

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

July 18, 2008

IN RE:

**PETITION OF TENNESSEE AMERICAN WATER
COMPANY TO CHARGE AND INCREASE CERTAIN
RATES AND CHARGES 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.
08-00039

**ORDER ON DISCOVERY DISPUTES ARGUED DURING
THE JUNE 20, 2008 STATUS CONFERENCE**

This matter came before the Hearing Officer upon various renewed motions to compel discovery filed with the Tennessee Regulatory Authority (“TRA” or the “Authority”) by certain parties, Tennessee American Water Company (“TAWC”), the Office of the Attorney General Consumer Advocate and Protection Division (“Consumer Advocate”), and the City of Chattanooga (the “City”). The Chattanooga Manufacturer’s Association (“CMA”), also a party in this docket, did not file a renewed motion to compel discovery. TAWC, Consumer Advocate, the City, and CMA are collectively referred to herein as the “Parties.”

RELEVANT PROCEDURAL BACKGROUND

Pursuant to the *Agreed Order Regarding Discovery and Disposing of Certain Outstanding Motions Following June 4, 2008 Status Conference (Amended by Hearing Officer) ("Agreed Order Regarding Discovery")* issued by the Hearing Officer on June 13, 2008, the parties were permitted to file renewed motions to compel at or before 12:00 noon (CDT) on June 17, 2008. Additionally, any responses to such renewed motions to compel were permitted to be

served on the parties on or before 12:00 noon (CDT) on June 18, 2008. Accordingly, TAWC, Consumer Advocate, and the City timely filed such renewed motions to compel and responses thereto. Also on June 13, 2008, the Hearing Officer issued a *Notice of Status Conference* reiterating the time deadlines for the filing of renewed motions to compel and responses thereto and further setting a Status Conference on June 19, 2008 at 10:30 a.m. (CDT).

JUNE 19-20, 2008 STATUS CONFERENCE

The Hearing Officer convened the Status Conference on June 19, 2008 in the Hearing Room on the Ground Floor of the Tennessee Regulatory Authority at 460 James Robertson Parkway, Nashville, Tennessee. Because additional time was required to address certain issues relating to discovery, the Status Conference was reconvened on June 20, 2008 at approximately 1:00 p.m. (CDT). The following parties and representatives were in attendance on June 19 and 20, 2008:

Tennessee American Water Company – R. Dale Grimes, Esq. and Ross I. Booher, Esq. Bass, Berry & Sims, PLC, 315 Deaderick Street, Suite 2700, Nashville, TN 37238-3001, Mr. Michael Miller and Mr. John S. Watson, Tennessee American Water Company, 1101 Broad Street, Chattanooga, TN 37402;

Consumer Advocate – Joseph Shirley, Esq., Timothy Phillips, Esq. and Ryan McGehee, Esq., Office of the Attorney General, Consumer Advocate and Protection Division, 425 5th Ave. N, John Sevier Building, P.O. Box 20207, Nashville, TN 37243;

City of Chattanooga – Michael A. McMahan, Esq., Office of the City Attorney, 801 Broad Street, Suite 400, Chattanooga, TN 37402; Frederick L. Hitchcock, Esq., Chambliss, Bahner, & Stophel, P.C., 1000 Tallan Building, Two Union Square, Chattanooga, TN 37402; and

Chattanooga Manufacturers Association – Henry M. Walker, Esq., Boulton, Cummings, Connors & Berry, PLC, 1600 Division Street, Suite 700, Nashville, Tennessee 37203; David C. Higney, Esq., Grant, Konvalinka & Harrison, P.C., Ninth Floor, Republic Centre, 633 Chestnut Street, Chattanooga, Tennessee 37450-0900.

Initially, the Hearing Officer opened up discussion of the issue of the confidentiality of the resume of Mr. Frank Impagliazzo, an expert witness retained by the Consumer Advocate.

The resume had been filed publicly in the docket, and TAWC requested that it be removed due to its confidential nature. The parties informed the Hearing Officer that they had been involved in discussions related thereto and requested an opportunity to attempt to resolve the matter informally along with other outstanding discovery issues. After a lengthy meeting between the parties, the Hearing Officer resumed the Status Conference, at which time the Parties informed the Hearing Officer that while much progress had been made, the confidentiality issue remained pending as well as a number of discovery disputes. The Parties requested additional time to meet in an attempt to resolve their disputes and after making some preliminary rulings, the Hearing Officer adjourned the Status Conference to be convened on the following day, June 20, 2008.

On June 20, 2008, the Parties reported to the Hearing Officer that a measure of progress had been achieved and requested additional time to continue to negotiate several of their disputes. The Hearing Officer granted the additional time and reconvened the Status Conference, at which time the Parties announced the following regarding outstanding discovery disputes. The Consumer Advocate stated that as to its specific discovery requests to TAWC, all requests had been resolved by mutual agreement of the parties except Requests Nos. Part II, No. 7 and Part III, Nos. 7, 8, 9, and 10. The City stated that a dispute remained as to its Questions Nos. 4, 7, 15, and 23. Thereafter, the Hearing Officer heard arguments of the parties on these specific discovery requests.

LEGAL FRAMEWORK

The process of discovery in contested cases before the TRA is governed by the Tennessee Rules of Civil Procedure.¹ According to Tenn. R. Civ. P. 26.02(1):

Parties may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action, whether it relates to the claim or defense of the party

¹ See Tenn. Comp. R. & Regs. 1220-1-2-.11(1).

seeking discovery or to the claim or defense of any other party, including the existence, description, nature, custody, condition and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of any discoverable matter. It is not ground for objection that the information sought will be inadmissible at the trial if the information sought appears reasonably calculated to lead to the discovery of admissible evidence.

Further, the Tennessee Court of Appeals has commented on relevancy as follows:

Relevancy is extremely important at the discovery stage. However, it is more loosely construed during discovery than it is at trial. The phrase “relevant to the subject matter involved in the pending action” has been construed “broadly to encompass any matter that bears on or reasonably could lead to any other matter that could bear on, any issue that is or may be in the case.”²

Nevertheless, Tennessee’s rules governing discovery do provide some limitations and protections. Specifically, Tenn. R. Civ. P. 26.02(1) provides:

The frequency or extent of use of the discovery methods set forth in subdivision 26.01 shall be limited by the court if it determines that: (i) the discovery sought is unreasonably cumulative or duplicative or is obtainable from some other source that is more convenient, less burdensome or less expensive; (ii) the party seeking discovery has had ample opportunity by discovery in the action to obtain the information sought; or, (iii) the discovery is unduly burdensome or expensive, taking into account the needs of the case, the amount in controversy, limitations on the parties’ resources, and the importance of the issues at stake in the litigation.

Additionally, Rule 26.03 permits a court to issue protective orders as justice requires.³ In

Duncan v. Duncan, the Tennessee Court of Appeals held that:

A trial court should balance the competing interests and hardships involved when asked to limit discovery and should consider whether less burdensome means for acquiring the requested information are available. If the court decides to limit discovery, the reasonableness of its order will depend on the character of the

² *Boyd v. Comdata Network, Inc.*, 88 S.W.3d 203, 220 n.25 (Tenn. Ct. App. 2002) (citations omitted) (quoting *Oppenheimer Fund, Inc. v. Sanders*, 437 U.S. 340, 351, 98 S.Ct. 2380, 2389, 57 L.Ed.2d 253 (1978)).

³ Tenn. R. Civ. P. 26.02 & .03.

information being sought, the issues involved, and the procedural posture of the case (citations omitted).⁴

While Rule 37.01(2) permits a party to file a motion to compel if a party fails to answer an interrogatory, including providing an evasive or incomplete answer, “[d]ecisions to grant a motion to compel rest in the trial court’s reasonable discretion.”⁵

CONSUMER ADVOCATE’S DISCOVERY REQUESTS

On May 12, 2008, the Consumer Advocate propounded its *First Discovery Request of the Consumer Advocate and Protection Division to the Tennessee American Water Company* (“*Consumer Advocate’s First Discovery Requests to TAWC*”). On May 28, 2008, *Tennessee American Water Company’s Responses to the First Discovery Request of the Consumer Advocate and Protection Division to the Tennessee American Water Company* (“*TAWC’s Responses to the First Discovery Requests of the Consumer Advocate*”) were filed with the Authority. On June 9, 2008, TAWC submitted additional responses to the *Consumer Advocate’s First Discovery Requests to TAWC* through its filing titled, *Tennessee American Water Company’s Responses to the Remainder of the Requests Contained in the First Discovery Request of the Consumer Advocate and Protection Division to Tennessee American Water Company* (“*TAWC Responses to Remaining Consumer Advocate’s First Discovery Requests to TAWC*”). During the Status Conference, the Consumer Advocate and TAWC advised the Hearing Officer that they wished to present oral argument only as to the Consumer Advocate’s Request Nos. Part II, No. 7 and Part III, Nos. 7, 8, 9, and 10.

⁴ *Duncan v. Duncan*, 789 S.W.2d 557, 561 (Tenn. Ct. App. 1990).

⁵ *Kuehue & Nagel, Inc. v. Preston, Skahan & Smith International, Inc.*, 2002 WL 1389615, *5 n.4 (Tenn. Ct. App. June 27, 2002).

I. Request Part II, No. 7

The *Consumer Advocate's First Discovery Requests to TAWC* included Part II: Depreciation and Weather Normalization, No. 7, which asks for all documentation underlying the Gannett Fleming depreciation study to be provided in Microsoft Excel, Word, or other comparable electronic format with the calculation formulas intact. In TAWC's response to the Consumer Advocate's Part II, No. 7, TAWC provided four attachments via compact disk that purportedly contained all documentation underlying the depreciation study. Further, TAWC objected to providing the documentation requested in an alternative format and asserted that such information was not available in either Microsoft Excel or Word.

During the Status Conference, the Consumer Advocate and TAWC reiterated certain arguments set forth in their written motions and responses filed previously on June 17, 2008 and June 18, 2008, respectively. Specifically, the Consumer Advocate contended that only the summary calculations of the depreciation study were provided, however, the detailed analysis and calculations behind the summary information is needed to make a sound assessment of the depreciation study. TAWC contended that all underlying data and analysis has been provided in response to the request, that the information sought is not available in an alternative format to what has already been provided because it is encompassed within the Gannett Fleming proprietary mainframe database and cannot be extracted therefrom. TAWC verbally asserted that such proprietary information exceeds a confidential designation and instead reaches further to an intellectual property privilege.

Following additional discussion with the parties, the Hearing Officer took the matter under advisement, ordered the Consumer Advocate to consult with its depreciation expert, identified as the firm of Snively King, and file in the docket a letter articulating with specificity what information or underlying data not already provided by TAWC would be needed to

evaluate and render an opinion on the depreciation study. As of the date of issuance of this Order, such a filing has not been made by the Consumer Advocate.

II. Request Part III, Nos. 7-10

Part III of the *Consumer Advocate's First Discovery Requests to TAWC* is a category entitled, Questions & Requests Regarding Cost of Capital & Miscellaneous. Part III, questions 7 through 10 ask for any study, document, e-mails, and all written materials wherein RWE or RWE Aqua Holdings GmbH and/or American Water Works has or will consider public offerings of common stock, determined or projected market value, issuance of a second class of stock, and the payment of dividends to the stockholders, of American Water Works.

In its responses to Part III, Nos. 7 through 10, TAWC objects that those requests are overbroad, unduly burdensome, not relevant, may be subject to attorney/client privilege and work product, and seek to elicit highly confidential information. Additionally, TAWC asserts that the requested information is not in its possession, control or custody and refers the Consumer Advocate to the Securities and Exchange Commission and American Water/Investor Relations websites for public information concerning American Water Works.

During the Status Conference, the Consumer Advocate and TAWC reiterated certain arguments set forth in their previously filed written motions and responses. Specifically, the Consumer Advocate asserted that the information which it seeks to elicit by Part III, Nos. 7 through 10, collectively concern the future equity and capital structure of the company. The Consumer Advocate contends that information pertaining to the plans or considerations of RWE or RWE Aqua Holdings GmbH and/or American Water Works which relate to the financial stability and overall capital structure of the company are discoverable.

TAWC disagrees that a double leverage methodology in determining capital structure is appropriate. Nevertheless, the Company has provided information concerning American Water

Works, the immediate parent company of TAWC. RWE is not a parent, immediate or otherwise. Following the closing of the public offering of stock, RWE has become only one of many shareholders and investors of the company. Further, TAWC contends that in determining capital structure, it is book value – not market value – that is important and book value information has been provided to the Consumer Advocate and the Intervenors. Finally, TAWC asserts that questions 7 through 10 ask whether any studies concerning market conditions for the sale of stock, anticipated market values of stock, creation of a second class of stock, or dividend policies have been performed or caused to be performed. To this, TAWC stated that no such studies have been performed by the Company and thus, there is nothing to produce in response to the requests.

Through questions during oral argument it was determined that RWE, though no longer the ultimate parent, is a significant shareholder, holding approximately 55-60% of the stock of American Water Works, and exercises broad influence over the affairs the company. During the Status Conference, the Hearing Officer determined that in the context of this docket and specifically as to Part III, No. 7, information requested as to RWE or RWE Aqua Holdings GmbH and/or American Water Works is relevant and took the motion to compel as to those Requests under advisement. On June 27, 2008, TAWC filed its supplemental responses to questions 7 through 10 stating generally that RWE or RWE Holdings GmbH is no longer the sole shareholder and TAWC is not in possession, custody, or control of information held by RWE.

During a telephone conference between the Parties and the Hearing Officer on July 11, 2008, the parties discussed certain outstanding discovery motions. TAWC stated that it had filed supplemental responses to discovery questions 7 through 10 and deemed those responses to be responsive. The CAPD indicated that those responses were still not responsive but acknowledged that it had not filed any further motion concerning questions 7 through 10 since

TAWC had filed its supplemental responses. The CAPD committed to make a filing regarding these responses and on July 11, 2008 filed a *Notice That Discovery Responses to the CAD's Discovery Requests 7, 8, 9 and 10 Remain Unsatisfactory*.

DISCOVERY REQUESTS PROPOUNDED BY THE CITY

On May 12, 2008, the City propounded *City of Chattanooga's First Discovery Requests to Petitioner Tennessee American Water Company* ("City's First Discovery Requests to TAWC"). On May 28, 2008, *Tennessee American Water Company's Responses to the City of Chattanooga's First Discovery Requests to Petitioner Tennessee American Water Company* ("TAWC's Responses to the City's First Discovery Requests") were filed with the Authority. On June 9, 2008, TAWC filed supplemental responses to certain questions propounded within the *City's First Discovery Requests to TAWC*. On June 13, 2008, TAWC filed additional supplemental responses to certain discovery requests of the City. During the Status Conference, the parties informed the Hearing Officer that a dispute remained only as to Question Nos. 4, 7, 15, and 23 and presented oral argument thereon.

I. *Question No. 4*

Question No. 4 of the *City's First Discovery Requests to TAWC* asks that TAWC "explain any addition, subtraction, acceleration, delay, deferral, or change in any recommended capital improvement projects identified in any Comprehensive Planning Study. . ." The parties stated that the request has been modified by agreement from its originally propounded time frame (from 1993 to 2000). Nevertheless, the parties were in disagreement concerning the format in which the information would be provided.

During the Status Conference, the City asserted that following a successful motion to compel on a similar request in Docket No. 06-00290, TAWC provided a chart or spreadsheet listing the capital investment projects and various information related to each. The City asserts

that the request was found to be relevant in that docket and the request in this docket should be found likewise. The City requests that TAWC simply update the spreadsheet.

TAWC contends that under the Tennessee Rules of Civil Procedure and the Hearing Officer's *Agreed Order Regarding Discovery* it is not required to go through the time and expense of sorting through its business records and updating the previously created spreadsheet. Rather, it has offered to make available at a mutually agreeable time TAWC's records, files, and data to the City to review and prepare its own spreadsheet.

In the *Agreed Order Regarding Discovery*, the Hearing Officer ruled that TAWC is "not required to 'manipulate raw data that will come out in a particular result' in response to Intervenor's discovery requests."⁶ Nevertheless, that ruling should not be interpreted as relieving TAWC of its obligation to provide information in such a way as to be usable to the requester. As to Question No. 4, the Hearing Officer ordered TAWC to respond to the discovery request and provide the information in the same format the Company did in Docket No. 06-00290.

II. Question No. 7

Question No. 7 of the *City's First Discovery Requests to TAWC* requests that TAWC "identify the location, by latitude and longitude or by census tract and block number, of each Capital Expense identified in the Request No. 6 in excess of Five Hundred Dollars (\$500.00)." TAWC responded to the request, providing to the City a map that allegedly depicts the location of all capital expense projects identified as such.

The City asserted that the map produced by TAWC is unreadable in its current format and requested that TAWC provide the specific locational information utilized to create the map so that the City could conduct its own mapping of the identified projects. The City explained that the information it seeks to elicit goes to issues of used and usefulness of the investments

⁶ *Agreed Order Regarding Discovery*, p. 3 (June 13, 2008).

made by TAWC. Further, the City the stated that question specifically asks for, and that the City had informed TAWC during certain discovery-related discussions that it required, the locational information in order to perform particular analyses which it had contemplated while preparing the discovery request.

TAWC stated that an employee of the Company obtained the street addresses of the capital expense projects from the Company's work order system and plotted the customized map produced in response to the City's discovery request. The employee did not track or maintain a listing of the street addresses that he used in creating the map. Therefore, TAWC asserted that to provide the locational information that the City is requesting, the Company would be required in essence to reassemble the information used to create the map, thereby incurring additional and duplicative time and expense. The Company offered to allow the City to inspect the file information used to create the map to obtain whatever additional information is deems necessary.

The Hearing Officer ruled that the locational information requested by the City is discoverable and ordered TAWC to produce to the City the street addresses of the capital expenditures in response to the discovery request at issue.

III. *Question No. 15*

Question No. 15 of the *City's First Discovery Requests to TAWC* requests that TAWC "provide a copy of all management audits completed since January 1, 1997. . . performed by or for TAWC, AWWSC [American Water Works Service Center], or any other TAWC Parent or Affiliate. . . ." TAWC objects to this request citing that the information requested is overbroad, unduly burdensome and in part not relevant. Further, the Company asserts that no audits of TAWC or American Water Works, other than the Booz Allen management study, have been conducted within the period of time specified in the request.

During the Status Conference, the City asserted that it has knowledge of at least one other management audit; an audit conducted of Pennsylvania American Water Company ordered by the Pennsylvania Public Service Commission. The City produced a document purporting to be the cover page of the Pennsylvania audit. The City asserted that management audits completed for operating companies or affiliates of American Water Works are relevant as to the consideration of whether the allocation of centralized costs are prudent, appropriate, or reasonable. The City contends that as the TRA ordered TAWC to conduct a management audit prior to the filing of this rate case, best practices or examples of what other regulatory bodies have undertaken on similar issues are relevant.

TAWC contends that the management audit that TAWC was ordered to produce in this docket concerns an audit of the allocation of management fees charged to it by the American Water Works Service Company. The audit conducted of the Pennsylvania American Water Company was an audit concerning the functions of the operating company itself. Its focus was not on the affiliate service company, and therefore, is not relevant to the issues in this rate case. Additionally, TAWC asserts that the management study conducted for this docket is the only such study performed of the American Water Works Service Company. TAWC offered to submit the Pennsylvania audit to the Hearing Officer to review *in camera* to determine whether the audit is relevant to the issues in this docket. The audit was subsequently submitted to the Hearing Officer by TAWC, and after review the Hearing Officer determined the Pennsylvania audit should be produced.

During the July 11, 2008 telephone conference, the City raised the discovery issue concerning the production of the Pennsylvania management audit. The Hearing Officer announced the decision and instructed TAWC to produce the Pennsylvania and New Jersey management audits to the City because they contain comparative information regarding water

company operations. TAWC raised the issue of the confidentiality of this information and argued that these documents were subject to the Amended Protective Order entered in this docket. As such, TAWC argued that, prior to production, the City should disclose the identity of persons that will be reviewing these documents. The City argued that these audits are public documents and that the Amended Protective Order had time requirements for disclosure prior to production that would be impossible to satisfy because of a very short period of time remaining for the Intervenor's to file Prefiled Testimony.⁷

It was agreed that the City would have its experts sign the non-disclosure agreement under the terms of the Amended Protective Order and the time periods set forth therein concerning objections of persons that are granted disclosure to information under the Amended Protective Order. TAWC agreed to produce the Pennsylvania and New Jersey management audits under the Protective Order and agreed to waive the time requirements pertaining to disclosure of such documents upon the City identifying those persons who will review the audits and submitting their non-disclosure statements.⁸

IV. *Question No. 23*

Question No. 23 of the *City's First Discovery Requests to TAWC* seeks “. . . all documents constituting, referencing, containing, relating to, responding to, or referring to other benchmarking studies or similar reports, performed by outside consulting or benchmarking firms. . . initiated or completed for TAWC or and TAWC Parent or Affiliate since January 1, 1997. . .” As part of its response to this question, TAWC produced a black-and-white copy of a report (“the Hackett Study”) that included a number of graphs and charts.

⁷ During the July 11, 2008 telephonic conference, the Parties agreed to a partial modification of the Procedural Schedule, moving the date for the filing of the Intervenor's' pre-filed testimony to July 18, 2008.

⁸ During the telephone conference, the City disclosed that Michael J. Majoros of the firm of Snively King would be granted access to such documents and later disclosed to TAWC that Glynn Stoffel, also of the firm of Snively King, would be the other person who would have access to the information on behalf of the City.

The City asserted that the copy of the Hackett Study it received in response to its discovery request was in a black-and-white format and was unreadable because the information contained in the charts is color-coded. The City requested that the Hackett Study be provided in color so that the graphs and charts encompassed within the report are decipherable. Additionally, some of the print is unreadable due to its small size and lack of copy quality. TAWC stated that it provided to the City the document in the same format that TAWC has in its possession. The benchmarking audit was performed approximately eight years ago, and although originally the Hackett Study was in color, the only version the Company has now is the black-and-white version. TAWC stated that if any time it discovers a better copy or one that is in color, it will be provided to the City.

The Hearing Officer ordered TAWC to make inquiry as to the availability of a more legible and color version of the Hackett Study and to file a statement as to the results of its inquiry by Tuesday, June 24, 2008. On June 24, 2008, TAWC filed a supplemental response to the City's Question 23 stating that it had located a color copy of the Hackett Study and produced it contemporaneously with its supplemental response.

IT IS THEREFORE ORDERED:

1. As to the City of Chattanooga's discovery Question No. 4, Tennessee American Water Company shall provide the requested information in the same format as provided in Docket No. 06-00290.⁹

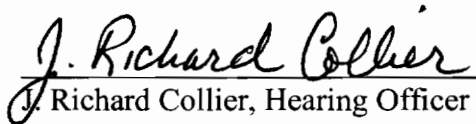
2. As to the City of Chattanooga's discovery Question No. 7, Tennessee American Water Company shall provide all street addresses responsive to the request.¹⁰

⁹ On June 27, 2008, TAWC filed a supplemental response to the City's Question No. 4 that purportedly included a updated spreadsheet responsive to the City's request.

¹⁰ On June 27, 2008, TAWC filed a supplemental response to City's Question No. 7 that included an attachment listing the locations for the capital expenditures.

3. As to the City of Chattanooga's discovery Question No. 15, Tennessee American Water Company will produce the Pennsylvania and New Jersey management audits to the City upon receipt of the names and executed non-disclosure agreements from the City. The time periods for objections to disclosure to certain persons set forth in the Amended Protective Order are waived in the instance of this production.¹¹

4. As to the City of Chattanooga's discovery Question No. 23, TAWC shall inquire, and produce if available, a legible copy of the Hackett Study, in color if possible.¹²


J. Richard Collier, Hearing Officer

¹¹ On July 11, 2008 and on July 15, 2008, TAWC filed a confidential supplemental response to the City's Question No. 15 pursuant to the *Amended Protective Order* entered in the docket.

¹² On June 24, 2008, TAWC filed a supplemental response that included a color copy of the Hackett Study.