony on rehearing of Utilities, Inc. ("UI") witness Ms. Lena Georgiev, and People of the State of Illinois ("AG") witnesses Mr. Michael Brosch and Mr. Scott Rubin pertaining to the issues I raised in my direct testimony on rehearing addressing the issue of rate shock in this proceeding. (ICC Staff Ex. 17.0.)

For purposes of this testimony, I refer to Camelot Utilities, Inc ("CU"), Great Northern Utilities, Inc. ("GNU"), and Lake Holiday Utilities Corporation ("LH") collectively as the "Companies" or "UI."

Q. Please summarize the AG witness Brosch's and AG witness Rubin's positions in this phase of the proceeding.

A. AG witness Brosch offers a method to ease the rate shock that led the Commission to grant rehearing in this proceeding. Specifically, Mr. Brosch presents a method to phase-in the authorized rate increases. (AG Ex. 2.0 Rhg, p. 5-17.) AG witness Rubin recommends that the Commission initiate an investigation into UI's Illinois operations, including all operating companies, to determine whether other rate mitigation options, including rate or revenue consolidation, would be achievable and in the public interest. Mr. Rubin also recommends that the Commission direct UI to prepare and file a cost of service study ("COSS") for its entire Illinois operation for its review and use in the investigation. (AG Ex. 3.0 Rhg, p. 4)

Q. Please summarize the arguments by the UI witness.

A. In general, UI witness Georgiev believes that the long term consequences of any phase-in plan are fiscally unsound and overwhelmingly negative. (UI Direct Testimony on Rehearing, at 1.) However, if the Commission approves a phase-in plan in this proceeding, Ms. Georgiev proposes the following conditions: (1) The phase-in period for any plan should be no longer than 3 years; (2) The carrying costs on the unrecovered costs for each Company should be set at granted cost of capital, which is 7.71%, not the cost of debt; (3) If the Companies need to file a rate case during the phase-in period, the Companies should be able to recover the outstanding carrying costs and interest as well as outstanding phase-in revenues; (4) The phase-in plan should only be voluntary; and (5) the phase-in plan should include an adjustment to incorporate the increase in future uncollectibles. (*Id.,* at 6-7.)

STAFF'S RESPONSE TO AG WITNESS RUBIN

Q. What does AG witness Rubin specifically state with respect to his consolidation and cost of service proposals?

A. Mr. Rubin states the following:

> In addition to providing immediate rate relief for the affected customers (such as through the adoption of AG witness Brosch's phase-in plan), I recommend that the Commission initiate an investigation into UI's system-wide cost of service, including an evaluation of possible statewide consolidation options. As part of that investigation, the Commission should direct UI to prepare and file a cost of service study for its entire Illinois operation. (AG Ex. 3.0 Rhg, Page 7.)

Q. What is your response to Mr. Rubin's consolidation proposal?

A. Generally speaking, I agree with Mr. Rubin's recommendation for a number of reasons. In my direct testimony on rehearing, I stated the following with respect to consolidation:

> <u>[T]he Commission should encourage UI to seriously consider some form of consolidation of its 23 water and wastewater subsidiaries in Illinois.</u> Consolidation would create increased efficiencies and has proven successful for other water utilities (For example, Aqua Illinois and Illinois American Water Company have consolidated its separate water and sewer divisions over the years.) Consolidation may also be beneficial for UI customers because not only may it protect them against dramatic rate increases but is also useful to address smaller system viability issues. Customers will also benefit from decreased rate case and administrative expenses due to the UI's ability to file single, consolidated rate cases for its many water and sewer operations. (ICC Staff Exhibit 17.0, pp. 10-11, emphasis added)

While it is legally permissible for UI to consolidate its operations, the Commission must ensure that UI's customers are treated properly under any such consolidation. Because some UI subsidiaries have high rates while others have lower rates, combining rates across UI subsidiaries would likely benefit customers of the former and harm customers of the latter. Thus, any consolidation proposal must be weighed carefully to ensure that no group of customers is unduly harmed.

By combining the data and information of the 23 utilities, consideration should be given to the historic costs which are the foundations of current rates. Because of the importance the Commission places on having reliable information and its interest in fostering cost-based rates, the Commission cannot disregard the embedded costs upon which the subsidiaries' current rates are based merely because a possible consolidation of UI service territories will produce lower rates for some of its customers. For that reason, Mr. Rubin's supplementary recommendation that the Commission direct UI to prepare and file a cost of service study for its entire Illinois operation for review and use in the investigation would facilitate the Commission's ability to set cost-based rates in the event of a future consolidation. Actually, in Docket Nos. 11-0561 (Cons.), a proposed general increase in water and sewer rates for 6 other UI companies, Staff made a similar proposal with respect to a COSS. Specifically, Staff recommended that the Commission should order UI to work with Staff to review and analyze UI's current method of cost of service and rate design methodology for use in future

UI rate cases. (Docket Nos. 11-0561 (Cons.), Staff Ex. 4.0, p. 9 and Staff Ex. 5.0, pp. 8-9.)

In addition to possible consolidation and a COSS assessment, rate mitigation and containment of potential wild swings in customer monthly bills could be fostered by rate design changes. In many UI jurisdictions, water and sewer ratemaking is based on rate design methods and principles established many decades ago. Therefore, especially in the case of consolidation, it may be necessary to revisit water and sewer rate design in all territories in order to produce better and much fairer uniform rates. But without knowing the actual cost of serving customers (or as best as is determinable in a typical rate case) in a particular rate area, the Commission cannot know whether the movement toward single-tariff pricing in any future rate case is appropriate. This is where Mr. Rubin's second proposal (i.e., direct UI to prepare and file a COSS for its entire Illinois operation) may turn out to be quite practical. Although a future UI consolidation proceeding may produce more uniform and fair rates, any movement toward this goal should be balanced against the Commission's long standing regulatory objective of setting cost-based rates.

Over the past two decades, there have been several water rate cases filed by various UI subsidiaries, but with long intervals between filings for each subsidiary. (See Staff Ex. 17.0, p. 9, Table A.) For example, prior to this proceeding, Camelot last filed its rate case in 1992. UI now states, however, that:

> The Companies anticipate filing rate cases on a three year cycle and a three year phase-in plan will facilitate the Companies' ability to file a rate case after the phase-in is complete.
>
> (UI Direct Testimony on Rehearing, p. 6.)

With this plan, it is likely that the rates for the 23 subsidiaries will be more in line with each other. I do not mean to suggest that the Commission must wait until such rates are similar among all 23 subsidiaries before consolidation could occur. I can envision a point in the future where the rates of serving customers may be fairly close among many of the UI subsidiaries and a partial or full consolidation would not necessarily result in significant rate increases.

Q. What is your overall recommendation with respect to Mr. Rubin's consolidation proposal?

A. Based on my own position with respect to consolidation in direct testimony on rehearing, and taking into consideration Mr. Rubin's consolidation and COSS proposal, I recommend the Commission initiate a proceeding that would investigate, or require UI to show cause, regarding how to best address the issue of UI rate shock.[1]

[1] The Commission has clear authority to initiate such a proceeding under its general supervisory powers under Article IV (*see e.g.,* 220 ILCS 5/4-101), general investigatory powers under Article X (*see e.g*., 220 ILCS 5/10-101), and of course under the ratemaking provisions of Article IX (see e.g., 220 ILCS 5/9-250).

Based on this proceeding, the Commission can then determine what changes, if any, are necessary to ensure that the rate structure of UI, with appropriate consideration of historic rate structures of its subsidiaries, and any subsequent UI rate proposals, do not result in such a degree of rate shock as seen in the last few years. However, to be clear, the Commission should not intend, in this investigation, to review or consider any changes in the revenue requirements it has most recently determined for UI in this proceeding.

STAFF'S RESPONSE TO AG WITNESS BROSCH

Q. What rate mitigation recommendation does Mr. Brosch's present for UI customers?

A. In direct testimony on rehearing, Mr. Brosch presents a phase-in plan which will recover UI's deferred revenues through base rates. His proposal is nearly identical to the one he proposed in Docket Nos. 11-0561 (Cons.) which is contested by Staff in that proceeding. With respect to his phase-in proposal in this case, Mr. Brosch states:

> I propose that the rate changes be limited to immediate, and then subsequent annual installment increases, that do not increase average residential monthly bills by more than $10 per month or 20 percent per year, whichever is higher. (AG Ex. 2.0, p. 11.)
>
> The largest percentage revenue and average bill increase is proposed for the Great Northern water customers … The AG's recommended rate moderation plan would limit the initial, and subsequent annual rate changes, to the greater of $10.00 or 20% higher monthly bills relative to presently effective rates … From year four to year nine, the rate and average bill would increase by 20% per year to increase the revenue produced through rates and

> eventually commence recovery of the deferral of expenses. (*Id.,* pp. 11-12.)
>
> At the Commission allowed revenue requirement, the phase-in periods for the Camelot water and sewer increases would be ten years and six years, respectively. The increase for Lake Holiday customers is less than $10 per month, and would not require any phase-in under my proposed criteria. (*Id.,* p. 12.)

Q. How do you assess his recommendation?

A. First, with respect to his first point, Mr. Brosch's proposal is to phase-in the recovery of each Company's approved revenue requirement from this proceeding over a period of many years. Mr. Brosch's proposal will not allow for the full recovery of the approved revenue requirement of any of the Companies until, potentially, many years (9 years for GNU, 10 years for CU-Water, and 6 years for CU-Sewer) from the issuance of the ICC's order in this proceeding. Thus, the phase-in proposal may result in a level of revenues insufficient to operate and maintain the Companies' water and sewer systems in a safe, adequate, and reliable manner.

Second, under his plan, although phased-in rates would provide relief in the short term, the long term consequences are overwhelmingly negative. It should be remembered that any benefits received in the deferral years of any phase-in plan must be repaid with interest in later years, so benefits in the short-run become higher costs later on. Thus, Mr. Brosch's plan not only stretches the recovery period over too many years, but in the recovery phase of his plan, the rates will be substantially higher than what customers are facing at present.

Staff Schedule 18.1 presents a comparison of Staff's and the AG's phase-in proposals for the average customer. As is evident from this schedule, although both plans will ease the transition for customers from current rates to the Final Order's compliance rates, in contrast to the phase-in plan proposed by Mr. Brosch, Staff's alternative plan has a much shorter deferral period and the rate caps are positioned at a much higher level for each of the deferral years. In turn, the higher rate caps would cause the amount of the deferrals to be lower and the potential for adverse bill impacts in years four through six to be lower as well.

Furthermore, Table A below presents 6 excerpts from several Camelot Homeowners Association witnesses with respect to the issues of rate shock. Although the these witnesses may not be representative of CU's overall population of ratepayers, it presents various scenarios where some customers indicate a willingness to pay higher rates than that proposed by the AG's phase-in plan (i.e., the lesser of an increase of $10/month or 20%).

TABLE A		
Camelot Homeowners Association - Select Rehearing Direct Summaries		
Ex.	**Witness**	**Rehearing Direct Testimony**
1	Daisy Austin	*"We would be able to handle a 70-80% increase immediately and then a 10-15% increase each year thereafter."*
2	Lou Chignoli	*"A 25% increase would be an acceptable increase."*
4	Jim Levenson	*"Willing to pay (a) a competitive rate for (b) good quality water based on (c) our consumption."*
5	Bobbe Marion	*"This should have been done in increments over the next few years - maybe a 50% per year increase at most; a 25% increase would have been better."*

8	Cathleen M. Vallarta	*"Perhaps cutting the increase to 20% per year over five years or 25% over four years would be less traumatic and would certainly be more attainable for us..."*
10	Tessa Werve	*"A 50% rate increase would at least allow us to pay our water bill without affecting our budget the way the current price hike has."*

Q. How would Mr. Brosch's phase-in plan be impacted by future rate proceedings?

A. In his direct testimony on rehearing, Mr. Brosch states:

> All planned phase-in rate changes that were not implemented at the date of a new rate case filing should be cancelled, to be superseded by new rate and revenue levels found reasonable by the Commission in any future rate case proceedings. (AG Ex. 2.0, p. 14)
>
> I believe that this proposal properly balances ratepayer and Company interests both by gradually increasing rates over time to give consumers time to adjust their usage and spending and by compensating the Companies for the time value of money during the period of deferral. (*Id.,* p. 15)

Q. Do you consider this reasonable?

A. No. While I am not an attorney, I believe his plan is inconsistent with the regulatory goals and objectives set forth by the General Assembly in the Public Utilities Act ("Act"). Specifically, I am concerned about the emphasis placed by Mr. Brosch almost exclusively on UI customers by his phase-in plan. While I agree that the Commission should consider fairness when making its determinations with regard to rate shock facing customers, the proper focus in this case should be on what is fair to both customers and the Companies, in light of the previously approved revenue requirement in this proceeding. The AG's prolonged phase-in plan would inappropriately shift too much of the burden to UI by phasing-in the recovery of its approved revenues from six years for Camelot Sewer to ten years for Camelot Water.

With such a prolonged deferral plan, UI's cash flow from operations may be insufficient to sustain or make needed improvements to its systems, and therefore, it may need access to capital funds from other sources in order to remain a going concern. Significant and continued investments in infrastructure can only be made, and sustained, when a fair return on investment are received on a timely basis.

In sum, the Commission is required to ensure fair treatment and to protect against any undue or sustained adverse impact on utility earnings. In fact, in a recent 2007 North Shore Gas Company and Peoples Gas Light and Coke Company rate case, the Commission stated the following:

> In the final analysis, we are simply unable to approve only those measures that benefit ratepayers and wholly ignore what the impacts of these benefits will have on the Utilities. To do so could well be unlawful as this Commission is put to the obligation of balancing both the interests of consumers and the interests of the Utilities. See *BPI*, 146 Ill. 2d 175, 208 (1991) (stating that the Commission is charged with setting rates which are just and reasonable not only to the ratepayers but to the utility and its shareholders).

Order, Docket Nos. 07-0241/07-0242 (Cons.), at 152 (emphasis added).

Hence, the Commission must weigh the evidence and arguments from both sides and determine a reasonable and fair outcome.

Q. Does Mr. Brosch believe the program should be offered on an opt-in or opt-out basis?

A. Mr. Brosch does not present a clear opinion on this matter. He states:

> I neither oppose nor support giving consumers the option of choosing the phase-in plan or choosing the one step rate increase. Although an optional plan would present more complexities, my proposal could work as an optional plan. That said, I would not expect many consumers to elect to pay utility bills that are suddenly among the highest in the state. (AG Ex. 2.0, p. 16)

Q. What is your opinion on this issue?

A. Any phase-in proposal should be offered on an optional basis only. A mandatory plan would be unfair to customers who do not wish to pay lower rates now and then pay higher rates plus interest, later. This is an important component that has not been fully addressed in Mr. Brosch's proposal; however, this consideration is incorporated in Staff's alternative proposal: Rider BSA. (Staff Ex. 17.0, p. 11.) Under Staff's alternative plan, customers will not only be able to opt-in, but customers will be able to terminate their participation in the plan voluntarily <u>at any time</u>, with the outstanding balance of deferral amounts due to UI. This gives customers greater flexibility in determining their ability to pay based on their individual situation, currently or in the future.

Q. In summary, what do you recommend with respect to rate mitigation of rate shock in this phase of the proceeding?

A. I continue to recommend that the Commission not adopt a program at this time to mitigate rates. Any rate mitigation proposal adopted in this proceeding may in fact place undue future financial stress on ratepayers and also compromise the Companies' ability to make timely infrastructure investments to maintain a safe, adequate and reliable water or sewer system. However, if the Commission is nonetheless inclined to adopt a rate mitigation plan at this point in time, then I recommend the following:

The Commission should reject Mr. Brosch's phase-in plan as:

1. It represents a fundamental departure from the Commission's reliance on cost-based rates development;
2. It may not allow the Companies to timely recover their revenue requirement, which may result in a level of revenues insufficient to operate and maintain the Companies' water and sewer systems in a safe, adequate, and reliable manner.
3. The recovery time for approved revenues is too lengthy; and
4. The bill impacts during the deferred recovery years are too high.

Instead, the Commission should direct the Company to offer a rate mitigation plan patterned after Commonwealth Edison's ("ComEd") Rider RRS with certain modifications as set forth in my direct testimony on rehearing (i.e., Rider BSA). This alternative plan places less future financial stress on UI customers than the AG's plan, is fairer to both UI and its customers, and addresses the concerns I have outlined above.

STAFF'S RESPONSE TO UI WITNESS GEORGIEV

Q. What statements by UI witness Georgiev would you like to address?

A. Ms. Georgiev states:

> The carrying costs on the unrecovered costs for each Company should be set at granted cost of capital, which is 7.71%, not the cost of debt. (UI Direct Testimony on Rehearing, p. 6.)
>
> and
>
> [T]the phase-in plan should include an adjustment to incorporate the increase in future uncollectibles. (*Id.,* at 7)

Q. What is your response to Ms. Georgiev?

A. First, I disagree with utilizing the Companies' cost of capital in the event the Commission is inclined to approve my proposed phase-in plan in this proceeding. The Company's suggestion to apply the weighted average cost of capital as the carrying cost for deferral programs would not be appropriate for Staff's alternative proposal. Under Staff's alternative proposal, the deferral of charges is effectively a short-term loan from the Company to its customers. The deferred charges, and the interest on those deferred charges, would then be recovered through, in essence, a customer-specific rider charge. Such a recovery mechanism would present less risk than rate base cost recovery, as the recovery of deferrals would not be subject to sales variability. Thus, if Staff's alternative proposal is adopted, the application of the Company's cost of short-term debt to deferral balances would be appropriate.

Second, I disagree with respect to her statement about whether the phase-in plan should include an adjustment to incorporate an expected increase in future uncollectibles. In my opinion, any increase in uncollectibles expense as well as any implementation and administrative costs stemming out of any applicable phase-in plan should be treated like any other cost that is incurred subsequent to a rate case. If the cost is an expense that is incurred in a subsequent test year, it would be considered for recovery in a rate case that uses that test year. If the cost is appropriately capitalized as an asset, then it would be considered as an addition to rate base in the next rate case. In fact, in Docket No. 06-0411, ComEd asked the Commission to make a similar finding regarding its costs for its rate mitigation program (Rider RRS) and the Commission declined to do so, stating:

> In its Initial Brief, ComEd asks the Commission to affirm that it should recover in a future rate case its prudent and reasonable costs of offering and maintaining the RRS Program. ComEd claims it is simply seeking a ruling that incurring such costs is appropriate, but does not seek their approval or recovery here. The AG and Staff object to this proposition claiming such relief would be inappropriate and illegal. As ComEd is well aware, in a rate case, it is entitled to request recovery of all prudent and reasonable operating expenses. Similarly, subject to test year rules and standards, the Commission is legally obligated to allow ComEd the opportunity to recover from its customers all prudent and reasonable expenses incurred to provide utility services. In the Commission’s view, there is nothing more it can say or do regarding the issue in this Order. (Final Order, Docket No. 06-0411, p. 22)

Q. Does this complete your rebuttal testimony?

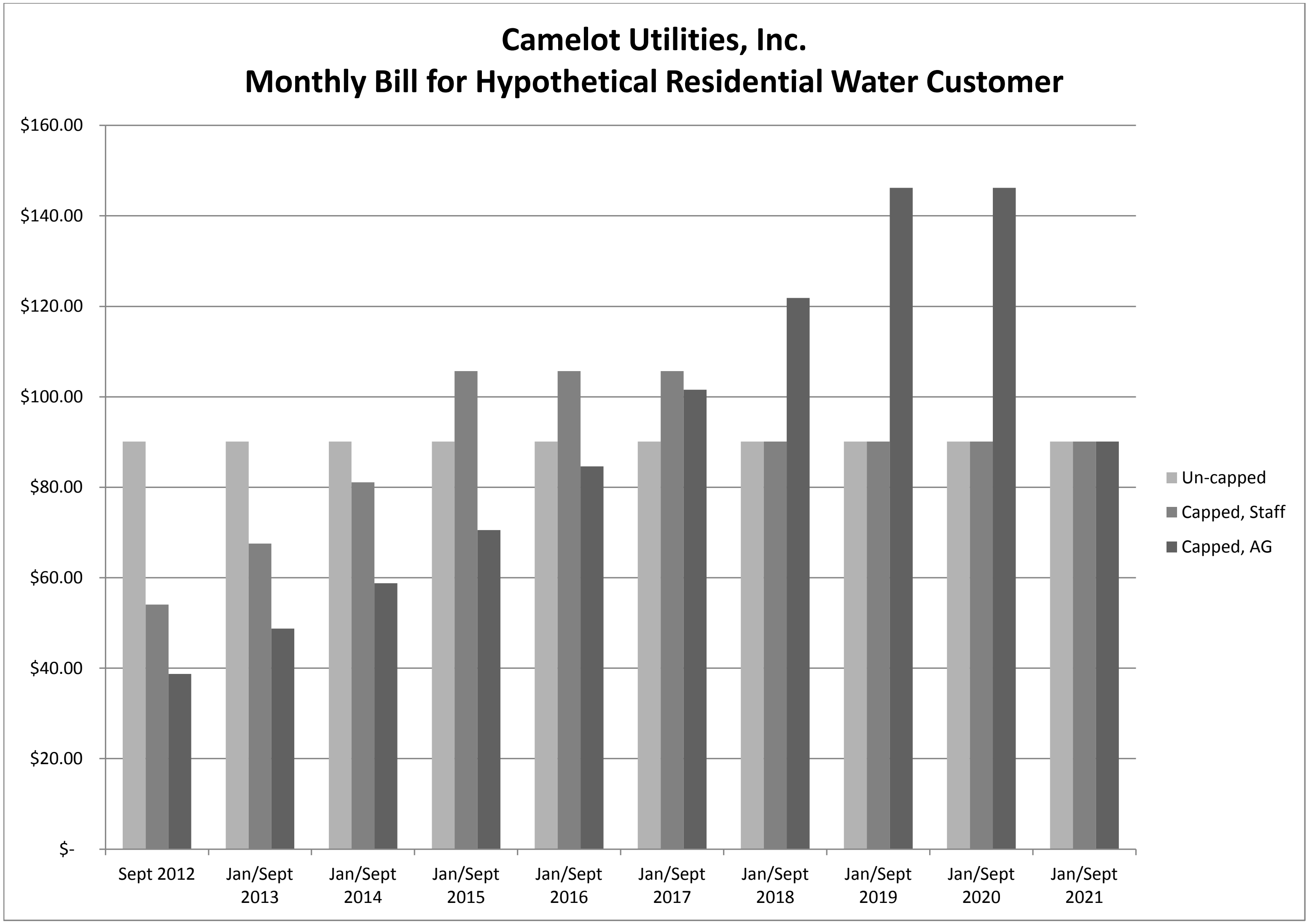
A. Yes, it does.

Comparison of Staff's and AG's Phase-In Plans for Utilities, Inc.
Docket No. 11-0059 (cons.) on Rehearing

Approximate Month for First Bill[1]	Camelot Water			Camelot Water & Sewer			Great Northern Water		
	Un-capped	Capped, Staff[2]	Capped, AG[3]	Un-capped	Capped, Staff[2]	Capped, AG[3]	Un-capped	Capped, Staff[2]	Capped, AG[3]
Sept 2012	$ 90.08	$ 54.05	$ 38.76	$ 166.93	$ 100.16	$ 89.76	$ 74.50	$ 44.70	$ 31.02
Jan/Sept 2013	$ 90.08	$ 67.56	$ 48.76	$ 166.93	$ 125.20	$ 109.96	$ 74.50	$ 55.88	$ 41.02
Jan/Sept 2014	$ 90.08	$ 81.07	$ 58.76	$ 166.93	$ 150.24	$ 132.20	$ 74.50	$ 67.05	$ 51.02
Jan/Sept 2015	$ 90.08	$ 105.71	$ 70.51	$ 166.93	$ 195.89	$ 158.64	$ 74.50	$ 87.43	$ 61.22
Jan/Sept 2016	$ 90.08	$ 105.71	$ 84.61	$ 166.93	$ 195.89	$ 190.36	$ 74.50	$ 87.43	$ 73.47
Jan/Sept 2017	$ 90.08	$ 105.71	$ 101.54	$ 166.93	$ 195.89	$ 178.76	$ 74.50	$ 87.43	$ 88.16
Jan/Sept 2018	$ 90.08	$ 90.08	$ 121.84	$ 166.93	$ 166.93	$ 199.06	$ 74.50	$ 74.50	$ 105.80
Jan/Sept 2019	$ 90.08	$ 90.08	$ 146.21	$ 166.93	$ 166.93	$ 223.43	$ 74.50	$ 74.50	$ 126.95
Jan/Sept 2020	$ 90.08	$ 90.08	$ 146.21	$ 166.93	$ 166.93	$ 223.43	$ 74.50	$ 74.50	$ 74.50
Jan/Sept 2021	$ 90.08	$ 90.08	$ 90.08	$ 166.93	$ 166.93	$ 166.93	$ 74.50	$ 74.50	$ 74.50

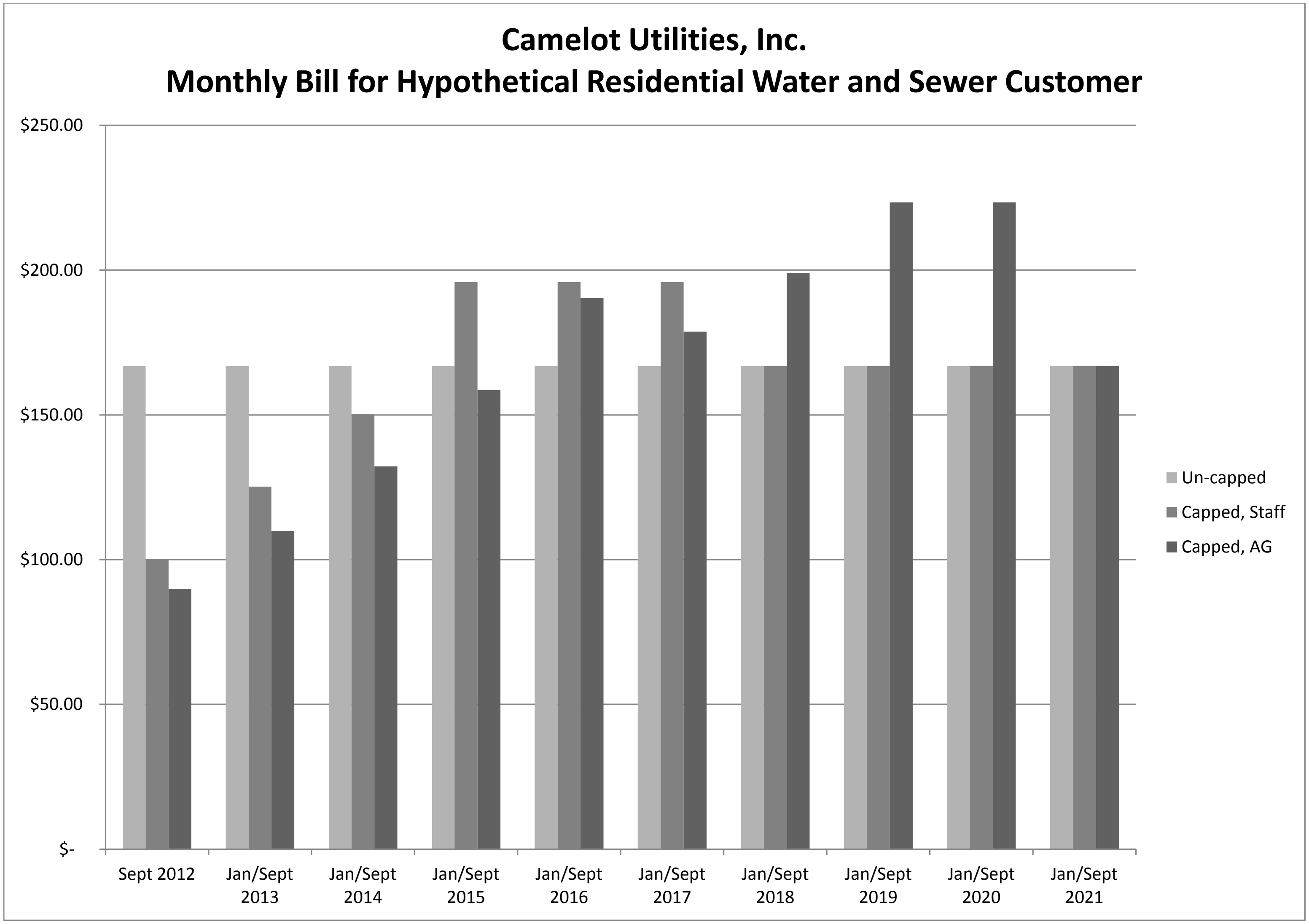
Notes

1. Staff's capped rates are implemented for the first billing period of each calendar year (starting January), except for the first year (i.e. 2012), when rates are implemented as directed by the Final Order on Rehearing. Assuming that Rider BSA will go into effect 90 days (plan's sign-up window) after the Final Order on Rehearing is issued on or about 05/19/2012, as a result, in 2012, there are approximately 4 months left for Rider BSA to accrue deferrals. AG's capped rates are in effect for a full 12 months at each stage, so it will be implemented in approximately September of each year.
2. Staff's capped rates are based on ICC Exhibit 17.0, Schedule 17.5, which only provides example rates for Camelot. Great Northern's capped rates and interest are calculated here in the same way. For interest calculations, Staff uses annual short-term debt cost of 2.85%, which equals to the cost of short-term debt that the Commission adopted in its Final Order in this Docket.
3. AG's capped rates are based on AG Exhibit MLB-2.3 on Rehearing. For interest calculations, AG uses long-term debt cost, 6.6%. AG also accounts for accumulated deferred income taxes (see pp. 13-14 of AG Ex. 2.0). AG's calculation of final rates in Ex. 2.3 differs from the above due to rounding.
4. The Company's proposal, which isn't detailed enough to include in this analysis, uses the overall cost of capital, 7.71%, for computing interest.



Notes

Monthly bill for hypothetical residential customer is based on average consumption. According to its Public Notice, the Company illustrated the impact of its rate increase based on an assumed average monthly consumption of 5,210 gallons.



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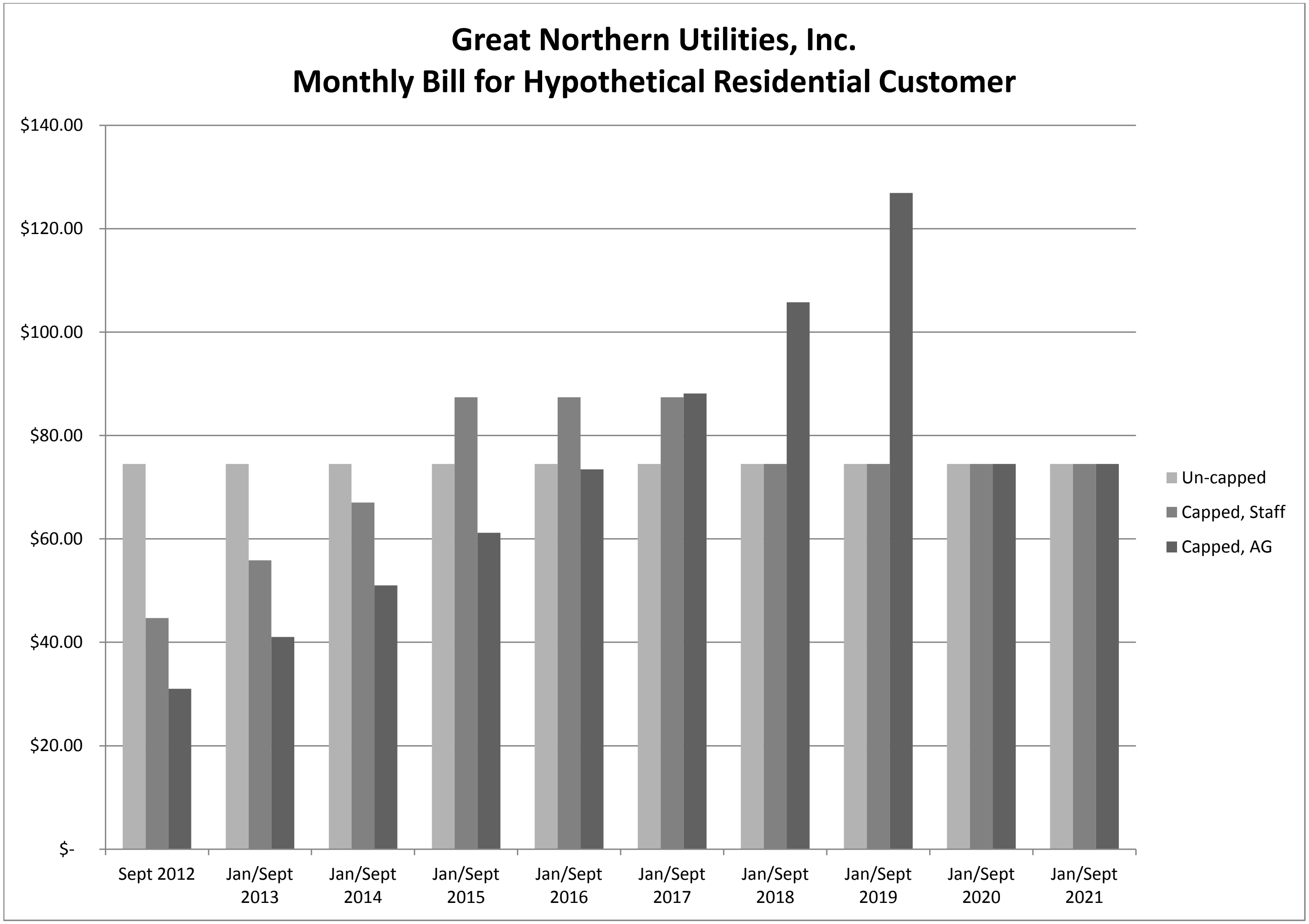

Notes

Monthly bill for hypothetical residential customer is based on average consumption. According to its Public Notice, the Company illustrated the impact of its rate increase based on an assumed average monthly consumption of 4,394 gallons.