

**IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE**

IN RE:)	
)	
PETITION OF TENNESSEE)	
AMERICAN WATER COMPANY TO)	
CHANGE AND INCREASE CERTAIN)	
RATES AND CHARGES SO AS TO)	DOCKET NO. 08-00039
PERMIT IT TO EARN A FAIR AND)	
ADEQUATE RATE OF RETURN ON)	
ITS PROPERTY USED AND USEFUL IN)	
FURNISHING WATER SERVICE TO)	
ITS CUSTOMERS)	

**CONSUMER ADVOCATE AND PROTECTION DIVISION'S MEMORANDUM IN
SUPPORT OF MOTION TO ASK ADDITIONAL DISCOVERY QUESTIONS**

Robert E. Cooper, Jr., Attorney General and Reporter for the State of Tennessee, by and through the Consumer Advocate and Protection Division of the Office of the Attorney General ("Consumer Advocate"), pursuant to TRA Rule 1220-1-2-.11(5)(a), hereby submits this memorandum in support of its request to ask additional discovery questions of Tennessee American Water Company ("TAWC" or "Company").

The process of utility rate-making is complex and involves numerous and often contested issues. *Tennessee Pub. Serv. Comm'n v. Nashville Gas Co.*, 551 S.W.2d 315, 318 (Tenn.1977). This is a complex rate case in which TAWC is seeking to substantially increase customers' water bills by \$7,644,859 each year, which represents an average bill increase of 21%. This annual rate increase proposal follows very closely on the heels of the 12% increase in water bills granted to TAWC by this Authority last year in Docket 06-00290. Should the Company's petition be granted in this case, TAWC's customers will experience a one-third hike in their water bills in just over a year's time.

The Company has proffered the direct testimony of nine witnesses in support of the proposed rate increase. The Company's petition and related testimony and exhibits total 970 pages; the Company has also submitted an additional 1,668 pages of information in support of its proposed rate increase in response to TRA staff data requests. The initial round of discovery -- which is the only round of discovery prior to the filing of the Consumer Advocate's direct testimony -- is essential for the Consumer Advocate to adequately and fully investigate the positions taken by the Company in these filings, to rebut the veracity of the Company's witnesses, to explore the purported deficiency of the sizeable rate increase the TRA awarded to TAWC just last year, and to formulate and present the Consumer Advocate's own expert opinions on material issues affecting just and reasonable water rates for TAWC's customers.

Although the Consumer Advocate has not determined all of the issues that it may investigate or litigate in this docket, its preliminary review of the case has revealed a substantial number of issues that are material to TAWC's petition. Significantly, some of these issues are new to this docket; as will be shown further below, the Company has included a depreciation study in this case, and the Consumer Advocate has retained an independent expert to analyze this study. Currently, the Consumer Advocate is without sufficient information to analyze these material issues, primarily because most of the information that is pertinent to such analyses is in the hands of the Company. Accordingly, the Consumer Advocate's initial round of discovery asks questions surrounding issues that have a material bearing on just and reasonable water rates in this matter, including, but not confined to, the following issues:

-- the appropriate amount of regulated revenues attributable to end-user customers, which requires analysis of billing determinates, such as the number of customers and meters by class

and by location and the volumes of water for customers and meters by class and by location, as well as the anticipated change in the number of customers and meters and volumes of usage for each customer class and location during the attrition period;

-- the appropriate amount of regulated revenues attributable to other resale customers, which requires analysis of information regarding the terms and conditions of applicable resale contracts, as well as historical resale volumes and anticipated changes in resale volumes during the attrition period;

-- the appropriate amount of salaries and wages for TAWC employees, which requires analysis of information regarding historical and projected employee counts by position, historical and projected periods of vacancies in various employee positions, historical and projected salary and wage rates by employee position, historical and projected overtime hours by employee position, historical and projected amounts of shift differential pay by employee position, historical and projected amounts of incentive compensation by employee position, as well as the data necessary to distribute applicable employee compensation to capital and noncapital projects in order to calculate the wage capitalization rate;

-- the appropriate amount of fuel and power and chemicals expenses for treatment of historical and projected water volumes billed to customers, as well as for treatment of historical and projected water volumes lost and unaccounted for;

-- the appropriate amount for nonrecurring expenses that the Company will not experience during the attrition period, such as nonrecurring expenses related to the STEP project, the STAR project, the business change project, divestiture-related costs, and costs incurred for Sarbanes-Oxley compliance;

-- the appropriate level of charges billed to TAWC's ratepayers from affiliated service companies, which requires analysis of data regarding allocations of costs to the Tennessee jurisdiction from such affiliated companies;

-- the appropriate amount of employee pension expense, which requires analysis of information regarding booked pension costs under FASB 87, actual pension contribution requirements, and other post employment benefits (OPEBs);

-- the appropriate amount of other operations and maintenance expenses, which requires analysis of information necessary to separate salaries and wages from total operations and maintenance expenses, as well as to analyze historical levels of other operations and maintenance expenses in light of general inflationary factors and management's operating budgets;

-- the appropriate amount of extraordinary maintenance expense for water pumping stations, which requires examination of information relating to management's review of these stations and its rationale for these extraordinary expenses;

-- the appropriate amount of expenses included in the Company's accounts that should be disallowed for ratemaking purposes, which requires analysis of information relating to items such as lobbying activities, fines and penalties, and entertainment-related costs;

-- the appropriate level of amounts charged to ratepayers for rate case expense and independent consultants, which requires review of supporting documentation for these charges;

-- the appropriate level of property tax expense, which requires analysis of information regarding property tax equalization percentages and property tax rates for each taxing jurisdiction where TAWC property is located;

-- the appropriate amount of federal income taxes, which requires information necessary

to determine the proper application of the effective federal statutory tax rate;

- the appropriate amount to include in utility plant in service, which requires analysis of information such as capital budgets and capital investment requirements to maintain appropriate levels of service and service quality, historical and projected plant account and related accumulated depreciation balances, the amount of historical and projected additions and retirements by plant account, as well as the amounts of historical and projected salvage and cost of removal by plant account;

- the appropriate amount of projected reimbursements to TAWC by the Tennessee Department of Transportation for utility plant relocations;

- the appropriate amount of depreciation charges due to proper application of depreciation rates, which requires analysis of information such as TAWC's historical and projected application of depreciation rates in light of the net book value of applicable plant account balances;

- the appropriate amount of construction work in progress (CWIP), which requires analysis of information regarding the methodology used to calculate CWIP;

- the appropriate amount of working capital, which requires analysis of information related to cash requirements, including, but not confined to, TAWC's lead/lag study;

- review of information related to the significant rise in customer service requests from 2005 to 2007;

- review of information related to the Company's proposal to increase the rates of some customers more than the rates of other customers;

- determination of an appropriate cost of capital, which requires analysis of information related to the Company's embedded cost of debt, fair return on owners' equity, as well as a

reasonable mix for capital structure; and

-- the appropriate gross-up revenue conversion factor to be used, which requires analysis of information necessary to compute the associated amount of revenue needed to satisfy a related deficiency in net operating income.

With respect to the issues discussed above, the Consumer Advocate has attempted to refrain from asking questions to discover information that is available to the Consumer Advocate from other sources besides the Company, as well as from asking duplicative or cumulative questions in light of the information the Company has already filed in this docket. Furthermore, the issues discussed above are not the only issues the Consumer Advocate intends to investigate and possibly raise in its prefiled direct testimony. The Consumer Advocate has not asked discovery questions concerning issues for which it already has sufficient data from other sources, such as the Company's petition, testimony and exhibits, responses to the TRA staff's data requests, or other public sources.

Additionally, the issues discussed above do not include questions in the Consumer Advocate's initial round of discovery for issues relating to the Company's proposed depreciation study and weather normalization adjustments. Both the depreciation study and weather normalization adjustments involve very complex analyses of large amounts of data; moreover, both depreciation and weather normalization have a substantial impact on the amount of rates that TAWC's customers pay for water and sewage services. The Consumer Advocate therefore has hired outside consultants to respond to these material and complex issues and has included questions in its initial round of discovery that these experts have drafted in order to gather information that is essential for their analyses of these important issues.

The Consumer Advocate has a statutory right to investigate the reasonableness of the Company's request for a \$7.6 million per year increase in customers' water bills. Tenn. Code Ann. § 65-4-118. The first, and perhaps most important, policy of discovery is that discovery should enable the parties and the court to seek the truth so that disputes will be decided by facts rather than by legal maneuvering. *White v. Vanderbilt Univ.*, 21 S.W.3d 215, 223 (Tenn. Ct. App. 1999). Discovery should allow both the court and the parties to have an intelligent grasp of the issues to be litigated and knowledge of the facts underlying them. *Vythoulkas v. Vanderbilt Univ. Hosp.*, 693 S.W.2d 350, 356 (Tenn. Ct. App. 1985). Furthermore, discovery is not confined to the issues raised in the pleadings, for discovery itself may be used to clarify and define the issues in controversy. *Id.* at 359. Accordingly, a party seeking discovery is entitled to obtain information about any matter, not privileged, which is relevant to the subject matter involved, whether it relates to the claim or defense of the party seeking discovery or to the claim or defense of any other party. *State ex. rel. Flowers v. Tennessee Trucking Assoc. Self Insurance Group Trust*, 209 S.W.3d 602, 615 (Tenn. Ct. App. 2006). The relevancy requirement is broadly construed to include any matter that bears on, or that reasonably could lead to other matters that could bear on, any of the case's issues. *Id.* If a party's discovery goes too far, however, the court may limit the discovery sought if it is unduly burdensome or expensive, taking into account the needs of the case, the amount in controversy, the importance of the issues at stake, limitations on the parties' resources, and whether less burdensome means for acquiring the requested information are available. *Id.* Nonetheless, Tennessee law favors discovery; thus, the party opposing discovery must demonstrate with more than conclusory statements and generalizations that the discovery limitations being sought are necessary to protect it from oppression or undue burden or expense. *Id.*

Consistent with these principles, the Consumer Advocate has drafted an initial round of discovery that is tailored to gathering essential information for its evaluation of the various material issues related to establishing just and reasonable water rates in this matter. Considering the substantial amount of the Company's rate increase request; the number of witnesses proffered by the Company in support of this rate increase; the volume of the Company's testimony, exhibits and responses to TRA staff's data requests; the number and importance of pertinent issues raised in this matter and the relevant facts pertaining to them; as well as the Consumer Advocate's inability to obtain the requested information from another source besides the Company itself -- all of which are discussed above -- it is impossible for the Consumer Advocate to gather the information it needs and adequately prepare its case based on eighty discovery questions alone. Moreover, it is not uncommon for the Consumer Advocate to ask more than eighty questions in major rate cases such as this one. For instance, in a recent major rate case decided by the Authority, the Consumer Advocate asked the company 243 discovery questions, including subparts, prior to the Consumer Advocate's submission of its prefiled direct testimony in that case. *See* First and Second Discovery Requests of the Consumer Advocate and Protection Division to Atmos Energy Corporation filed in Docket 07-00105 on May 25, 2007, and July 11, 2007, respectively.

If the Consumer Advocate's request to ask discovery questions in excess of eighty requests is denied or if the Consumer Advocate's discovery questions are otherwise limited, such denial or limitation will prejudice the Consumer Advocate by impeding its ability to fully investigate the Company's petition for a rate increase, as well as to sufficiently analyze and litigate the material issues that should be considered in this matter. The Consumer Advocate recognizes that, in prior rate cases, the usual procedural course has generally allowed the Consumer Advocate to discover the

information it needs based solely on written questions alone. Nonetheless, the Consumer Advocate reserves its right to discover information by taking the pre-trial depositions of the Company's witnesses and consultants in the event unreasonable limitations are placed on the written questions the Consumer Advocate may ask in this docket. *White*, 21 S.W.3d at 224; Tenn.R.Civ.P. 26.02(4)(A)(ii); TRA Rule 1220-1-2-.11(1).

For the foregoing reasons, the Consumer Advocate requests the Hearing Officer to approve its request to ask additional discovery questions of TAWC, which questions are submitted contemporaneously with this memorandum.

RESPECTFULLY SUBMITTED,

A handwritten signature in black ink, appearing to read 'Ryan L. McGehee', is written over a horizontal line.

RYAN L. McGEHEE
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Dated: May 12, 2008

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing is being served via U.S. Mail and/or electronic mail upon:

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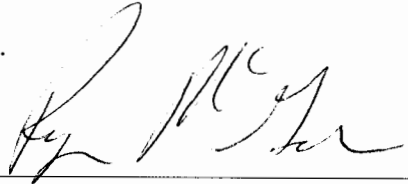
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This the 12 day of MAY, 2008.



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