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April 24, 2007

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

filed electronically in docket office on 04/24/07

Re: *Tennessee American Water Company Rate Case*
TRA Docket No. 06-00290

Dear Chairman Kyle:

Enclosed please find Terry Buckner's Supplemental Responses to No. 3 of the Company's discovery requests to the Consumer Advocate Division.

Very truly yours,

Steve Butler

Steve Butler
Assistant Attorney General
(615) 741-8722

cc: Mr. R. Dale Grimes
Mr. J. Richard Collier
Mr. Henry W. Walker
Mr. Michael A. McMahan
Mr. David G. Higney
Mr. Fredrick L. Hitchcock

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OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
ANALYSIS OF MANAGEMENT FEES
TENNESSEE AMERICAN WATER COMPANY - TRA DOCKET #06-00290

LINE #	CATEGORY	COMPANY FORECAST TRA DOCKET #04-00288		COMPANY FORECAST TRA DOCKET #06-00290		PERCENT GROWTH
1	Labor	$ 4,383,883		$ 4,702,966		7.28%
2	Group Insurance	1,386,004		1,513,667		9.21%
3	Pensions	892,790		595,798		-33.27%
4	Management Fees	3,062,940		4,064,421		32.70%
5	Total	$ 9,725,617	A/	$ 10,876,852	D/	11.84%

LINE #	CATEGORY	CAPD FORECAST TRA DOCKET #04-00288		COMPANY FORECAST TRA DOCKET #06-00290		PERCENT GROWTH
6	Labor	$ 4,082,080		$ 4,702,966		15.21%
7	Group Insurance	1,339,248		1,513,667		13.02%
8	Pensions	829,731		595,798		-28.19%
9	Management Fees	3,219,932		4,064,421		26.23%
10	Total	$ 9,470,991	B/	$ 10,876,852	D/	14.84%

LINE #	CATEGORY	ACTUAL		COMPANY FORECAST TRA DOCKET #06-00290		PERCENT GROWTH
11	Labor	$ 3,765,383		$ 4,702,966		24.90%
12	Group Insurance	1,563,967		1,513,667		-3.22%
13	Pensions	318,289		595,798		87.19%
14	Management Fees	3,752,617		4,064,421		8.31%
15	Total	$ 9,400,256	C/	$ 10,876,852	D/	15.71%

A/ CAPD Work Paper E-REC-1, Lines 1, 6, 7, and 8.
B/ Settlement Agreement, Exhibit CAPD-RTB, Schedule 5, Lines 1, 6, 7, and 8.
C/ Company Rebuttal Exhibit MAM-15, Page 2 of 2.
D/ Company Exhibit, No. 2, Schedule 3, Page 1 of 1, Lines 1, 11, 13, and 15.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
ANALYSIS OF MANAGEMENT FEES
TENNESSEE AMERICAN WATER COMPANY - TRA DOCKET #06-00290

LINE #	CATEGORY	(1)	(2)	(3)	(4)	(5)	(6)		(7)	(8)
	A/ TN American	TRA DOCKET #03-00118 3/31/2004	2004	2005	2006	2007	TRA DOCKET #06-00290		MANAGEMENT FEES VARIANCE	TOTAL VARIANCE
1	Labor	$ 5,066,666	$ 5,228,799	$ 5,396,121	$ 5,568,797	$ 5,746,998	$ 4,702,966			
2	Group Insurance	1,463,924	1,725,805	2,060,248	1,912,718	1,729,041	1,513,667			
3	Pensions	387,985	141,820	344,846	1,151,099	665,606	595,798			
4	Management Fees	2,507,276	2,535,587	2,607,538	3,010,950	2,771,251	4,064,421			
5	Total	$ 9,425,851	$ 9,632,011	$ 10,408,753	$ 11,643,564	$ 10,912,896	$ 10,876,852		$ 10,876,852	$ 10,876,852
	CAPD			TRA DOCKET #04-00288 12/31/2005	2006	2007	TRA DOCKET #06-00290			
6	Labor			$ 4,383,883	$ 4,524,167	$ 4,668,941	$ 4,397,377			
7	Group Insurance			1,386,004	1,597,632	1,444,250	1,386,168			
8	Pensions			892,790	1,169,074	675,962	12,662			
9	Management Fees			3,062,940	3,177,800	3,296,968	3,021,111			
10	Total			$ 9,725,617	$ 10,468,674	$ 10,086,120	$ 8,817,318		$ 10,086,120	$ 8,817,318
				B/	C/	C/	D/			
11	Capitalization Rate Change							E/	(245,793)	
12	Net Total								$ 9,840,328	
13	Net Variance (Line 5 minus Line 12)								$ 1,036,524	$ 2,059,534
14	CAPD/Company Management Fee Forecast Difference							F/	1,043,310	(1,043,310)
15	CAPD/Company Labor Forecast Difference							G/		(305,589)
16	Group Insurance Forecast Difference							H/		(127,499)
17	Pension Expense Forecast Difference							I/		(583,136)
18	Total of Lines 13-17									$ -

A/ Company Rebuttal Exhibit MAM-15, reconciled for $7,000 error in Group Insurance to Company Forecast Amount in Docket #06-00290.
B/ CAPD Work Paper, E-REC-1, P1, Column 1, Lines 1, 6, 7, and 8 per Company Exhibit No. 2, Schedule 3, Lines 1, 11, 13, and 15.
C/ Column 3 Labor amount grown at 3.2% per year per Company Rebuttal Exhibit MAM-15
Group Insurance Cost per employee per Company Rebuttal Exhibit MAM-15, Page 2 of 2, times 106 employees
Pension Expense per employee per Company Rebuttal Exhibit MAM-15, Page 2 of 2, times 106 employees
Management Fees grown at 3.75% per year.
D/ CAPD Work Paper E-REC-1, P1, Column 10, Lines 1, 6, 7, and 8.
E/ Capitalization Rate of 16.61% in Docket #04-00288 and 21% in Docket #06-00290 per CAPD Work Paper E-PAY-4, P5.
F/ CAPD Work Paper E-REC-1, P1, Column 11, Line 6.
G/ CAPD Work Paper E-REC-1, P1, Column 11, Line 1.
H/ CAPD Work Paper E-REC-1, P1, Column 11, Line 7.
I/ CAPD Work Paper E-REC-1, P1, Column 11, Line 8.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
ANALYSIS OF MANAGEMENT FEES
TENNESSEE AMERICAN WATER COMPANY - TRA DOCKET #06-00290

	ACTUAL	(1) TRA DOCKET #03-00118 3/31/2004	(2) 2004	(3) 2005	(4) 2006	(5) COMPANY FORECAST TRA DOCKET #06-00290
1	Labor	$ 4,631,351	$ 4,212,010	$ 3,765,383	$ 4,256,528	$ 4,702,966
2	Group Insurance	1,345,749	1,362,217	1,563,967	1,542,409	1,513,667
3	Pensions	516,005	136,107	318,289	1,128,624	595,798
4	Management Fees	2,492,981	4,012,316	3,752,617	4,312,528	4,064,421
5	Total	$ 8,986,086	$ 9,722,650	$ 9,400,256	$ 11,240,089	$ 10,876,852
		A/	B/	B/	B/	B/
	Growth Rate of Company Forecast from 2005 actual					15.71%

	COMPANY FORECASTS	TRA DOCKET #03-00118 3/31/2004	TRA DOCKET #04-00288 12/31/2005	TRA DOCKET #06-00290 2/29/08
6	Labor	$ 5,066,666	$ 4,383,883	$ 4,702,966
7	Group Insurance	1,463,924	1,386,004	1,513,667
8	Pensions	387,985	892,790	595,798
9	Management Fees	2,507,276	3,062,940	4,064,421
10	Total	$ 9,425,851	$ 9,725,617	$ 10,876,852
		C/	D/	B/

	CAPD FORECASTS	TRA DOCKET #03-00118 3/31/2004	TRA DOCKET #04-00288 12/31/2005	TRA DOCKET #06-00290 2/29/08
11	Labor	$ 5,066,666	$ 4,082,080	$ 4,397,377
12	Group Insurance	1,463,924	1,339,248	1,386,168
13	Pensions	387,985	829,731	12,662
14	Management Fees	2,507,276	3,219,932	3,021,111
15	Total	$ 9,425,851	$ 9,470,991	$ 8,817,318
		B/	E/	F/

A/ Company Exhibit No. 2, Schedule 3, Lines 1, 11, 13, and 15.
B/ Company Rebuttal Exhibit MAM-15, Page 2 of 2.
C/ Company Rebuttal Exhibit MAM-15, Page 1 of 2.
D/ CAPD Work Paper, E-REC-1, P1, Column 1, Lines 1, 6, 7, and 8.
E/ Per TRA Docket #04-00288 Settlement Agreement, Schedule 5, Lines 1, 6, 7, and 8.
F/ CAPD Work Paper, E-REC-1, P1, Column 11, Lines 1, 6, 7, and 8.

Public Utility Accounting: Theory and Application

by

James E. Suelflow

1973

MSU Public Utilities Studies
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ciate them on an item-by-item basis. It is doubtful that such reasoning is as valid today, since methods and tools are available which allow the utility to do this. Electronic data processing equipment can perform the necessary calculations required for unit depreciation with very little effort. The question that must be asked, however, is how much more accurate is unit depreciation versus a group method. The point should be clear: If accuracy is not sacrificed under a group method and may, in fact, be greater than under a single unit method, the use of group depreciation is not only proper and expedient, but also almost a requirement. Whether or not group depreciation is used is certainly a management decision. The utility manager, however, must be aware of the shortcomings as well as the advantages of the method to ensure that within the legal confines and uniform accounting systems prescribed no more or less than the cost of the assets should be reflected through depreciation accounting.

Accounting for Depreciation

The procedure of accounting for depreciation involves a systematic converting of unexpired asset costs into periodic expenses. Expressed another way, it is the appropriate matching of revenues with expenses—depreciation expense representing the extinguishing of an asset's useful life to produce revenues for the particular accounting period. Accounting for depreciation expense recognizes that: (1) the cost of the asset less salvage value is the amount to be systematically allocated as depreciation; (2) no more nor no less than the cost of the asset is depreciable; and (3) by considering this cost only depreciation will keep the initial investment of nominal dollars intact. The asset remains on the utility's accounting records until it is either retired or replaced, and only then are the accounting records relieved of a particular item.

The journal entries involved in the life of an asset are presented below.

(1) To record the asset placed into utility service:

Dr. Electric Plant in Service

Cr. Accounts Payable, Cash, Construction Work in Process, or Materials and Supplies

ACCOUNTING FOR PUBLIC UTILITIES

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Contributing Authors: The following were the original contributing authors of *Accounting for Public Utilities*. While much of what these individuals originally wrote has been removed or replaced through the annual update process, we wish to continue to recognize their contributions in the creation of this book.

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to produce revenues adequate to cover operating expenses plus depreciation, taxes, and capital costs.

This measure is used primarily in rate proceedings of transportation companies and, in some instances, in establishing water or wastewater company rate levels. It has been used as a substitute for the rate base/rate of return approach in situations in which investor-provided capital and the related capital costs have not been a significant factor in the total cost of providing services.

[2] Considerations Affecting the Ratemaking Approach

The particular ratemaking approach used must fit into a framework of conceptual, practical, and legal considerations.

[a] Conceptual

Conceptually, any of these approaches may be acceptable in the determination of revenue requirements for a regulated utility. The utility incurs costs in providing customer services and is entitled to a reasonable opportunity to recover those costs (presumably incurred at reasonable levels for prudent purposes). Accordingly, the ratemaking process, by whatever means employed, should result in producing rates that, when applied to sales or to services rendered, generate revenues equal to the cost of service incurred. This is fundamental to traditional ratemaking philosophies and procedures, and the structuring of the cost components in a particular format (i.e., the style of ratemaking) should facilitate this objective.

[b] Practical

Practical considerations typically have more effect on the ratemaking style or format than conceptual considerations. Most often, the physical, economic, and financial characteristics of the regulated entity dictate the approach used. Capital intensive companies, such as electric, gas, and telephone utilities, require large fixed investments in plant facilities and are generally financed with substantial amounts of debt and equity capital. In these instances, the rate base has a significant role in measuring service costs. Concurrently, the capital markets provide a ready source of data for assessing the costs of debt and equity capital supporting the rate base. These conditions are ideally suited for application of the rate base/rate or return measure.

Some regulated companies do not have the attributes that are suited for rate base/rate of return applications. Transportation companies, for example, generally are not capital intensive because so many of them lease a large portion of the operating facilities. As a result, operating costs dominate the cost of service, and capital investment (and the related capital cost requirements) are much less significant. In these situations, an alternative measure, such as the operating ratio approach, is more useful in establishing revenue levels required to offset the costs of service.

Other examples of companies not having the attributes that are conducive to rate base/rate of return measurements are found in the water/wastewater industry. Although water/wastewater companies are capital intensive, many situations exist in which customers provide substantial portions of the capital funds in the form of contributions in aid of construction. These customer-provided funds are normally deducted from the rate base and often result in nominal (or even negative) rate base amounts. If the capital that *investors* supply is relatively insignificant or even nonexistent, that capital does not provide an adequate foundation for using the rate base/rate of return measure of service costs, and an alternative measure, such as the operating ratio, is applied.

In addition, a utility may be involved in nonregulated or nonjurisdictional operations or in a variety of classes or types of service. These conditions require practical considerations in choosing the ratemaking approach to cost measurement. An example may be given as follows:

Company *A*	Company *B*
—Electric services only. —One regulatory jurisdiction. —One class of service under one general rate schedule. —No nonutility investments or operations.	—Electric and gas service. —Regulated by several states for retail sales and by the Federal Energy Regulatory Commission (FERC) for wholesale sales. —Multiple classes of service and multiple rate schedules (e.g., residential, commercial, industrial, special, etc.). —Investments in nonregulated operations.

The differences between the above companies could result in differing approaches because an approach that functions well in Company *A* may be somewhat cumbersome in Company *B*.

[c] Legal

Legal provisions under controlling regulatory statutes may also limit the mechanics that may be used to develop revenue requirements. Statutory language may differ considerably between rate jurisdictions. In some instances, the regulator has wide discretion as to the measure used, while in others, the statutes may specify the approach in some detail. Illustrations are as follows:

State *A*

The commission is responsible for fixing just and reasonable rates at a level that will provide the utility with a reasonable opportunity to recover all costs prudently incurred in providing utility service.

State *B*

The commission is responsible for fixing just and reasonable rates at a level that will provide the utility with a reasonable opportunity to recover prudently incurred:

(1) operating costs;

(2) depreciation;

TENNESSEE-AMERICAN WATER COMPANY
CASE NO. TRA03-00118
DIRECT TESTIMONY
ROY L. FERRELL, SR.

1. Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Roy L. Ferrell and my address is 1600 Pennsylvania Avenue, Charleston, WV 25302.

2. Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by American Water Works Service Company, Inc. ("Service Company"), as Director of Rates and Planning for the Service Company's Southeast Region (the "Southeast Region"). My primary responsibilities are to supervise the preparation and filing of rate cases, annual business plans, and five-year strategic business plans for American affiliates assigned to the Southeast Region, consisting of; Tennessee, Virginia, West Virginia, Maryland and Kentucky.

3. Q. WOULD YOU DESCRIBE YOUR EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE?

A. Yes. In September 1968, I joined the Service Company as a junior accountant for what was then known as the Southern Division. From January 1971 to November 1973, I was assigned as a rate accountant and assisted in the preparation of rate cases for both West Virginia Water Company and Huntington Water Corporation in West Virginia. In December 1973, I received a Bachelor of Science in Business Administration from the wage rates through the attrition year. The wage rates for each pay class in effect for the attrition year were pro-rated based upon the number of days in the attrition year. The result is an average attrition year wage rate for each union employee.

For non-union hourly and clerical employees, current wage rates that became effective on April 1, 2002 were adjusted for wage increases of 3% on April 1, 2003. As was done for union wage rates, the test year wage rate was calculated based upon the number of days each of those wages were in effect.

21. Q. HOW WERE THE ATTRITION YEAR WAGE LEVELS FOR SALARIED EMPLOYEES DETERMINED?

A. Salaried employees are exempt from overtime pay. For that reason, the current annual salary for each employee has been adjusted for expected wage increases of 3% on April 1, 2003. Consistent with the other employee classes, the 2003 salaries were calculated based upon the number of days each of the salary amounts would be in effect.

PENSION ADJUSTMENT

22. Q. PLEASE EXPLAIN THE COMPANY'S PENSION ADJUSTMENT IN THIS CASE.

A. The Company participates with all its American Water Services ("AWS") affiliates in a system-wide Pension Plan. Its actuary, Towers Perrin, prepares the AWS's pension calculations. The Company's adjustment to pension expense is based on Towers

Perrin's Actuarial Report for 2002-2003.

23. Q. HAVE THE COMPANY'S CIRCUMSTANCES REGARDING PENSION EXPENSE CHANGED SINCE 1996?

A. Yes. In 1996, the Company was advised that the mutual insurance company that held most of the AWS pension assets was converted to a stock company, and the stock was distributed as a one-time dividend to the respective policyholders. AWS's pension fund, as one of the largest policyholders, received a one-time $47,000,000 gain from the sale of this stock. This gain caused the Plan to become fully funded; that is, the Plan reached the "full funding limit" under ERISA when the Plan's assets on July 1, 1996, exceeded actuarial accrued liability plus normal cost. As a result, no ERISA contribution had been required until the test year in this case.

OTHER POSTRETIREMENT EMPLOYEE BENEFITS <u>("OPEBs"):</u>

24. Q. MR. FERRELL, WHAT ARE THE SPECIFIC AREAS OF OPEBs THAT YOU WILL BE ADDRESSING?

A. I will address the Company's actual booking of OPEBs expensed and capitalized during the test year, twelve months ended July 31, 2002. I will also explain the Company's OPEB recovery sought in this case.

25. Q. WHAT OPEBs COST IS REFLECTED ON THE COMPANY'S BOOKS FOR THE TEST YEAR?

Commission recommended a disallowance of eight vacant positions.[7] Consequently, there appears to be a pattern of petitioning for funding by the American Water Companies for vacant positions in their cost of service. Further, in TAWC's last rate proceeding, an employee level of 119[8] was included in TRA Order in Docket #03-00118 dated June 25, 2004. Yet, almost immediately after the TRA Order was approved, TAWC cut the number of employee positions from 123 at the end of June 2003 to 108 at the end of July 2003, a cut of 15 employee positions.[9] This systematic bloating of employee levels by TAWC should not be allowed.

Therefore, it is the CAPD's contention that the forecast of Operation and Maintenance Labor should be based on a known and measurable employee level and not a speculative employee level.

TAWC has included $105,157 in its forecast of Operations and Maintenance Labor for "incentive payroll."[10] The incentive payroll is based on three performance goals: (1) Financial; (2) Operational; and

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[7]Public Service Commission of West Virginia Case No. 03-0353-W-42T, Page 32.

[8]M. Miller direct testimony, Page 14, Lines 17-18.

[9]TAWC response to CAPD First Set of Discovery, Question 12.

[10]TAWC response to CAPD First Set of Discovery, Question 16.

Interrogatories and Requests for Production
Of Documents by the Staff of the
State Corporation Commission (First Set)
To Tennessee-American Water Company
Rate Case No. 04-00288

GENERAL:

9. Q. IF TAWC, ITS PARENT, MULTI-STATE UTILITY, OR AFFILIATED UTILITY SERVICE COMPANY, SEEKS TO RECOVER IN ITS RATES TO THE TENNESSEE RATEPAYERS ANY EMPLOYMENT SPEARATION PAYMENTS MADE UNDER ANY OF THE CONTRACTS, STATE THE AMOUNT OF ANY SPEARATION PAYMENTS SINCE THE LAST RATE FILING IN TENNESSEE.

A.

Tennessee American Water Severed Employees			
Name	Severance Date	Amount of Severance	
Dwight Falls	8/3/2003	$	29,946.40
Pat Freeman	8/3/2003	$	16,960.00
Erleen Jones Ok	8/3/2003	$	25,100.80
Nancy Head Ok	8/3/2003	$	30,528.00
Margaret Jacobs Ok	8/3/2003	$	35,955.20
Sandra Smith Ok	8/3/2003	$	19,673.60
Elizabeth Caudle	8/3/2003	$	19,673.60
Thomas Morrow Ok	8/3/2003	$	40,206.00
Dianna Holland Ok	8/3/2003	$	30,012.00
Laurie Moore	8/3/2003	$	18,300.00
Frank Henderson Ok	8/31/2003	$	16,960.00
Beverly Scheidt	9/28/2003	$	13,400.00
Marilyn Cotton	11/23/2003	$	21,030.40
Mike Loftin	6/6/2004	$	6,820.00
Shirley Frazier	8/15/2004	$	47,479.64
Dan Bailey	8/29/2004	$	93,659.02
Larry Stanley	8/29/2004	$	46,079.05
Donald Walker	8/29/2004	$	45,379.72
Joseph Harris	9/12/2004	$	69,850.48
Kim Durham	9/12/2004	$	15,919.80
Henry Janow	9/12/2004	$	50,895.76
Beth Ortega	9/26/2004	$	14,697.20
Total Severance		$	708,526.67

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

July 21, 2005

IN 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. 04-00288**

ORDER APPROVING SETTLEMENT AGREEMENT

This matter came before Chairman Pat Miller, Director Deborah Taylor Tate and Director Sara Kyle of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this Docket, at a Hearing held on January 31, 2005 for consideration of the *Proposed Settlement Agreement* ("*Settlement Agreement*") between the Tennessee American Water Company ("TAWC" or "the Company"), the Consumer Advocate and Protection Division of the Office of the Attorney General of Tennessee ("Consumer Advocate"), the City of Chattanooga ("Chattanooga") and the Chattanooga Manufacturers Association ("CMA") (collectively "the parties").

Background

On October 25, 1999, TAWC and Chattanooga entered into a settlement agreement of a previously-filed condemnation lawsuit[1] wherein Chattanooga sought to acquire certain assets of TAWC. Section 2.B of the settlement agreement stated as follows:

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[1] *See City of Chattanooga v Tennessee-American Water Company et al*, Case No 99-C-1081, Circuit Court of Hamilton County, Division IV

> [The Company] and the City will file a joint petition with the Tennessee Regulatory Authority ("TRA") seeking permission to reduce over a two-year period the current charge of $301.00 a year per fire hydrant to $50.00 a year per fire hydrant at the end of that period. If the TRA does not approve this provision, then this section is null and void.

In accordance with the settlement agreement, on November 17, 1999 TAWC filed a tariff for approval in TRA Docket No. 99-00891. TAWC proposed to decrease, in quarterly reductions, its annual charges to Chattanooga for fire hydrants from the rate of $301.20 per hydrant to a reduced rate of $50.00 per hydrant. According to TAWC, the reductions would result in an annual revenue impact of negative $1,127,964.[2] During an Authority Conference held on January 11, 2000, a majority[3] of the Directors voted to approve the proposed reduction in annual fire hydrant charges to Chattanooga. In its Order approving TAWC's tariff filing, the Authority recognized that the lost revenues would be imputed into TAWC's subsequent rate filings, thus reflecting the decision of the Company and its stockholders to absorb the contribution loss.[4]

On February 7, 2003, in Docket No. 03-00118, TAWC sought TRA approval of an increase in annual revenues of $3,866,813 and an overall rate of return of 8.559% with an 11% return on equity during the attrition year ending March 31, 2004. In the proposed tariffs filed by TAWC, the additional annual revenues would be recovered by increased charges to all classes of customers. Chattanooga, the Consumer Advocate and CMA intervened in that docket and participated in the hearing held on June 30 and July 1, 2003. In advance of the hearing, TAWC and the Consumer Advocate filed with the Authority a Proposed Settlement Agreement relating to specific issues, including a return of 7.73%

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[2] *See In re Tariff Filing to Reduce Fire Hydrant Annual Charges as Part of a Settlement Agreement Between the City of Chattanooga and Tennessee-American Water Company*, Docket No 99-00891, Company's Response to Authority Data Request, December 20, 1999, Attachment A

[3] Director Lynn Greer voted not to approve the tariff

[4] *See In re Tariff Filing to Reduce Fire Hydrant Annual Charges as Part of a Settlement Agreement Between the City of Chattanooga and Tennessee-American Water Company*, Docket No 99-00891, *Order Approving Tariff*, p 5 (September 26, 2000)

on investments and a 9.9% return on equity.

The panel voted unanimously to accept the Proposed Settlement Agreement[5] and, by its acceptance, determined the rate base to be $87,062,756, the return on investment to be 7.73% and the return on equity to be 9.9%. The two issues remaining for determination were the question of continued imputation of the reduction of fire hydrant charges and the appropriate rate design for implementing the rate increase. In Docket No. 99-00891, the TRA approved the tariff filing by TAWC that voluntarily reduced rates to Chattanooga by $1,127,964 per year for public fire protection service. As part of its Petition in Docket No. 03-00118, TAWC requested the TRA reinstate this revenue stream. The parties in Docket No. 03-00118 were unable to reach a settlement on this issue. The panel found that while the record contained no evidence necessitating a modification of the Order in Docket No. 99-00891, there was evidence to support TAWC's claim that additional revenue requirement may be necessary. For these reasons, a majority of the panel found that the imputation of reduced fire hydrant rates to Chattanooga should be discontinued.[6] The Authority concluded that TAWC was entitled to a rate increase of $2,745,411. As to $1,127,964 of the rate increase, the amount of $563,982 was ordered to be recovered directly from Chattanooga through an increase to the fire hydrant rate.

Travel of this Docket

On September 10, 2004, TAWC filed a petition to change and increase certain rates and charges so as to permit it to earn a fair and adequate rate of return on its

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[5] *Id* at 44

[6] *See In 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 03-00118, *Final Order Approving Rate Increase and Rate Design and Approving Rates Filed by Tennessee American Water Company* and *Concurrence and Dissent of Director Pat Miller* (June 25, 2004)

property used and useful in furnishing water service to its customers ("*Petition*") The pre-filed direct testimonies of Mr. Paul T. Diskin, Mr. Michael A. Miller, Mr. John S. Watson, Mr. James H. Vander Weide, Dr. Edward L. Spitznagel, Jr., Mr. Paul Herbert, and Mr. Monty L. Bishop were filed along with the *Petition*.

TAWC's *Petition* was considered at a regularly scheduled Authority Conference held on September 27, 2004, at which time the panel voted unanimously to suspend the proposed rate increase for ninety (90) days, from October 10, 2004 to January 7, 2005 and to appoint the Authority's General Counsel or his designee as Hearing Officer in the proceeding to hear preliminary matters prior to the Hearing, to rule on any petitions for intervention, and to set a procedural schedule to completion.

On October 1, 2004, the Consumer Advocate filed a *Petition to Intervene* in this proceeding, which was granted by the Hearing Officer on October 11, 2004.[7] On October 25, 2004, CMA filed its *Petition to Intervene by the Chattanooga Manufacturers Association* and on October 26, 2004, Chattanooga filed its *Petition to Intervene*. In an Order issued on October 28, 2004, the Hearing Officer granted both petitions for intervention.

Following discovery in the form of interrogatories and requests for production of documents, the intervening parties submitted pre-filed direct testimony as follows. Chattanooga filed the direct testimony of Mr. Trevor Hamilton, Ms. Daisy Madison and Mr. James "Tony" Quarles; CMA filed the direct testimony and exhibit of Mr Michael Gorman, Mr. Jack Callaghan and Mr. Dan Nuckolls, and the Consumer Advocate filed the direct testimony of Dr. Steve N. Brown, Mr. Michael D. Crysler, and Mr. Terry Buckner. Rebuttal testimony of Mr. Paul T. Diskin, Mr. Michael A. Miller, Mr. John S.

[7] *See Order Granting Petition For Intervention And Establishing Procedural Schedule* (October 11, 2004)

Watson, Dr. James H. Vander Weide and Mr. Paul Herbert was filed by TAWC. CMA filed rebuttal testimony of Mr. Michael Gorman.

On December 15, 2004, the Hearing Officer ordered that the proposed rate increase, which was initially suspended on September 27, 2004, should be re-suspended through March 9, 2005 or until the panel acted on the merits of the *Petition*, whichever occurred first. A Hearing was scheduled in this Docket to begin on January 31, 2005.

On January 27, 2005, TAWC and the Consumer Advocate filed the *Settlement Agreement* relating to specific issues and in which those parties stipulated to the following.

1. The Parties stipulate and agree that Tennessee-American is entitled to earn a 7.76% return on investments with a 9.9% return on equity, as shown in attached Schedule 9.

2. The Parties further stipulate and agree that a 7.76% return on investment generates a revenue deficiency of $297,005. The revenue deficiency is shown in attached Schedule 1.

3. The Parties further stipulate and agree that Tennessee-American shall withdraw its request for the "Low Income Tariff" as referenced and described in paragraph 13 of its Petition.

4. The Parties further stipulate and agree that Tennessee-American shall measure and report service metrics as summarized in attached Schedule 10.

5. The Parties further stipulate and agree that the increase in rates attributable to the revenue deficiency of $297,005 shall be allocated to all classes of customers in an across-the-board percentage increase of 0.93% to the metered tariffs, as shown in attached Schedule 11.

6. In light of the General Assembly's enactment of Tenn. Code Ann. § 65-5-101(d)(2004) prohibiting privately-owned water utilities from charging municipal governments for fire hydrant service, the Attorney General and Tennessee-American further stipulate and agree that public fire hydrant service charges of $897,285 approved by the Tennessee Regulatory Authority ("TRA") in TRA Docket No. 03-00118 to be allocated to municipal governments shall be allocated to all classes of customers exclusive of municipal

> governments in an across-the-board percentage increase of 2.90% to the metered tariffs, as shown in attached schedule 11 . . .

The Hearing

The Hearing in this matter was held before the voting panel assigned to this Docket on January 31, 2005. Participating in the Hearing were the following parties and their respective counsel:

> **Tennessee American Water Company** - R. Dale Grimes, Esq. and J. Davidson French, Esq., Bass, Berry and Sims, PLC, 315 Deaderick Street, AmSouth Center, Suite 2700, Nashville, Tennessee 37238-3001;
>
> **Consumer Advocate and Protection Division** – Timothy C. Phillips, Esq. and Joe Shirley, Esq., Office of the Attorney General, P.O. Box 20207, Nashville, Tennessee 37202;
>
> **Chattanooga Manufacturers Association** – Kristy Godsey, Esq., Boult, Cummings, Conners & Berry, PLC, 1600 Division St., #700, Nashville, Tennessee 37203 and David C. Higney, Esq., Grant, Konvalinka & Harrison, P.C., 633 Chestnut Street, 9th Floor, Chattanooga, Tennessee 37450; and
>
> **City of Chattanooga, Tennessee** - Michael A. McMahan, Esq. and Phillip A. Noblett, Esq., Special Counsel, 801 Broad Street, Suite 400, Chattanooga, Tennessee 37402.

At the Hearing, the parties presented information to the panel regarding the *Settlement Agreement*. At the time of the Hearing, TAWC and the Consumer Advocate had signed the *Settlement Agreement* and, although Chattanooga and CMA had not signed the *Settlement Agreement* at the time of the Hearing, they confirmed their intent to become signatories. Additionally, at the time of the Hearing, the *Settlement Agreement* contained an error which the parties agreed to delete. Specifically, the *Settlement Agreement* presented at the Hearing contained language in numbered paragraph 6 on page 2 that stated, ". . . allocated to all classes of customers exclusive of municipal governments in an across-the-board percentage increase . . . ." The parties agreed that the language in paragraph 6 should not have contained the phrase "exclusive of municipal governments."

After hearing from all the parties, the panel voted unanimously to accept the *Settlement Agreement* contingent on the aforementioned correction and all parties becoming signatories. By acceptance of the *Settlement Agreement*, the Authority determined the rate base to be $87,611,390, the return on investment to be 7.76% and the return on equity to be 9.9%. Additionally, the panel voted unanimously to authorize the Hearing Officer to dispense with a written motion by TAWC to end the suspension of the rate increase proposed in the *Petition*. On February 4, 2005, consistent with the panel's decision, the parties filed a corrected *Settlement Agreement* signed by all parties.

IT IS THEREFORE ORDERED THAT:

1. The *Proposed Settlement Agreement* filed by the Tennessee American Water Company, the Consumer Advocate and Protection Division of the Office of the Attorney General of Tennessee, Chattanooga Manufacturers Association and the City of Chattanooga, Tennessee, attached hereto as Exhibit A, is accepted and approved and is incorporated into this Order as if fully rewritten herein.

2. The Hearing Officer is authorized to dispense with any written motion by TAWC to end the suspension of the proposed rate increase.

Pat Miller

Pat Miller, Chairman

Deborah Taylor Tate

Deborah Taylor Tate, Director

Sara Kyle

Sara Kyle, Director

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IN THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN 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. 04-00288**

PROPOSED SETTLEMENT AGREEMENT

For the sole purpose of settling the case of 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, TRA Docket No. 04-00288, the Office of Attorney General through the Consumer Advocate and Protection Division ("Attorney General"), the City of Chattanooga ("City"), the Chattanooga Manufacturers Association ("CMA"), and Tennessee-American Water Company ("Tennessee-American") (collectively, the "Parties") hereby agree and stipulate as follows in the above-styled case set for hearing on January 31, 2005:

1. The Parties stipulate and agree that Tennessee-American is entitled to earn a 7.76% return on investments with a 9.9% return on equity, as shown in attached Schedule 9.

2. The Parties further stipulate and agree that a 7.76% return on investment generates a revenue deficiency of $297,005. The revenue deficiency is shown in attached Schedule 1.

EXHIBIT
A

3. The Parties further stipulate and agree that Tennessee-American shall withdraw its request for the "Low Income Tariff" as referenced and described in paragraph 13 of its Petition.

4. The Parties further stipulate and agree that Tennessee-American shall measure and report service metrics as summarized in attached Schedule 10.

5. The Parties further stipulate and agree that the increase in rates attributable to the revenue deficiency of $297,005 shall be allocated to all classes of customers in an across-the-board percentage increase of 0.93% to the metered tariffs, as shown in attached Schedule 11.

6. In light of the General Assembly's enactment of Tenn. Code Ann. § 65-5-101(d) (2004) prohibiting privately-owned water utilities from charging municipal governments for fire hydrant service, the Parties further stipulate and agree that public fire hydrant service charges of $897,285 approved by the Tennessee Regulatory Authority ("TRA") in TRA Docket No. 03-00118 to be allocated to municipal governments shall be allocated to all classes of customers in an across-the-board percentage increase of 2.90% to the metered tariffs, as shown in attached Schedule 11.

7. The Parties further stipulate and agree that Tennessee-American shall submit with its next rate case petition a cost of service study in the same form as that submitted by Dr. Herbert in Tennessee-American's last rate case, TRA Docket No. 03-00118. The Parties further stipulate and agree that in any future proceeding each Party reserves its right to proffer its own testimony and evidence regarding the sufficiency, conclusions, weight and relevancy of such cost of service study.

8. In the event that the TRA does not accept the Proposed Settlement in whole or in part, the Parties are not bound by any position set forth herein.

TENNESSEE-AMERICAN WATER COMPANY

BY: ______________________

R. Dale Grimes (BPR #6223)
BASS, BERRY & SIMS PLC
(615) 742-6200

BY: ______________________

J. Davidson French (BPR #15442)
BASS, BERRY & SIMS PLC
(615) 742-6200

CHATTANOOGA MANUFACTURERS ASSOCIATION

BY: ______________________

Henry M. Walker (BPR #282)
BOULT, CUMMINGS, CONNERS & BERRY
(615) 252-2363

BY: ______________________

David C. Higney (BPR #14888)
GRANT, KONVALINKA & HARRISON
(423) 756-8400

CONSUMER ADVOCATE AND PROTECTION DIVISION OF THE OFFICE OF THE TENNESSEE ATTORNEY GENERAL

BY: ______________________

Timothy C. Phillips (BPR #12751)
Senior Counsel
(615) 741-3533

BY: ______________________

Joe Shirley (BPR #22287)
Assistant Attorney General
(615) 741-3549

CITY OF CHATTANOOGA

BY: ______________________

Michael A. McMahan (BPR #810)
Special Counsel
(423) 757-5338

Dated: February 3, 2005

CERTIFICATE OF SERVICE

I hereby certify that a true and exact copy of the foregoing has been forwarded by facsimile and/or first-class mail, postage prepaid on February 4th, 2005, to the following:

T.G. Pappas, Esq.
R. Dale Grimes, Esq.
J. Davidson French, Esq.
Bass, Berry & Sims, PLC
AmSouth Center
315 Deaderick Street, Suite 2700
Nashville, TN 37238-3001

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633 Chestnut Street, 9th Floor
Chattanooga, TN 37450

TIMOTHY C. PHILLIPS
Senior Counsel

#81968

Tennessee-American Water
Index to Schedules
For the 12 Months Ending December 31, 2005

Tennessee-American Water
Revenue Deficiency
For the 12 Months Ending December 31, 2005

Line No.		CAPD		Company		Difference
1	Rate Base	87,611,390	A/	87,611,390	A/	-
2	Operating Income at Present Rates	6,616,813	B/	5,846,425	B/	770,388
3	Earned Rate of Return (Line 2/Line 1)	7.55%		6 67%		0 88%
4	Cost of Capital	7.76%	C/	7 997%	E/	-0 24%
5	Required Operating Income (Line 1*Line 4)	6,798,644		7,006,283		(207,639)
6	Operating Income Deficiency (Line 5-Line 2)	181,830		1,159,858		(978,027)
7	Gross Revenue Conversion Factor	1 633418	D/	1 69890763	E/	(0.065490)
8	Revenue Deficiency (Line 6*Line 7)	297,005		1,970,491		(1,673,486)

A/ Schedule 2
B/ Schedule 3
C/ Schedule 9
D/ Schedule 8
E/ Diskin REVISED Exhibit 1, Schedule 1

Tennessee-American Water
Comparative Rate Base
For the 12 Months Ending December 31, 2005

Line No.		CAPD A/	Company A/	Difference
1	Utility Plant in Service	160,157,718	160,157,718	-
2	Construction Work in Progress	801,659	801,659	-
3	Utility Plant Capital Lease	1,590,500	1,590,500	-
4	Limited-Term Utility Plant - Net	(3,270)	(3,270)	-
5	Working Capital	1,385,205	1,385,205	-
6	Def Maint	5,641	5,641	-
7	Total Additions	163,937,453	163,937,453	-
8	Accumulated Depreciation	51,928,414	51,928,414	-
9	Accumulated Amort of Utility Capital Lease	742,234	742,234	-
10	Accumulated Deferred Income Taxes	13,486,419	13,486,419	-
11	Customer Advances for Construction	2,432,851	2,432,851	-
12	Contributions In Aid of Construction	7,765,092	7,765,092	-
13	Unamortized Investment Tax Credit	45,733	45,733	-
14	RWIP	(74,680)	(74,680)	-
15	Total Deductions	76,326,063	76,326,063	-
16	Rate Base	87,611,390	87,611,390	-

A/ Company Exhibit 1, Sch 2

Tennessee-American Water
Income Statement at Current Rates
For the 12 Months Ending December 31, 2005

Line No		CAPD		Company		Difference
1	Operating Revenues	33,057,417	A/	33,057,417	A/	-
2	Operations and Maintenance Expense	16,262,091	B/	16,709,359	B/	(447,268)
3	Depreciation and Amortization Expense	4,558,016	C/	4,558,016	C/	-
4	Taxes Other Than Income	3,314,870	D/	3,456,977	G/	(142,107)
5	State Excise Tax	170,901	E/	378,505	H/	(207,604)
6	Federal Income Tax	2,163,517	E/	2,136,926	H/	26,591
7	Total Operating Expense	26,469,395		27,239,783		(770,388)
8	AFUDC	28,791	F/	28,791	F/	-
9	Net Operating Income for Return	6,616,813		5,846,425		770,388

A/ Company Exhibit 2, Sch 2
B/ Schedule 5
C/ Company Exhibit 2, Sch. 1
D/ Schedule 6
E/ Schedule 7
F/ Company Exhibit 2, Sch 3
G/ Company Exhibit 2, Sch 1, but does not tie to Company's supporting workpapers (See Sch. 6)
H/ Company Exhibit 2, Sch. 6

Docket No 04-00288
Exhibit CAPD-RTB
Schedule 4

Tennessee-American Water
Income Statement at Proposed Rates
For the 12 Months Ending December 31, 2005

Line No.		Current Rates	A/	Adjustments	C/	Proposed Rates
1	Operating Revenues	32,522,732	B/	297,005		32,819,737
2	Forfeited Discount Revenues	534,685	B/	4,990		539,675
3	Total Revenues	33,057,417		301,995		33,359,412
4	Operations and Maintenance Expense	16,262,091		2,809		16,264,900
5	Depreciation and Amortization Expense	4,558,016				4,558,016
6	Taxes Other Than Income	3,314,870				3,314,870
7	State Excise Tax	170,901		19,447		190,348
8	Federal Income Tax	2,163,517		97,909		2,261,425
9	Total Operating Expense	26,469,395				26,589,559
10	AFUDC	28,791				28,791
11	Net Operating Income for Return	6,616,813				6,798,644

A/ Schedule 3
B/ Company Exhibit 2, Sch. 2
C/ Schedule 1, Line 8 x appropriate factor from Schedule 8

Tennessee-American Water
Operation & Maintenance Expenses
For the 12 Months Ending December 31, 2005

Line No		CAPD A/	Company B/	Difference
1	Salaries and Wages	4,082,080	4,383,883	(301,803)
2	Purchased Water	26,148	15,330	10,818
3	Fuel and Power	1,650,433	1,755,680	(105,247)
4	Chemicals	861,861	861,861	-
5	Waste Disposal	118,201	133,438	(15,237)
6	Management Fees	3,219,932	3,062,940	156,992
7	Group Insurance	1,339,248	1,386,004	(46,756)
8	Pensions	829,731	892,790	(63,059)
9	Regulatory Expense	58,000	58,000	-
10	Insurance Other Than Group	673,430	657,000	16,430
11	Customer Accounting	570,625	572,893	(2,268)
12	Uncollectible Expense	289,530	289,530	-
13	Rents	37,888	38,286	(398)
14	General Office Expense	208,057	193,122	14,935
15	Miscellaneous Expense	1,715,487	1,661,970	53,517
16	Other Maintenance Expense	581,440	746,632	(165,192)
17	Total O&M Expense	16,262,091	16,709,359	(447,268)

A/ CAPD Workpapers
B/ Company Exhibit 2, Sch. 3

Tennessee-American Water
Taxes Other Than Income Taxes
For the 12 Months Ending December 31, 2005

Line No		CAPD		Company D/	Difference
1	Other General Taxes	900		900	-
2	Gross Receipts Tax	356,815	A/	566,595	(209,780)
3	TRA Inspection Fee	59,413		59,413	-
4	Property Taxes	2,300,000	B/	2,503,629	(203,629)
5	Franchise Tax	259,938		259,938	-
6	FICA Taxes	332,999	C/	332,999	-
7	Unemployment Taxes	4,805	C/	4,805	-
8	Total Taxes Other Than Income Taxes	3,314,870		3,728,279	(413,409)

A/ CAPD Workpaper T-OTAX2
B/ CAPD Workpaper T-OTAX1
C/ CAPD Workpaper T-OTAX3
D/ Company Exhibit 2, Sch. 5 adjusted by Company Response to CAPD Data Request #17

Tennessee-American Water
Excise and Income Taxes
For the 12 Months Ending December 31, 2005

Line No		Attrition Amount A/	
1	Operating Revenues	33,057,417	B/
2	Salaries and Wages	4,082,080	
3	Purchased Water	26,148	
4	Fuel and Power	1,650,433	
5	Chemicals	861,861	
6	Waste Disposal	118,201	
7	Service Company Charges	3,219,932	
8	Group Insurance	1,339,248	
9	Pensions	829,731	
10	Regulatory Expense	58,000	
11	Insurance Other Than Group	673,430	
12	Customer Accounting	570,625	
13	Uncollectible Expense	289,530	
14	Rents	37,888	
15	General Office Expense	208,057	
16	Miscellaneous Expense	1,715,487	
17	Other Maintenance Expense	581,440	
18	Depreciation and Amortization Expense	4,558,016	
19	Taxes Other Than Income	3,314,870	
20	NOI Before Excise and Income Taxes	8,922,440	
21	AFUDC	28,791	
22	Interest Expense	(3,200,900)	C/
23	Pre-tax Book Income	5,750,331	
24	Schedule M Adjustments	**(4,479,690)**	D/
25	Excise Taxable Income	1,270,641	
26	Excise Tax Rate	6.50%	
27	Excise Tax Payable	82,592	
28	Excise Tax Deferred	88,309	
29	Excise Tax Expense	170,901	
30	Pre-tax Book Income	5,750,331	
31	Preferred Dividend Credit	**(28,824)**	E/
32	Excise Tax	(170,901)	
33	Schedule M Adjustments	(4,479,690)	D/
34	FIT Taxable Income	1,070,917	
35	FIT Rate	35 00%	
36	Federal Income Tax Payable	374,821	
37	ITC Amortization	**(76,368)**	
38	Federal Income Tax Deferred	**1,865,064**	
39	Federal Income Tax Expense	2,163,517	

A/ Schedule 5
B/ Schedule 4
C/ Schedule 1, line 1 * Weighted Cost of Debt per Schedule 9
D/ This is the net difference of the Permanent Differences of $2,950 and the Temporary Differences of $4,482,640 shown on E/
E/ Exhibit No. 2, Schedule 6, Page 2 of 2

Tennessee-American Water
Revenue Conversion Factor
For the 12 Months Ending December 31, 2005

Line No.		Amount		Balance
1	Operating Revenues			1 000000
2	Add: Forfeited Discounts	0 0168	A/	0.016800
3	Balance			1.016800
4	Uncollectible Ratio	0 0093	B/	0.009456
5	Balance			1.007344
6	State Excise Tax	0 0650	C/	0.065477
7	Balance			0 941866
8	Federal Income Tax	0 3500	C/	0 329653
9	Balance			0 612213
10	Revenue Conversion Factor (Line 1 / Line 11)			1.633418

A/ Company Exhibit 2, Sch. 2 ($534,685/$31,840,192)
B/ Company Workpapers
C/ Statutory Rate

Tennessee-American Water
Cost of Capital
For the 12 Months Ending December 31, 2005

Line No	Parent	Ratio	Cost	Weighted Cost	Tax Deductible
1	Short Term Debt	6.30%	2 40%	0.15%	0 12%
2	Long Term Debt	42.30%	6 00%	2 54%	2 05%
3	Preferred Equity	0 30%	5 00%	0.02%	
4	Common Equity	51 10%	9 90%	5 06%	
5	Total	100 00%		**7.77%**	

Line No	Tennessee American.	Ratio	Cost	Weighted Cost	
6	Short Term Debt	0 00%	0 00%	0 00%	
7	Long Term Debt	19 20%	7 71%	1 48%	1.48%
8	Common Equity	80.80%	7 77%	6.28%	
9	Total	100 00%		**7.76%**	**3.65%**

Final Capital Structure

Line No	Parent	Ratio	Cost	Weighted Cost	Tax Deductible
10	Short Term Debt	5 09%	2 40%	0.12%	0.12%
11	Long Term Debt	34.18%	6.00%	2.05%	2.05%
12	Preferred Equity	0.24%	5.00%	0.01%	
13	Common Equity	41.29%	9 90%	4.09%	
	Total Parent	80 80%	**7.76%**	6.27%	
	Tennessee American				
14	Short Term Debt	0.00%	0.00%	0.00%	0.00%
15	Long Term Debt	19.20%	7 71%	1.48%	1 48%
16	Total Subsidiary	19.20%	7 71%	1 48%	
17	Total	100 00%		**7.75%**	**3.65%**

Source Exhibit CAPD-SB, Schedules 37 and 38

TENNESSEE AMERICAN WATER COMPANY
Settlement Agreement Regarding Service Metrics and Reporting
TRA Docket # 04-00288
January 27, 2005
SCHEDULE 10.

Customer Service - Call Center:

1. Begin Reporting Monthly Customer Care Scorecard (as identified in Mike Miller's Rebuttal Testimony) on a monthly basis and reporting to the Tennessee Regulatory Authority (TRA), the CAPD by March 1, 2005.

2. Develop similar Monthly Customer Care Scorecard with "Tennessee Specific" Statistics reporting by January 1, 2006 to TRA and CAPD. TAWC is not currently able to measure dropped calls from TN ratepayers, but will work with the Consumer Advocate toward establishing the necessary mechanisms to measure dropped calls, if practicable.

Tennessee Local Operations:

3. TAWC Employee Reporting by job title with its quarterly reporting to the TRA including allocated Tennessee specific Call Center employees.

4. Field Service (Tennessee Office) - Monthly Reporting To TRA and CAPD by March 1, 2005

   A. Service Orders Worked - Monthly
   B. Appointment Orders - % on-time
   C. Appointments Missed
   D. Meter Reading
      a. Total meters
      b. Meters read
      c. Estimates
      d. % Estimated
      e. Number of Meters not billed 3 months, 6 months, 12 months

Customer Surveys:

5. Customer Survey Responses Reported To TRA and CAPD On A Quarterly Basis beginning 2005) detailed by affiliate:

   A. Satisfaction in Reaching American Water Call Center
   B. Satisfaction with Call Center Operation Problem Resolution
   C. Satisfaction with company response for service
   D. Satisfaction with water quality

Tennessee American Water Company
Rate Design - Docket #04-00288

Schedule 11

	A/ Present	Fire Hydrant Shift	Post Shift	%	Increase	%	Total
Residential	$ 13,302,692	$ 385,753	$ 13,688,445	2.90%	$ 127,686	0.93%	$ 13,816,131
Commercial	9,464,969	274,466	9,739,435	2.90%	90,849	0.93%	9,830,285
Industrial	3,399,370	98,575	3,497,945	2.90%	32,629	0.93%	3,530,574
Other Public Authority	2,500,771	72,518	2,573,289	2.90%	24,004	0.93%	2,597,292
Sales for Resale	920,714	26,699	947,413	2.90%	8,837	0.93%	956,250
Private Fire	1,354,352	39,274	1,393,626	2.90%	13,000	0.93%	1,406,625
Public Fire	897,285	(897,285)	-	-100.00%		0.00%	-
Total	$ 31,840,153	$ -	$ 31,840,153	0.00%	$ 297,005	0.93%	$ 32,137,158

A/ TAWC witness Herbert Exhibit

TENNESSEE-AMERICAN WATER COMPANY
CASE NO. ____________
DIRECT TESTIMONY
Paul T. Diskin

1. Q. WILL YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE RECORD?

A. My name is Paul T. Diskin and my business address is 800 W. Hershey Park Drive, Hershey, PA 17033.

2. Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by American Water as the Manager of Rates and Regulations.

3. Q. WHAT ARE YOUR RESPONSIBILITIES IN THIS POSITION?

A. I supervise and coordinate the preparation of data and various exhibits in rate matters as well as maintaining and administering the Company's tariffs. I also present testimony in formal rate cases and other regulatory proceedings. I have testified in the various Pennsylvania Public Utility Commission proceedings which are listed in Appendix A and B.

4. Q. WOULD YOU PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE?

A. I received a Bachelor of Science degree in Business Administration with a dual concentration in Accounting and Management from Clarion State College in December of 1977. In December of 1992, I was awarded an MBA from York College of Pennsylvania. I have completed the continuing education program conducted by the National Association of Regulatory Utility Commissioners (NARUC) and the University of Utah. In addition, I am a Certified Management Accountant (CMA) recognized by the Institute of Management Accountants. I also serve as the Chairman of the Rates and Revenue Committee of the Pennsylvania Chapter of the National Association of Water Companies.

My experience in the water utility industry began in 1979 when I was employed as a Junior Accountant in the Continuing Property Records Section of the American Water Works Service Company, Inc. My principal duties were to process investment and retirement work orders and to record additions and retirements of utility plant in the subsidiary ledgers of the various districts of the Company's predecessor corporations. Later in the same year, I was assigned to the Rates and Revenue Section to aid in the preparation of rate filings. In 1980, I was promoted to the position of Rate Analyst I, and in 1981 was promoted to Rate Analyst II. Effective January 1982, I was promoted to the position of Revenue Requirement Specialist. On July 1, 1988, I became Assistant Director of Rates and Revenue for the Pennsylvania Region. Effective January 1, 1993, I was transferred to Pennsylvania-American. On July 1, 2001, I became Director of Rates and Planning. Effective July 15, 2004, I was appointed as Manager of Rates and Regulations for the Southeast Region of American Water.

5. Q. WAS THE COMPANY'S ACCOUNTING EXHIBITS PREPARED BY YOU OR UNDER YOUR SUPERVISION?

A. Yes, they were.

6. Q. WHAT IS THE SOURCE OF THE INFORMATION USED IN THE COMPANY'S ACCOUNTING EXHIBITS?

A. The information contained in the Accounting Exhibits was prepared from the financial and operational records of the Company.

7. Q. PLEASE EXPLAIN THE INCREASE IN RATES THAT THE COMPANY IS SEEKING IN THIS PROCEEDING?

A. The Company is seeking a rate increase that would produce additional annual revenues of $1.9 million or 5.9%. The Company last filed for a rate increase in 2003.

8. Q. WHAT ARE THE TEST YEAR AND ATTRITION YEAR SELECTED BY THE COMPANY FOR THIS FILING?

A. The Company has selected the twelve months ending March 31, 2004, as its test year and an attrition year starting on January 1, 2005 and ending December 31, 2005.

9. Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?

A. A. My testimony will 1) sponsor the Company's Accounting Exhibits Nos. 1, 2, and 3 which support the proposed revenue increase of $1,970,887 and 2) support the Company's attrition year level of Revenue, Labor, Fuel and Power, Chemicals, Waste Disposal, Group Insurance, Regulatory Expense, Insurance Other than Group, Uncollectible Expense, Rents, General Office Expense, Miscellaneous Expense, Other Maintenance Expense, AFUDC, General Taxes and Rate Base. Next, I will address the Company's proposed rate base shown on Exhibit No. 1, Schedule 2, consisting of 3 pages. Then, I will address the Company's proposed Computation of Working Capital shown on Exhibit No. 1, Schedule 3, consisting of six pages. I will also address the Company's Operating Revenues Per Books for the Test Year and for the Attrition Year under both Present and Proposed Rates, except for average daily usages for both the residential and commercial customer classes.

10. Q. WHO WILL ADDRESS THE COMPANY'S PROPOSED AVERAGE DAILY USAGE FOR THE RESIDENTIAL AND COMMERCIAL CUSTOMER CLASSES?

A. The Company has retained the services of Dr. Edward L. Spitnagel, Jr., Professor, Washington University in St. Louis, Missouri, to provide weather normalizations for both the residential and commercial customer classes. I will explain how Dr. Spitnagel's averages were used in the Company's bill analysis.

11. Q. WHAT IS THE TEST PERIOD REFLECTED IN THIS CASE?

A. The Company has used a historical test period of twelve months ending March 31, 2004. The Company has adjusted the test period for two levels of adjustments. The first adjustment normalizes the test year. The second level adjusts the normalized year to arrive at the attrition year which is the twelve months ended December 31, 2005.

12. Q. MR. DISKIN, ARE THERE ANY EXHIBITS YOU WISH TO SPONSOR BEFORE YOU CONTINUE?

A. Yes, I would like to give a brief description of the accounting schedules which detail and support the rate base, revenues, expenses, and capitalization for the test year and attrition year.

Exhibit 1 is a financial summary of the filing which details how the Company arrived at the amount of the requested revenue increase. There is also a rate base summary for the test year and attrition year with supporting schedules.

Exhibit 2 is an operating income summary for the test year and attrition year with supporting schedules broken down by major account group.

Exhibit 3 provides a cost of capital summary for the attrition year and supporting schedules which provide detail on each component of the capital structure.

14. Q. HOW DID THE COMPANY DETERMINE THE OPERATING REVENUES SHOWN IN ITS ACCOUNTING EXHIBIT?

A. The Company's operating revenues are obtained from (i) metered sales, (ii) private and public fire service, and (iii) miscellaneous, service revenues, rents from property, and other water revenues.

(i) Metered Sales

The Company uses a bill analysis reflecting the actual billing determinants for the test year, twelve months ended March 31, 2004. Exhibit No. 4, Schedules 1 and 2, sets forth the individual bill analysis by customer classes. This schedule multiplies attrition year billing determinants by present and proposed rates.

15. Q. DID THE COMPANY MAKE ANY ADJUSTMENTS TO PER BOOK REVENUES FOR THE TEST YEAR?

A. Yes, the Company made a total of four adjustments, as follows: (1) weather normalization adjustment for the residential and commercial customer classes, (2) eliminated net change in accrued revenues, (3) annualization of the rate increase that became effective August, 2003 and (4) added revenue for the estimated number of new customers to be added during the attrition year. The estimate is based on historical results. The reasons for these adjustments are identified in the Company's work papers that are filed under separate cover.

16. Q. HOW WERE THE OPERATING EXPENSE ADJUSTMENTS IN THE ACCOUNTING EXHIBIT CALCULATED?

A. The adjustments reflect an ongoing level of operating expenses consistent with the test year matching principles. Known and measurable price adjustments have been included to restate test year expense levels to rate year levels, the first 12-month period in which new rates will be in effect.

17. Q. WHAT IS YOUR TESTIMONY ON THE ISSUE OF COMPANY LABOR EXPENSE?

A. I will address the methodology used by the Company in developing the Going-level provision for labor expense.

18. Q. HOW DID THE COMPANY CALCULATE GOING-LEVEL LABOR EXPENSE IN ITS COST OF SERVICE?

A. The Company calculated labor expense by individual employee. Each employee's wages during the twelve months ended March 31, 2004 were adjusted to account for the wage level to be paid during the first twelve-months in which the new rates will be in effect. This is the same approach the Company has used in prior filings.

19. Q. HOW WERE THE WAGE LEVELS FOR THE ATTRITION

YEAR DETERMINED?

A. For hourly employees, the hours worked during the test year were obtained from the Company's actual payroll records. Adjustments were then made to overtime hours to restate those hours to a level equivalent to the employee's hourly pay rate. For example, the hours paid at time and a half wage rates were multiplied by 1.5 to yield hours that could be applied to the employee's hourly wage rate. Similar adjustments were made for other premium overtime hours. Each employee's equivalent hours were then applied to their average test year wage rate to determine going-level wages.

20. Q. HOW WERE THE AVERAGE RATE YEAR WAGE RATES CALCULATED?

A. For union employees, the Company's existing bargaining agreements were examined. The agreements contain negotiated wage rates through the attrition year. The wage rates for each pay class in effect for the attrition year were pro-rated based upon the number of days in the attrition year. The result is an average attrition year wage rate for each union employee.

For non-union hourly and clerical employees, current wage rates that became effective on April 1, 2003 were adjusted for wage increases of 3% on April 1, 2004. As was done for union wage rates, the test year wage rate was calculated based upon the number of days each of those wages were in effect.

21. Q. HOW WERE THE ATTRITION YEAR WAGE LEVELS FOR SALARIED EMPLOYEES DETERMINED?

A. Salaried employees are exempt from overtime pay. For that reason, the current annual salary for each employee has been adjusted for wage increases that became effective on April 1, 2004. Consistent with the other employee classes, the 2004 salaries were calculated based upon the number of days each of the salary amounts would be in effect.

22. Q. WHAT IS THE BASIS UPON WHICH FUEL AND POWER COST WAS CALCULATED FOR THIS RATE ADJUSTMENT?

A. The basis for fuel and power is based upon expected water pumped to the system during the attrition year (system delivery), and its cost to pump and treat. Attrition year water sales, non-revenue usage water (which is water used for system flushing, street cleaning, sewer flushing, etc.) and an estimated unaccounted for water is combined to arrive at system delivery. Fuel and power is based on KWH's per million gallons system delivery.

Fuel and power costs are based on estimated KWH usage and KWD required to produce the projected system delivery for the attrition year. KWH's per thousand gallons is used to calculate energy charges. The KWH's per thousand gallons required is based on the latest 12 months actual, with adjustments for any known changes that will affect KWH usage. Both KWH and KWD usage is priced at the rates currently being charged by the Chattanooga Electric Power Board. The total attrition year fuel and power expense is $ 1,755,680 which represents an increase of $ 204,058 over the test year expense due to an increase in overall system delivery.

23. Q. WHAT IS THE BASIS FOR THE CHEMICAL COSTS?

A. Chemical costs are based upon expected water pumped to the system (system delivery) for the attrition year and the cost to treat that water. Attrition year water sales, non-revenue usage (used for street cleaning, sewer flushing, etc.) and an estimated unaccounted for water is combined to arrive at system delivery. System delivery, plus water used at the treatment plant, is combined to produce total treatment rate. The total attrition year chemical expense is $861,861 which is an increase of $121,330 over the test year expense due to the increase in system delivery.

24. Q. WHAT IS THE BASIS FOR THE COST OF WASTE DISPOSAL?

A. Waste disposal is based upon the 2005 budget. This amount is slightly higher than that during the test year.

25. Q. PLEASE EXPLAIN THE DEVELOPMENT OF THE ADJUSTMENT FOR GROUP INSURANCE.

A. The group insurance expense for the normalized test year was calculated first by determining the annualized group insurance cost. The cost is determined by applying the group insurance rates in effect at January 1, 2004 to the pro forma insurance coverages based upon the employee complement and salary and wage information. From this amount, an amount representing the employee contribution for their healthcare coverage is subtracted. The result is the Company's annualized group insurance cost.

Since group insurance is an employee benefit, the cost for group insurance is charged based upon direct labor charges. Since 16.61 percent of labor was not charged to expenses (as previously explained) this percentage of group insurance cost is excluded from the Company's claim for group insurance expense.

26. Q. ARE THERE ANY OTHER PAYROLL-RELATED EXPENSES?

A. Yes, there are. The Company's claim for payroll taxes is based on historic and future test year salary and wage expense. As is the case with group insurance, 16.61% of the calculated payroll taxes are eliminated, representing the portion not charged to operations.

27. Q. PLEASE EXPLAIN THE COMPANY'S CLAIM FOR OPEBS.

A. The Company's claim for OPEB expense represents the test year amount accrued of $996,796 less the capitalized portion of $114,043 or a net amount of $882,753.

28. Q. PLEASE EXPLAIN THE COMPANY'S PENSION ADJUSTMENT IN THIS CASE.

A. The Company participates with all its American Water Services ("AWS") affiliates in a system-wide Pension Plan. Its actuary, Towers Perrin, prepares the AWS's pension calculations. The Company's adjustment to pension expense is based on Towers Perrin's Actuarial Report for 2003-2004.

29. Q. MR. DISKIN, YOU LISTED A NUMBER OF OTHER EXPENSE CATEGORIES THAT YOU WILL BE SUPPORTING, WOULD YOU PLEASE DISCUSS EACH ONE?

A. Yes. Each of the following expense categories were reviewed for the test year and adjusted to reflect a normalized test year and further adjusted to an appropriate level of expense for the attrition year. Some of the expense categories were adjusted for an inflation factor of 3.3%.

30. Q. HOW DID YOU ARRIVE AT THE 3.3% INFLATION

FACTOR?

A. I used the Value Line Forecast for the US Economy Gross Domestic Product estimated inflation rate. For the attrition year, I used the annual amount of change of 3.3%.

31. Q. PLEASE CONTINUE.

A. <u>REGULATORY EXPENSE</u>

The company has estimated the cost of the preparation and presentation of this current filing to be $150,000. The Company is proposing to amortize these costs over a three year period resulting in an annual cost of $50,000. Also, included in the attrition year cost is the Cost of Service Study Expense in the amount of $40,000 which the company is proposing an amortization period of five years resulting in an annual cost of $8,000. Total attrition year expense is $58,000.

<u>INSURANCE OTHER THAN GROUP</u>

The Company's proposed level for this expense for the attrition year is $657,000 and is based on the Company's 2005 budget. This expense category includes costs for general liability, workers compensation, and property insurance.

<u>CUSTOMER ACCOUNTING EXPENSE</u>

Customer accounting expense for the test year was $572,632. The Company applied the inflation factor of 3.3% to these expenses, excluding uncollectibles and postage to arrive at an increase of $1,713.

This category includes costs associated with the customer billing and collecting function. It includes costs for office supplies, report forms, computer supplies, postage, collection agency fees, lock box expenses, janitorial service, telephone expense, and other miscellaneous customer accounting expense.

<u>UNCOLLECTIBLE EXPENSE</u>

The uncollectible percentage of .93% was derived by taking the net charge offs, less recoveries as a percentage of total revenues for the test year. The attrition year uncollectible expense is

$307,859.

GENERAL OFFICE EXPENSE

General office expense for the test year was $189,347. The inflation factor of 3.3% was applied to the remaining expenses (excluding postage) to arrive at an attrition year expense of $193,122. This expense category includes costs associated with the general expenses for the offices. These include report forms, office supplies, computer supplies, overnight mail expenses, janitorial services, telephone expense, electrical expense, employee expenses, credit line fees, bank service charges, and other miscellaneous general office expenses.

MISCELLANEOUS EXPENSE

Miscellaneous expense for the test year totaled $1,596,601. The Company is proposing four adjustments to this category. The first adjustment reflects the inflation factor adjustment of 3.3%. This results in an increase of $50,067. The Company did not apply the inflation factor to the Employee Stock Option Plan (ESOP) expense or the 401K expense.

The second adjustment eliminated the cost of temporary employees and normalized the test year. This resulted in a decrease of $18,671.

The third adjustment was to include the cost of leasing vehicles for an amount of $9,780. The Company is in the process of switching from purchasing vehicles to leasing vehicles.

The fourth adjustment is the amortization of the transition costs for the Shared Services Center and the Customer Call Center annualized for an entire year.

The proposed miscellaneous expense for the attrition year is $1,661,970 which includes adjustments totaling $(140,306)

MAINTENANCE EXPENSE

Maintenance expense for the test year was $630,331. An adjustment was made to include the costs of preventative programs totaling $92,450. The Company is proposing to increase this total by $23,851 to reflect the inflation factor to arrive at an attrition year balance of $746,632.

This expense category includes costs associated with maintaining the property of the Company. This would include repair parts, tools, maintenance supplies, contracted services, paving, maintenance agreements, and other miscellaneous maintenance expenses.

AFUDC

The Company's proposed amount for AFUDC is $28,791 and is based upon the 2005 budget. This adjustment was made to reflect the AFUDC as an above the line item for ratemaking purposes.

TAXES OTHER THAN INCOME

PROPERTY TAXES

Property taxes for the test year were $2,625,029. An additional amount was accrued during the last quarter of the test year to true-up the prior years' actual payment. This resulted in a normalized adjustment of ($320,865). The attrition year adjustment of $199,465 reflects the increase in the appraised value of the Company property through the attrition year.

GROSS RECEIPTS TAXES

Gross receipts tax was calculated based on projected jurisdictional revenues for Tennessee including Other Operating revenues. The result was reduced by Vendor's Compensation, Franchise Tax, Excise Tax, a $5,000 exemption, and multiplied by the 3% tax rate.

PSC FEES

The PSC Inspection Fee was based on projected 2004 jurisdictional revenues. This was reduced by uncollectibles and a $5,000 exemption to arrive at taxable revenues. The result is multiplied by the Tennessee statutory rates that were taken from the 2003 return.

FRANCHISE TAX

Franchise tax, as imposed by the state of Tennessee, applies to the company's apportioned net worth or value of property owned and used in Tennessee, whichever is greater, as shown at the close of the corporation's fiscal year. The Franchise Tax is paid in arrears and is based on the previous years original cost of assets. For this filing, we utilized the balances as of March 31, 2004 as a basis for the tax and multiplied it by the statutory rate of $.25 per $100.

RATE BASE:

32. Q. HAS THE COMPANY CHANGED THE METHODOLOGY OF CALCULATING REQUESTED RATE BASE FROM THE APPROACH ADVOCATED IN ITS LAST CASE?

A. No, it has not. This is the same approach used and approved in Case No. 03-00118. Shown on Exhibit No. 1, Schedule 2, Column No. 1 of the Company's Accounting Exhibit, is the rate base for the historical test year totaling $85,553,595. In Column No. 2, the Company has summarized it's requested ratemaking adjustments to rate base totaling $2,057,796 over and above the historical test year. In Column number 3, the Company has shown its requested rate base for the mid-point of the Attrition Year, aggregating $87,611,392.

33. Q. PLEASE DETAIL THE COMPONENTS THAT COMPRISE RATE BASE SHOWN ON EXHIBIT 1, SCHEDULE 2.

A. UTILITY PLANT IN SERVICE

Includes the actual undepreciated original cost of all land and land rights, easements, structures and improvements, together with equipment in service at March 31, 2004. To this actual March 31, 2004 balance, the budgeted cumulative effect of additions and retirements to Utility Plant for the Period January 1, 2005 through December 31, 2005 have been reflected to arrive at utility plant balance at the mid-point of the attrition year. These additions and retirements are summarized on Exhibit 1, Schedule 2, page 3 of 3 and are addressed in greater detail in Mr. Bishop's Direct Testimony.

CONSTRUCTION WORK IN PROGRESS

This amount is shown in both March 31, 2004 actual and December 31, 2005 budgeted balances. These amounts are representative of all actual or budget project work for utility plant that are not in service at December 31, 2005.

LIMITED-TERM UTILITY PLANT-NET

WORKING CAPITAL

Working capital shown on Exhibit 1, Schedule 2, is further detailed on Exhibit 1, Schedule 3, and I will explain those components that make-up working capital.

<u>Average Cash</u>

Average cash represents a monthly average which was computed based on 12 monthly averages of daily cash balances per bank statements for the year ended July 31, 2002. The monthly average was computed by dividing the total daily balances for the month by the same month's total days.

<u>Prepaid Insurance, Prepaid Taxes, and Materials and Supplies</u>

Prepaid insurance, prepaid taxes, and materials and supplies represent an average of the thirteen month end balances for the test year ending July 31, 2002.

<u>Deferred Regulatory Expense</u>

The deferred regulatory expense consists of an average of two cases unamortized balances at the September 30, 2003 attrition year mid point. The amounts included in rate base include $187,000 for the current rate case expense and $36,000 for the current Cost of Service Study.

Unamortized Debt Expense

Unamortized debt expense was calculated by starting with the July 31, 2002 unamortized debt expense and subtracting the cumulative amortizations to arrive at the balances of the beginning and ending of the attrition year. The average of these two balances, plus the unamortized debt expense of the proposed debt issue, result in a $238,260 balance at the attrition year midpoint.

Other Deferred Debits

Other deferred debits consist of three items detailed below:

- Unamortized transition costs of the Customer Call Center which total $915,709.
- Unamortized transition costs of the Shared Services Center which total $343,096.
- Unamortized security costs which total $250,458.

Lead-Lag Study

The Company is using a Lead/Lag Study that was performed based on historical data for the twelve months ending July 31, 2002, which includes a working capital allowance of $525,000.

Incidental Collections

Incidental collections represent the average balance of funds for sewer billing and sales tax not yet remitted or paid for the 12 months ending July 31, 2002. The average balances resulting in a reduction to rate base working capital for sewer billing and sales tax are $1,895,262 and $85,819 respectively.

RATE DESIGN

34. Q. HOW DID THE COMPANY DEVELOP THE TARIFF RATES REQUESTED IN THIS CASE?

A. The proposed tariff rates are based upon an across the board increase.

35. Q. PLEASE EXPLAIN THE COMPANY'S ATTRITION LEVEL OF INCOME TAXES?

A. The Company's calculated level of Income Taxes for the attrition year is the present rate amount of $2,515,431. This is broken down into three components:

1. Current provision for federal and state income taxes of $348,230 and $65,347 as shown on pages 1 and 2 of Accounting No. 2, Schedule 6.
2. Deferred federal and state income taxes of $1,865,064 and $313,158 are also shown on pages 1 and 2 of Accounting Exhibit No. 2, Schedule 6.
3. The annual amortization of the 3%, 4% and 10% is ($76,368) Investment tax credits for the test year.

36. Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

APPENDIX A

	DOCKET NO
Pennsylvania-American Water Company (Wastewater)	R-00005212
	R-00973973
Collection System Improvement Charge	R-00027982
Pennsylvania-American Water Company (Water)	
	R-00038304
Facility Protection Charge	R-00027983
	R-00964438
	R-00973944
	R-00943231
	R-00932670
	R-922428
	R-911909
	R-901652
	R-891208
Pennsylvania-American Water Company (Pre-merger)	R-880916
Keystone Water Company	R-850245
Berwick District	R-842759
Northeast Region	R-842755
Southern Central Region	R-842756
Riverton Consolidated Water Company	R-850153
Western Pennsylvania Water Company	R-870825
	R-860397
Butler District	R-842624
Clarion-Punxsutawney District	R-842625
Indiana-Kane	R-842623
Warren District	R-842622
	R-850097
Western Region	R-842621
	R-850096

APPENDIX B

FORMAL CUSTOMER COMPLAINT PROCEEDINGS

DOCKET NO.	***COMPLAINTANT***
C-00971106	Gilbert
C-00981273	Drew
C-00992304	Sayegh
C-00992569	Waste Recycling
C-00003629	Ellis
C-00004511	Valvanno
C-20016173	Noll
C-00014733	Morra
C-20016207	Collier Township
C-00015337	Parks, et al
Z-015005197	Lamberton

TENNESSEE REGULATORY AUTHORITY

STATE OF PENNSYLVANIA

COUNTY OF DAUPHIN

BEFORE ME, the undersigned authority, duly commissioned and qualified in and for the State and County aforesaid, personally came and appeared Paul T. Diskin, 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 testimony would set forth in the annexed transcript consisting of 21 pages.

Paul T Diskin

Paul T. Diskin

Sworn to and subscribed before me
this 3rd day of September 2004.

Emily T. Hicks

Notary Public

My commission expires ________________.

NOTARIAL SEAL
Emily T. Hicks, Notary Public
Derry Township Dauphin County
My Commission Expires March 4, 2006

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Overall Financial Summary

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 1
Page 1 of 1

Line No	Description	Reference to Supporting Exhibit	Proposed Test Year
1			
2			
3			
4			
5			
6			
7	Rate Base	Exhibit 1, Schedule 2	$87,611,392
8			
9	Operating Income at Attrition Year Present Rates	Exhibit 2, Schedule 1	5,157,576
10			
11	Earned Rate of Return		5 890%
12			
13	Rate of Return	Exhibit 3, Schedule 1	8 263%
14			
15	Required Operating Income		7,239,329
16			
17	Operating Income Deficiency		2,081,753
18			
19	Gross Revenue Deficiency Factor		1 69890763
20			
21	Revenue Deficiency		3,536,706
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Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Computation of Attrition Year Rate Base

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 2

Line No		Footnote Reference	Per Books Rate Base @ 3/31/2004	Adjustments	Rate Base at Mid-Point of Attrition Year
4	Additions				
6	Utility Plant in Service (UPIS)	(1)	$150,299,728	$9,857,990	$160,157,718
8	Construction Work in Progress	(2)	3,059,985	(2,258,326)	801,659
10	Utility Plant Capital Lease		1,590,500		1,590,500
12	Deferred Maintenance		10,286	(4,645)	5,641
14	Limited-Term Utility Plant - Net	(3)	(3,270)	0	(3,270)
16	Working Capital		1,385,205	0	1,385,205
18	Total Additions		156,342,435	7,595,019	163,937,453
20	Deductions				
22	Accumulated Provision for Depreciation UPIS	(4)	46,581,674	5,346,740	51,928,414
24	RWIP		(74,680)	0	(74,680)
26	Accumulated Amortization of Utility Plant Capital Lease	(5)	618,528	123,706	742,234
28	Deferred Income Taxes	(6)	13,019,768	466,651	13,486,419
30	Customer Advances for Construction	(7)	3,066,640	(633,789)	2,432,851
32	Contributions in Aid of Construction	(8)	7,527,564	237,527	7,765,092
34	Unamortized Investment Tax Credit	(9)	49,345	(3,612)	45,733
36	Utility Plant Acquisition Adjustment	(10)	0	0	0
38	Total Deductions		70,788,839	5,537,223	76,326,062
40	Rate Base		85,553,595	2,057,796	87,611,392

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Attrition Year Rate Base
Footnotes

Line No	FOOTNOTE REFERENCE	DESCRIPTION	AMOUNT
6	(1)	Net Additions to UPIS through December 31, 2005	$9,857,990
8	(2)	Adjustment to CWIP through December 31, 2005	(2,258,326)
10	(3)	Adjustment to Deferred Maintenance	(4,645)
12	(4)	Adjustment to Limited -Term Utility Plant - Net	0
14	(5)	Adjustment to Accumulated Provision for Depreciation of UPIS	5,346,740
16	(6)	Adjustment to Accumulated Amortization of Utility Plant - Capital Lease	123,706
18	(7)	Adjustment to Deferred Income Taxes	466,651
20	(8)	Change in Customer Advances	(633,789)
22	(9)	Change in Contributions in Aid of Construction	237,527
24	(10)	Change in Unamortized Investment Tax Credit	(3,612)
26	(11)	Adjustment to Utility Plant Acquisition Adjustment	0

Net Additions to Utility Plant in Service
From End of Test Year to Mid-Point of Attrition Year

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 2

Line No	Account Number	Account Description	4/1/2004 to 12/31/2004 Additions	1/1/2005 to 12/31/2005 Additions	4/1/2004 to 12/31/2004 Retirements	1/1/2005 to 12/31/2005 Retirements	Net Additions to Utility Plant in Service 8/1/02-9/30/03
3	301 00	Organization	$0	$0	$0	$0	$0
4	303 00	Land & Land Rights	$0	$0	$0	$0	$0
5	303 99	Comprehensive Planning Study	$0	$0	$0	$0	$0
6	304 22	Pumping Structures	$0	$0	$0	$0	$0
7	304 31	Water Treatment Structures	$0	$0	$0	$0	$0
8	304 32	Water Treatment Structures-Painting	$0	$0	$0	$0	$0
9	304 40	T & D Structures	$0	$0	$0	$0	$0
10	304 51	Office Structures	$0	$0	$0	$0	$0
11	304 52	Stores , Shop, & Garage Structures	$0	$0	$0	$0	$0
12	304 53	Miscellaneous Structures	$111,000	$40,450	$0	$0	$151,450
13	306 20	Lakes, Rivers, & Other Intakes	$0	$0	$0	$0	$0
14	310 20	Power Generation Equipment	$0	$0	$0	$0	$0
15	311 22	Electric Pumping Equipment	$0	$0	$0	$0	$0
16	311 23	Deisel Pumping Equipment	$0	$0	$0	$0	$0
17	311 27	Other Pumping Equipment	$0	$0	$0	$0	$0
18	320 31	Water Treatment Equipment	$0	$0	$0	$0	$0
19	320 33	Granular Activated Carbon	$0	$0	$0	$0	$0
20	330 41	T & D Reservoirs & Standpipes	$175,000	$15,000	$0	$0	$190,000
21	330 42	T & D Reservoirs & Standpipes-Painting	$0	$1,590,000	$0	$0	$1,590 000
22	330 43	Elevated Tanks & Standpipes	$0	$0	$0	$0	$0
23	331 40	T & D Mains not Classified	$2,043,435	$872,752	$62,300	$13,100	$2,840,787
24	331 41	T & D Mains - Mains (4" or less)	$0	$0	$0	$0	$0
25	331 44	T & D Mains - Mains (6" - 8")	$0	$0	$0	$0	$0
26	331 42	T & D Mains - Mains (6" - 10")	$0	$0	$0	$0	$0
27	331 45	T & D Mains - Mains (10" - 16")	$564,972	$0	$12 758	$0	$552,214
28	331 43	T & D Mains - Mains (12" or More)	$0	$0	$0	$0	$0
29	333 40	Services	$0	$438,083	$0	$14,500	$423,583
30	334 41	Meters	$1 040,074	$762,777	$0	$40,000	$1,762,851
31	334 42	Meters-Metal Case/Old Style	$558,517	$0	$6 500	$0	$552,017
32	334 43	Meters - Plastic Case	$0	$0	$0	$0	$0
34	334 44	Meters - Metal Case/New Style	$56 000	$0	$3,500	$0	$52,500
35	334 45	Meter Installations	$0	$0	$0	$0	$0
36	335 40	Hydrants	$214,000	$115,370	$11,000	$9 500	$308,870
37	339 00	Other P/E SS	$0	$0	$0	$0	$0
38	340 51	Office Furniture	$0	$0	$0	$0	$0
39	340 53	Computer & Peripheral Equipment	$500,000	$235,000	$0	$0	$735 000
40	340 56	Computer & Periph Personal	$397,573	$50 000	$0	$30,000	$417,573
41	340 57	Computer & Periph Other	$0	$0	$0	$0	$0
42	340 55	Computer Software	$0	$0	$0	$0	$0
43	340 58	Computer Software Personal	$0	$0	$0	$0	$0
44	340 59	Computer Software Other	$0	$0	$0	$0	$0
45	340 54	Other Office Equipment	$127,200	$0	$0	$0	$127,200
46	341 52	Light Trucks	$0	$0	$33,500	$0	($33,500)
47	341 53	Heavy Trucks	$0	$0	$0	$0	$0
48	341 54	Automobiles	$0	$0	$0	$0	$0
49	341 55	Transportation-Other	$0	$0	$0	$0	$0
50	342 50	Stores Equipment	$0	$0	$0	$0	$0
51	343 50	Tools, Shop, & Garage Equipment	$124,945	$62 500	$0	$0	$187,445
52	344 50	Laboratory Equipment	$0	$0	$0	$0	$0
53	345 50	Power Operated Equipment	$0	$0	$0	$0	$0
54	346 51	Communication Equipment	$0	$0	$0	$0	$0
55	346 53	Communication Equipment-Telephone	$0	$0	$0	$0	$0
56	347 51	Miscellaneous Equipment	$0	$0	$0	$0	$0
57		Total Plant in Service	5 912,716	4 181 932	129,558	107,100	9,857 990

Tennessee Regulatory Authority
Company. Tennessee American Water
Docket No

Computation of Working Capital

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 3

Line No	Item	Amount
7	Average Cash	366,929
9	Prepaid Insurance	92,558
11	Prepaid Taxes	234,228
13	Materials & Supplies	346,535
15	Deferred Regulatory Expenses	223,500
17	Unamortized Debt Expense	106,689
19	Other Deferred Debits	1,452,847
21	Lead - Lag Study	543,000
23	Total	3,366,286
25	Less	
27	Customer Deposits	0
29	Incidental Collections	1,981,081
31	Total	1,981,081
33	Working Capital Requirement	1,385,205

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Computation of Working Capital
Lead/Lag Study

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 3

Line No	Description	Days	Amount
2			
4	Net Operating Funds		30,485,321
6	Average Daily Operating Funds		83,521
8	Composite Average Days Interval Between		
10	(A) Date Service Furnished and Date Collections Deposited	42 07	
12	(B) Date Expenses Incurred and Date of Payment	35 57	
14	(C) Net Interval	6 5	
16	Operating Funds Advanced		542,887
18	Lead/Lag Study Capital		542,887
20	Use		543,000

Tennessee Regulatory Authority
Company Tennessee Amencan Water
Docket No

Composite Average Days Interval between Date Expenses are Incurred and Date of Payment

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 3

Line No	Description	Amount	Post Payment or (Lead) Days	Dollar Days
1				
2				
3				
4	Payrolls Charged to Expense - Hourly	3,107,510	5 50	17,091,305
5	Payrolls Charged to Expense - Salary	1,871,463	14 02	26,237,915
6	Fuel and Power	1,551,622	50 65	78,589,653
7	Chemicals	740,531	28 27	20,934,819
8	Waste Disposal	179,951	31 23	5,619,870
9	AWWS Charges	2,507,276	(4 46)	(11,182,451)
10	Group Insurance	862,753	(1 31)	(1,130,207)
11	Pensions	387,895	0 00	0
12	Insurance Other than Group	709,686	(21 72)	(15,414,380)
13	Rents	28,624	9 24	264,486
14	Telephone Expense	153,334	(2 73)	(418,602)
15	Postage Expense	265,193	24 77	6,568,832
16	Amortizations	0	0 00	0
17	Stock E	51,951	23 77	1,234,875
18				
19				
20	Other Operating and Maintenance Expenses	3,694,518	20 51	75,774,559
21	Total O & M Expenses	16,112,307		
22				
23	Depreciation and Amortization	4,121,753	0 00	0
24	Taxes, Other than Income			
25	Payroll	457,400	10 61	4,853,016
26	Other	3,276,201	174 52	571,762,599
27	FIT-Current	224,991	37 00	8,324,667
28	SIT-Current	42,872	58 63	2,513,585
29	Deferred Taxes	1,092,221	0 00	0
30	Interest Expense	3,255,531	87 97	286,389,062
31	Preferred Dividends	70,000	89 48	6,263,600
32	Net Earnings	1,832,045	0 00	0
33	Net Operating Funds	30,485,321		1,084,277,203
34				
35				
36	Average Days Interval between Date Expenses are Incurred and Date of Payment		35 57	
37				
38				
39				
40				
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42				
43				
44				
45				

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Average Days Interval between Number of Days
From Date Services are Furnished to Date Collections are Received

	Revenues Amount	Median Service Days	Dollar Days
Revenues less private fire	28,082,480	15 21	427,134,524
Private Fire billed in advance	1,048,596	(45 63)	(47,847,435)
Total	29,131,076		379,287,089

Average Median Service Days	13 02
Number of Days between the Reading Date and the Date the Bills are Mailed	4 62
Number of Days between the Reading Date and the Date the Bills are Mailed	24 43
Total Average Days' Interval between Number of Days from Date Services are Furnished to Date Collections are Received	42 07

Notes private fire Quarterly is billed in advance
All monthly customers are billed in arrears

Tennessee Regulatory Authority
Company Tennessee American Water
Docket No

Computation of Average Materials & Supplies Paid

Test Year Twelve Months Ended March 31, 2004
Exhibit No 1, Schedule 3

Line No	End of Month Date	Amount
7	Jul-01	440,599
9	Aug-01	494,423
11	Sep-01	469,586
13	Oct-01	389,330
15	Nov-01	339,416
17	Dec-01	389,297
19	Jan-02	405,581
21	Feb-02	412,027
23	Mar-02	361,829
25	Apr-02	358,597
27	May-02	368,397
29	Jun-02	362,666
31	Jul-02	364,209
33	Total	5,155,957
39	Average Balance	396,612

Tennessee Public Service Commission
Company Tennessee-American Water Company
Docket No

Computation of Average Materials and Supplies Unpaid

Line No	End of Month Date	Amount
7	Jul-01	49,999
9	Aug-01	51,015
11	Sep-01	80,838
13	Oct-01	52,586
15	Nov-01	18,040
17	Dec-01	38,256
19	Jan-02	66,200
21	Feb-02	42,800
23	Mar-02	72,819
25	Apr-02	37,813
27	May-02	44,500
29	Jun-02	41,302
31	Jul-02	54,837
33	Total	651,005
39	Average Balance	50,077

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Statement of Income Per Books for the Test Year and for the Attrition Year under both Present and Proposed Rates

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 1
Page 1 of 1

Line No	Description	Adjustment Shown on Schedule No	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
1	Operating Revenues	2	$30,890,359	$1,962,223	$32,852,582	$204,835	$33,057,417	$1,970,887	$35,028,304
2									
3	Operation and Maintenance Expenses	3	15,444,029	1,681,869	17,125,898	(445,330)	16,680,568	18,068	16,698,636
4	Depreciation and Amortization	4	4,249,882	(78,174)	4,171,708	386,308	4,558,016	0	4,558,016
5	Taxes, Other than Income	5	3,656,650	(287,776)	3,368,874	88,103	3,456,977	53,491	3,510,468
6	Income Taxes	6	2,278,494	476,570	2,755,064	(239,633)	2,515,431	697,297	3,212,728
7									
8	Total Operating Expenses		25,629,055	1,792,489	27,421,544	(210,553)	27,210,991	768,856	27,979,847
9									
10	Utility Operating Income		5,261,304	169,734	5,431,038	415,388	5,846,426	1,202,031	7,048,457
11									
12	Other Income								
13	AFUDC		147,213	(147,213)	0	0	0	0	0
14	Income from M & J and Contract Work		(24,247)	24,247	0	0	0	0	0
15	Interest Income		100,031	(100,031)	0	0	0	0	0
16	Gain/Loss on Sale of Property		0	0	0	0	0	0	0
17									
18	Total Other Income		222,997	(222,997)	0	0	0	0	0
19									
20	Other Deductions								
21	Miscellaneous Amortization		0	0	0	0	0	0	0
22	Miscellaneous Other Deductions		56,247	(56,247)	0	0	0	0	0
23									
24	Total Other Deductions		56,247	(56,247)	0	0	0	0	0
25									
26	Taxes Applicable to Other Income and Deductions								
27	General Taxes		0	0	0	0	0	0	0
28	State Income Taxes		0	0	0	0	0	0	0
29	Federal Income Taxes		0	0	0	0	0	0	0
30									
31	Total Taxes Applicable to Other Income and Deductions		0	0	0	0	0	0	0
32									
33	Income before Interest Charges		5,428,054	2,984	5,431,038	415,388	5,846,426	1,202,031	7,048,457
34									
35	Interest Charges								
36	Interest on Long-Term Debt		1,925,116	755,793	2,680,909	0	2,680,909	0	2,680,909
37	Interest on Long-Term Capital Lease		142,283	(142,283)	0	0	0	0	0
38	Amortization of Debt and Discount Expense		19,525	(19,525)	0	0	0	0	0
39	Interest on Short-Term Debt		248,055	(135,912)	112,143	0	112,143	0	112,143
40	Other Interest		0	0	0	0	0	0	0
41	Allowance for Borrowed Funds Used During Construction		(83,895)	83,895	0	0	0	0	0
42	Total Interest Charges		2,251,084	541,968	2,793,052	0	2,793,052	0	2,793,052
43									
44	Net Income		3,176,970	(538,984)	2,637,986	415,388	3,053,374	1,202,031	4,255,405
45									

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Operating Revenues Per Books for the Test Year and for the Attrition Year under both Present and Proposed Rates

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 2

Line No	Description	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
1	Sales of Water							
2								
3	Metered Sales to General Customers							
4								
5	Residential	$12,048,536	$1,234,572	$13,283,108	$19,585	$13,302,693	$1,220,903	$14,523,596
6								
7	Commercial	9,345,680	38,092	9,383,772	81,198	9,464,970	867,029	10,331,999
8								
9	Industrial	3,227,598	171,772	3,399,370	0	3,399,370	310,607	3,709,977
10								
11	Other Public Authorities	2,381,918	89,780	2,471,698	29,072	2,500,770	228,910	2,729,680
12								
13	Sales for Resale	882,779	37,935	920,714	0	920,714	84,148	1,004,862
14								
15	Private Fire Service	1,183,197	101,914	1,285,111	69,279	1,354,390	124,025	1,478,415
16								
17	Public Fire Service	642,114	253,671	895,785	1,500	897,285	(897,285)	0
18								
19	Total Sales of Water	29,711,822	1,927,736	31,639,558	200,634	31,840,192	1,938,337	33,778,529
20								
21								
22	Other Operating Revenues							
23								
24	Activity / New Service Fees	103,523	0	103,523	0	103,523	0	103,523
25								
26	Late Payment Penalty	498,944	32,372	531,316	3,369	534,685	32,550	567,235
27								
28	Rents from Water Property	102,336	0	102,336	0	102,336	0	102,336
29								
30	Sewer Billing Revenues	361,987	2,115	364,102	832	364,934	0	364,934
31								
32	Miscellaneous	25,630	0	25,630	0	25,630	0	25,630
33								
34	Reconnection Fee	86,117	0	86,117	0	86,117	0	86,117
35								
36	Total Other Operating Revenues	1,178,537	34,487	1,213,024	4,201	1,217,225	32,550	1,249,775
37								
38								
39	Total Operating Revenues	30,890,359	1,962,223	32,852,582	204,835	33,057,417	1,970,887	35,028,304
40								
41								
42								
43								
44								
45								

Summary of Adjustments to Operation and Maintenance Expenses

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 3

Line No	Adjustment Number Reference	Description	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
1	1	Operation and Maintenance Labor	$4,631,351	$805,084	$5,436,435	($1,052,551)	$4,383,883	$0	$4,383,883
2									
3	2	Purchased Water	$15,330	0	15,330	0	15,330	0	15,330
4									
5	3	Fuel and Power	$1,520,849	231,077	1,751,926	3,754	1,755,680	0	1,755,680
6									
7	4	Chemicals	$723,833	135,575	859,408	2,452	861,861	0	861,861
8									
9	5	Waste Disposal	$129,719	3,256	132,975	463	133,438	0	133,438
10									
11	6	Management Fees	$2,492,981	0	2,492,981	569,959	3,062,940	0	3,062,940
12									
13	7	Group Insurance	$1,345,749	198,767	1,544,516	(158,512)	1,386,004	0	1,386,004
14									
15	8	Pensions	$516,005	384,607	900,612	(7,822)	892,790	0	892,790
16									
17	9	Regulatory Expense	$113,844	(113,844)	0	58,000	58,000	0	58,000
18									
19	10	Insurance Other than Group	$670,413	(85,413)	585,000	72,000	657,000	0	657,000
20									
21	11	Customer Accounting	$559,654	3,849	563,503	9,390	572,893	0	572,893
22									
23	12	Uncollectible Expense	$269,736	17,928	287,664	1,866	289,530	18,068	307,598
24									
25	13	Rents	$38,286	0	38,286	0	38,286	0	38,286
26									
27	14	General Office Expense	$189,347	(2,394)	186,953	6,169	193,122	0	193,122
28									
29	15	Miscellaneous Expense	$1,596,601	39,718	1,636,319	25,651	1,661,970	0	1,661,970
30									
31	16	Other Maintenance Expense	$630,331	92,450	722,781	23,851	746,632	0	746,632
32									
33	17	Interest on Customer Deposits	0	0	0	0	0	0	0
34									
35	18	AFUDC		(28,791)	(28,791)	0	(28,791)	0	(28,791)
36									
37									
38									
39									
40									
41		Total Operation and Maintenance Expenses	15,444,029	1,681,869	17,125,898	(445,330)	16,680,568	18,068	16,698,636
42									
43									
44									

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Summary of Adjustments to Depreciation and Amortization Expenses

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 4
Page 1 of 2

Line No	Adjustment Number Reference	Description	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
1	1	Depreciation Expense	$4,129,281	($78,174)	$4,051,107	$386,308	$4,437,415	$0	$4,437,415
2									
3	2	Amortization of Utility Plant Acquisition Adjustment	0	0	0	0	0	0	0
4									
5	3	Amortization of Utility Capital Lease	$120,601	0	120,601	0	120,601	0	120,601
6									
7	4	Amortization of Leased Alteration Expense	0	0	0	0	0	0	0
8									
9	5	Amortization of Accumulated Depreciation on CIAC	0		0	0	0	0	0
10									
11									
12									
13			4,249,882	(78,174)	4,171,708	386,308	4,558,016	0	4,558,016
14									
15									
16									
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Attrition Year Provision for Depreciation Expense
For Utility Plant in Service

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 4

Line No	Account Number	Account Description	Depreciable Property at 3/31/2004	Normalized Test Year Depreciation Expense	ADDITIONS	RETIREMENTS	Depreciable Property at Mid-Point of Attrition Year	Depreciation Rate	Attrition Year Depreciation Expense
1	303 99	Comprehensive Planning Study	$405,132	$81,026	0	0	$405,132	20 00%	$81,026
2	304 22	Pumping Structures	1,897,305	73,236	0	0	1,897,305	3 86%	73,236
3	304 31	Water Treatment Structures	1,706,175	77,972	0	0	1,706,175	4 57%	77,972
4	304 32	Water Treatment Structures-Painting	1,700,789	170,079	0	0	1,700,789	10 00%	170,079
5	304 40	T & D Structures	502,632	17,642	0	0	502,632	3 51%	17,642
6	304 51	Office Structures	151,528	6,031	0	0	151,528	3 98%	6,031
7	304 52	Stores , Shop, & Garage Structures	319,733	14,868	151,450	0	471,183	4 65%	21,910
8	304 53	Miscellaneous Structures	383,138	21,609	0	0	383,138	5 64%	21,609
9	306 20	Lakes, Rivers, & Other Intakes	281,452	9,569	0	0	281,452	3 40%	9,569
10	310 20	Power Generation Equipment	222,196	7,644	0	0	222,196	3 44%	7,644
11	311 22	Electric Pumping Equipment	5,676,202	98,198	0	0	5,676,202	1 73%	98,198
12	311 23	Deisel Pumping Equipment	119,296	2,350	0	0	119,296	1 97%	2,350
13	311 27	Other Pumping Equipment	5,145	203	0	0	5,145	3 94%	203
14	320 31	Water Treatment Equipment	12,260,179	523,510	0	0	12,260,179	4 27%	523,510
15	320 33	Granular Activated Carbon	0	0	190,000	0	190,000	36 42%	69,198
16	330 41	T & D Reservoirs & Standpipes	4,840,436	87,128	1,590,000	0	6,430,436	1 80%	115,748
17	330 42	T & D Reservoirs & Standpipes-Painting	551,948	55,195	0	0	551,948	10 00%	55,195
18	330 43	Elevated Tanks & Standpipes	170,895	3,076	0	0	170,895	1 80%	3,076
		330400 Clearwell	680,784						
19	331 40	T & D Mains not Classified	1,991,820	28,085	2,916,187	75,400	4,832,607	1 41%	68,140
20	331 41	T & D Mains - Mains (4" or less)	3,796,632	61,505	0	0	3,796,632	1 62%	61,505
21	331 44	T & D Mains - Mains (6" - 8")	826	11	0	0	826	1 36%	11
22	331 42	T & D Mains - Mains (6" - 10")	48,824,310	664,011	0	0	48,824,310	1 36%	664,011
23	331 45	T & D Mains - Mains (10" - 16")	3,087,274	43,839	564,972	12,758	3,639,488	1 42%	51,681
24	331 43	T & D Mains - Mains (12" or More)	19,813,012	281,345	0	0	19,813,012	1 42%	281,345
			102,029						
25	333 40	Services	14,819,223	337,878	438,083	0	15 257,306	2 28%	347,867
26	334 41	Meters	2,431,779	23,831	1,802,851	0	4,234,630	0 98%	41,499
27	334 42	Meters-Metal Case/Old Style	0	0	558,517	0	558,517	2 45%	13,684
28	334 43	Meters - Plastic Case	91,620	14,064	0	0	91,620	15 35%	14,064
29	334 44	Meters - Metal Case/New Style	130,726	1,281	56,000	59,339	127,387	0 98%	1,248
30	334 45	Meter Installations	6,608,879	108,386	0	0	6,608,879	1 64%	108,386
31	335 40	Hydrants	6,029,971	133,262	329,370	61,000	6,298,341	2 21%	139,193
32	339 00	Other P/E SS	8,526	505	0	0	8,526	5 92%	505
33	340 51	Office Furniture	519,029	14,169	0	0	519,029	2 73%	14,169
34	340 53	Computer & Peripheral Equipment	142,602	22,674	735,000	0	877,602	15 90%	139,539
35	340 56	Computer & Periph Personal	1,133,900	180,290	447,573	30,000	1,551,473	15 90%	246,684
36	340 57	Computer & Periph Other	137,208	21,816	0	0	137,208	15 90%	21,816
37	340 55	Computer Software	3,783,604	601,593	0	0	3,783,604	15 90%	601,593
38	340 58	Computer Software Personal	166,142	26,417	0	0	166,142	15 90%	26,417
39	340 59	Computer Software Other	89,590	14,245	0	0	89,590	15 90%	14,245
40	340 54	Other Office Equipment	137,196	5,584	127,200	0	264,396	4 07%	10,761
41	341 52	Light Trucks	1,127,656	105,549	0	33,500	1,094,156	9 36%	102,413
42	341 53	Heavy Trucks	697,241	69,654	0	0	697,241	9 99%	69,654
43	341 54	Automobiles	148,897	15,694	0	0	148,897	10 54%	15,694
44	341 55	Transportation-Other	35,388	248	0	0	35,388	0 70%	248
45	342 50	Stores Equipment	43,392	2,161	0	0	43,392	4 98%	2,161
46	343 50	Tools, Shop, & Garage Equipment	754,851	29,062	187,445	0	942,296	3 85%	36,278
47	344 50	Laboratory Equipment	351,219	39,056	0	0	351,219	11 12%	39,056
48	345 50	Power Operated Equipment	229,342	21,122	0	0	229,342	9 21%	21,122
49	346 51	Communication Equipment	321,298	14,234	0	0	321,298	4 43%	14,234
50	346 53	Communication Equipment-Telephone	141,250	21,060	0	0	141,250	14 91%	21,060
51	347 51	Miscellaneous Equipment	258,043	7,457	0	0	258,043	2 89%	7,457
52		Amortization of CIAC		(108,317)					(114,521)
53									
54		Total Plant in Service	149,829,441	4 051,107	10,094,648	271,997	158,869,279		4,437,415
55									

Tennessee Regulatory Authority
Company Tennessee-American Water Company
Docket No

Summary of Adjustments to Taxes Other than Income

Test Year Twelve Months Ended March 31, 2004
Exhibit No 2, Schedule 5

Adjustment Number Reference	Description	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
1	Property Taxes	$2,625,029	($320,865)	$2,304,164	$199,465	$2,503,629	$0	$2,503,629
2	Other General Taxes	657,574	0	657,574	(42,030)	615,544	53,491	669,035
3	F U T A Taxes	5,034	1,093	6,127	(1,550)	4,577	0	4,577
4	F I C A Taxes	363,925	36,777	400,702	(67,703)	332,999	0	332,999
5	S U T A Taxes	5,088	(4,781)	307	(79)	228	0	228
	Total	3,656,650	(287,776)	3,368,874	88,103	3,456,977	53,491	3,510,468

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Summary of Income Taxes

Test Year Twelve Months Ended Ma[illegible]31, 2004
Exhibit No [illegible]dule 6
[illegible]1 of 2

Line No	Description	Per Books 12 Months Ended 3/31/2004	Test Year Adjustments Present Rates	Normalized Test Year	Attrition Year Adjustments	Attrition Year at Present Rates	Adjustments for Proposed Rates	Attrition Year at Proposed Rates
					$0			
					0			
1	Federal Income Tax - Current	$86,904	$462 953	$549 857	($201,627)	$348,230	$535,526	$883,756
2								
3	State Income Tax - Current	88,501	13,617	102,118	(36,771)	65,347	161,771	227,118
4								
5	Deferred Federal Income Tax	1,484,214		1,484 214	380 850	1 865 064	0	1,865,064
6								
7	Deferred State Income Tax	313,158	0	313,158	0	313,158	0	313,158
8								
9	Amortization of ITC	(76,368)	0	(76 368)	0	(76,368)	0	(76,368)
10								
11	Adjustment of Prior Years - FIT	0	0	0	0	0	0	0
12								
13	Adjustment of Prior Years - SIT	0	0	0	0	0	0	0
14								
15	Total	2,278,494	476 570	2 372 979	142,452	2 515,431	697,297	3 212,728
16								

Ten[...]gulatory Authority
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Computation of Current Federal and State Income Taxes Based on Current Rate for the
Normalized and Attrition Years and Propos[...]ates for the Attrition Year

Test Year Twelve Months Ended March 31 2004
Exhibit No 2, Schedule 6
Page 2 of 2

Line No	Description	Per Books Test Year Present Rates Federal	Per Books Test Year Present Rates State	Normalized Year Present Rates Federal	Normalized Year Present Rates State	Attrition Year Present Rates Federal	Attrition Year Present Rates State	Attrition Year Proposed Rates Federal	Attrition Year Proposed Rates State
1									
2	Operating Revenues	$30 890 359	$30 890 359	$32 852 582	$32 852 582	$33 057 417	$33 057 417	$35 028 304	$35 028 304
3									
4	Operation and Maintenance Expenses	15 444 029	15 444 029	17 125 898	17 125 898	16 680 568	16 680 568	16 698 897	16 698 897
5	Depreciation and Amortization	4 249 882	4 249 882	4,171 708	4 171 708	4 558 016	4 558 016	4 558 016	4 558 016
6	Taxes Other than Income	3 656 650	3 656 650	3 368 874	3 368 874	3 456 977	3 456 977	3 511,242	3 511 242
7	State Income Taxes Current	88 501	88 501	88 501	88 501	65 347	65 347	227 037	19 635
8	State Income Taxes Deferred	313 158	313 158	313 158	313 158	313 158	313 158	313 158	313 158
9	Federal Income Taxes Current	86 904	86 904	86,904	86 904	86 904	86 904	883 451	86 904
10	Federal Income Taxes - Deferred	1 484 214	1 484 214	1 484 214	1 484 214	1 865 064	1,865 064	1 865 064	1 865 064
11	Investment Tax Credit	(76 368)	(76,368)	(76,368)	(76 368)	(76 368)	(76,368)	(76,368)	(76,368)
12	Subtotal	25,246,970	25,246,970	26 562 889	26,562 889	26,949 665	26,949,685	27,980,496	26 976,547
13	Total Income Before Deductions	5 643 389	5 643,389	6 289 693	6 289 693	6 107 752	6 107 752	7 047 808	8 051,757
14									
15	Total Other Income	222 997	222 997						
16									
17	Total Other Deductions	56 247	56 247						
18									
19	Total Taxes Applicable to Other Income and Deductions	0	0						
20									
21	Total Interest Charges	2 251 084	2 251,084	2 793 052	2 793 052	2 793 052	2 793 052	2 793 052	2,793 052
22									
23	Net Income	3 559 055	3 559 055	3 496 641	3 496 641	3 314 700	3 314 700	4 254 756	5 258 705
24									
25	State Income Taxes	439 248	439 248	102 118	102 118	378,505	378 505	332,793	332 793
26	Federal Income Taxes	1 494 750	1 494 750	1 494 750	1 494 750	1,875 600	1 875 600	2 672 147	2 672 147
27									
28	Pretax income	5 493 053	5 493 053	5 093 509	5 093 509	5 568 805	5 568 805	7 259 696	8 283 645
29	Statutory Additions (Deductions)								
30	Permanent Difference								
31	617 001 Book Over Tax Travel and Entertainment	2 427	2 427	2,427	2 427	2 427	2 427	2,427	2 427
32	618 006 Nondeductible Dues	352	352	352	352	352	352	352	352
33	618 008 Lobbying Expenses	0	0	0	0	0	0	0	0
34	638 006 Nondeductible Penalties	171	171	171	171	171	171	171	171
35									
36	Total Permanent Differences	2 950	2 950	2 950	2 950	2 950	2,950	2 950	2,950
37									
38	Financial Taxable Income	5 496 003	5 496 003	5 096 459	5 096 459	5,571 755	5 571 755	7 262 646	8 286 595
39									
40	Temporary Differences								
41	604 004 Contributions and Advances	74 046	74 046	74 046	74 046	74 046	74 046	74 046	74 046
42	606 001 Book Over Tax Depreciation	1 176	1 176	1 176	1 176	1 176	1 176	1 176	1 176
43	612 001 Book Over Tax Bad Debts	4 756	4 756	4 756	4 756	4 756	4 756	4,756	4 756
44	618 002 Amortization of Regulatory Assets - AFUDC	14 568	14,568	14,568	14 568	14 568	14 568	14 568	14 568
45	618 019 Cost of Service Study	(26 743)	(26 743)	(26,743)	(26 743)	(26 743)	(26 743)	(26 743)	(26 743)
46	618 023 Supplemental Pension	432	432	432	432	432	432	432	432
47	618 028 Accrued OPEB Expense	(85 164)	(85 164)	(85 164)	(85 164)	(85 164)	(85 164)	(85 164)	(85,164)
48	618 029 Incentive Plan Expense	(265 848)	(265 848)	(265 848)	(265 848)	(265 848)	(265 848)	(265 848)	(265 848)
49	618 030 Regulatory Pension Expense (Pension 2 & [...]	16 130	16 130	16,130	16 130	16 130	16 130	16 130	16 130
50	618 032 Miscellaneous Deferred Expenses	150 457	150 457	150 457	150 457	150 457	150 457	150 457	150 457
51	618 036 Vacation Pay	(1 252)	(1 252)	(1 252)	(1 252)	(1,089 396)	(1 089 396)	(1 089 396)	(1 089 396)
52	626 001 Tax Over Book Depreciation	(1 097 563)	(1 097 563)	(1 097 563)	(1 097 563)	(1 097,563)	(1 097 563)	(1,097 563)	(1 097 563)
53	638 014 Cost of Removal	1 144	1 144	1 144	1 144	1 144	1 144	1 144	1,144
54	638 015 AFUDC over Interest Capitalized for Taxes	(186 461)	(186 461)	(186 461)	(186 461)	(186 461)	(186 461)	(186 461)	(186 461)
55	638 019 Deferred Maintenance Expense	3 981	3 981	3 981	3 981	3 981	3 981	3 981	3 981
56	638 027 Abandonment Losses	(627 068)	(627 068)	(627 068)	(627 068)	(627,068)	(627 068)	(627 068)	(627 068)
57	638 028 Management Study Expense	0	0	0	0	0	0	0	0
58	638 034 Regulatory Pension (Pension 1)	(342 639)	(342 639)	(342 639)	(342 639)	(342 639)	(342 639)	(342 639)	(342 639)
	638 036 Miscellaneous Deferred Expenses	(1 044 983)	(1 044 983)	(1 044 983)	(1 044 983)	(1 044 983)	(1,044 983)	(1 044 983)	(1 044 983)
	638 041 Rate Case Expense	(189,312)	(189 312)	(189 312)	(189 312)	(189 312)	(189 312)	(189 312)	(189 312)
	638 055 Deferred Security Costs	14 243	14 243	14 243	14 243	14,243	14 243	14 243	14 243
	638 056 Deferred Customer Service Center Costs	169 784	169 784	169 784	169,784	169,784	169 784	169 784	169 784
59	638 057 Deferred Financial Services Costs	21 820	21 820	21 820	21 820	21 820	21,820	21,820	21 820
60	Total Temporary Differences	(3 394 496)	(3 394 496)	(3 394 496)	(3 394 496)	(4 482 640)	(4,482 640)	(4 482 640)	(4 482 640)
61									
62									
63	Federal Taxable Income Before SIT	2 101 507	2 101 507	1 701 963	1 701 963	1,089,115	1 089 115	2 780 006	3 783 955
64	Preferred Dividend Credit			(28 824)		(28 824)		(28 824)	
65									
66	State Income Tax	126 090		102 118		65 347		227 037	
67	Taxable Income	1,975 417	2,101,507	1,571,021	1 701,963	994 944	1,089,115	2,524,145	3,783,955
68									
69	Computation of Taxes								
70	State Income Tax @ 8 00%		126 090		102 118		65 347		227 037
71	Federal Income Tax @ 35 00%	691 396		549 857		348 230		883 451	
72	Less Tax Credits	(76 368)	0	(76 368)	0	(76,368)	0	(76,368)	0
73	Total Current Income Tax	615 028	126 090	473 489	102 118	271,862	65,347	807 083	227,037
74									
75	Deferred SIT								
76									
77	Deferred FIT Including ITC	623 062						1 529 201	

Rate of Return Summary
At the Mid-Point of the Attrition Year

Tennessee Regulatory Authority
Company: Tennessee American Water
Docket No: 04-

Test Year: Twelve Months Ended: March 31, 2004
Exhibit No. 3, Schedule 1

Line No	Class of Capital	Reference	Amount	Percent of Total	Cost Rate	Weighted Cost of Capital
1						
2						
3	Long-term Debt	Schedule 2	$43,040,110	48.88%	6 26%	3.060%
4						
5	Short-term Debt		4,699,624	5 34%	2 40%	0.128%
6						
7	Preferred Equity	Schedule 3	1,400,000	1 59%	5 00%	0 080%
8						
9	Common Equity					
10	Common Stock		18,537,633	21.05%	10 70%	2 252%
11	Retained Earnings		20,384,057	23.15%	10 70%	2 477%
12						
13	Total Capitalization		88,061,424	100 01%		7.997%
14						
15						
16						
17						
18	Total Common Equity Return Proposed		10 70%			
19						
20						
21						
22						
23						
24						
25						
26						
27						
28						
29						
30						

Embedded Cost of Long-Term Debt
At the Mid-Point of the Attrition Year

Tennessee Regulatory Authority
Company: Tennessee American Water
Docket No: 04-

Test Year: Twelve Months Ended: March 31, 2004
Exhibit No. 3, Schedule 2
Page 1 of 1

Line No	Debt Issue Type, Coupon Rate	Interest Rate	Issue Date	Maturity Date	Principal Amount	Face Amount Outstanding	Unamortized (Issuance) Debt Exp	Carrying Value	Annual Interest Expense	Annual Amortization of Issue Expense	Total Cost
4											
5	General Mortgage Bonds										
6											
7	9 25% Series	9 25%	01/12/90	12/01/19	2,500,000	2,500,000	21,989	2,478,011	231,250	1,524	232,774
8	8 25% Series	8 25%	06/25/92	06/01/05	0	0	0	0	0	0	0
9	6 77% Series	6 77%	06/08/93	06/01/03	0	0	0	0	0	0	0
10	7 84% Series	7 84%	09/04/96	08/03/26	5,700,000	5,700,000	48,208	5,651,792	446,880	2,278	449,158
11	6 50% Series	6 50%	05/31/98	06/01/08	6,500,000	6,500,000	21,689	6,478,311	422,500	7,434	429,934
12	6 87% Series	6 87%	03/31/01	03/29/11	5,100,000	5,100,000	28,779	5,071,221	350,370	5,004	355,374
13	4 25% Series	4 75%	03/01/04	03/01/14	19,000,000	19,000,000	0	19,000,000	902,500	0	902,500
14	6 76% Series (proposed)	6 76%	06/01/04	06/01/34	3,200,000	3,200,000	0	3,200,000	216,320		216,320
15	Capital Lease 9 489%	9 489%	06/01/98	05/31/13	1,590,500	1,160,775		1,160,775	110,146	0	110,146
16											
17											
18	Total				$43,590,500	$43,160,775	$120,665	$43,040,110	$2,679,966	$16,240	$2,696,206
19											
20											
21	Embedded Cost of Long-Term Debt										6 26%
22											
23											
24											
25											
26											
27											
28											
29											
30											

Embedded Cost of Preferred Stock
At the Mid-Point of the Attrition Year

Tennessee Regulatory Authority
Company: Tennessee American Water
Docket No: 04-

Test Year: Twelve Months Ended: March 31, 2004
Exhibit No. 3, Schedule 3

Line No	Debt Issue Type, Coupon Rate	Issue Date	Face Amount Outstanding	Premium or Discount	Unamortized (Issuance) Pfd Stk Exp	Net Proceeds	Annual Dividends	Annual Amort of Issuance Expense	Total Annual Cost
1									
2									
3									
4	Cumulative Preferred								
5	5% Series	12/20/40	$1,400,000	$0	$0	$1,400,000	$70,000	$0	$70,000
6	4-1/2% Series	7/29/54	0	0	0	0	0	0	0
7									
8									
9	Total		1,400,000	0	0	1,400,000	70,000	0	70,000
10									
11									
12	Embedded Cost of Preferred Stock								5 00%
13									
14									
15									
16									
17									
18									
19									
20									
21									
22									
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