

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
COUNTY DEPARTMENT, CHANCERY DIVISION

CITY OF EVANSTON,)
an Illinois Municipal Corporation,)
)
Plaintiff,) Case No.
)
vs.)
)
VILLAGE OF SKOKIE,)
an Illinois Municipal Corporation)
)
Defendant.)

**CITY OF EVANSTON’S COMPLAINT FOR DECLARATORY JUDGMENT AND
UNJUST ENRICHMENT AGAINST THE VILLAGE OF SKOKIE**

NOW COMES the Plaintiff, City of Evanston (“Evanston”), by its attorneys, the City of Evanston Law Department, and for its Complaint against the Defendant Village of Skokie (“Skokie”), states:

Summary of Claims

Evanston operates a water treatment plant that treats Lake Michigan water and in turn supplies and sells water to hundreds of thousands of wholesale water customers in the Chicagoland area. Since 1944, Evanston sold drinking water to Skokie at reasonable rates. Evanston and Skokie are unable to mutually agree on a reasonable rate to pay Evanston for water. Unfortunately, Evanston now has no choice but to seek a declaratory judgment establishing that the equitable and reasonable rate chargeable to Skokie is \$2.06 per 1,000 gallons of water supplied. Unfortunately, Evanston must seek the application of this Court’s equitable powers to prevent Skokie’s unjust enrichment that could result if it paid an inequitably low wholesale water rate.

Allegations Common To Both Counts

1. Evanston and Skokie are municipal corporations created and existing under the laws of Illinois. Evanston operates a water treatment plant drawing water from Lake Michigan, which is then treated to serve as potable water for use by Evanston residents and other municipal customers. Evanston supplies water to the Villages of Arlington Heights, Palatine, Wheeling, Buffalo Grove, and the City of Des Plaines, through an entity known as the Northwest Water Commission (“the Commission”). The Commission purchases water from Evanston for resale to the Commission's member communities. Commencing sometime in 2018 or 2019, Evanston will supply water to new wholesale water customers, the Villages of Niles and Morton Grove. The Village of Lincolnwood may also become a possible new customer. All told, Evanston will likely supply water to over 400,000 Chicagoland residents by the end of 2019.

2. Since 1944, Evanston sold water to its wholesale customer Skokie. This water is subsequently resold by Skokie to its residents. Since 1944, all of the water used by Skokie residents came from Evanston.

3. Evanston delivers water to Skokie primarily through three connection points located in Evanston, at the Evanston-Skokie border. The water is transmitted to those delivery points by 36-inch water pipelines that run through Evanston from the Evanston water plant located on the shore of Lake Michigan to Evanston's border with Skokie. Evanston bills Skokie monthly for the bulk sale of water. Evanston maintains the water pressures for the Skokie system, which is a substantive departure from a traditional wholesale water supplier-customer relationship. This novel arrangement meets Skokie's expectation that its water system be completely integrated with Evanston's water system. Evanston also maintains a high level of redundancy in the water service by utilizing 3 points of connection/service, thus conferring major benefits to Skokie.

4. Since 1963, Evanston and Skokie executed 2 long-term wholesale water supply contracts with Evanston that set forth the terms of Evanston's water service. The most recent contract was executed in 1997 for a 20-year term.

5. This contract expired on December 31, 2016.

6. The rate Skokie paid Evanston for water under the terms of the Prior Contract increased over the years in accordance with a pre-determined formula and periodic recalculations. Water rate charges were calculated per 1,000 gallons of water supplied. After December 31, 2016, Evanston and Skokie agreed to an interim water rate, such interim rate which expired at 11:59 p.m. September 30, 2017. Under this interim rate, Skokie paid Evanston \$1.0797 per 1,000 gallons. Although the interim rate expired, and there is no written water supply contract between Evanston and Skokie currently in effect, there is nonetheless an implied contract requiring Evanston to supply Skokie with water. Also, under Illinois law, Evanston cannot terminate water supply service to Skokie unless and until Skokie first secures an alternative water supply from another source. Since there is no alternative source for Skokie in place, Evanston cannot sit back and let the inequitably low rate exist for an indeterminate amount of time.

The Present Dispute

7. Beginning in 2012, knowing that the water contract would expire at the end of 2016, Evanston met with Skokie numerous times and provided hundreds of pages of information in order to negotiate a mutually agreeable new water supply contract. Before the Prior Contract expired on December 31, 2016, and during the first half of 2017, Evanston asked Skokie to agree to a reasonable and justifiable increase in its wholesale water rate. Evanston discussed with Skokie generally accepted principles for determining rates based on cost of service. It also discussed changes in infrastructure and capital investment that occurred in the past 20 years that

affected Evanston's enterprise risk, and supported a revised contractual water rate calculation methodology.

8. Despite Evanston's supporting evidence regarding a reasonable rate, Skokie instead expressed its desire that the parties go back decades in time to return the Skokie water rate to a level not seen since the mid-1990's. Skokie's preferred rate, which on information and belief is somewhere in the vicinity of \$0.70 per 1,000 gallons, is far below a fair and reasonable rate. Based upon Evanston's cost of serving Skokie, this preferred rate violates generally accepted rate making principles, including a reasonable return for Evanston on its investment in water plant and water main assets benefiting Skokie.

9. Thus, at this time, Evanston and Skokie are unable to agree upon a water rate. Skokie refuses to pay a reasonable rate, and instead insists upon paying an excessively low, inequitable, arbitrary and unreasonable rate, in violation of Illinois law and generally accepted water industry standards. As a result, there exists an actual controversy between the parties. An "actual controversy" means that the case presents a concrete dispute admitting of an immediate and definitive determination of the parties' rights, the resolution of which will aid in the determination of the controversy or a part thereof. *Kaske v. City of Rockford*, 450 N.E.2d 314 (1983). The purpose of this requirement is to distinguish properly justiciable issues from purely hypothetical disputes. *Id.*

10. Additionally, Skokie refused to execute an extension of the previously agreed-to interim contractual water rate of \$1.0797 per 1,000 gallons.

11. On September 25, 2017, the Evanston City Council adopted Ordinance 95-O-17 establishing a water rate payable by Skokie for water supplied by Evanston of \$2.06 per 1,000 gallons. Exhibit 1. Evanston had no choice but to take legislative action and proceed with

litigation in order to protect its taxpayers and ensure all Evanston wholesale water rate customers are treated equitably.

COUNT I - DECLARATORY JUDGMENT

(Evanston's Water Rate Charged to Skokie is Reasonable under Illinois Common Law, Is Lower Than Wholesale Rates Paid by Comparable Communities, and Conforms to Nationally Accepted Industry Standards)

12. Evanston realleges and incorporates the allegations set forth in paragraphs 1 through 11 as if fully set forth herein as the allegations of paragraph 12.

13. As a municipal utility, Evanston's water rates are not subject to regulation by the Illinois Commerce Commission ("ICC"). The standard of reasonableness is always applied by courts in evaluating the utility rates charged by municipal corporations acting in their proprietary capacities. *Village of Niles v. City of Chicago*, 401 N.E.2d 1235, 1239-40 (1st Dist. 1980)[Referred to in the rest of this Complaint as *Niles I, supra*]. In applying this standard, "a reasonable rate would be one which would fully compensate [Evanston] for the cost of serving [Skokie]." *Village of Niles v. City of Chicago*, 558 N.E.2d 1324, 1338 (1st Dist. 1990)[Referred to in the rest of this Complaint as *Niles II, supra*].

14. The Illinois Supreme Court held long ago that a city may realize a reasonable revenue surplus or profit from operating its water system. *Wagner v. City of Rock Island*, 146 Ill.139 (1893).

15. Water rate ordinances are presumed valid, and a challenger to a water rate ordinance bears a heavy burden of proving that the rates charged are unjustly discriminatory and unreasonable. *Niles I* at 1242. In order to overcome the presumption, 'it must be established by clear and convincing evidence that the ordinance, as applied to (the challenging party), is arbitrary and unreasonable and has no substantial relation to the public health, safety or welfare.' *Niles II* at 1330, citing *City of Evanston v. Ridgeview House*, 64 Ill.2d 40 (1976).

16. **Skokie therefore bears a heavy burden to prove by clear and convincing evidence that Evanston's water rate ordinance is invalid.** This is a burden Skokie has not and cannot meet.

17. Water rate classifications are entitled to minimal scrutiny by a Court. *Niles II* at 1330. After determining minimal scrutiny was the applicable standard for a reviewing court, the City of Chicago defeated suburban wholesale water customers' challenge to a Chicago water rate ordinance. *Id.*

18. In construing the validity of a municipal ordinance, the same rules are applied as those which govern the construction of statutes, namely, that statutes are presumed constitutional and the burden of rebutting that presumption is on the party challenging the validity of the statute to clearly demonstrate a constitutional violation. *Napleton v. Village of Hinsdale*, 229 Ill. 2d 296, 306 (2008).

19. The court has a duty to uphold the constitutionality of a statute/ordinance when reasonably possible, and if a statute's/ordinance's construction is doubtful, the court will resolve the doubt **in favor** of the statute's/ordinance's validity. *Napleton*, 229 Ill. 2d at 306-07, *citing People ex rel. Sherman v. Cryns*, 203 Ill. 2d 264, 291 (2003). To reiterate, Skokie may only defeat Evanston's ordinance by overcoming that presumption of validity by means of clear and convincing evidence. *Niles II* at 662. The standard for reviewing legislation is whether **any** set of facts may reasonably be conceived which would justify the classification. *Id.*

20. Evanston's rates for water are equitably generated by revenues from water sales that conform to Evanston's cost of providing the water service. This includes a reasonable return on Evanston's investment in the water system benefiting all customers, one of which is Skokie. In fact, and important to the equities applied to this issue, Evanston's water rate for its residents

recovers more of the cost of service, on a *pro-rata* basis, than costs recovered by water charges realized from external customers, which includes Skokie.

21. Evanston's most recently passed water rate ordinance for internal customers, Ordinance 145-O-16, increased water rate charges assessed to Evanston residents 6%, effective January 1, 2017. That rate is \$3.09 per 1,000 gallons for internal (resident) Evanston customers.

22. In July 2017, Skokie raised the water rate it charged to Skokie residents by 8.48%, yet admitted its water rates: "will still be less than the water rates for Evanston, Wilmette, Glenview, Lincolnwood, Niles, and several other communities." See Skokie Ordinance 17-8-C. The legislative record for that ordinance indicated that even with this 8.48% increase, Skokie's rate "remains the second lowest among area comparable communities."

23. The interim rate of \$1.0797 per 1,000 gallons paid to Evanston through September 30, 2017 was artificially low, both in a relative and absolute sense. Skokie wishes to further depress its rate going forward, in order to obtain an artificially low rate contrary to Illinois law and established rate making principles. It seeks to obtain an artificially subsidized rate to unjustly benefit and enrich Skokie residents, while prejudicing hundreds of thousands of other similarly situated wholesale water rate customers.

24. In fact, as compared to other communities and already admitted by Skokie, the rate charged by Evanston to Skokie is in many cases less than that paid by other water customers in comparable communities. The water rates set forth below illustrate this incontrovertible point.

Provider	Customer	Rate per 1,000 gallons	Contract Expires
Evanston	Evanston	\$3.09	N/A
Evanston	Skokie	\$2.06 (new rate 10-1-17)	In controversy ¹
Chicago	60+ other municipalities	\$3.88	Varies
Highland Park	Deerfield, others	\$2.69	2033
Wilmette	Glenview	\$1.78	2050
Northbrook	Riverwoods	\$3.06	2036
Waukegan	Park City	\$4.71	2018
Winnetka	Northfield	\$1.69	2033
Glenview	Golf	\$3.38	2066

Provider	New Customer	Rate per 1,000 gallons	Contract Expires
Evanston	Morton Grove - Niles ("MG-N")	\$0.78	2048 ²

25. The rate of \$2.06 per 1,000 gallons billed by Evanston to Skokie fully complies with the legal standard of reasonableness enunciated by *Niles II*, and is supported by abundant affirmative evidence of its reasonableness.

26. The Skokie rate involves three components:

- First, Skokie must pay Evanston an annual 9.5% return on rate base ("RoR"), the rate base being the value of that portion of Evanston's waterworks assets attributable to providing water for Skokie.

¹ For illustrative purposes, the water rate methodology by Evanston to the Northwest Water Commission for the current rate of \$0.67 per 1,000 gallons was set over 20 years ago in 1995. That was subject to wholly different economic conditions, contract specifications and logistical considerations attendant to pumping water to 200,000 newly added wholesale customers 15+ miles away from the Evanston water plant. Evanston will negotiate a dramatically different and reasonable new contract with NWC at the appropriate time. In any event, the NWC water contract is in its later stages of existence and the Commission's existence as an Evanston water customer benefits Skokie. Skokie pays a lower rate than what could otherwise be charged to Skokie if the Commission's 200,000+ water customers did not pay into Evanston. Evanston, under AWWA principles explained below, spreads the costs of service amongst a larger pool of wholesale municipal water customers, thereby lowering each municipal customer's overall rate.

² MG-N is scheduled to begin taking water from Evanston at the end of 2018. It will issue over \$80 Million Dollars in bonds for capital improvements over the next 30 years to build the necessary infrastructure to connect to Evanston, and which will allow it to cease paying Chicago \$3.88+ per 1,000 gallons. When MG-N comes online, those 2 new municipal wholesale water customers will lower Skokie's rate, again, because the water rate payable by each individual wholesale customer is reduced as costs of service are allocated to more customers.

- Second, Skokie must pay Evanston a "depreciation charge" representing the depreciation on the portion of Evanston's waterworks assets attributed to providing water for Skokie.
- Third, Skokie must pay Evanston a "quantity rate" of a certain number of cents for every 100 cubic feet of water delivered to Skokie, derived from Evanston's annual operating expenses in providing the water service.

27. This method also corresponds to the formula contractually agreed to in March 2017 by Evanston and new municipal wholesale water customers Niles and Morton Grove. This 3-part rate formula is an acceptable method for establishing a utility rate, recognized and accepted by both the Illinois Commerce Commission ("ICC") and Illinois courts applying common law standards.³

28. The American Water Works Association Manual of Water Supply Practices, colloquially known as the "M-1", sets forth generally accepted industry standards for setting a reasonable wholesale water rate. The AWWA Manual is regarded as "...manual of standard practices for the development and establishment of cost-based water rates, fees and charges." The 6th edition of the M-1 was relied upon the City and its wholesale water rate valuation experts, in setting the Skokie rate enacted in Ordinance 95-O-17. The utility basis approach followed by Evanston is analyzed in the M-1, and the manual states in pertinent part:

It is considered an appropriate method for calculating the costs of service applicable to all classes of customers, **but is particularly applicable to those customers located outside the geographical limits of a government-owned utility.** [emphasis added] AWWA M-1, 6th Edition, p.14

³ While the ICC has no regulatory authority over Evanston water rates, return on rate ("RoR") awards in ICC rate decisions may be argued by Skokie as being relevant. Anticipating that eventuality, Evanston points out that the 2 most recently published ICC decisions regarding RoR's are 7.47% and 8.09 % in March 2015 and December 2016, with the historic trend of RoR being **9.35%**. ICC Financial Analysis Division, Water and Sewer Rate Case Analysis 1975-2012. Morton Grove - Niles agreed to pay Evanston a **9.5%** RoR, all the while those 2 new customers bond and finance over \$80M in new capital construction costs to connect to Evanston. Skokie unreasonably contends that it should pay somewhere in the vicinity of 4.5% RoR.

29. The general methodology of this water rate formula is recognized and accepted, and "... recognize[s] the inherent risk factors involved in developing infrastructure and delivering services to outside-city users." AWWA M-1, 6th Edition, p. 164. The figures used by Evanston in applying the formula to fairly calculate the Skokie rate compensate Evanston for its "enterprise operations" in providing water service to Skokie, and Evanston's "ownership risk factors". *Id.*

30. The current Skokie water rate provides Evanston a fair return on its investment in waterworks facilities. This investment in waterworks facilities is referred to as the "fair value rate base." This cost-share concept is not foreign to Skokie, and was previously incorporated in the 1963-1993 water contract. The cost-share in that contract was calculated at 50% original cost less depreciation and 50% reproduction cost less depreciation. This ratio is the same as the ratio used/will be used in the Niles and Morton Grove fair value rate base(s). Evanston fairly states the reproduction cost less depreciation component of the rate base in order to fully reflect actual depreciation on the waterworks facilities. Illinois common law allows both original cost and reproduction cost to be considered in determining a fair value rate base. *Niles II* at 1339, citing *Union Electric Co. v. ICC*, 396 N.E. 510 (1979).

31. When Skokie's water rate is calculated using the AWWA approved method properly reflecting Evanston's true cost of serving Skokie, the resulting rate is \$2.06 per 1000 gallons. On this basis, the preferred rate demanded by Skokie of something in the vicinity of \$0.70 per 1,000 gallons would result in Evanston losing over \$1 million of reasonable return per year.

32. Even the interim rate of \$1.0797 per 1,000 gallons rate is too low under AWWA principles, and would result in Evanston losing hundreds of thousands of dollars of reasonable return per year.

33. The utility basis utilized by the City to accurately and fairly compute the rate payable by Skokie was specifically approved by the Court in *Niles II*. *Id.* at 1333. The *Niles II* court reviewed the AWWA's consideration of the utility basis approach, and specifically said the utility basis was "acceptable" under AWWA principles. *Id.* The *Niles II* court viewed with favor the fair value concept (followed by Evanston) which includes replacement cost new, less depreciation, and specifically rejected Plaintiff ratepayers' attempts in that case to disallow the use of this method. *Id.* at 1334. Furthermore, the as-applied 50/50% rate of return was acceptable as well. Therefore, the \$2.06 per 1000 gallons rate being charged by Evanston to Skokie is reasonable and complies with Illinois law set forth in the *Niles II* case.

34. The *Niles II* court also specifically stated that money that flows back to a wholesale water supplier's water fund that is paid by both the supplier and external suburban customers will benefit the entire water system. *Id.* at 1336.

35. The City in the next years will be required to complete a necessary replacement of an 85+ year old reservoir, which will cost approximately \$20 Million Dollars. This necessary capital expansion and improvement fully justifies the rate payable by Skokie, as the rate captures fair and *pro-rata* shares of costs allocated amongst all wholesale water customers. Skokie wants to underpay and unfairly shift those infrastructure costs to others.

36. Evanston's prior offers in good faith to sell water to Skokie at generally accepted principles complied with Illinois law, but there was no mutual agreement on a rate. The Evanston water rate ordinance adopted on September 25, 2017 complies with Illinois law. Skokie seeks to obtain an unsupportable, inequitable, and unreasonable water rate subsidy. This subsidy is contrary to Illinois law, will unjustly enrich Skokie, and unfairly discriminate against hundreds of thousands of others wholesale water customers throughout Chicagoland.

37. There is an actual dispute between Evanston and Skokie regarding the reasonable and proper rate for wholesale water. Evanston reserves the right to amend this Complaint to also seek damages owed to Evanston taxpayers for underpayments by Skokie on all water supplied and billed after October 1, 2017, in the event Skokie refuses to pay for water charged at the \$2.06 per 1,000 gallons water rate.

WHEREFORE, Evanston prays that this Court enter judgment in favor of Evanston and against Skokie as follows:

- (a) Finding and declaring that the \$2.06 per 1,000 gallons water rate being charged by Evanston pursuant to Ordinance 95-O-17 is reasonable and complies with Illinois law.
- (b) Finding and declaring that the current, reasonable and proper water rate for Evanston to charge Skokie is proven by the evidence presented by Evanston.
- (c) Finding and declaring that the proper methodology to be used in setting future rates to be charged by Evanston to Skokie, is according to the evidence and methodology presented by Evanston.
- (d) Awarding Evanston its costs and attorneys' fees.
- (f) Award such other relief as this Court deems just and proper.

COUNT II - UNJUST ENRICHMENT

38. Evanston realleges and incorporates the allegations set forth in paragraphs 1 through 37 as if fully set forth herein as the allegations of paragraph 38.

39. To state a cause of action based on a theory of unjust enrichment, a plaintiff must allege that the defendant unjustly retained a benefit to the plaintiff's detriment, and that defendant's retention of the benefit violates the fundamental principles of justice, equity, and good conscience. "*HPI Health Care Services, Inc. v. Mt. Vernon Hospital, Inc.*, 545 N.E.2d 672 (1989). A cause of action based on unjust enrichment does not require fault or illegality on the part of the defendant; the essence of the cause of action is that one party is enriched and that it

would be unjust for that party to retain the enrichment. This principle is based on an implied contract. *People ex rel. Hartigan v. E & E Hauling, Inc.*, 607 N.E.2d 165 (1992). Evanston seeks recovery since there is no current written contract with Skokie to provide water service. *Stathis v. Geldermann, Inc.*, 692 N.E.2d 798 (1st Dist. 1998). However, Skokie is entitled to continue to receive water from Evanston due to life safety reasons under Illinois law, provided it also pays a legally and equitably justifiable rate to Evanston.

40. Skokie will accept the benefit of being supplied with Evanston water, but seeks to pay an unreasonable water rate. Evanston has no choice but to seek the application of this Court's equitable powers to prevent Skokie from unjustly retaining the benefits derived from underpaying for water supplied by Evanston.

WHEREFORE, Evanston prays that this Court enter judgment in favor of Evanston and against Skokie as follows:

- (a) Finding and declaring that the \$2.06 per 1,000 gallons water rate being charged by Evanston pursuant to Ordinance 95-O-17 is reasonable and complies with Illinois law.
- (b) Finding and declaring that the current, reasonable and proper water rate for Evanston to charge Skokie is proven by the evidence presented by Evanston.
- (c) Finding and declaring that the proper methodology to be used in setting future rates to be charged by Evanston to Skokie, is according to the evidence and methodology presented by Evanston, and that Skokie would be unjustly enriched if this methodology were not followed.
- (d) Awarding Evanston its costs and attorneys' fees.
- (f) Award such other relief as this Court deems just and proper.

City of Evanston

By:



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