

# BASS

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January 12, 2011

## VIA HAND DELIVERY

Chairman Mary W. Freeman  
c/o Sharla Dillon  
Tennessee Regulatory Authority  
460 James Robertson Parkway  
Nashville, Tennessee 37243

filed electronically in docket office on 01/12/11

**Re: Docket No. 10-00189: *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***

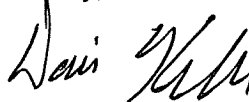
Dear Chairman Freeman:

Enclosed please find an original and five (5) sets of copies of Tennessee American Water Company's Motion to Call Schumaker & Company to Present Testimony Regarding its Affiliate Audit Report of Tennessee American Water Company for the Tennessee Regulatory Authority.

Please file the original and four copies of the Motion and stamp the additional copy as "filed." Then please return the stamped copy to me by way of our courier.

Should you have any questions concerning this matter, please do not hesitate to contact me at the email address or telephone number listed above.

Sincerely,



David Killion

Enclosures

January 12, 2011

Page 2

cc: Mr. David Foster, Chief of Utilities Division (w/o enclosure)  
Mr. Jerry Kettles, Chief of Economic Analysis & Policy Division (w/o enclosure)  
Ryan McGehee, Esq. (w/enclosure)  
Mary L. White, Esq. (w/enclosure)  
David C. Higney, Esq. (w/enclosure)  
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Katharine M. Mapes, Esq. (w/enclosure)  
Donald L. Scholes, Esq. (w/enclosure)

9117699.1

**BEFORE 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. 10-00189**

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**MOTION TO CALL SCHUMAKER & COMPANY TO PRESENT TESTIMONY  
REGARDING ITS AFFILIATE AUDIT REPORT OF TENNESSEE AMERICAN  
WATER COMPANY FOR THE TENNESSEE REGULATORY AUTHORITY**

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On January 5, 2011, intervenors submitted pre-filed testimony questioning the procedures, methodology and conclusions contained in the comprehensive independent management audit that Schumaker & Company ("Schumaker") recently completed for the Tennessee Regulatory Authority. Accordingly, Tennessee American Water Company ("TAWC") respectfully requests that the Authority call Pat Schumaker to present testimony in this docket regarding the Authority's ordered audit. In the event the Authority does not choose to call Schumaker as a witness, TAWC requests that the Authority enter an order stating that TAWC's act of calling Schumaker to present testimony regarding the Authority's ordered audit will in no way affect Schumaker's status as an independent auditor.

In the 2008 rate case filed in Docket No. 08-00039 the Authority ordered TAWC to develop a Request for Proposal ("RFP") for a management audit. TAWC complied with this request and the Authority then oversaw each step of the audit procurement process. On March 23, 2009, TAWC began the process by filing its draft RFP with the Authority. On June 15,

2009, the Authority addressed the draft RFP and opened Docket No. 09-00086 to oversee the management audit.

The Authority considered the management audit process at multiple Directors' Conferences in 2009 and made numerous revisions to the RFP originally submitted by TAWC before finally issuing an Order approving the final version of the RFP on September 8, 2009. The Authority next reviewed all responses to the RFP and reviewed TAWC's recommendation and rationale for selecting an auditing proposal. TAWC filed its request for approval of Schumaker & Company as the auditor on October 28, 2009. On December 14, 2009 the Authority approved Shumaker as the auditor.<sup>1</sup> On January 25, 2010 the Authority revised the draft contract between TAWC and Shumaker and then approved the contract which set forth in detail all procedures, requirements, standards, terms, and conditions for the audit. The Authority later issued a written Order on March 24, 2010 documenting its approval of the contract. Shortly after the completion of the audit TAWC filed a copy of the audit with the Authority on September 10, 2010. TAWC currently has pending in Docket No. 09-00086 a motion requesting that the Authority take final action and adopt the findings contained in the management audit that the Authority requested.

The Authority has stated the purpose of its ordered audit was to determine "whether the amount requested by the company to pay its service company is a just and reasonable amount based on prudent expenditures." Hrg. Tr. at 8-9, Docket No. 08-00039 (Sept. 22, 2008). TAWC respectfully submits that the audit completed by Schumaker – and conducted pursuant to the RFP and contract approved by the Authority – did in fact confirm that the fees charged by AWWSC are necessary to provide the level of quality service that TAWC's customers and the Authority expect. In fact, the audit found, among other things, that each and every scope item that the RFP

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<sup>1</sup> The Authority later issued this written Order on March 12, 2010.

required to be studied was at or above adequate levels. The findings of the audit were attested to by an independent certified public accountant as required by the Authority.

The conclusions contained in the audit strongly indicate that TAWC is unfairly shouldering the burden of a large and growing deficiency between what TAWC must pay in reasonable management fees to provide the required level of quality service and what it is currently allowed to recover in revenue. Indeed, the Authority stated when ordering the audit that “if the management audit ultimately shows that the fees being allocated for services are prudent, the authority can on its own motion or the motion of a party revisit the issue of management fees.” Hrg. Tr. at 8-9, Docket No. 08-00039 (Sept. 22, 2008). In addition, the audit was obtained at a cost to TAWC of \$184,964, which was approved in advance by the Authority, and which TAWC seeks to recover in this rate case. It is imperative, therefore, that Schumaker be called to present testimony regarding the audit it completed for the Authority so that the Authority may determine the proper level of management fees appropriate in this case.

At a status conference in that matter held on December 13, 2010, the City of Chattanooga’s counsel stated: “Our position is there’s a management audit, we’ve got a right to look behind it and to test the information and the conclusions that are contained in there.” *See* Hearing Conf. Trans. at 18:7-18:10 (Dec. 13, 2010), Docket No. 10-00189. Indeed, the testimony filed last week by the intervenors clearly shows that the intervenors now wish to attack in this rate case the procedures, methodology and conclusions contained in the audit that Schumaker completed for the Authority. *See, e.g.* Pre-filed Testimony of Terry Buckner, at 24-31 (Jan. 5, 2011) (challenging the scope of the audit approved by the Authority, the allocation method used by Schumaker, and whether each conclusion contained in the audit is adequately supported by a proper analysis); Pre-filed Testimony of Kimberly Dismukes, at 6, 46 (Jan. 5, 2011) (“The TRA should reject any conclusion that the AWWSC charges to the Company are reasonable based upon the Schumaker comparison.”).

Although none of the intervenors chose to provide any input or comments with respect to the audit throughout the entire 21 month history of the preparations by TAWC and this Authority, it appears that the intervenors now believe they can collaterally attack in this rate case the Orders the Authority issued in Docket No. 09-00086 approving the audit's scope and procedures. It is TAWC's position that if allowed, this tactic would solely serve to frustrate TAWC's ability to recover the proper level of management fees and would also simultaneously impede the Authority's ability to obtain finality on its ordered management audit while unnecessarily increasing rate case expense.

Nonetheless, should the Authority allow the intervenors in this case the leeway to perform a limited examination of the conclusions contained in the management audit completed by Schumaker for the Authority, TAWC requests that the Authority call Schumaker to present testimony regarding the procedures, methodology and facts that support the conclusions contained in the Authority's ordered audit. If the Authority chooses not to call Schumaker itself, TAWC requests that the Authority enter an order stating TAWC's act of calling Schumaker would in no way affect Schumaker's status as an independent auditor.

In the 2008 rate case the Authority held that the independence of the firm that conducted the previous management audit was impaired solely because the firm had been called by TAWC previously to provide testimony.<sup>2</sup> See Docket No. 08-00039, Order at 20-21 ("The Booz Allen witness, Joe Van den Berg, who performed the management audit required by the TRA also provided testimony on behalf of TAWC in other dockets, both before the TRA and other utility commissions. For this reason, the panel determined that the independence of the selected audit firm was impaired."). Schumaker & Company has never provided testimony on behalf of

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<sup>2</sup> The Authority also stated on appeal: "The Booz Allen management audit was not an independent audit. Mr. Van Den Berg, a principal at Booz, Allen, Hamilton who sponsored the management audit to the TRA provided testimony in this docket. Mr. Van Den Berg also provided testimony before the TRA in the 2006 rate case and has testified in several other rate cases for American Water." Brief of Respondent Tennessee Regulatory Authority, at 50, Appeal No. M2009-005533-COA-R12-CV (June 15, 2010).

TAWC in other dockets. Regardless, TAWC requests that in the event the Authority does not call Schumaker itself, the Authority simply clarify that TAWC's act of calling Schumaker would in no way affect Schumaker's status as an independent auditor.

Respectfully submitted,



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*Counsel for Petitioner  
Tennessee American Water Company*

## CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been served by way of the method(s) indicated, on this the 12<sup>th</sup> day of January, 2010, upon the following:

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<input type="checkbox"/> Overnight	and Protection Division
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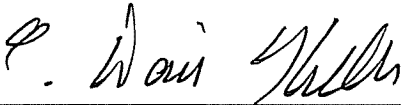
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