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April 9, 2007

VIA HAND-DELIVERY

Chairman Sara Kyle
c/o Sharla Dillon
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243-0505

Re: Petition Of Tennessee American Water Company To Change And Increase Certain Rates And Charges So As To Permit It To Earn A Fair And Adequate Rate Of Return On Its Property Used And Useful In Furnishing Water Service To Its Customers; Docket No. 06-00290

Dear Chairman Kyle:



Enclosed please find an original and sixteen (16) copies of Rebuttal Testimony of Paul R. Herbert.

Please return three copies of each Rebuttal, which I would appreciate your stamping as "filed," and returning to me by way of our courier.

Should you have any questions concerning any of the enclosed, please do not hesitate to contact me.

With kindest regards, I remain

Yours very truly,

 by permission

R. Dale Grimes

RDG/ms
Enclosures

Chairman Sara Kyle

April 9, 2007

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cc: Hon. Pat Miller (*w/o enclosure*)
Hon. Ron Jones (*w/o enclosure*)
Hon. Eddie Roberson (*w/o enclosure*)
Ms. Darlene Standley, Chief of Utilities Division (*w/o enclosure*)
Richard Collier, Esq. (*w/o enclosure*)
Mr. Jerry Kettles, Chief of Economic Analysis & Policy Division (*w/o enclosure*)
Ms. Pat Murphy (*w/o enclosure*)
Michael A. McMahon, Esq. (*w/enclosure*)
Frederick L. Hitchcock, Esq. (*w/enclosure*)
Vance Broemel, Esq. (*w/enclosure*)
Henry Walker, Esq. (*w/enclosure*)
David Higney, Esq. (*w/enclosure*)
Mr. John Watson (*w/enclosure*)
Mr. Michael A. Miller (*w/enclosure*)

BEFORE THE
TENNESSEE REGULATORY AUTHORITY

REBUTTAL TESTIMONY OF
PAUL R. HERBERT

ON BEHALF OF TENNESSEE-AMERICAN WATER COMPANY

CASE NO. 06-00290

CONCERNING

COST OF SERVICE ALLOCATION

AND

CUSTOMER RATE DESIGN

APRIL 2007

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T.R.A. DOCKET ROOM

BEFORE THE TENNESSEE REGULATORY AUTHORITY

RE: TENNESSEE-AMERICAN WATER COMPANY

CASE NO. 06-00290

REBUTTAL TESTIMONY OF PAUL R. HERBERT

1 1. Q. Please state your name and address.

2 A. My name is Paul R. Herbert. My business address is 207 Senate
3 Avenue, Camp Hill, Pennsylvania.

4 2. Q. By whom are you employed?

5 A. I am employed by Gannett Fleming, Inc.

6 3. Q. Are you the same Paul R. Herbert that submitted direct testimony in
7 this case?

8 A. Yes, I am.

9 4. Q. What is the subject of your rebuttal testimony?

10 A. My rebuttal testimony will address Chattanooga Manufacturers
11 Association (CMA) witness Mr. Michael Gorman direct testimony and
12 exhibits, concerning the cost of service and proposed rates.

13 5. Q. Please address the testimony of Mr. Gorman concerning cost
14 allocation.

15 A. Mr. Gorman generally accepts the cost of service study I prepared but
16 offers one minor adjustment to my study which involves the allocation
17 of purchased power costs. Mr. Gorman suggests that the demand
18 charge portion of the Company's electric bills be allocated on an extra

1 capacity basis, using my Factor 6 instead of Factor 1 which is based
2 on average daily sales. The result of his revision would allocate
3 more purchased power costs to the residential, commercial, public
4 authority and private fire classes and less to industrial and other water
5 utilities classes. The reduction to the industrial class would be
6 \$57,391 or approximately 1.5% - a relatively minor adjustment.

7 6. Q. Do you agree with Mr. Gorman's revision?

8 A. I would agree with the concept of this refinement but not to the extent
9 that Mr. Gorman suggests.

10 7. Q. Please explain.

11 A. I have conducted an analysis of another large water company's power
12 bills and noticed that most of the bills include a monthly demand
13 charge regardless of the level of service. Most electric rates are
14 structured with a customer charge, a demand charge and commodity
15 charges. Depending on the rate schedule, there will be a monthly
16 demand charge even if power is taken at a steady rate 24 hours a
17 day, 7 days a week. The extent that the demand charge fluctuates
18 from month to month I would consider to be the extra capacity portion
19 of the Company's power purchases. In my analysis of the other water
20 company, the difference between the minimum demand charge for
21 the lowest demand month and the demand charges for the remaining
22 months resulted in approximately 5% of the total purchased power
23 expense attributable to extra capacity. I would support a refinement

1 to my cost allocation that would allocate 5% of purchased power to
2 the extra capacity function.

3 8. Q. Does the AWWA Manual M1 support your method of allocating
4 purchased power in this manner?

5 A. Yes, it does. It states that "the demand portion of power costs should
6 be allocated to extra capacity **to the degree that it varies with the**
7 **demand pumping requirements."** (emphasis added). It does not
8 suggest that the total demand portion of power costs should be
9 allocated to extra capacity, only to the degree that it varies with
10 pumping requirements.

11 9. Q. What is the result of allocating power costs using your alternative
12 method?

13 A. As shown on Exhibit No. PRH-R1, the result of allocating 5% of the
14 power costs on an extra capacity basis reduces the industrial cost of
15 service by \$6,354 or 0.16% - an insignificant amount.

16 10. Q. Please address Mr. Gorman's testimony regarding the proposed rate
17 design.

18 A. Mr. Gorman objects to the Company's proposal to increase rates
19 based on an across-the-board increase which maintains the interclass
20 subsidies that exist based on cost of service indications. He
21 recommends that the subsidies be phased out over three rate cases.

22 11. Q. Do you agree with this conclusion?

23 A. Although the Company would support the gradual movement toward
24 the cost of service indications shown in the cost of service study, the

1 proposal for an across-the-board increase was determined to be more
2 appropriate at this time.

3 12. Q. Does this conclude your rebuttal testimony?

4 A. Yes, it does.

EXHIBIT No. PRH-R1

TENNESSEE-AMERICAN WATER COMPANY

COMPARISON OF PRO FORMA COST OF SERVICE WITH REVENUES UNDER PRESENT AND PROPOSED RATES
FOR THE TWELVE MONTHS ENDED JUNE 30, 2006

Customer Classification (1)	Pro Forma Cost of Service, as of June 30, 2006		Pro Forma Revenues Under Present Rates		Pro Forma Revenues Under Proposed Rates		Proposed Increase	
	Amount (2)	Percent of Total (3)	Amount (4)	Percent of Total (5)	Amount (6)	Percent of Total (7)	Amount (8)	Percent Increase (9)
Residential	\$19,439,367	50.5%	\$13,681,917	42.5%	\$16,354,136	42.5%	\$2,672,219	19.5%
Commercial	10,464,491	27.2%	10,230,156	31.8%	12,242,287	31.8%	2,012,131	19.7%
Industrial	3,940,061	10.2%	3,428,902	10.7%	4,103,407	10.7%	674,505	19.7%
Other Public Authority	2,705,939	7.1%	2,404,176	7.4%	2,877,105	7.5%	472,929	19.7%
Other Water Utilities	1,359,278	3.5%	1,048,255	3.3%	1,254,459	3.2%	206,204	19.7%
Private Fire Protection	566,273	1.5%	1,373,647	4.3%	1,644,020	4.3%	270,373	19.7%
Public Fire Protection	0	0.0%	0	0.0%	0	0.0%	0	0.0%
Total Sales of Water	38,475,409	100.0%	32,167,053	100.0%	38,475,414	100.0%	6,308,361	19.6%
Other Water Revenues	1,336,761		1,265,235		1,336,761		71,526	5.7%
Total	<u>\$39,812,170</u>		<u>\$33,432,288</u>		<u>\$39,812,175</u>		<u>\$6,379,887</u>	19.1%

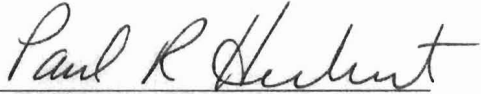
TENNESSEE REGULATORY AUTHORITY

COMMONWEALTH OF PENNSYLVANIA


COUNTY OF CUMBERLAND

BEFORE ME, the undersigned authority, duly commissioned and qualified in and for the State and County aforesaid, personally came and appeared Paul R. Herbert, being by me first duly sworn deposed and said that:

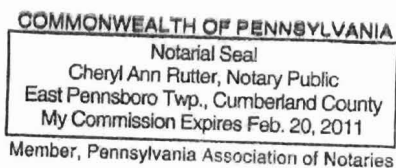
He is appearing as a witness on behalf of Tennessee-American Water Company before the Tennessee Regulatory Authority, and if present before the Authority and duly sworn, his rebuttal testimony would set forth in the annexed transcript consisting of six (6) pages.


Paul R. Herbert

Sworn to and subscribed before me
this 9th day of April 2007.


Notary Public

My commission expires February 20, 2011.



CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been served via the method(s) indicated, on this the 9th day of April, 2007, upon the following:

<input type="checkbox"/> Hand	Michael A. McMahan
<input type="checkbox"/> Mail	Special Counsel
<input type="checkbox"/> Facsimile	City of Chattanooga (Hamilton County)
<input checked="" type="checkbox"/> Overnight	Office of the City Attorney
<input checked="" type="checkbox"/> Email	Suite 400
	801 Broad Street
	Chattanooga, TN 37402
<input type="checkbox"/> Hand	Timothy C. Phillips, Esq.
<input type="checkbox"/> Mail	Vance L. Broemel, Esq.
<input type="checkbox"/> Facsimile	Stephen Butler
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	425 5th Avenue North
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