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January 14, 2011

Via Hand-Delivery

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

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

Dear Chairman Freeman:

Enclosed you will find an original and five (5) copies of Tennessee American Water Company's Response to the City of Chattanooga's Third Motion to Compel. This material is also being filed today by way of email to the Tennessee Regulatory Authority Docket Manager, Sharla Dillon.

Please file the original and four copies of this material and stamp the additional copy as "filed". Then please return the stamped copies 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.

With kindest regards, I remain

Very truly yours,

R. D Grimes

R. Dale Grimes

RDG:smb
Enclosures

cc: Hon. Sara Kyle (*w/o enclosure*)
Hon. Eddie Roberson (*w/o enclosure*)
Mr. David Foster, Chief of Utilities Division (*w/o enclosure*)
Richard Collier, Esq. (*w/o enclosure*)
Mr. Jerry Kettles, Chief of Economic Analysis & Policy Division *(w/o enclosure*)
Ryan McGehee, Esq. (*w/enclosure*)
Mary L. White, Esq. (*w/enclosure*)
David C. Higney, Esq. (*w/enclosure*)
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Mark Brooks, Esq. (*w/enclosure*)
Scott H. Strauss, Esq. (*w/enclosure*)
Katharine M. Mapes, Esq. (*w/enclosure*)
Donald L. Scholes, Esq. (*w/enclosure*)

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**

TENNESSEE AMERICAN WATER COMPANY'S RESPONSE TO THE CITY OF CHATTANOOGA'S THIRD MOTION TO COMPEL

In its ***Third*** Motion to Compel, the City of Chattanooga (the "City") now seeks production of materials identified in Tennessee American Water Company's ("TAWC") privilege log filed on December 30, 2010. TAWC has appropriately claimed work product protection for all the materials contained in its privilege log and has appropriately asserted the attorney-client privilege for any materials that are also internal communications with in-house counsel. The City's Motion completely fails to address TAWC's claims of work product protection and its argument in opposition to TAWC's attorney-client privilege claims lack legal merit. Additionally, the City's requested relief – immediate production of all materials in the privilege log – has no legal basis, contradicts the Authority's Order of December 23, 2010 and otherwise does nothing to advance the rate-making process. For these reasons, the Motion should be denied.

THE TRA'S MANAGEMENT AUDIT AND ITS DECEMBER 23, 2010 DISCOVERY ORDER

I. The TRA Management Audit

In its final order in TAWC's 2006 contested rate case, the Authority ordered TAWC to file a management audit to support its request for management fees in the future. Subsequently, in filing its 2008 contested rate case, TAWC submitted a management audit conducted by Booz Allen Hamilton; nevertheless, the Authority denied recovery of a significant portion of TAWC's requested management fees stating that the management audit did not meet the Authority's expectations. *See* Order at 21-22, Docket No. 08-00039. Accordingly, the Authority ordered that a new management audit be conducted that was ultimately subject to the Authority's review and approval of the RFP process, scope of the audit, selection of the auditor, and the audit contract. TRA Director Roberson, whose motion regarding management fees was adopted by the panel, explicitly stated that if the management audit determined that the fees allocated for management services are prudent, either the Authority or the parties could revisit the issue of management fees in the 2008 rate case by motion. Hrg. Tr. at 8-9, Docket No. 08-00039 (Sept. 22, 2008).[1]

After TAWC submitted a draft RFP as had been ordered in the 2008 rate case, the Authority then opened Docket No. 09-00086 to oversee its management audit, ultimately

[1] Then Chairman Roberson stated: "Regarding the amount of management fees allowed, there is no doubt in my mind that legitimate expenses are incurred from the service company. The problem I had is in determining whether the amount requested by the company to pay its service company is a just and reasonable amount based on prudent expenditures. The management audit ordered in 06-290 could have answered this important question if conducted properly.... I am anxious for the conclusion of the comprehensive audit ordered in 06-290 and restated in my motion for this docket. *I want to stress 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.*" (emphasis added)

selecting Schumaker & Company to be the management auditor. When the TRA-approved management auditor completed its audit, TAWC filed the audit report in Docket No. 09-00086.

The TRA auditor eventually found that every item within the scope of its review, as defined in the RFP, was at or above adequate levels. Meanwhile, throughout the entire process from the preparation of the draft RFP through the filing of the completed audit, TAWC believed that, regardless of the conclusion reached by the auditor, the audit and everything related to it would likely become the subject of litigation in either the 08-00039 Docket, 09-00086 Docket, or in any subsequently filed rate case. Accordingly, the internal communications by and among TAWC and its parent company and affiliated service company were undertaken in anticipation of this likelihood of litigation.

II. The TRA's December 23, 2010 Discovery Order

On December 23, 2010, the Authority entered an Order with respect to the parties' first round of discovery, including the City's request that TAWC submit a privilege log.[2] In its Order, the Authority correctly noted that the burden and expense of compiling a privilege log outweighed any benefit that it might have in this rate-making proceeding. *See* Order at 18-19. Nevertheless, without requiring a full-blown privilege log, the Authority did order TAWC to describe the nature of any information not produced on the grounds of privilege or protection in a manner that would enable the TRA and other parties to assess the claim of privilege or protection. *See* Order at 19.

TAWC spent numerous hours compiling the required information and timely filed a list of documents not produced in this litigation due to their privileged status, consisting of internal communications and related documents concerning the TRA management audit prepared in

[2] The parties agreed during the hearing on these motions that if TAWC were to be required to submit a privilege log the intervenors would be required to do so as well. Hr'g Tr. at 31:6-9 (Nov. 22, 2010). To date, no party other than TAWC has submitted a privilege log or description of documents withheld on the grounds of privilege.

anticipation of litigation. As required by the Order, the list identifies the parties involved in these communications, the specific topic(s) of the communications, the date and which ground(s) of protection apply. Of course, what is not on the list and what has already been produced to the City are the communications between TAWC and Schumaker & Co., the TRA-approved management auditor.

THE CITY'S MOTION TO COMPEL SEEKS DOCUMENTS THAT ARE PROTECTED FROM PRODUCTION AND SEEKS RELIEF THAT IS CONTRARY TO THE TRA'S ORDER AND THE PURPOSE OF THIS RATE-MAKING PROCEEDING

I. The Documents Identified in TAWC's Privilege Log are Protected by the Work Product Doctrine or Attorney-Client Privilege

TAWC is not required to produce documents or communications that are protected from discovery by the work product doctrine or the attorney client privilege. Interestingly, the City relies entirely on its understanding of the attorney-client privilege doctrine to support its Motion to Compel, despite the fact that TAWC has asserted that all the documents are protected by work product, while only specific documents are also subject to the attorney-client privilege. The City's Motion thus fails because all the materials are protected by the work product doctrine and the City does not address why the work product doctrine would not apply. Accordingly, even assuming that the City is correct and the attorney-client privilege does not apply to these documents (which TAWC denies), the City's Motion is still without merit. The Hearing Officer accordingly should deny the Motion because the City has not challenged TAWC's claim of work product protection, which applies to all the documents identified by the Company, and because there is otherwise no legal basis for denying work product protection to these documents.

A. Work Product Doctrine

The work product doctrine shields documents from production that are "prepared in anticipation of litigation", regardless of whether an attorney or someone else prepares the

materials. *See* Tenn. R. Civ. P. 26.02(3); *see also Eoppolo v. National Railroad Passenger Corp.*, 108 F.R.D. 292, 295 (E.D. Pa. 1985) ("It is not necessary for an attorney to be involved in the proceeding to bar discovery") (memoranda from meetings held by defendant officials regarding the plaintiff's accident were protected by the doctrine even though no attorneys were present). Further, the doctrine protects materials prepared in the course of ongoing litigation and also applies to anticipated litigation that is not even imminent. *See Arnold v. City of Chattanooga*, 19 S.W.3d 779, 784 (Tenn. Ct. App. 1999). Also, "materials which are prepared in anticipation of litigation need not be prepared for the specific case in which discovery is sought in order to be protected by the work product doctrine." *Id.* Accordingly, if a document is protected in past litigation, it remains protected in subsequent litigation, especially when the subsequent litigation is closely related. *Swift v. Campbell*, 159 S.W.3d 565, 573 (Tenn. Ct. App. 2004) (citations omitted). Finally, the work product protection applies even if the document also happens to serve an ordinary business purpose as long as the party anticipated litigation in creating the document and that anticipation was objectionably reasonable. *In re Professionals Direct Ins. Co.*, 578 F.3d 432, 439 (6th Cir. 2009) (citing *United States v. Roxbury*, 457 F.3d 590, 594, 598-99 (6th Cir. 2006)). The work product doctrine clearly applies to this case for the following reasons.

First, in discussing the entirely separate *attorney-client privilege*, the City's Motion points out that many of the entries in the privilege log do not have an attorney listed as the sender or recipient. Although it is unclear what point the City is trying to make, it is clear that this does not matter for TAWC's claim of work product. Application of the work product doctrine does not require involvement by an attorney.[3] *See Eoppolo*, 108 F.R.D. at 295.

[3] In addition to being privileged, to the extent that the correspondences listed by the Company involve an attorney and involve attorney input, there is a heightened work product protection as well. *See, e.g.*, Tenn. R. Civ. P.

Second, all internal correspondence and documents created with respect to the ongoing TRA management audit were created in anticipation of litigation. The management audit was born out of existing litigation and an Order of the Authority in a contested rate case involving many of the parties to the present case. At that time, Director Roberson explicitly stated that the management audit could be used to reconsider the amount of management fees allowed in the 2008 rate case. Internal emails and documents regarding the audit prepared during the course of this ongoing litigation were clearly covered by the doctrine.

Third, when the Authority created Docket No. 09-00086 to manage the audit process, the intervenors in this case, including the CAPD, were offered the opportunity and could have elected to intervene and contest the management audit. Anticipating that litigation could ensue at any time during the audit process was certainly reasonable, and has now come to pass as the CAPD has moved to intervene to oppose TAWC's request that the Authority accept and approve the audit. Moreover, given the contentious history of TAWC's recent rate cases, especially over the issue of the amount of management fees, TAWC also was reasonable in anticipating that the management audit could be the subject of future litigation in any subsequently filed rate case, as has also now come to fruition.

Accordingly, the correspondence and documents identified in TAWC's privilege log related to the planning of, or preparation for, or proceedings about the management audit were made in the course of either ongoing litigation or in anticipation of future litigation. The sole purpose of the TRA management audit is to either confirm or reject the reasonableness of the management fees sought in contested litigation before the TRA. Any additional business-related purpose that the audit might serve is incidental and ancillary. Thus, the internal correspondence

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26.02(3); *Upjohn Co. v. United States*, 449 U.S. 383, 400-02 (1981); *Hickman v. Taylor*, 329 U.S. 495, 510-13 (1947).

about the management audit, withheld in this case, was made with the anticipation of litigation over its findings and was appropriately withheld from production as work product.

B. Attorney-Client Privilege

The only documents withheld on the grounds of attorney-client privilege are confidential communications with in-house legal counsel regarding the TRA management audit.

The purpose of the attorney-client privilege is to "encourage clients to make full disclosure to their attorneys." *Upjohn*, 449 U.S. at 389. The privilege applies to both communications with in-house counsel as well as outside counsel. *Curtis v. Alcoa, Inc.*, No. 3:06-CV-448, 2009 WL 838232, at *2 (E.D. Tenn. March 27, 2009) (internal quotations omitted). Moreover, correspondences remain privileged even if they are only copied to in-house counsel rather than addressed primarily to him/her. *See generally Christie v. Alliance Imaging, Inc.*, No. 5:06-CV-1430, 2007 WL 1974913 (N.D. Ohio July 3, 2007). Although all communications with in-house counsel are not protected by the privilege, where business and legal considerations are "inextricably entwined" in corporate communications, "[t]he mere fact that business considerations are weighed in the rendering of legal advice does not vitiate the attorney-client privilege." *See Curtis*, at *2 (quoting *Picard Chem. Profit Sharing Plan v. Perrigo Co.*, 951 F.Supp. 679, 686 (W.D. Mich. 1996)).

TAWC's employees, parent and affiliates sent internal communications to one another and in-house counsel to ensure that any legal issues that might be raised during the management audit were identified and addressed. Such are the communications identified in TAWC's privilege log with respect to the management audit. Accordingly, these communications were protected by the attorney-client privilege.

The City attempts to argue that these communications are not protected because they "appear" to have a dominant business or commercial purpose. This argument completely ignores the fact that the internal communications are about the TRA management audit, an audit that has little, if any, commercial or business purpose for the Company outside these contested rate cases.

TAWC appropriately withheld the identified documents pursuant to the work product doctrine and/or attorney-client privilege and the City's Motion must be denied.

II. TAWC's Privilege Log Fully Complies with the TRA's Order and the City's Requested Relief Would Otherwise Vitiate the Order and the Purpose of this Rate-Making Proceeding

Recognizing that the burden of creating a privilege log was outweighed by any potential benefit it might bring to this rate-making proceeding, the TRA ordered that TAWC comply with Tenn. R. Civ. P. 26.02(5) by describing the nature of the documents not produced so that protection might be assessed. *See* Order at 19. TAWC met, and exceeded, this requirement providing detailed information regarding the sender, recipient, date, applicable protection, and subject of the withheld document. Not to mention the increased cost and burden on the party claiming privilege, requiring any additional detailed information about the contents of the entries would do little to enhance the parties' or Authority's ability to make a privilege determination but would heighten the risk that the content of the privileged communication would be inappropriately disclosed. This is not required by Rule 26.02(5) or the TRA's Order.

The City's continued litigation over these documents does nothing to advance this rate-making proceeding; it only serves to drive up cost. The City previously argued that TAWC should be required to produce a list of documents withheld on the basis of privilege or protection. Pursuant to the Order of the Hearing Officer, TAWC did so. Upon receiving what it requested, the City immediately filed this ***third*** motion to compel seeking production of each

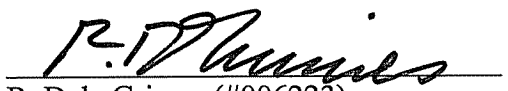
listed document, except for one. The City's design in pursuing this course is obvious: to make litigating rate cases more expensive for the Company.

Finally, the Company's internal communications about the management audit have no relevance or impact on the Authority's ability to set rates in this case, which is the only purpose of this proceeding. Although the City claims there is no dispute that these documents are relevant, TAWC has always maintained that they are neither relevant nor likely to lead to the discovery of relevant evidence. Indeed, any relevant communications regarding the management audit – those between TAWC and Schumaker & Company – have already been provided to all the parties.

CONCLUSION

Because the City has failed to address the work product doctrine or identify any valid legal basis for requiring TAWC to produce privileged documents and work product, and because the City's requested relief will do nothing to further this rate-making proceeding, the City's Motion to Compel must be denied.

Respectfully submitted,



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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 14th day of January, 2011, upon the following:

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