IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF TENNESSEE AMERICAN	)	
WATER COMPANY TO CHANGE AND	)	
INCREASE CERTAIN RATES AND	)	**DOCKET NO. 10-00189**
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	)	

****

TERRY BUCKNER
NON-CONFIDENTIAL DIRECT TESTIMONY
AMENDMENT

****

January 28, 2011

Q. Please state your name for the record.

A. My name is Terry Buckner.

Q. By whom are you employed and what is your position?

A. I am employed by the Consumer Advocate and Protection Division ("Consumer Advocate") in the Office of the Attorney General for the state of Tennessee ("Office") as a Regulatory Analyst.

Q. Are you the same Terry Buckner who previously filed direct testimony in this docket?

A. Yes.

Q. What is the purpose of your testimony?

A. The of my testimony is to amend my pre-filed direct testimony, the forecasted financial exhibits ("Exhibits of Consumer Advocate") and certain work papers ("work papers of Terry Buckner") for forecasted Operation and Maintenance expenses, Depreciation Expense, Taxes Other Than Income, Income Taxes, and Rate Base for Tennessee American Water Company ("TAWC") for the attrition year ending December 31, 2011.

Q. Please describe the first amendment.

A. The first amendment is to incorporate the percent of double leverage capital structure accounted for by Parent Common Equity and the overall weighted cost of capital as disclosed by Consumer Advocate witness, Dr. Christopher C. Klein on January 21, 2011. This amendment is reflected on Schedule 9 of the Amended Exhibits of Consumer Advocate.

Q. **Please describe the second amendment.**

A. The second amendment is to account for the numerical amounts in response to the TRA's data request dated January 28, 2011.

Q. **What are the required corrections to your direct testimony due to the two amendments?**

A. The corrections are as follows:

Page 2, Line 25 should be $1.007 million and not $.589 million;

Page 2, Lines 25 and 26 should be $8.977 million and not $9.395 million;

Page 3, Line 12 should be $1.172 million and not $2.167 million;

Page 3, Line 15 should be $3 million and not $2.47 million;

Page 3, Line 20 should be $8.977 million and not $9.395 million;

Page 6, Line 19 should be $1.172 million and not $2.167 million;

Page 6, Line 22 should be $10.6 million and not $18.9 million;

Page 6, Line 24 should be $8.1 million and not $16.5 million;

Page 7, Line 1 should be $3 million and not $2.47 million;

Page 7, Line 7 should be $3 million and not $2.47 million;

Page 51, Line 5 should be $225,496,162 and not $225,457,700;

Page 51, Line 8 should be $888,328 and not $926,750;

Page 52, Line 22 should be $714,285 and not $758,675;

Page 52, Line 4 should be $176,761 and not $132,701;

Page 54, Line 3 should be $25,288,933 and not $33,664,910;

Page 54, Line 4 should be $8,135,118 and not $16,511,095;

Page 57, Line 30, should be $10.6 million and not $18.9 million;

Q. Have amended direct testimony, exhibits, and work papers been prepared?
A. Yes. Amended public and confidential direct testimonies, exhibits, and work papers are being filed along with this amendment.

Q. Does this conclude your amendment?
A. Yes.

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 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**

AFFIDAVIT

I, Terry Buckner, Analyst, for the Consumer Advocate Division of the Attorney General's Office, hereby certify that the attached Terry Buckner Direct Testimony Amendment represents my opinion in the above-referenced case and the opinion of the Consumer Advocate Division.

Terry Buckner
TERRY BUCKNER

Sworn to and subscribed before me this 28th day of January, 2011.

Emily Knight
NOTARY PUBLIC

EMILY KNIGHT STATE OF TENNESSEE NOTARY PUBLIC DAVIDSON COUNTY, TENN.
My Commission Expires AUG. 23, 2011

My commission expires: Aug. 23, 2011

Q. Please state your name for the record.

A. My name is Terry Buckner.

Q. By whom are you employed and what is your position?

A. I am employed by the Consumer Advocate and Protection Division ("Consumer Advocate") in the Office of the Attorney General for the state of Tennessee ("Office") as a Regulatory Analyst.

Q. How long have you been employed in conjunction with the public utility industry?

A. I have been employed in conjunction with the public utility industry for over thirty-two years. Before my current employment with the Office, I was employed by the Comptroller's Office for the state of Tennessee for nearly two years as the Assistant Director responsible for public utility audits after approximately eight years of prior employment with the Office. Formerly, I was employed with the Tennessee Public Service Commission ("Commission") in the Utility Rates Division as a financial analyst for approximately six years. My responsibilities included testifying before the Commission as to the appropriate cost of service for public utilities operating in Tennessee. Prior to my employment with the Commission, I was employed by TDS Telecom for eight years and the First Utility District of Knox County for three years.

Q. What is your educational background and what degrees do you hold?

A. I have a Bachelors degree in Business Administration from the University of Tennessee, Knoxville with a major in Accounting. I am also a Tennessee Certified Public Accountant ("CPA") and a member of the American Institute of Certified Public Accountants.

Q. Would you briefly describe your responsibilities as a Regulatory Analyst with the Consumer Advocate?

A. I prepare testimony and financial exhibits in rate proceedings as an employee with the Consumer Advocate. Additionally, I review filings by Tennessee public utilities, which are subject to the jurisdiction of the Tennessee Regulatory Authority ("TRA").

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to represent the forecasted financial exhibits prepared by the Consumer Advocate ("Exhibits of Consumer Advocate") and provide my exhibit of work papers ("work papers of Terry Buckner") for forecasted Operation and Maintenance expenses, Depreciation Expense, Taxes Other Than Income, Income Taxes, and Rate Base for Tennessee American Water Company ("TAWC") for the attrition year ending December 31, 2011.

SUMMARY OF RESULTS

Q. Please summarize the results of the Consumer Advocate forecast of TAWC's earnings for the attrition year.

A. The attrition year in this case is the twelve months ending December 31, 2011. For the attrition year, TAWC asked for a $9.984 million rate increase in its original petition before the TRA, whereas the Consumer Advocate's forecasted results show that customer rates should actually be increased by $1.007 million instead, which is a difference of $8.977 million between TAWC's forecast and the Consumer Advocate's forecast. The $8.977 million difference is primarily due to the following areas of disagreement between TAWC and the Consumer Advocate: (1) The Consumer Advocate believes that TAWC will collect about $1.1 million more in operating revenue than the revenue estimates included in TAWC's rate increase petition. Consumer Advocate witnesses, Mr. John Hughes and Mr. Hal Novak, will address the difference in revenue forecasts; (2) The Consumer Advocate is projecting about $2.88 million less in operation and maintenance expenses than the amount projected by TAWC; (3) The Consumer Advocate's calculation of depreciation expense is approximately $0.174 million less than the depreciation expense projected by TAWC; (4) The Consumer Advocate forecasts approximately $0.274 million less in "taxes other than income taxes" than the taxes projected by TAWC; (5) The Consumer Advocate's calculation of rate base is about $1.172 million less in revenue requirement when applying the Consumer Advocate's recommended rate of return; and (6) The amount of revenue required for TAWC to have an opportunity to earn a fair profit is about $3 million less in the Consumer Advocate's forecast due to the Consumer Advocate's computation of a lower cost of capital. The difference in gross revenue conversion factors and interest synchronization comprised the remainder of the revenue requirement difference.

Accordingly, the Consumer Advocate's position is that TAWC has requested over $8.977 million more in customer rates than the company actually needs to meet their expenses and provide a fair return to their shareholders while providing quality water services to TAWC's customers. Although there are many underlying details supporting the Consumer Advocate's position, all of which are discussed below and shown in the testimony, work papers, and exhibits of the Consumer Advocate's witnesses, the six areas discussed above serve as an overview of the primary areas of disagreement between TAWC and the Consumer Advocate in this case.

Q. Please summarize why the Consumer Advocate is projecting about $2.88 million less in Operation and Maintenance ("O&M") expenses than TAWC.

A. The $2.88 million difference in O&M expenses between the Consumer Advocate and TAWC is due to the Consumer Advocate's projecting: (1) about $0.765 million in lower O&M Labor; (2) about $0.1 million less in Fuel and Power Expense; (3) approximately $0.138 million less in Chemical Expense (4) about $1.6 million less in management fees; (5) about $0.092 million less in Pension Expense; (6) $0.185 million less in regulatory expense; and (7) about $0.164 million less in Insurance Other than Group.

The salaries and wages difference of $0.765 million is due to the Consumer Advocate's rejection of TAWC's forecasted employee levels for the attrition year. The Consumer Advocate rejects this projection because TAWC continues to demonstrate in case after case an overstated number of employees when compared to what they actually keep on the payroll. As a result, TAWC's customers have actually been charged for an employee level that TAWC never achieved for the entire forecast period. Customers' water rates should not be set on employee levels that are never sustained. In addition, the Consumer Advocate rejects TAWC's plan to charge customers for bonuses paid to salaried employees for increasing the regulated earnings of the company, an activity that benefits TAWC's shareholders by moving money to their pockets from the pockets of TAWC's customers. Since customers are provided no benefit from this activity, they should not have to pay any costs associated with it.

The $0.1 million in Fuel and Power is primarily driven by the growing level of unaccounted for water loss. This is the same reason for the $0.138 million difference in Chemical Expense. The Consumer Advocate's calculations with the limit of a fifteen percent unaccounted for water percentage is consistent with TRA Order #08-00039.[1]

The difference in TAWC's and the Consumer Advocate's management fee forecast is about $1.6 million. TAWC's growth in management fees exceeds any economic or cost-savings justification, and has far out-stripped inflation. Furthermore, the allocation of costs from the service company to TAWC is not cost causative.

The $0.092 million difference in Pension Expense is due to the adoption of a higher capitalization rate by the Consumer Advocate for the attrition year.

The $0.185 million difference in regulatory expense stems from the Consumer Advocate's disagreement with the reasonableness of these charges. In particular, the actual regulatory expense that TAWC wants to charge customers includes costs from TRA Docket #06-00290, which had a three year amortization period. Also, the Consumer Advocate does not believe that customers should be called upon to pay TAWC's legal bills for pursuing a rate increase which, as demonstrated by the testimony and exhibits of the Consumer Advocate's witnesses, is without merit. As a result, the Consumer Advocate has included 50% of the projected rate case costs in this docket.

The $0.163 million difference in Insurance Other Than Group is primarily due to the use of a later test period.

[1] TRA Order dated January 13, 2009, TRA Docket No. 08-00039, Page 17.

Q. Please summarize why the Consumer Advocate is projecting about $0.174 million less in depreciation expenses than the amount projected by TAWC.

A. This difference in depreciation expense is primarily attributable to the Consumer Advocate's application of the current depreciation rates to projected ending monthly plant in service balances with a starting point of September 30, 2010. This methodology is more precise than TAWC's method, which applied the current depreciation rates to a thirteen month average plant in service balance.

Q. Please summarize why the Consumer Advocate's forecast of taxes other than income taxes is about $0.274 million lower than TAWC's other tax calculations.

A. This difference is primarily due to the Consumer Advocate's computation of lower property taxes. In computing its property tax forecast, the Consumer Advocate used a more recent property assessment value than TAWC.

Q. Please summarize the $1.172 million difference in revenue requirements attributable to the Consumer Advocate's computation of a lower rate base for TAWC.

A. The Consumer Advocate's rate base is approximately $10.6 million lower than the forecasted amount by TAWC. The Consumer Advocate's Accumulated Deferred Income Taxes make up $8.1 million of this difference. TAWC has improperly departed from recognizing the Accumulated Deferred Income Taxes recorded on their books at September 30, 2010.

Q. Please summarize the $3 million difference in revenue requirements attributable to the Consumer Advocate's computation of a lower cost of capital for TAWC.

A. Based on the cost of capital testimony of Consumer Advocate witness Dr. Chris Klein, the Consumer Advocate incorporated a lower overall rate of return on rate base than TAWC requested in its rate increase petition. This lower return decreases the revenue requirements of TAWC by about $3 million. The testimony of Consumer Advocate witness Klein sets forth the details of the Consumer Advocate's position on the cost of capital in this case.

RATEMAKING THEORY AND PRACTICE

Q. What is a public utility?

A. In the context of this case, a public utility is a business formed as a shareholder-owned corporation. Even though the public utility in this case is a for profit corporation, it is also important to note that this public utility is:

> an organization that has been designated by law as a business affected with a significant public interest, and that also possesses all of the following characteristics: (1) The business is essentially free from direct competition, i.e., it operates in a monopolistic environment; (2) The business is required by law to charge rates for its services that are reasonable and not unjustly discriminatory; (3) The business is allowed to earn (but not guaranteed) a "reasonable" profit; and (4) The business is obligated to provide adequate service to its customers, on demand.[2]

Q. Does TAWC possess these public utility characteristics?

A. Yes. TAWC is a shareholder-owned public utility[3] that has been granted the advantage of operating in a monopolistic environment in exchange for special obligations, namely, the requirement to provide adequate service to all customers at rates that are just, reasonable, and non-discriminatory.

Q. From a regulated ratemaking perspective, what is the TRA called upon to do in this proceeding?

A. In a rate case such as this one, the TRA is asked to establish the amount of revenues that the utility should collect in order to cover its reasonable and necessary expenses and to reasonably compensate the utility's investors for their investment in the plant and equipment necessary to provide utility service to the public. The following ratemaking formula can be used to express this concept:

Revenue Requirement = (Rate Base X Rate of Return) + Operations and Maintenance Expense + Depreciation Expense + Taxes.

In this equation, "Rate Base" is essentially the plant and equipment paid for by the investors in the utility. The "Rate of Return" is comprised of two major components: (1) the "Cost of Debt," which constitutes the interest rate on borrowed money and (2) the "Return on Shareholders' Equity" ("ROE"), which is the rate of compensation that flows to the owners of the utility for their investment. "Operations and Maintenance Expense" is the costs of operating the utility day-to-day, such as payroll, employee benefits, fuel and power to pump the water, chemicals to treat the water supply,

[2] *Accounting for Public Utilities,* Hahne and Aliff §1.01.

rents, office supplies, postage and billing costs, etc. "Depreciation Expense" is the systematic recovery of the cost of the plant and equipment over their useful lives. "Taxes" are the business taxes owed by the utility to federal, state, and municipal governments, such as income taxes, payroll taxes, property taxes, and franchise taxes. In order to arrive at the appropriate amounts for each component of the ratemaking formula, the TRA should consider the expert witness testimony of economists, accountants, and other subject matter experts. These experts usually calculate the amount of each component of the ratemaking formula for the "Attrition Year." In making their "Attrition Year" forecast, ratemaking experts often consider "Test Year" data.

Q. Please explain the difference between a "Test Year" and an "Attrition Year."

A. A "Test Year" is a measure of a utility's financial operations and investment over a specific twelve month period. It is the "raw material" for developing an Attrition Year measure of the utility's financial operations and investment (that is, the utility's Rate Base, Operations and Maintenance Expense, Depreciation Expense, and Taxes). Therefore, the selection of the test year is quite important:

> The selection of the timing of the test year may be the most significant single factor in the rate-making process. The more outdated the test year levels of operations, the more critical is the need for significant restatement to produce representative levels of future conditions.[4]

An "Attrition Year," also known as a forecast period, is the "finished product"

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[3] TAWC is a subsidiary of American Water Works Company, Inc. ("AWWC").
[4] *Accounting for Public Utilities,* Hahne and Aliff §7.03.

and is to be representative of the period for any rate adjustment. The Attrition Year can also be viewed as the first year during which the TRA's rate order will be applied.

In this docket, TAWC's filing used a test year ended March 2010 and an attrition year ending December 2011. In an effort to eliminate outdated financial information and to shorten the forecast window, the Consumer Advocate has adopted the test year ended September 2010 in its forecast for the attrition year ending December 2011.

Q. **Has TAWC made an issue of the "Test Year"?**

A. Yes, the Company's direct testimony provides a section on "The Proper Test-Year."[5]

Q. **Does the Consumer Advocate agree with TAWC's assertions?**

No. TAWC confuses updating financial information with the use of multiple test periods. The issues between the parties should be the different forecasted amounts within the attrition year. Consumer Advocate witness, Hal Novak, will address the historical rate making practice of updating test periods in Tennessee. The Consumer Advocate regularly updates the test year for all the public utility rate filings in Tennessee. TAWC is the only public utility in Tennessee to make an issue of the Consumer Advocate's practice of updating test periods. The Consumer Advocate would also cite the rebuttal testimony of Mr. David Foster in TRA Docket #05-00258 in support of updating test periods. (Terry Buckner Exhibits) Mr. Foster testified that the TRA may use a historical test period, forecast test period, or a

[5] TAWC Direct Testimony, M. Miller Pages 16-20.

combination of both in setting rates.

Q. **Please explain how the TRA should calculate any adjustment in customer rates to be applied during the attrition year.**

A. Once the TRA arrives at the appropriate Revenue Requirement for the attrition year (as described above), it must then determine whether a rate adjustment is needed. If the Revenue Requirement is greater than the amount of operating revenue forecasted for the attrition year at present customer rates, then a rate increase is required. However, if the Revenue Requirement is less than the amount of operation revenue forecasted for the attrition year at present customer rates, then a rate decrease is required.

In determining whether a rate increase or rate decrease is warranted, the TRA should again consider the testimony of the parties' expert witnesses. In addition to forecasting the Revenue Requirement for the attrition year, these experts also forecast the amount of operating revenue that the utility is expected to collect during the attrition year at the current customer rates set forth in the utility's tariff.

OPERATION AND MAINTENANCE EXPENSES

Q. **Please describe the components of O&M Expenses.**

A. There are 17 O&M Expense categories subject to forecast in this docket. The first category is forecasted O&M Labor. This category was projected based on a payroll price-out.

In two categories, Fuel & Power and Chemicals, there is a direct correlation between TAWC's forecasted revenues and the volume of water filtration expenses accounted for in these two O&M Expense categories. Thus, these two categories were projected based on the volume of water filtration built into the revenue forecast.

For the categories of Management Fees, Pension Expense, Regulatory Expense and Insurance Other than Group, the Consumer Advocate has forecasted these amounts based on TRA precedent and the history of O&M Expenses for TAWC.

For the other eleven categories, the Consumer Advocate primarily adopted the amounts per account for the twelve months ended September 30, 2010 and grew each amount by half of the customer growth of .89%[6] plus the annual GDP Chained Price Deflator growth rate of .76%.[7] The combined growth rate from September 2010 through December 31, 2011 is approximately 1.51%. This methodology is the standard procedure that the Consumer Advocate uses to forecast non-salary and wage O&M Expenses in rate proceedings before the TRA. Due to the large number of differences between the Consumer Advocate and TAWC in the amounts within O&M expense categories, as well as the amounts within expense accounts within each category, the Consumer Advocate will address only the significant net differences in its O&M expense forecast and the O&M expense forecast of TAWC. The details of the forecast, however, are presented in the Consumer Advocate's work papers, which are referenced in the following discussion of each O&M category.

Q. What are the significant differences between TAWC and the Consumer

[6] John Hughes work paper, R-CUSTOMER GROWTH, Index of work papers, page 97.
[7] Terry Buckner work paper, E-GDP, Index of work papers, page 45.

Advocate in O&M Expenses for the forecasted attrition year?

A. Consumer Advocate work paper E-REC-1[8] provides a reconciliation of the differences in the calculation of O&M Expenses.

The significant differences in O&M Expense for the forecasted attrition year are: (1) $765,188 in lower labor costs; (2) $100,370 in lower Fuel and Power costs; (3) $138,408 in lower Chemicals expense; (4) $1,555,185 in lower Management Fees; (5) $92,701 in lower Pension costs; (6) $184,634 in lower Regulatory Expense and (7) $163,642 in lower Insurance Other than Group. Accordingly, the Consumer Advocate's total O&M Expense forecast is $2,876,208 lower than TAWC's forecast.

Q. Please describe your forecast methodology for O&M Labor.

A. Total O&M Labor was primarily calculated using actual employee levels, actual wage rates per employee, actual overtime hours as of September 2010, and prospective pay raises at January 1 of each year per TAWC's policy for salary and non-union employees. The union employees receive an annual pay raise at November 1 of each year per their contract.[9] The O&M Labor amount was derived from the calculated total salary and wage dollars minus salary and wage dollars charged to capitalization, i.e., work on capital projects. The capitalized salaries and wages were calculated using TAWC's actual average capitalization rate for the twelve months ended December 31, 2008. The capitalization rate utilized by TAWC is not representative of the plant additions to be incurred during the attrition year. TAWC opted to limit their capital additions in 2009 to the amount of internal financing, i.e.,

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[8] Terry Buckner work paper, E-REC-1, Index of work papers, page 1.

[9] TAWC response to TRA request #33, TN-TRA-Q033-ATTACHMENT, Page 8 of 31.

depreciation expense. The capitalized salaries and wages removed from the total calculated salaries and wages forecast is accounted for in rate base. Forecasting O&M salaries and wages through this price-out methodology is the standard procedure that the Consumer Advocate uses to forecast salaries and wages in rate proceedings before the TRA.

Q. Please explain the differences in the calculation of O&M Labor.

A. Consumer Advocate work paper E-PAY-6[10] provides a reconciliation of the differences in the calculation of O&M Labor. In summary, O&M Labor as forecasted by TAWC for the attrition year is overstated by $765,187.

The significant differences between TAWC and the Consumer Advocate in the calculation of O&M Labor are attributable to the following:

(1) According to TAWC's testimony, the forecast of O&M Labor includes 110 employees for the attrition year;[11] TAWC adopted the overtime hours and the capitalization rate of 15.83%[12] for the test period ended March 2010; TAWC's O&M Labor is $5,680,299[13].

(2) Consumer Advocate work papers E-PAY-1, E-PAY-2, and E-PAY-3[14] provide a price out of all employees for the attrition period. The Consumer Advocate adopted an employee level of 104. The Consumer Advocate used the actual capitalization rate for the twelve months ended December 31, 2008 of 20.57% and the Consumer Advocate excluded 70% of TAWC's Annual Incentive Plan ("AIP").

[10] Terry Buckner work paper, E-PAY-6, Index of work papers, page 9.
[11] TAWC Direct Testimony, J. Watson, Page 21, Question 24, Line 15.
[12] TAWC Direct Testimony, S. Miller, Page 7, Line 6.
[13] TAWC Exhibit No. 2, Schedule 3, Page 1 of 1, Line No. 1.
[14] Terry Buckner work papers, Index of work papers, pages 2-4.

Q. Why did the Consumer Advocate use current employee levels in its forecast rather than TAWC's projection of future employee levels?

A. The Consumer Advocate primarily used current employee levels because TAWC has a known and measurable history of inflating its employment levels. Historically, TAWC does not achieve or maintain their forecasted employment levels. TAWC's continued requests to set rates on an inflated employee level instead of a realized employee level should be denied.

In TRA Docket #03-00118, TAWC included in its forecast 119 employees.[15] Subsequent to the TRA Order, TAWC cut the number of employees to 108 at the end of July 2003. The actual average employee level for the attrition year in TRA Docket #03-00118 was 113[16] rather than the 119 TAWC had forecasted. As a result, the actual O&M Labor expense for TRA Docket #03-00118 was $4,631,351[17] instead of TAWC's forecast of $5,066,066[18].

In TRA Docket #04-00288, TAWC included in its forecast 106[19] employees for the attrition year ended December 2005. Yet, the average employee level for that period was only 99.[20] TAWC forecasted O&M Labor expense of $4,383,883[21] for the attrition year. Again, TAWC's forecasted O&M Labor expense was significantly overstated for the TRA Docket #04-00288 attrition year. The actual O&M Labor expense for the same period

[15] TRA Docket #04-00288, Direct Testimony, M. Miller, Page 14, Lines 17-18.
[16] Terry Buckner work paper, E-PAY-5, Index of work papers, page 8.
[17] TRA Docket #04-00288, TAWC Exhibit No.2, Schedule 3, Page 1 of 1, Line 1.
[18] TRA Docket #03-00118, S. Valentine Exhibit No. 2, Schedule 3, Page 1 of 1, Line 1.
[19] TRA Docket #04-00288, Direct Testimony, M. Miller, Page 14, Lines 16-17.
[20] Terry Buckner work paper, E-PAY-5, Index of work papers, page 8.

was $3,765,383[22] rather than TAWC's forecast of $4,383,883.

In TRA Docket #06-00290, TAWC contended that it would need 111 employee positions.[23] Yet, TAWC averaged only 108 employees. At one point, TAWC stated in the proceeding it would have 110 employees by the following Monday in April of 2007.[24] Yet, based on TAWC's response, that employment level either did not occur or was quite brief. Consumer Advocate work paper E-PAY-5[25] compares the actual employee levels of TAWC with the forecasted employee levels by TAWC. A Consumer Advocate chart[26] from this data demonstrates that TAWC has repeatedly maintained employee levels below their forecasted employee levels included in their rate filings before the TRA.

As previously mentioned, TAWC has included 110 employees in this docket, which is an additional three new positions, according to TAWC's testimony. The three new positions are: Finance Manager; Government Affairs Specialist, and Non-Revenue Water Supervisor.[27] The Consumer Advocate has excluded the salary of the Government Affairs Specialist. Ratepayers should not be required to compensate for lobbying and political influence activities, which are not necessary in the provision of water service. The Indiana Utility Regulatory Commission found:

Based on the evidence presented, the Commission is not

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[21] TRA Docket #04-00288, Exhibit No. 2, Schedule 3, Line 1.
[22] TRA Docket #06-00290, TAWC Rebuttal Exhibit MAM-15, Page 2 of 2.
[23] TRA Docket #06-00290, Rebuttal Testimony, J. Watson, Page 6.
[24] TRA Docket #06-00290, Transcript dated 4/18/07, afternoon session, Page 272, J. Watson.
[25] Terry Buckner work paper, E-PAY-5, Index of work papers, page 8.
[26] Terry Buckner work paper, Index of work papers, page 12.
[27] TAWC Direct Testimony, J. Watson, Question 18, Pages 17-18.

> convinced that government affairs is more or something other than a lobbying group, and Indiana American has not convinced the Commission that lobbying activities are beneficial to the provision of utility service to its customers.[28]

The position of Finance Manager was eliminated in TRA Docket #04-00288 as a part of TAWC's reorganization. In fact, TAWC paid $93,659[29] in severance pay to Mr. Dan Bailey, who was the business/finance manager at TAWC. Yet, in this docket, TAWC petitions that the Finance Manager position be restored. Historically, TAWC has difficulty in finding the appropriate employee configuration for providing water service to its customers.

Further, the Consumer Advocate has learned of the retirements of TAWC employees, Monty Bishop and Randall Taylor. The Consumer Advocate has not included the salaries for these two positions in its payroll expense forecast. Ratepayers should not have to continue to pay for salaries and wages for retirees.

Given the history of TAWC's employment representations and management practices, the Consumer Advocate recommends to the TRA that only known and measurable salaries and wages necessary for the provision of water service be included in the attrition year. TAWC averaged 104 employees for the test year ended September 2010.

Therefore, the TRA should reject the O&M Labor Expense forecast of TAWC and set rates on actual employee levels, not on speculative employment positions that never materialize. Indeed, the employment history clearly demonstrates that such speculative levels are not achieved and therefore

[28] Re Indiana-American Water Company, Inc. Cause No. 43680, Order dated April 30, 2010, Page 68.
[29] TRA Docket #04-00288, TRA Data Request #9.

are not proper for rate making purposes. TAWC "can be subject to economic downturns and must hold the line on expenses and employee growth during lean times."[30] TAWC's employment history also demonstrates that the current employee level is sufficient for operation of the company. According to the Affiliate Audit Report of TAWC, the company's "success at meeting service appointments has generally exceeded 99% in the last six years with only two exceptions".[31]

Q. Are there any other differences in O&M Labor that you wish to discuss?

A. Yes. The Consumer Advocate also has disallowed seventy percent, or $102,646 of O&M Labor for "incentive payroll." The incentive payroll known as AIP is based on two performance measures: (1) Financial; and (2) Operational.[32] Seventy percent of the AIP is based on the financial operating results of TAWC.[33] Under the incentive plan, TAWC increases the compensation to its employees for increasing TAWC's regulated earnings. Because there is no mechanism under the incentive plan for TAWC's ratepayers to share in these increased earnings, TAWC's employees and shareholders will reap all of the financial rewards of these higher earnings. Additionally, ratepayers are the sole source of TAWC's regulated earnings; therefore, the incentive plan is a circular one whose success is built into this very docket, rewarding TAWC's employees and shareholders for merely increasing water rates charged to ratepayers. This is illustrated by the following: If TAWC's

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30 TRA Order #08-00039, dated January 13, 2009, Page 13.

31 Schumaker & Company Affiliated Audit Report dated August 2010, Page 121.

32 TAWC response to TRA Data Request #37 and 2010 Plan per Direct Testimony of Ralph C. Smith, Consumer Advocate Division, W. Va. Case No. 10-0920-W-42T, dated November 12, 2010, Page 35, Exhibit RCS-2.

33 TAWC response to TRA-01-Q-037-ATTACHMENT, Page 7 of 36.

employees are successful in increasing the company's earnings, even to the point of earning above the authorized rate of return set by the TRA, TAWC will reward its employees for this effort through the AIP. In such a case, ratepayers would not only be unreasonably burdened by the over-earnings, but under TAWC's proposal, they also would have to pay an "over earnings surcharge" in the form of the AIP. The Consumer Advocate does not object if the company wants to reward its employees for increasing its earnings from regulated operations; however, the cost of these rewards should be charged to those that benefit from the AIP — the company's shareholders — not the ratepayers. For these reasons, there is no reasonable basis to charge this portion of the cost of the incentive plan to ratepayers, as these plan benefits will inure entirely to TAWC's employees and shareholders whereas the incentive plan's associated burdens will fall directly on ratepayers. In fact, TAWC paid out financial rewards to its salary employees in 2009 following the rate increase awarded to it in January 2009.

As a result, seventy percent of the incentive amount has been excluded and should be borne solely by TAWC's shareholders. The Consumer Advocate's treatment of incentive payroll is in accord with established TRA precedent.[34] Of note, utility incentive plans have been recently limited or disallowed in Louisiana, Kentucky, Idaho, Connecticut, Illinois and Oklahoma.[35]

Q. What is the primary issue with Fuel and Power Expense?

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[34] TRA Docket #06-00290, Order dated June 10, 2008, Page 24.

[35] *Entergy Louisiana, Inc., Ex Parte*, 2005 WL 372935 (May 25, 2005); *Commonwealth Edison Co. v. Illinois Commerce Commission*, 2009 WL 3048420 (September 17, 2009); *In re Public Service Co. of Oklahoma*, 270 P.U.R. 4th 205 (January 14, 2009); *In re United Water Idaho Inc.*, 2005 WL 3091674 (September 20, 2005); and *In re Kentucky-American Water Co.*, 2010 Case No. 2010-00036, December 14, 2010.

A. The primary difference between TAWC and the Consumer Advocate concerns the amount of Fuel and Power Expense for the loss of unaccounted for and non-revenue water. The unaccounted for and non-revenue water loss has continued to grow.[36] Consistent with the TRA's Order in Docket No. 08-00039[37], the Consumer Advocate has capped the amount of unaccounted for and non-revenue water loss to fifteen percent in its calculation of Fuel and Power Expense. Also, the Consumer Advocate has incorporated the fuel cost adjustment as of November 1, 2010.

Therefore, the Consumer Advocate recommends that $2,410,868[38] be adopted by the TRA to take into account known and measurable price increases and capping the loss of unaccounted for and non-revenue water at 15% as established by the TRA.

Q. What is the primary issue with Chemicals Expense?

A. Again, the primary difference between TAWC and the Consumer Advocate concerns the amount of Chemicals Expense for the loss of unaccounted for and non-revenue water. The unaccounted for and non-revenue water loss has continued to grow.[39] Consistent with the TRA's Order in Docket No. 08-00039[40], the Consumer Advocate has capped the amount of unaccounted for and non-revenue water loss to fifteen percent in its calculation of Chemicals Expense. Additionally, the Consumer Advocate has incorporated the price adjustments as disclosed to the TRA.[41]

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[36] TAWC response TRA-01-Q013-FUEL AND POWER, Page 20 of 20.
[37] TRA Order dated January 13, 2009, Page 15.
[38] Terry Buckner work paper E-FP, Index of work papers, Page 14
[39] TAWC response TRA-01-Q013-FUEL AND POWER, Page 20 of 20.
[40] TRA Order dated January 13, 2009, Page 15.
[41] TAWC response TRA-02-Q117-ATTACHMENT 3.

Therefore, the Consumer Advocate recommends that $930,961[42] be adopted by the TRA to take into account known and measurable price increases and capping the loss of unaccounted for and non-revenue water at 15% as established by the TRA.

Q. **What are Management Fees?**

A. Management Fees are the result of a service agreement between American Water Works Service Company ("AWWSC") and TAWC in effect as of January 1, 1989. AWWSC

> is a service company that is designed to aid, assist, and advise other subsidiaries, such as TAWC, in their business operations by providing accounting, administration, communications, corporate secretarial, engineering, financial human resources, information technology, operations, rates and revenue, risk management, and water quality services.[43]

Management Fees may be directly charged or allocated from AWWSC to TAWC.

Q. **What is the history of the Management Fees issue for TAWC?**

A. Management Fees have been an issue in Tennessee for the last five years.

In TRA Docket #04-00288, as a result of reorganization, TAWC included a 22% increase of $555,664 in Management Fees which brought the total forecasted 2005 Management Fees to $3,062,940. TAWC represented that this increase would "enable the Company to operate more efficiently

[42] Terry Buckner work paper E-CHEM2, Index of work papers, Page 16.

[43] Schumaker & Company, Affiliate Audit Report, August 2010, Page 13.

and cost effectively while at the same time improving and enhancing the service that the Company provides."[44] Reorganization in this instance meant the elimination of jobs in Chattanooga and the creation of jobs in other AWWSC locations. However, TAWC has booked $3,716,559 in 2005 and $4,376,059 in 2006 for Management Fees.[45]

Subsequently, in TRA Docket #06-00290, TAWC forecasted $4,064,421 for the attrition year ended February 2008, a 33% increase over the 2005 forecast amount. In support for this level of increase, TAWC claimed that full time employees ("FTEs") had been shifted to the Regional Service Company.[46] Further, TAWC claimed that it was not appropriate to use the 2005 forecasted amount because it was a settlement amount.[47] In support of their forecasted Management Fees, TAWC filed a an exhibit using a starting point of March 31, 2004 per TRA Docket #03-00118 to compare an inflated fully loaded company labor to their forecasted management fees and forecasted labor.[48] TAWC had management fees of $4,734,432 for 2007[49] which results in a 56% increase over the forecasted December 2005 amount. Despite the claims of TAWC, rates were set in TRA Docket #04-00288 for the forecast period ending December 31, 2005 and a Management Fee amount of approximately $3 million. This Management Fee amount was not the result of settlement, but was simply TAWC's amount included in its filing.

In TRA Docket #08-00039, the Consumer Advocate based its forecast of an appropriate Management Fees amount using the 2005 amount as a starting point. The Consumer Advocate contended that TAWC's level of Management Fees was simply <u>not</u> just and reasonable for the ratepayers.

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[44] TRA Docket #04-00288, Direct Testimony of M. Miller, Pages 14-15, Lines 15-16 and Lines 2-4.
[45] Schumaker & Company, Affiliate Audit Report, August 2010, Exhibit II-10, Page 25.
[46] TRA Docket #06-00290, Rebuttal Testimony, M. Miller, Page 53, lines 29-30.
[47] TRA Docket #06-00290, Rebuttal Testimony, M. Miller, Page 54, lines 7-10.
[48] TRA Docket #06-00290, Rebuttal Exhibit MAM-15, Page 1 of 2.
[49] Schumaker & Company, Affiliate Audit Report, August 2010, Exhibit II-10, Page 25.

While TAWC's other expenses continue to rise, there was no offset anywhere in TAWC's forecast to account for the rise in Management Fees. Therefore, contrary to TAWC's position, their forecasted Management Fees did not provide a more cost efficient operation. Even TAWC concedes this.[50] Additionally, TAWC's management audit known as the Independent Cost Assessment Report ("ICAR") concluded that the growth from 2005 to 2006 was "Above the average cost change"[51] of the peer group. A 33% increase without any offset is also unreasonable and out of step with TAWC's current growth indicators such as inflation and customer growth.

As a result, in Docket #08-00039, the TRA found that the performed management audit "did not adequately address the issue of prudency of the management fees, and that the audit was not an independent audit as ordered in TRA Docket No. 06-00290."[52] Also, "a majority of the panel voted to set the Management Fee attrition year expense amount at $3,529,933."[53] Finally, the TRA,

> ordered the Company to develop a Request for Proposal ("RFP") for a comprehensive management audit by an independent certified public accountant....Further, the audit shall evaluate and attest to the charges allocated to TAWC, including the efficiency of processes and/or functions performed on behalf of TAWC, as well as the accuracy and reasonableness of the allocation factors utilized.[54]

On September 10, 2010, an Affiliate Audit Report was filed by Schumaker & Company in TRA Docket #09-00086.

By TAWC's own admission, the forecasted 2011 Management Fees for

[50] TRA Docket #06-00290, Rebuttal Testimony, M. Miller, Page 54, Lines 10-13.
[51] TRA Docket #08-00039, TAWC Direct Testimony, J. Van Den Berg, Page 12.
[52] TRA Docket #08-00039, Order dated January 13, 2009, page 20.
[53] TRA Docket #08-00039, Order dated January 13, 2009, page 21.
[54] TRA Docket #08-00039, Order dated January 13, 2009, page 22.

TAWC will be 46.55%[55] higher than their 2005 Management Fees amount. A 2005 amount which was $.7 million more than the original TAWC forecasted amount in TRA Docket #04-00288.

Therefore, the forecasted Management Fees in this docket are more than double the amount in 2004 for an annual increase of over 14% annually. This annual growth rate exceeds any just and reasonable economic growth measurement.

Q. In your previous answer, you referred to the Affiliate Audit Report filed by Schumaker & Company in TRA Docket #09-00086. What is the Consumer Advocate's general opinion of the Schumaker & Company Report?

A. In the opinion of the Consumer Advocate, the Schumaker & Company Report is somewhat limited in scope. However, the Consumer Advocate would caution the TRA against issuing a clean bill of health for the amount requested for Management Fees in this rate case as TAWC seems to imply. My concerns with the Schumaker Report fall into two main categories: (1) the correctness of the allocation method between AWWSC and TAWC; and (2) the regulatory correctness of the total amount generated by AWWSC before it is allocated. In summary, the Consumer Advocate is concerned about how much is allocated and how that amount is allocated to Tennessee.

Q. What is the Consumer Advocate's concern with the use of the Schumaker & Company Report to attempt to validate the allocation method used by AWWSC?

A. As the Consumer Advocate will discuss in more detail later, the Schumaker & Company Report notes that "cost allocation methodologies impacting TAWC are generally reasonable", but then points out the method

[55] TAWC Direct Testimony, Mr. Mike Miller, Exhibit MAM-10, Page 1 of 1.

used is a "simplification mechanism that is not necessarily based on cost-causative factors."[56] As discussed later, the TRA should not accept the overly "simple" method proposed by TAWC, but should adopt a more "cost-causative" approach it has used in other recent dockets involving Tennessee utilities.

Q. What is the Consumer Advocate's concern with the use of the Schumaker & Company Report to attempt to validate the total costs of AWWSC that are allocated to TAWC?

A. The Consumer Advocate believes that the TRA should not read too much into the Schumaker & Company Report. Upon examining the Schumaker & Company Report at Page 42, one will see that their analysis of total costs is based on a review of various studies performed by TAWC witness, Mr. Baryenbruch. Thus the real test for determining what is the proper costs to be allocated will be determined in this case, where Mr. Baryenbruch can be cross-examined, and are not from the Schumaker & Company Report. The Consumer Advocate wants to make clear that it is not finding fault with the Schumaker & Company Report on this point, but simply making the TRA aware that the Schumaker & Company Report did not have the scope to go into the various studies performed by Mr. Baryenbruch in as much detail as can be done in this docket.

In addition to various studies by Mr. Baryenbruch, the Schumaker & Company Report also referred to a "Service Company Cost Study" performed by Deloitte and Touche in 2009. This study compared the cost of certain services expected to be obtained by Illinois American Water Company ("IAWC") from AWWSC to the costs that would be incurred if such services were obtained in the open market.[57]

[56] Schumaker & Company, Affiliate Audit Report, August 2010, Finding II-2, Page 40.

[57] Schumaker & Company, Affiliate Audit Report, August 2010, Page 44.

However, the Illinois Commerce Commission, the regulatory body that ordered the report, found that the report did not have the information as requested and concluded as follows:

> However, IAWC did not provide the information specified above in this rate filing. With no basis for comparison of the lower of cost or market for these services, the Commission cannot adequately determine whether the increases in management fees proposed in this case by IAWC are just and reasonable. Thus the Commission agrees with AG's position on this issue and concludes that the Service Company Fees should be capped at 5% over the amount approved in the 07-0507 Order.[58]

Q. Has the Consumer Advocate reviewed the "Customer Based Cost Allocation Analysis" submitted on behalf of TAWC?

A. Yes. The "Customer Based Cost Allocation Analysis"[59] was provided by TAWC on December 28, 2010.

Q. Regarding the "Customer Based Cost Allocation Analysis" ("Analysis"), what are the Consumer Advocate's conclusions?

A. The Schumaker & Company Report of TAWC dated August 2010 has a finding that the cost allocation methodologies of AWWSC are not necessarily based on cost causative factors.[60] The Analysis, however, does not support the finding, instead it supports the concept of cost allocation based on the number of customers as "a rational and reasonable way to allocate."[61] The Analysis reasons that the number of customers is less

[58] Order dated April 13, 2010 Illinois Commerce Commission, Page 47, Docket No, 09319.
[59] TAWC response TN-CAPD-01-PART III-Q110-SUPPLEMENTAL ATTACHMENT.
[60] Schumaker & Company, Affiliate Audit Report, August 2010, Finding II-2, Page 40.
[61] TAWC response TN-CAPD-01-PART III-Q110-SUPPLEMENTAL ATTACHMENT, Page 5.

"volatile" than other cost allocation metrics. As a result, once the veneer is removed, the Analysis ends up with over 70% of the costs subject to allocation being allocated based on customers, i.e., business as usual.

The Consumer Advocate, however, believes that the weighting of cost allocation based on customers is too heavy and does not fully follow cost causative factors. Allocated costs from AWWSC are sometimes referred to as indirect costs. Indirect costs and their allocation are explained as follows:

> ....indirect costs include costs such as administrative and general costs, sometimes referred to as indirect overhead costs, and cannot be identified with a particular service or product. These indirect or "residual" costs which cannot be specifically attributed to a product, service or affiliate and for which there are no cost causative relationships, are typically accumulated or "pooled" and then allocated in the same ratio as all other costs are assigned or allocated (using a general allocator based on total company expenses). One method for allocating indirect costs would be to spread such costs using a general allocator based on how all operation and maintenance ("O&M") costs are assigned or allocated. Allocation of indirect costs, which have no readily identifiable cost causative relationships, on the basis of how all other costs have been allocated on a cost causative basis is a proxy or surrogate for allocating indirect costs on a cost causative basis. Some companies allocate indirect costs using multi-factor allocation formulas based on factor such as labor costs, plant investment or revenues.[62]

It is within this context, that the Consumer Advocate's allocation methodology as described later is developed.

Therefore, the Analysis and its related costs should be dismissed by

[62] COST ALLOCATION AND AFFILIATE TRANSACTIONS, A Survey and Analysis of State Cost Allocation issues and Transfer Pricing Policies, Robert L. Hahne, Bernard L. Uffelman, Michael Ambrosio, Kent Francois, June 1999, Pages 9-10.

the TRA and not borne by the ratepayers.

Q. What is the appropriate amount of Management Fees to be included for setting rates in this docket?

A. The Consumer Advocate recommends a Management Fee attrition year amount of $3.671 million[63] in this docket. This amount is consistent with the TRA's adopted methodology in Docket #08-00039.

Q. What amount of Management Fees is TAWC seeking in this docket?

A. TAWC is seeking $5.226 million.[64] In support of their amount, the Company has performed numerous mathematical gymnastics in an attempt to show that the increased Management Fee increases resulting from reorganization provided savings to the customers: (1) in TRA Docket #06-00290, the savings were calculated to be $(41,016)[65]; (2) in TRA Docket #08-00039, the savings were calculated to be $25,902[66]; and (3) in this docket, the savings are $1,229,864[67]. The $1.2 million amount was included in TAWC's Tennessee State Court of Appeal in TRA Docket #08-00039. With each numeric invention, the numbers and the assumptions used by the Company in their fruit basket comparisons cast doubt as to their veracity.

Q. Is the amount of Management Fees sought by TAWC in this docket just and reasonable for setting rates?

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[63] Terry Buckner work paper E-MANAGEMENT FEES SUMMARY, Index of work papers, Page 18.

[64] Direct Testimony of M. Miller, Page 40, Line 6.

[65] TRA Docket #06-00290, TAWC Rebuttal Testimony, Exhibit MAM-15, column (7). Page 1 of 2.

[66] TRA Docket #08-00039, TAWC Rebuttal Testimony, Exhibit MAM-10, column (7). Page 1 of 2.

[67] TAWC Direct Testimony, M. Miller, Exhibit MAM-11, column (11), Page 1 of 2.

A. No.

Q. Please provide an overview of why the Management Fees amount as proposed by TAWC is not just and reasonable for setting rates.

A. The reorganization of TAWC has been an expensive endeavor for its customers. Total service company charges were $98,876,416[68] in 2004, when AWWSC had 1,204[69] employees. Of that amount, TAWC incurred $2,129,911. At the end of 2009, AWWSC's total charges were $217,863,671[70] when AWWSC had 1,559[71] employees (1,642 at August 2009)[72]. Of the total AWWSC charges, TAWC incurred $4,881,682.[73] This comparison alone does not demonstrate efficiency or effectiveness. In fact, it is contrary to what should occur with economies of scale and business synergy. In fact, TAWC exhibit MAM-1, Page 1 of 2 reflects a simultaneous decline in TAWC's earnings with the reorganization of American Water.

The TAWC Management Fee amount is not just and reasonable because it includes costs unnecessary for the provision of water service, which includes the following: (1) It over-allocates charges to TAWC primarily based on non-cost causative factors; (2) It includes Annual Incentive Plan ("AIP") compensation, which is primarily based on financial goals; (3) It includes Stock Based Compensation Expense, also known as Long Term Incentive Plan ("LTIP") compensation; (4) It includes Business

[68] TAWC response TRA Docket #06-00290, TN-CAPD-01-PART II-Q018-ATTACHMENT, Page 1 of 18.
[69] TAWC response TN-CAPD-01-PART III-Q-35-SECOND SUPPLEMENTAL ATTACHMENT, Page 4 of 4.
[70] Schumaker & Company, Affiliate Audit Report, August 2010, Exhibit II-9, Page 24.
[71] TAWC response TN-CAPD-01-PART III-Q-35-ATTACHMENT, Page 4 of 4.
[72] Schumaker & Company, Affiliate Audit Report, August 2010, Page 19.
[73] Schumaker & Company, Affiliate Audit Report, August 2010, Exhibit II-9, Page 24.

Development expense, which is devoted to non-regulated operations[74]; (5) It includes External Affairs expense, which is devoted to marketing, advertising, lobbying, and political influence; (6) It includes non-recurring accounting charges for changes in financial reporting to the IRS; (7) It includes double counting and excessive growth for payroll increases; (8) It does not comport with current economic conditions; and (9) It includes non-normalized salaries. Consumer Advocate work paper E-TAWC MGMT FEES SUMMARY documents the amounts for each correction.

Q. Please explain how it over-allocates costs to TAWC.

A. As previously mentioned, the Schumaker & Company affiliate audit report of TAWC dated August 2010 has a finding that the cost allocation methodologies of AWWSC are not necessarily based on cost causative factors.[75] The Consumer Advocate agrees with the finding. Moreover, the AWWSC method of allocating costs using the number of customers has been described as a "relatively blunt" method of allocation.[76] Direct costs are caused through installing facilities, operating and maintaining facilities, and serving ratepayers. As a result, the Consumer Advocate believes an allocation factor should be applied to indirect costs based on direct cost causative factors through the use of equally weighted percentages of Plant in Service, Direct Operations and Maintenance Expense and Number of Customers. This is the same composite allocation methodology used by

[74] AWWSC Declaration of J. Young, PUC of California Docket #09-07-021, dated Oct. 7, 2009, Tier One Allocations, Page 10 of 15.

[75] Schumaker & Company, Affiliate Audit Report, August 2010, Finding II-2, Page 40.

[76] Overland Consulting, Regulatory Audit of California American Water Company, dated September 11, 2008, Page 2-18.

Atmos Energy Corporation.[77] Also, this allocation methodology was applied to Tennessee Wastewater Systems in TRA Docket #08-00202. Moreover, Chattanooga Gas Company uses a composite allocation factor for many of the services provided by its service company within Atlanta Gas Light. The Consumer Advocate's cost causative allocation factor is 1.87% of the regulated water companies[78], which is much lower than the 2.24% allocation factor for TAWC's test period ending March 2010. When the Consumer Advocate's regulated cost causative allocation factor is incorporated into the total regulated and non-regulated costs of AWWSC at September 2010, the resulting cost causative factor for TAWC is 1.76%.[79] The cost causative allocation methodology is even more relevant given that TAWC's plant additions could be deferred or delayed due to a lack of funding, i.e., if Company management deems that other jurisdictions receive the funding for plant additions over Tennessee, then those jurisdictions should pay its fair share of Management Fees.

Using the Consumer Advocate's allocation cost causative factor reduces TAWC's forecasted Management Fees by $1,060,971.[80]

Q. Please explain why the AIP amount is not just and reasonable.

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[77] TRA Docket #08-00197, MFR #57.
[78] Terry Buckner work paper E-MANAGEMENT FEES ALLOCATION, Index of work papers, Page 20.
[79] Terry Buckner work paper E-TAWC MGMT FEES ALLOC, Index of work papers, Page 21.
[80] Terry Buckner work paper E-TAWC MGMT FEES ALLOC1, Index of work papers, page 23.

A. The AIP was revised in 2009 and 2010. Within each annual AIP, 70%[81] of the compensation is based on financial metrics. The financial metrics are Diluted Earnings Per Share and Operating Cash Flow. AWWSC charges TAWC for AIP. Again, because there is no mechanism under the incentive plan for TAWC's ratepayers to share in these increased earnings, TAWC's employees and shareholders will reap all of the financial rewards of these higher earnings. Additionally, ratepayers are the sole source of TAWC's regulated earnings; therefore, the incentive plan is a circular one whose success is built into this docket, rewarding TAWC's employees and shareholders for merely increasing water rates charged to ratepayers. This is illustrated by the following: If TAWC's employees are successful in increasing the company's earnings, even to the point of earning above the authorized rate of return set by the TRA, TAWC will reward its employees for this effort through the AIP. In such a case, ratepayers would not only be unreasonably burdened by the over-earnings, but under TAWC's proposal, they also would have to pay an "over earnings surcharge" in the form of the AIP. The Consumer Advocate does not object if the company wants to reward its employees for increasing its earnings from regulated operations; however, the cost of these rewards should be charged to those that benefit from the AIP — the company's shareholders — not the ratepayers. For these reasons, there is no reasonable basis to charge this portion of the cost of the incentive plan to ratepayers, as these plan benefits will inure entirely to TAWC's employees and shareholders whereas the incentive plan's associated burdens will fall directly on ratepayers. In fact, TAWC paid out financial rewards to its salary employees in 2009 following the rate increase awarded to it in January 2009.

[81] 2009 and 2010 Annual Incentive Plan Highlight Brochure, Page 5.

Therefore, the Consumer Advocate believes a re-allocated $142,610[82] from AIP should be removed from TAWC's Management Fees amount. The Consumer Advocate's treatment of incentive payroll is in accord with established TRA precedent.[83]

Q. Please explain why the Stock Compensation Expense is not just and reasonable.

A. Again, the Stock Compensation Expense is to provide executive or director compensation based on the financial performance of American Water's stock price. There is no just and reasonable basis to charge this type of compensation to the ratepayers. Furthermore, Stock Compensation Expense was excluded by the Kentucky Public Service Commission.[84]

Therefore, the Consumer Advocate has removed a re-allocated $64,703[85] of Stock Compensation Expense from TAWC's Management Fees amount.

Q. Please explain why the Business Development Expense is not just and reasonable.

A. Business Development Expense is devoted primarily to non-regulated operations and is not specifically disclosed in the original affiliate agreement between TAWC and AWWSC. TAWC cited the Walden's Ridge revenues as a result of Business Development Expense.[86] However, Walden's Ridge was not included in regulated revenues until the TRA ordered TAWC to treat Walden's Ridge revenues consistently with the Signal Mountain

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[82] Terry Buckner work paper, E-TAWC MGMT FEE AIP, Index of work papers, Page 25.
[83] TRA Docket #06-00290, Order dated June 20, 2008, Page 24.
[84] *In re Kentucky-American Water Co.*, 2010 Case No. 2010-00036, December 14, 2010, Page 33.
[85] Terry Buckner work paper, E-TAWC MGMT FEE STOCK, Index of work papers, Page 29.
[86] TAWC response to City of Chattanooga DR #69.

revenues[87], i.e., regulated revenues. Furthermore, Business Development Expense was excluded by the Public Utilities Commission of the State of California[88] and the Kentucky Public Service Commission.[89]

Therefore, the Consumer Advocate has removed a re-allocated \$79,034[90] of Business Development Expense from TAWC's Management Fees amount.

Q. Please explain why the External Affairs Expense is not just and reasonable.

A. External Affairs Expense includes marketing, advertising, and government affairs. These activities are unnecessary in the provision of water service. Regulators have traditionally removed costs incurred to influence politicians or legislation. Also, marketing and advertising involving brand and reputation building, image building, and support for business development should not be included in the cost of service to ratepayers, because the monopolistic character of a water company makes these activities unnecessary.

Therefore, the Consumer Advocate has removed a re-allocated \$138,802[91] of External Affairs Expense from TAWC's Management Fees amount.

Q. Please explain why non-recurring accounting expense is not just and reasonable.

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[87] TRA Docket #08-00039, Order dated January 13, 2009, Page 11.

[88] *In re California-American Water Co.*, Decision 09-07-021, July 9, 2009, Page 102.

[89] *In re Kentucky-American Water Co.*, 2010 Case No. 2010-00036, December 14, 2010, Pages 39-41.

[90] Terry Buckner work paper, E-TAWC MGMT FEE BUS DEV, Index of work papers, Page 26.

[91] Terry Buckner work paper, E-TAWC MGMT FEE EXT AFF, Index of work papers, Page 24.

A. TAWC incurred an allocation of $27,978 in accounting expense due to an accounting change filed with the Internal Revenue Service ("IRS"). This amount is non-recurring and has not been properly normalized by TAWC. The accounting change has been partially approved by the IRS and has been incorporated in this docket.

Therefore, the Consumer Advocate has removed a non-recurring re-allocated accounting expense amount of $21,991[92] from TAWC's Management Fees amount.

Q. Please explain why double counting and excessive growth of payroll increases is not just and reasonable.

A. TAWC has increased their Management Fees amount for the test period ending March 2010 by an annual 3% growth factor through the attrition year. However, a portion of the payroll amount has already received a 2.5% increase effective January 1, 2010.[93] It is not just and reasonable to add a 3% increase on payroll for the test period ending March 2010, when the Management Fee payroll has already received an increase effective January 1, 2010. Also, if a 2.5% increase is appropriate for 2010, then a 2.5% increase is appropriate for the attrition year of 2011.

Therefore, the Consumer Advocate has removed a re-allocated $40,836[94] from TAWC's Management Fees amount consistent with annual payroll increase of 2.5% for years 2010 and 2011.

Q. Please explain how the growth rate for Management Fees does not comport with current economic conditions.

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[92] TAWC response to Consumer Advocate Discovery Request #108.

[93] Direct Testimony of Britton P. Ellis, Virginia State Corporation Commission, Page 27, Q22, Case No. PUE-2010-00001, dated September 24, 2010, E-TAWC MGMT FEE PAYROLL1.

[94] Terry Buckner work paper, E-TAWC MGMT FEE PAYROLL1, Index of work papers, Page 30.

A. Again, TAWC has increased their test period ending March 2010 by an annual 3% growth factor through the attrition year. However, the Consumer Advocate believes that an annual growth factor of 1.65% from March 2010 through the attrition year is more appropriate and consistent with the TRA Order in Docket No. 08-00039, given the current state of the economy.

Therefore, the Consumer Advocate has removed $150,728[95] from TAWC's Management Fees amount for the attrition year 2011.

Q. Please explain why non-normalized payroll is not just and reasonable.

A. AWWSC has fewer employees at September 2010 than December 31, 2009.[96] The functions of CSC and Finance have incurred the majority of the reductions in employees. Severance pay has been appropriately excluded from TAWC's Management Fee forecast, but not the payroll amount.

Therefore, the Consumer Advocate has removed a re-allocated $28,331[97] from TAWC's Management Fees amount for the attrition year 2011.

Q. Please summarize the net effect of the Consumer Advocate adjustments to TAWC's forecasted Management Fees.

A. The net effect of the Consumer Advocate adjustments results in a Management Fee forecasted amount of $3,515,578[98], which is slightly lower than the TRA methodology amount of $3,670,849 adopted in TRA Docket No. 08-00039 for the attrition year.

Q. Have Management Fees been an issue in other state jurisdictions?

A. Yes. Management Fees are known to have been an issue in California,

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[95] Terry Buckner work paper, E-TAWC MGMT FEE GDP, Index of work papers, Page 27.
[96] TAWC response to Consumer Advocate DR #35.
[97] Terry Buckner work paper, E-TAWC MGMT FEE PAYROLL2, Index of work papers, Page 31.
[98] Terry Buckner work paper, E-TAWC MGMT FEE SUMMARY, Index of work papers, Page 22.

Illinois, New Jersey, Ohio, and West Virginia.

In California, California American Water Company ("Cal-Am") proposed an increase of 51% for AWWSC management fees, from $5,532,550 authorized for 2006 to $8,357,126 for test year 2009. In its Order dated July 10, 2009, the Public Utilities Commission of the State of California states the following:

> Confronted with "seemingly endless" increases in administrative costs, the Commission has adopted the rate of customer growth as a guideline for evaluating proposed increases in Administrative and General Costs such as those proposed by Cal-Am in its General Office application. Although not an absolute cap, proposed increases that exceed the rate of customer growth must meet a "heavy burden" to demonstrate reasonableness. Inflation is often added in as well, resulting in inflation plus the rate of customer growth as the overall standard beginning point for analysis of this type of proposed increases.

In Illinois, the Illinois Commerce Commission ruled on April 13, 2010 that Illinois American Water Company's ("IAWC") Service Company Fees (i.e. Management Fees) should be capped at 5% over the amount approved in the 07-0507 Order. Also, the April 13, 2010 Order stated the following:

> The Commission points out that it does question whether IAWC is doing everything possible to be efficient in controlling its management fees to avoid passing unnecessary costs to ratepayers.

In New Jersey, as of the date of this testimony, a management audit is awaiting completion.

In Ohio, the Public Utilities Commission of Ohio ruled on June 23, 2010 that of the $4,060,453 in Management Fees sought by Ohio American Water Company, amounts of $962,568 and $499,435 should be excluded for setting rates. Moreover, the Staff of the Public Utilities Commission of Ohio stated in their report dated November 27, 2009 the following:

> Clearly the cost for support services, those services provided at regional and/or corporate sites, enjoyed an aggressive growth curve in relation to overall Ohio American Water O&M costs.

In West Virginia, the Public Service Commission of West Virginia ruled on March 25, 2009 that 50% of the 3% payroll increase in Management Fees would be allowed. Also, the March 25, 2009 Order stated the following:

> On March 28, 2008, the Company in *West Virginia American Water Company*, Case No. 07-0998-W-42T ("2007 Rate Case"), received a $14.5 million dollar rate increase pursuant to a settlement that all parties, including the Company, agreed was fair and reasonable. The Commission approved that settlement. On April 30, 2008, little more than a month after receiving the $14.5 million in additional revenue, the Company filed a notice of intent to file another rate case. On May 30, 2008, barely two months after receiving approval of that $14.5 million dollar rate increase settlement, the Company filed this rate case seeking an additional $14,755,000. It is that rate increase that we are now called upon to decide.
>
> One of the central arguments advanced by the Company in this proceeding is that, because of the way the Company is regulated (actually much the same as other utilities are regulated), it is difficult for the Company to meet revenue and rate of return expectations at the parent company level and in the "real world" financial

community.

Something, however, is sorely missing in the Company's testimony. That is the extent to which the Company made diligent efforts to live within the total revenues that resulted from the last rate case and to which the Company freely agreed. The Company, at the time of making its May 2008 filing had the impact of less than two months of the $14.5 million annual increment in revenues approved in the 2007 Rate Case when it filed this case.

It is difficult to believe that the Company, in generating another rate case within 60 days of its last rate order, gave meaningful contemplation and consideration to how it might operate differently in order to achieve its authorized rate of return or what efforts it might take to produce a reasonable financial performance within a budget that recognized the revenue limits of its last rate case. It would have been commendable if the Company had concluded that, while the 2008 settlement (the $14.5 million) was not everything that it had asked for, it was a reasonable settlement proposal that the Company had supported and to which it had agreed. Such an attitude should have led the Company management to plan for ways to live within its income rather than to plan for an immediate new rate increase request.

The Commission would like to have seen some acknowledgement of the possible need for belt tightening; some indication of possible deferral or reconsideration of capital projects; some effort to operate in a more conservative manner; some possible deferral of acquisitions; or some expressed understanding and concerns for the financial hardships facing its customers that were beginning to become evident in early 2008. These statements might have required the Company to attempt to lower its public profile, but the Company could also have expressed its concern that it must balance its historic spending patterns and the interests of its shareholders with the interests of its customers, employees, and the State of West Virginia. The Company

> could have acknowledged that its customers are having a tough time with their expenses, including the rates of the Company, and that the Company would be looking closely at its budget and operations to see if, for at least the next year or so, the (sic) it could live within the revenues generated by the last rate proceeding. It, instead, immediately filed another rate case.

Therefore, the concerns and the action of the TRA on this issue have not been unwarranted. The Management Fees of AWWSC have been and remain a concern across the regulatory landscape.

Q. Regarding the current AWWSC/TAWC affiliate agreement, what does the Consumer Advocate recommend?

A. While TAWC contends that the services provided in the 1989 agreement are "materially the same services", the Consumer Advocate agrees with Finding II-4 of the Schumaker & Company affiliate audit report that the current agreement is not sufficiently descriptive.

Therefore, the Consumer Advocate recommends that the TRA order AWWSC and TAWC to initiate a new affiliate agreement outlining the services to be provided, the basis for the services, the method of allocation, and the current organizational structure.

Q. Regarding the service company costs comparison with other utility organizations, what are the comments of the Consumer Advocate?

The Schumaker & Company affiliate audit report has an exhibit comparing the 2008 service company operating expenses per customer with other service company organizations.[99] Additionally, TAWC compares their cost per customer to the cost per customer for service companies reporting

[99] Schumaker & Company, Affiliate Audit Report, August 2010, Exhibit IV-15, Page 112.

to the Federal Energy Regulatory Commission ("FERC").[100]

The Consumer Advocate, however, does not believe that TAWC's service company comparisons are particularly meaningful just because they are easily accessible through FERC. For example, TAWC neglected to include Atmos Energy's ("Atmos") service company costs to Tennessee, which are about $39[101] per customer compared to $59[102] per customer for TAWC. Furthermore, Atmos has approximately 3.2[103] million meters in service at September 2010, which is equivalent to American Water's total customers. Atmos, however, is not required to identify its service company costs with FERC.

Q. **What are the primary issues with Pension Expense?**

A. Secondly, the Consumer Advocate used the actual capitalization rate for the twelve months ended December 31, 2008 of 20.57%, which is consistent with the level of TAWC's forecasted plant additions.

Therefore, the Consumer Advocate's forecasted Pension Expense of $1,552,412 is just and reasonable.

Q. **Please explain the difference in the calculation of Regulatory Expense.**

A. Regulatory Expense includes the following items: (1) Cost of Service studies; (2) Cost of Depreciation studies; and (3) Cost of Rate Case expenses. In its calculation of Regulatory Expense for the attrition year, the Consumer Advocate has included only the amortization of the cost of service studies performed in TRA Docket #06-00290[104] at $8,000 per year; and in

[100] TAWC Direct Testimony, P. Baryenbruch, Page 4 of 8, Lines14 and 15.
[101] TRA Docket #08-00197, MFR #43, March 2010 TRA 3.03 Surveillance Report.
[102] TAWC Direct Testimony, P. Baryenbruch, Exhibit IV-Question 1. Page 9.
[103] Atmos Form 10-K for the fiscal year ended September 30, 2010, Page 10.
[104] TRA Docket #06-00290, Direct Testimony, S. Miller, Page 12, Lines 1-3.

TRA Docket #08-00039 at $3,200[105] per year. The results of the cost of service study performed in this docket should not be adopted by the TRA or its related cost for setting rates. The cost of service study is discussed in Consumer Advocate witness, Mr. Hal Novak's direct testimony. Additionally, the Consumer Advocate has included the remaining amortization of the depreciation study in TRA Docket #08-00039 amounting to $7,826[106]. Finally, the Consumer Advocate has included the amortization of rate case costs sought by TAWC in TRA Docket #08-00039[107] at $68,750; and one half of the rate case costs sought at $107,500[108] per year in this docket, which is consistent with the TRA's Order in Docket No. 08-00039. The total of all the amortization amounts to $195,284 in Regulatory Expense for the attrition year.

Yet, TAWC now seeks to set rates on Regulatory Expense amounting to $379,918[109] per year. TAWC has included $65,579[110] in rate case amortization from TRA Docket No. 06-00290. The rates from that docket went into effect in May 2007. TAWC proposed, and the TRA adopted, a three year rate case amortization, which expired May 2010.[111] Much of the rate case costs incurred by TAWC are for the protection of its shareholders' interests and to the detriment of the ratepayers. TAWC recorded $2,766,525[112] in

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105 TRA Docket #08-00039, Direct Testimony, M. Miller, Page 20, Lines 21-22.
106 Terry Buckner work paper, RB-DEPR STUDY, Index of work papers, Page 94.
107 Terry Buckner work paper, RB-DEFERRED RATE CASE EXPENSE, Index of work papers, Page 93.
108 Ibid.
109 TAWC Direct Testimony, M. Miller, Page 53, Line 21.
110 TAWC response TN-TRA-02-Q92d-ATTACHMENT, Page 11 of 28.
111 TRA Docket #06-00290, Order dated June 20, 2008, Page 28.
112 TAWC response TN-CAPD-01-PART III-Q70-ATTACHMENT, Page 1 of 1, Line No. 17.

Regulatory Expense for the attrition year in the last docket, most of which was at the discretion of company management. TAWC should be more circumspect in their rate case expenditures because it is not indicative of a soundly managed utility. Finally, the Consumer Advocate would echo the following:

> We recommend the Commission require CalAm to organize rate filing and workpaper support in hierarchical fashion, with summarized rate filing information rolling up from more detailed work paper support. Quantitative information in the work papers should tie forward either to more summarized workpapers, or to tables in the rate filing. All rate filing schedules and workpapers should be referenced so that the source data, and the workpapers that contain detail tying forward to the schedules can be located. In other words, the filing and workpapers should contain referencing and cross-referencing and source identification that is standard in utility regulatory filings containing accounting data.[113]

The Consumer Advocate believes that a better documented rate filing by TAWC would lessen discovery issues with all the parties and the TRA.

Therefore, the TRA should reject TAWC's Regulatory Expense amount of $379,918 as unduly unjust and unreasonable to ratepayers for setting prospective rates, and adopt the Consumer Advocate's calculation of $195,284.

Q. What are the primary issues with Insurance Other than Group Expense?

A. The first primary difference between TAWC and the Consumer Advo-

[113] Overland Consulting Regulatory Audit of California American Water Company, dated September 11, 2008, Page 1-9.

cate is the lack of recognition by TAWC in its forecast for retrospective credits for workman's compensation claims. Also, this is one of the categories, which is significantly different due to the utilization of a test period by the Consumer Advocate. TAWC's forecasted amount "is based on the Company's 2010 actual insurance premiums and adjusted for inflationary increases for the attrition year."[114]

Therefore, the Consumer Advocate recommends that $322,262 be adopted by the TRA to take into account known and measurable changes.

Q. Please summarize the forecast differences in O&M expense.

A. TAWC attributes 41%[115] of their requested increase to O&M expense. TAWC's forecasted O&M of $23.6 million is 42%[116] higher than their forecasted amount of $16.7 million for the year ending 2005, which is a 7% annual growth rate. TAWC claims that O&M expenses have "increased <u>only</u> 2.5% per year on average"[117] over the last eight years. However, the 2.5% per year average is based on numerous exclusions.[118] The cumulative GDP growth rate over the same period is less than one third of TAWC's cumulative O&M growth rate.

Moreover, the Ohio Staff of the Public Service Commission of Ohio stated the following:

> Staff concludes that Ohio American Water needs to change it business model to better control costs and to better reflect economic conditions in the market it

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[114] TAWC Direct Testimony, S. Miller, Page 13, Lines 12-14.

[115] TAWC Direct Testimony, Exhibit MAM-2.

[116] Terry Buckner work paper, E-REC-1, Line 20, Column (5), Index of work papers, Page 1.

[117] TAWC Direct Testimony, J. Watson, Page 7, Lines 21-22.

[118] TAWC Direct Testimony, Exhibit MAM-4, Page 2 of 2, Note 1.

> serves....Staff believes that costs have reached a serious point at Ohio American where major processes need to be altered and institutional changes need to be implemented....No longer can Ohio American afford to absorb corporate costs at will.[119]

The Consumer Advocate has reached the same conclusions for TAWC. As a result, the Consumer Advocate's forecast of O&M amounts to $20.7 million, which is a 24% growth rate over the forecasted $16.7 million for the year ending 2005. This growth rate exceeds the cumulative GDP growth rate.

Some of this increase is related to the forecasted volumetric usage, which incurs more fuel & power and chemical costs. As previously mentioned, the Consumer Advocate capped these costs, which allowed the lost and unaccounted for water percentage not to exceed 15%.

Therefore, since TAWC's actual O&M growth rate exceeds any just and reasonable economic basis, the TRA should reject their O&M expense forecast.

DEPRECIATION EXPENSE

Q. Please explain the calculation of Consumer Advocate Depreciation and Amortization Expense.

A. TAWC has forecasted Depreciation and Amortization Expense of $4,877,687[120] for the attrition year. TAWC calculated Depreciation Expense by applying the current depreciation rates times a 13 month average of de-

[119] Ohio American Water Company, Case Number 09-391-WS-AIR, Pages 79-80.

[120] TAWC Exhibit No. 2, Schedule 4, Page 1 of 2, Line 13.

preciable property through the end of the attrition year. TAWC and the Consumer Advocate did not calculate depreciation expense on plant accounts having a book value of zero or less. Specifically, accounting for depreciation expense is "no more nor no less than the cost of the asset"[121]. Based on the depreciation rates approved in TRA Docket #08-00039, the Consumer Advocate calculated Depreciation and Amortization Expense of $4,703,804[122], which is $173,883 less than the projected depreciation expense of TAWC. The Consumer Advocate applied the current depreciation rates to the actual September 30, 2010 plant in service balances and the net monthly plant additions and retirements[123] by month through December 31, 2011.

Therefore, the Consumer Advocate recommends that $4,703,804 be adopted by the TRA for Depreciation and Amortization Expense.

TAXES OTHER THAN INCOME TAXES

Q. What are the significant differences from TAWC in Taxes Other Than Income for the forecasted attrition year?

A. The significant differences in Taxes Other Than Income for the attrition year are: (1) higher Gross Receipts Tax and State Franchise Tax in the Consumer Advocate forecast; and (2) lower TRA Fees, Property and Payroll Taxes in the Consumer Advocate forecast. The Consumer Advocate's Taxes Other Than Income amount is $273,813 lower than TAWC's forecasted

[121] *Public Utility Accounting: Theory and Application*, James E. Suelflow, Michigan State University Public Utilities Studies, P. 102.
[122] Terry Buckner work paper, E-DEP, Index of work papers, Page 53.
[123] TAWC response TRA DR #52 and Consumer Advocate DR #59.

amount.

Q. Please explain the Consumer Advocate's calculation of Gross Receipts Tax and State Franchise Tax.

A. In August of each tax year, TAWC pays a tax to the State of Tennessee on gross receipts for the tax year ending the following June 30, which is based on the gross receipts from TAWC's prior year ending December 31. Therefore, state gross receipts tax paid in August of 2010 will be based on gross receipts for the fiscal year ending December 31, 2009. This tax will be amortized from the period July 1, 2010 through June 30, 2011. The last half of the attrition year was based on actual gross receipts for the twelve months ending September 30, 2010. The Consumer Advocate's calculation of Gross Receipts Tax is $174,347 higher than TAWC's forecast and is predicated on a zero State Excise Tax amount. The State Franchise and Excise Taxes are deducted from the calculated Gross Receipts Tax using identical reporting periods. TAWC's 2009 State Franchise and Excise Tax return indicates an $8,179,643 Net Operating Loss ("NOL") from prior years.[124] The Company utilized $1,619,035 of the NOL. Therefore, there was zero State Excise Taxes due in 2009. TAWC, however, deducted $150,586[125] in estimated State Excise Taxes from its Gross Receipts Tax calculation.

The State Franchise Tax was calculated using forecasted plant in service and accumulated depreciation net of forecasted plant additions and retirements. This forecasting method appropriately matches the Gross Receipts Tax and State Franchise Tax years with the attrition period in this docket. The Consumer Advocate's forecasted State Franchise Tax is $13,565

[124] TAWC response TN-CAPD-01-PART III-Q-55-ATTACHMENT, Page 49 of 90.

higher than TAWC's forecasted amount.

Q. Please explain the Consumer Advocate's calculation of Property Taxes.

A. Consumer Advocate work paper T-OTAX1A provides the calculation of property taxes. The Consumer Advocate adopted the 2010 gross assessment for the attrition year 2011, even though Consumer Advocate work paper T-OTAX1 shows that TAWC's gross assessment has declined over the last two years. The current economic climate has contributed to the decline in property values. While the appraisal of public utility property can use two different approaches, the balance sheet approach and the income approach, it is largely a matter of judgment by the appraiser. Yet, the appraiser should not ignore current economic conditions. Consequently, municipalities must raise property tax rates to offset the decline in appraisal values of public utility property. The City of Chattanooga is one such municipality with this circumstance.

As a result, the Consumer Advocate took a ratio of 2009/2010 assessments times the 2009 taxes paid for the Georgia jurisdictional property and a ratio of 2009/2010 assessments times the current 2010 tax rates for Tennessee jurisdictional property.

TAWC, however, ignores the decline in assessments and uses the 2008 assessment amount times the new City of Chattanooga tax rate to forecast its attrition year property tax amount.

Therefore, the Consumer Advocate property tax amount of $2,572,725, which is $363,343 lower than TAWC's forecasted amount should be adopted by the TRA.

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[125] TAWC response TN-TRA-02-Q92f-ATTACHMENT, Page 7 of 9.

Q. Please explain the Consumer Advocate's calculation of Payroll Taxes.

A. Consumer Advocate work paper T-OTAX3 provides a comparative summary of the differences in the calculation of Payroll Taxes.

The work paper indicates lower payroll taxes of $52,369. In part, this variance is due to the differing capitalization rates as previously alluded to in the discussion of the O&M salaries and wages. The Consumer Advocate has performed empirical calculations on forecasted Tennessee employees for the test period ending September 2010, which averaged 104 employees. However, TAWC has 110[126] employees for their payroll tax calculation.

Therefore, the payroll tax calculation for TAWC is too high because of the differing employee levels, supporting documentation, and the capitalization rates and should be rejected by the TRA.

Q. Please compare the calculation of TRA Inspection Fee between the Consumer Advocate and TAWC.

A. Consumer Advocate work paper T-OTAX2 provides the Consumer Advocate's calculation, which uses the revenues and uncollectible expense for the twelve months ended September 30, 2010. In large part, the difference in the two forecasted amounts is due to TAWC forecasting much higher revenues for 2010.[127] TAWC's forecasted 2010 revenues are higher than their forecasted attrition year revenues at present rates.

Therefore, the Consumer Advocate's TRA Inspection Fee amount properly matches known and measurable revenues with the current TRA Inspection Fee rates and should be adopted by the TRA.

[126] TAWC Direct Testimony of J. Watson, Page 21, Question 24, Line 15.

RATE BASE

Q. Please explain the difference in forecasted Plant in Service.

A. The Consumer Advocate forecasted plant in service by using actual plant balances as of September 30, 2010. Forecasted plant additions and retirements, which were provided by TAWC itself, were then added to actual balances at September 30, 2010 to arrive at monthly plant in service amounts through December 31, 2011. A thirteen month plant in service average was calculated in the amount of $225,496,162.[128]

TAWC has forecasted $226,384,490[129] for plant in service.

The Consumer Advocate's attrition year forecast of plant in service is $888,328[130] lower than the TAWC's forecasted amount due to the utilization of a more recent test period balance.

Q. Please explain the difference in Construction Work in Progress ("CWIP").

A. The Consumer Advocate forecasted CWIP using a thirteen month average based on the balance of $5,889,966 at September 30, 2010 and forecasted capital spending and plant additions by TAWC.

As a result of using a later test period, the Consumer Advocate's attrition year forecast of CWIP is $1,520,103[131] lower than the TAWC forecasted

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[127] TAWC response TN-TRA-02-Q92f-ATTACHMENT, Page 6 of 9.
[128] Terry Buckner work papers, AMENDED RB-PLANT, Index of work papers, Page 86.
[129] TAWC Exhibit No. 1, Schedule 2, Page 3 of 3, Line 62.
[130] Amended Consumer Advocate Exhibit, Schedule 2, Line 1.
[131] Amended Consumer Advocate Exhibit, Schedule 2, Line 2.

amount.

Q. Please explain the difference in Working Capital Requirement.

A. TAWC has included the following items in their calculation of Working Capital Requirement: Prepaid Taxes; Materials & Supplies; Deferred Regulatory Expenses; Unamortized Debt Expense; Other Deferred Debits; Lead/Lag Study; and less Incidental Collections. TAWC used a thirteen month average for the test year ended March 2010 to calculate Prepaid Taxes, and Materials and Supplies for the attrition year ending December 2011. The Consumer Advocate included thirteen month averages for each using the test period ended September 2010.

Regarding the Deferred Regulatory Expenses, the Consumer Advocate has forecasted $310,734,[132] while TAWC has forecasted $630,897[133] for a difference of $320,163. The difference is primarily due to the level of rate case costs submitted by TAWC in a previous TRA docket, which were approved, and the actual costs TAWC claims it incurred for the rate cases.

Again, the TRA should reject TAWC's Deferred Regulatory Expense amount of $630,897 as unduly unjust and unreasonable to ratepayers for setting prospective rates. TAWC should not profit from the inclusion in rate base of their excessive regulatory expenses.

TAWC performed a new Lead/Lag study for this case. The Consumer Advocate believes that a payment lag for the current portions of state excise tax and federal income tax should be calculated on the basis of the statutory payment requirements of a calendar year's liability paid in four equal installments on April 15, June 15, September 15, and December 15. On this basis, a

[132] Terry Buckner work paper, RB-DEFERRED REGULATORY EXPENSE, Index of work papers, page 92.

[133] TAWC response TRA-01-Q013-WORKING CAPITAL, Page 36 of 56.

lag of approximately 37 days is calculated.[134]

Using the Consumer Advocate's forecasted revenue, expenses, and Lead/Lag changes, the Lead/Lag Study amount is $714,285.[135] The Consumer Advocate did not thoroughly examine each and every Lead/Lag as offered by TAWC and its silence at this date should not be construed as agreement.

Therefore, the Consumer Advocate's forecasted Working Capital Requirement is $176,761 lower than the forecasted TAWC amount.

Q. Please explain the difference in forecasted Accumulated Depreciation.

A. The Consumer Advocate forecasted Accumulated Depreciation by using actual balances as of September 30, 2010. Forecasted monthly depreciation expense and retirements were then added to actual balances at September 30, 2010 to arrive at monthly Accumulated Depreciation amounts through December 31, 2011. A thirteen month Accumulated Depreciation average was calculated for the attrition year Accumulated Depreciation in the amount of $73,137,622,[136] which is $559,578[137] greater than TAWC.

Q. Please explain the difference in Accumulated Deferred Income Tax.

A. The Consumer Advocate forecasted Accumulated Deferred Income Tax by using actual book balances as of September 30, 2010 and their projected balances through December 31, 2011. The incremental change for the attrition year resulted from the projected tax depreciation less the book de-

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[134] *Accounting for Public Utilities,* Hahne & Aliff § 5.04[4], Page 5-25.

[135] Terry Buckner work paper, AMENDED RB-CWC, Index of work papers, page 91.

[136] Terry Buckner work paper, RB-ACCUMULATED DEPRECIATION, Index of work papers, Page 101.

[137] Amended Consumer Advocate Exhibit, Schedule 2, Line 8.

preciation times the statutory state and federal tax rates. Forecasted temporary differences were spread evenly from the starting point to the end of the attrition year. A thirteen month average was then calculated for the attrition year, which is consistent with the methodology used for all primary rate base categories. In this docket, tax depreciation in excess of book depreciation is the only component of Accumulated Deferred Income Taxes generating deferred tax differences. As a result, the Consumer Advocate forecasts Accumulated Deferred Income Tax in the amount of $25,288,933,[138] which is $8,135,118[139] higher than the forecasted amount of TAWC.

TAWC has utilized a rather maverick approach to calculating its Accumulated Deferred Income Taxes. In this docket, their approach completely ignores the book balances for Accumulated Deferred Income Taxes and has limited the temporary differences to accelerated depreciation on post 1980 assets. Apparently, their approach is some vague response to the language within the TRA's Order in Docket #08-00039.[140]

Q. **Did the Consumer Advocate include Statement of Financial Accounting Standard ("SFAS") 109 assets and liabilities in its calculation of Accumulated Deferred Taxes, and why?**

A. Yes. SFAS 109 was effective for fiscal years beginning after December 15, 1992.[141] SFAS 109 superseded SFAS 96 and APB No. 11 adopting a balance sheet approach for measuring deferred tax liabilities and assets using the enacted tax rates. A deferred tax liability is recognized for "temporary differ-

[138] Terry Buckner work paper, AMENDED RB-ADIT, Index of work papers, page 104.
[139] Amended Consumer Advocate Exhibit, Schedule 2, Line 10.
[140] TRA Order dated January 13, 2009, TRA Docket #08-00039, Page 44.
[141] AICPA, Accounting for Deferred Income Taxes: SFAS No. 109/FIN48, Page 1-21.

ences" that will result in taxable amounts in future years. The term "temporary differences" replaced the term "timing differences" used in APB 11. A deferred tax asset is recognized for temporary differences that will result in deductible amounts in future years and for carryforwards. SFAS 109 requires financial statement disclosure of deferred tax liabilities and deferred tax assets. In the 2008 audit report of TAWC's external auditors, SFAS 109 financial statement disclosure is provided.[142] However, in the 2009 audit report, SFAS 109 financial statement disclosure is not provided.

The Consumer Advocate has included the net SFAS 109 assets and liabilities in the rate base calculation because they represent a source of funds that are cost free by the U. S. Treasury in support of rate base investment.

Q. Did the Consumer Advocate include the FIN 48 amount in its calculation of Accumulated Deferred Taxes, and why?

A. Yes. FIN 48 is an interpretation issued in June 2006 to clarify the accounting for uncertain tax positions under SFAS 109. TAWC has set aside an amount in compliance with FIN 48 due to their accounting change to expense small units of property formerly capitalized for tax purposes. The accounting change was partially approved in October 2009 with the Company receiving final approval in February 2010. "In addition, the change in tax accounting method generated a net operating loss which the Company has substantially monetized."[143] At December 2009, the FIN amount was $1.852 million.[144] SFAS 109 requires that interest and penalties must also be recognized on FIN 48 amounts and must be recognized in the financial state-

[142] TAWC response TRA-01-Q005-ATTACHMENT 2, page 20 of 25.
[143] TAWC response TRA-01-Q005-ATTACHMENT 3, page 20 of 26.
[144] Ibid.

ments. TAWC, however, has not accrued any interest or penalties related to income tax matters such as FIN 48.[145] "Interest must be accrued on any amount recorded as a liability under FIN 48 at the rates imposed by the relevant taxing authorities on tax underpayments. In addition, where appropriate, any applicable penalties must be accrued."[146] The statute of limitations on a portion of this amount will begin to expire in 2010.[147]

While uncertainty remains about the final disposition of the FIN 48 amounts with the IRS, the Consumer Advocate recommends that the FIN 48 amount be included as a deduction from rate base. Conversely, TAWC has excluded the FIN 48 amount for setting rates in this docket.

Given TAWC's propensity for bi-annual rate filings, if a portion of the FIN 48 amount reverses, then the TRA can take corrective action on the amount in the next docket.

Q. Please discuss SFAS 71 assets and liabilities.

A. While the overall objective of SFAS 109 is to recognize the future tax consequences of events that have been recognized between the financial statements and tax returns, the SFAS 71 goal is to recognize the future inflows and outflows that result from the rate-making process for regulated companies when compared to financial reporting. Temporary differences occur under SFAS 71, which create regulated assets and regulated liabilities. For example, financial reporting for pension expense is subject to SFAS 87, but in Tennessee pension expense is based on cash contributions to the pension plan. Consequently, an amount is recorded for the temporary differ-

[145] TAWC response TRA-01-Q005-ATTACHMENT 3, page 21 of 26.
[146] KAWC, Case No. 2010-00036, Rebuttal testimony of Mr. James I Warren, page 34, Lines 2-4.
[147] TAWC response TRA-01-Q005-ATTACHMENT 3, Page 21 of 26.

ence between regulated accounting and financial accounting. The regulatory assets and liabilities under SFAS 71 are typically not included in the calculation of rate base. In an attempt to capture all of the SFAS 109 regulatory assets and liabilities in TRA Docket #08-00039, the Consumer Advocate mistakenly included SFAS 71 amounts in its calculation of rate base.

Additionally, TAWC,

> ....has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the Commission of full normalization for rate-making purposes. The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between state and federal income tax rates under prior law and the current statutory rates, reversed over the average remaining lives of the related assets.[148]

It is this regulatory asset which TAWC has failed to demonstrate and document when the tax effects of the temporary difference to customers has reversed over the lives of the related assets. Moreover, TAWC has failed to show the Orders of the TRA or its predecessor the PSC authorizing the establishment of a regulatory asset.

Q. Please summarize the calculation of Rate Base amounts for the attrition year.

A. With the recognition of TAWC's forecasting errors, the use of a more

[148] TAWC response TRA-01-Q005-ATTACHMENT 3, Page 17 of 26.

recent test period, and the inclusion of FIN 48 amounts, the forecasted net rate base of the Consumer Advocate is $10.6 million lower than the rate base amount submitted by TAWC for the period ended December 31, 2011.

CONCLUSIONS REGARDING REVENUE REQUIREMENTS

Q. Please summarize the comparison of the forecasts of TAWC and Consumer Advocate.

A. TAWC is asking the TRA for a 26% to 28% or $9.984 million[149] increase for most of their tariffed rates. According to TAWC, the primary reasons for the increase are: (1) Increased Rate Base; (2) Increased Operation and Maintenance Expenses; (3) Increased Cost of Capital and (4) Declining growth in Revenues.[150] As previously discussed, the Consumer Advocate forecast takes issue with TAWC's forecast of Revenues, Operation and Maintenance Expenses, Rate Base, and TAWC's Cost of Capital (See Dr. Chris Klein's direct testimony).

Therefore, the Consumer Advocate asks the TRA to adopt its forecast and deny TAWC's forecast as unjust and unreasonable for the ratepayers.

Q. What is TAWC currently earning?

A. The September 2010 TRA 3.06 surveillance report for TAWC indicates a 4.24%[151] rate of return for the twelve months ended September 2010. For TAWC's test period ending March 2010 in this docket, the March 2010 TRA 3.06 surveillance report for TAWC indicates a 4.29% rate of return. It is the

[149] TAWC direct testimony, M. Miller, direct testimony, Page 2, Lines 12-13.
[150] TAWC direct testimony, M. Miller direct testimony, Exhibit MAM-2.

Consumer Advocate's contention that TAWC's reported return is prospectively understated due to non-recurring Operations and Maintenance Expenses, understated Accumulated Deferred Taxes and excessive Management Fees.

Q. What is the history of rate increases for TAWC?

A. In TRA Docket #03-00118, the 2003 rate filing of TAWC, the TRA authorized a revenue increase of $2,745,274. This increase resulted in an average rate increase of 9.48% for water service. In TRA Docket #04-00288, the TRA authorized a .93% increase in tariffed rates amounting to $297,005. In TRA Docket #06-00290, the TRA authorized a revenue increase of $4,079,865[152], which resulted in a 13% increase. In docket #08-00039, TAWC requested an additional revenue increase of $7,644,859, the TRA authorized a revenue increase of $1,655,541 or 4.37% for most customers.

Q. What about TAWC's inability to achieve the 10.20% Return on Equity ("ROE") authorized by the TRA in Docket No. 08-00039?

A. TAWC wrongly blames the TRA for its inability to achieve the 10.20% ROE as authorized by the TRA in Docket No. 08-00039.[153] TAWC complains about the imposition of the double leverage capital structure, which is a long-standing regulatory practice in Tennessee. Further, TAWC complains about disallowing the cost to process a rate request when it incurs $2.7 million in regulatory cost for the attrition year ended August 2009. In fact, if the TRA had granted the entire request of TAWC, TAWC would still

[151] Page 2, Line 42.
[152] TRA Docket #06-00290, Order dated June 10, 2008, Page 51.
[153] TAWC Direct Testimony, M. Miller, Pages 8 and 9.

not have achieved a 10.20% ROE for the attrition year. This fact is exacerbated when the delay and deferrals of plant additions during the attrition year are considered. Moreover, only one American Water Company earned an ROE above 10% in 2009.[154] The source of TAWC'S inability to achieve a 10.20% ROE is found in their mirror. A faulty cost of service structure is the main source of TAWC's inability to achieve a just and reasonable rate of return. American Water concedes as much with their admission of "inefficiencies, workarounds, and rework" as a basis for their business transformation initiative.[155] Ironically, American Water boasts to investors that its Earnings Per Share ("EPS") growth has surpassed Water, Gas and Electric Peers.[156]

Q. Please summarize TAWC's petition for a rate increase in this docket.

A. TAWC's petition for a rate increase would be onerous on Chattanoogans; it would outstrip inflation and it is not supported by the faulty cost structure of TAWC or the economic environment in which the company operates. TAWC claims that its "customers are receiving water at a great value."

However, it is the Consumer Advocate's contention in this docket that the customers should not have to pay more because recent history indicates that TAWC is unable to operate within their own budgets. TAWC's current earnings are not due to a lack of revenues, but are due to excessive and unwarranted spending. Finally, continuance of large price increases in water rates will stunt usage and revenue growth.[157]

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[154] TAWC response TN-CAPD-SUPPLEMTAL-Q126-ATTACHMENT, Page 1 of 1.
[155] American Water 2009 Form 10-K, Page 33.
[156] Institutional Investor Meetings, August 2010, Page 6.
[157] American Water 2009 Form 10-K, Page 45.

Q. Did the Consumer Advocate review TRA Discovery Request #109 to TAWC in this docket?

A. Yes. The request describes what is generally known as a "decoupling mechanism" and then requests TAWC to state a position as to whether it supports the implementation of such a mechanism. TAWC did not request a decoupling mechanism in its petition.

Q. Did the TRA issue a similar discovery request to the Consumer Advocate in this docket?

A. Yes. The Consumer Advocate stated its opposition to the implementation of a decoupling mechanism.

Q. What is a decoupling mechanism?

A. A decoupling mechanism is a "tracker" or true-up mechanism, which insures, in this docket, a water utility with a fixed level of revenues regardless of customer's volumetric water usage. At the end of a period, revenue per customer would be trued-up with the actual revenues per customer collected by TAWC during the period. Ratepayers would be responsible for any short-fall in revenues due to economic or business reason on a per customer basis.

Q. What are the Consumer Advocate's concerns regarding the implementation of a decoupling mechanism?

A. The Consumer Advocate has several concerns. Current rate base regulation affords the utility an "opportunity" to earn a just and reasonable rate of return. A decoupling mechanism "guarantees" a utility a fixed level of revenue with ratepayers acting as an insurer for a substantial amount of business risk. Revenues can fall for many economic reasons. By placing the ratepayers of Chattanooga in the role of acting as an insurer of TAWC's revenues, TAWC would be immune to all manner of economic risks that formerly affected revenues. In my opinion, a decoupling mechanism can further erode the incentive of a utility to control its operating costs.

Q. Are decoupling mechanisms widespread among water utilities?

A. No. California has recently implemented decoupling for water utilities in concert with utility sponsored and ratepayer funded water conservation programs. Obviously, California has a large population with many different types of commerce and limited water resources.

Q. What would be the effect of a decoupling mechanism on TAWC's ratepayers?

A. Ratepayers would be paying more for less volumetric usage. The burden of any true-ups would apply equally to all ratepayers even though some consumers are actively conserving water.

Q. Does the Consumer Advocate believe that now is the appropriate time to consider implementing a decoupling mechanism for TAWC?

A. No. Shifting the burden of risk to ratepayers is not good public policy, especially in light of the current economic conditions. This was noted by the Connecticut Department of Public Utility Control in 2010 in rejecting a decoupling mechanism for a water utility:

> Quite simply, now is not the appropriate time for the Company to propose implementing a revenue adjustment mechanism such as the WCAM on the Company's ratepayers, whom the Company has readily

acknowledged are facing difficult and uncertain times.[158]

Q. What other options does the TRA have in considering the encouragement of water conservation in this docket?

A. The Consumer Advocate believes that the TRA should consider water conservation in the context of TAWC's level of unaccounted for water, which has not improved since the last rate case. Any gains ratepayers make in using less water is seemingly erased when the level of unaccounted for water increases. While the level of unaccounted for water increases for TAWC, Kentucky American Water Company's unaccounted for water loss averaged 13.51% for the three years ended December 2008 and the current water loss percentage is 11.8%.[159] The Kentucky Public Service Commission recognized this as a significant achievement and applauded Kentucky American's efforts.[160]

RATE DESIGN

Q. Please discuss TAWC's proposed rate design.

A. TAWC state that the average water bill will change by the following percent increases and decreases for residential customers: Chattanooga, 28.16%; Lookout Mountain, 21.79%; Lakeview, 37.32%; Lone Oak, -9.20%; and Suck Creek, -12.41%[161].

The Consumer Advocate proposes that any change in revenue requirements ordered by the TRA in this docket be spread uniformly to all cus-

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[158] *Re: Connecticut Water Company,* Docket No. 09-12-11, Order of the Connecticut Department of Public Utility Control (July 13, 2010), 283 P.U.R. 4th 217, 2010 WL 2801007*76.

[159] Kentucky American Water Company, Case No. 2010-00036 Order dated December 14, 2010, Pages 34-35.

[160] Ibid.

[161] TAWC response TN-TRA-01-Q023-ATTACHMENT.

tomer classes and all customer locations. This approach would assure that the benefits or burdens created by any rate adjustment in this case are shared proportionately by all customers. This rate design is a long-standing recommendation and could be described as a "default position" of the Consumer Advocate in rate cases such as this one.

Q. Does this conclude your testimony?

A. Yes.

IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF TENNESSEE AMERICAN	)	
WATER COMPANY TO CHANGE AND	)	
INCREASE CERTAIN RATES AND	)	DOCKET NO. 10-00189
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	)	

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CONSUMER ADVOCATE EXHIBITS AMENDMENT

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January 28, 2011

Tennessee-American Water Company
Index to Schedules
For the 12 Months Ending December 31, 2011

Tennessee-American Water Company
Revenue Deficiency
For the 12 Months Ending December 31, 2011

Line No.		Consumer Advocate		TAWC		Difference
1	Rate Base	114,967,598	A/	125,472,973	A/	(10,505,375)
2	Operating Income at Present Rates	7,195,510	B/	4,547,326	B/	2,648,184
3	Earned Rate of Return (Line 2/Line 1)	6.26%		3.62%		2.63%
4	Cost of Capital	6.79%	C/	8.380%	E/	-1.59%
5	Required Operating Income (Line 1*Line 4)	7,808,479		10,514,635		(2,706,157)
6	Operating Income Deficiency (Line 5-Line 2)	612,968		5,967,309		(5,354,341)
7	Gross Revenue Conversion Factor	1.643047	D/	1.67319346	E/	(0.030146)
8	Revenue Deficiency (Line 6*Line 7)	1,007,136		9,984,463		(8,977,327)

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

TRA Docket #10-00189
Amended Consumer Advocate Exhibit
Schedule 2
1/28/2011 15:40

Tennessee-American Water Company
Comparative Rate Base
For the 12 Months Ending December 31, 2011

Exhibit 1, Page 2 of 9

Line No.		Consumer Advocate B/	TAWC A/	Difference
1	Utility Plant in Service	**225,496,162**	226,384,490	(888,328)
2	Construction Work in Progress	**2,681,318**	4,201,421	(1,520,103)
3	Utility Plant Capital Lease	**1,590,500**	1,590,500	-
4	Limited-Term Utility Plant - Net	-	-	-
5	Working Capital	834,497	1,011,258	(176,761)
6	Def. Maint.	-	-	-
7	Total Additions	230,602,477	233,187,669	(2,585,192)
8	Accumulated Depreciation	**73,137,622**	72,578,044	559,578
9	Accumulated Amort. of Utility Capital Lease	**1,387,268**	1,387,269	(1)
10	Accumulated Deferred Income Taxes	**25,288,933**	17,153,815	8,135,118
11	Customer Advances for Construction	**5,786,757**	6,383,603	(596,846)
12	Contributions In Aid of Construction	**9,932,550**	10,131,112	(198,562)
13	Unamortized Investment Tax Credit	**26,899**	26,899	-
14	Utility Plant Acquisition Adj.	**74,850**	53,954	20,896
15	Total Deductions	115,634,879	107,714,696	7,920,183
16	Rate Base	114,967,598	125,472,973	(10,505,375)

A/ TAWC Exhibit 1, Sch. 2
B/ Consumer Advocate work papers.

Tennessee-American Water Company
Income Statement at Current Rates
For the 12 Months Ending December 31, 2011

Line No.		Consumer Advocate		TAWC		Difference
1	Operating Revenues	38,399,479		37,296,455	A/	1,103,024
2	Operations and Maintenance Expense	20,796,612	B/	23,679,011	B/	(2,882,399)
3	Depreciation and Amortization Expense	4,703,804	I/	4,877,687	C/	(173,883)
4	Taxes Other Than Income	4,126,459	D/	4,400,272	G/	(273,813)
5	State Excise Tax	307,801	E/	12,999	H/	294,802
6	Federal Income Tax	1,473,293	E/	(16,840)	H/	1,490,133
7	Total Operating Expense	31,407,969		32,953,129		(1,545,160)
8	AFUDC	204,000	F/	204,000	F/	-
9	Net Operating Income for Return	7,195,510		4,547,326		2,648,184

A/ TAWC Exhibit 2, Sch. 2
B/ Schedule 5
C/ TAWC Exhibit 2, Sch. 1
D/ Schedule 6
E/ Schedule 7
F/ TAWC Exhibit 2, Sch. 3
G/ TAWC Exhibit 2, Sch. 1
H/ TAWC Exhibit 2, Sch. 6
I/ Consumer Advocate work paper E-DEP

Tennessee-American Water Company
Income Statement at Proposed Rates
For the 12 Months Ending December 31, 2011

Line No.		Current Rates	A/	Adjustments	C/	Proposed Rates
1	Operating Revenues	38,090,878		1,007,136		39,098,014
2	Forfeited Discount Revenues	308,601	B/	8,158		316,759
3	Total Revenues	38,399,479		1,015,294		39,414,773
4	Operations and Maintenance Expense	20,796,612		6,707		20,803,319
5	Depreciation and Amortization Expense	4,703,804				4,703,804
6	Taxes Other Than Income	4,126,459				4,126,459
7	State Excise Tax	307,801		65,558		373,359
8	Federal Income Tax	1,473,293		330,060		1,803,353
9	Total Operating Expense	31,407,969				31,810,294
10	AFUDC	204,000				204,000
11	Net Operating Income for Return	7,195,510				7,808,479

A/ Schedule 3
B/ 12 MTD September 2010.
C/ Schedule 1, Line 8 x appropriate factor from Schedule 8

Tennessee-American Water Company
Operation & Maintenance Expenses
For the 12 Months Ending December 31, 2011

Line No.		Consumer Advocate A/	TAWC B/	Difference
1	Salaries and Wages	4,915,111	5,680,299	(765,188)
2	Purchased Water	47,657	50,962	(3,305)
3	Fuel and Power	2,410,868	2,511,238	(100,370)
4	Chemicals	930,961	1,069,369	(138,408)
5	Waste Disposal	172,151	197,386	(25,235)
6	Management Fees	3,670,849	5,226,034	(1,555,185)
7	Group Insurance	2,165,261	2,034,757	130,504
8	Pensions	1,552,412	1,645,113	(92,701)
9	Regulatory Expense	195,284	379,918	(184,634)
10	Insurance Other Than Group	321,913	485,904	(163,991)
11	Customer Accounting	840,475	857,278	(16,803)
12	Uncollectible Expense	250,290	198,122	52,168
13	Rents	8,436	8,706	(270)
14	General Office Expense	218,213	217,933	280
15	Miscellaneous Expense	1,954,046	2,005,675	(51,629)
16	Other Maintenance Expense	1,142,685	1,110,317	32,368
17	Total O&M Expense	20,796,612	23,679,011	(2,882,399)

A/ Terry Buckner work papers
B/ TAWC Exhibit 2, Sch. 3

Tennessee-American Water Company
Taxes Other Than Income Taxes
For the 12 Months Ending December 31, 2011

Exhibit 1, Page 6 of 9

Line No.		Consumer Advocate		TAWC	D/	Difference
1	Other General Taxes	-		-		-
2	Gross Receipts Tax	704,308	A/	529,961		174,347
3	TRA Inspection Fee	71,766		117,779		(46,013)
4	Property Taxes	2,572,725	B/	2,936,068		(363,343)
5	Franchise Tax	391,255		377,690		13,565
6	FICA Taxes	370,627	C/	421,089		(50,462)
7	Unemployment Taxes	15,778	C/	17,685		(1,907)
8	Total Taxes Other Than Income Taxes	4,126,459		4,400,272		(273,813)

A/ Terry Buckner work paper T-OTAX2.
B/ Terry Buckner work paper T-OTAX1.
C/ Terry Buckner work paper T-OTAX3.
D/ TAWC Exhibit 2, Sch. 5, TAWC response TN-TRA-02-Q92f-ATTACHMENT, Pages 1 through 9.

Tennessee-American Water Company
Excise and Income Taxes
For the 12 Months Ending December 31, 2011

Line No.		Attrition Amount A/	
1	Operating Revenues	38,399,479	B/
2	Salaries and Wages	4,915,111	
3	Purchased Water	47,657	
4	Fuel and Power	2,410,868	
5	Chemicals	930,961	
6	Waste Disposal	172,151	
7	Service Company Charges	3,670,849	
8	Group Insurance	2,165,261	
9	Pensions	1,552,412	
10	Regulatory Expense	195,284	
11	Insurance Other Than Group	321,913	
12	Customer Accounting	840,475	
13	Uncollectible Expense	250,290	
14	Rents	8,436	
15	General Office Expense	218,213	
16	Miscellaneous Expense	1,954,046	
17	Other Maintenance Expense	1,142,685	
18	Depreciation and Amortization Expense	4,703,804	
19	Taxes Other Than Income	4,126,459	
20	NOI Before Excise and Income Taxes	8,772,604	
21	AFUDC	204,000	
22	Interest Expense	(4,248,162)	C/
23	Pre-tax Book Income	4,728,442	
24	Schedule M Adjustments	**6,961**	D/
25	Excise Taxable Income	4,735,403	
26	Excise Tax Rate	6.50%	
27	Excise Tax Payable	307,801	
28	Excise Tax NOL	-	
29	Excise Tax Expense	307,801	
30	Pre-tax Book Income	4,728,442	
31	Preferred Dividend Credit	-	
32	Excise Tax	(307,801)	
33	Schedule M Adjustments	6,961	D/
34	FIT Taxable Income	4,427,602	
35	FIT Rate	35.00%	
36	Federal Income Tax Payable	1,549,661	
37	ITC Amortization	**(76,368)**	E/
38	Federal Income Tax NOL	-	
39	Federal Income Tax Expense	1,473,293	

A/ Schedule 5
B/ Schedule 4
C/ Schedule 1, line 1 * Weighted Cost of Debt per Schedule 9
D/ TAWC Exhibit No. 2, Schedule 7, Line 36.
E/ TAWC Exhibit No. 2, Schedule 7, Line 11.

Tennessee-American Water Company
Revenue Conversion Factor
For the 12 Months Ending December 31, 2011

Line No.		Amount		Balance
1	Operating Revenues			1.000000
2	Add: Forfeited Discounts	0.0081	A/	0.008100
3	Balance			1.008100
4	Uncollectible Ratio	0.0066	B/	0.006660
5	Balance			1.001440
6	State Excise Tax	0.0650	C/	0.065094
7	Balance			0.936347
8	Federal Income Tax	0.3500	C/	0.327721
9	Balance			0.608625
10	Revenue Conversion Factor (Line 1 / Line 11)			1.643047

A/ 12 MTD 9/30/10 ($308,601/$38,139,091)
B/ 12 MTD 9/30/10 ($250,290/$37.886,523)
C/ Statutory Rate

Tennessee-American Water Company
Cost of Capital
For the 12 Months Ending December 31, 2011

Exhibit 1, Page 9 of 9

Line No.	Final Capital Structure	Ratio	Cost	Weighted Cost	Tax Deductible
1	Short Term Debt	6.45%	1.20%	0.077%	0.077%
2	Long Term Debt	48.71%	6.20%	3.020%	3.020%
3	Preferred Stock	1.24%	5.00%	0.06%	
4	Common Equity	43.60%			
5	Parent Short Term Debt	0.43%	1.20%	0.005%	0.005%
6	Parent Long Term Debt	9.45%	6.27%	0.59%	0.593%
7	Parent Common Equity	33.72%	9.00%	3.03%	
8	Total	100.00%		6.79%	3.695%

Source: Consumer Advocate Exhibit Dr. Chris Klein.

IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF TENNESSEE AMERICAN	)	
WATER COMPANY TO CHANGE AND	)	
INCREASE CERTAIN RATES AND	)	**DOCKET NO. 10-00189**
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	)	

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TERRY BUCKNER WORK PAPERS AMENDMENT

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January 28, 2011

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
OPERATING EXPENSE RECONCILIATION SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 31, 2011

AMENDED E-REC-1
01/28/11
03:29 PM

Line #		A/ (1) COMPANY TRA DOCKET #04-00288 12/31/05	A/ (2) COMPANY TRA DOCKET #06-00290 6/30/06	A/ (3) COMPANY TRA DOCKET #08-00039 11/30/2007	A/ (4) COMPANY TRA DOCKET #08-00039 ATTRITION YR	A/ (5) COMPANY TRA DOCKET #10-00189 ATTRITION YR	(6) EMPLOYEE POSITIONS	(7) 15% CAP ON UNACCOUNTED	(8) GROWTH	(9) TEST PERIOD	(10) INCENTIVE PAY PLAN	(11) CAP PERCENTS	(12) B/ CAPD AMOUNT	(13) DIFFERENCE
1	O&M LABOR	$ 4,383,883	$ 4,001,878	$ 4,641,460	$ 5,058,987	$ 5,680,299	$ 430,231		$ (76)		$ 102,648	$ 232,385	$ 4,915,111	$ 765,188
2	PURCHASED WATER	15,330	52,331	58,216	52,110	50,962			3,464	$ (159)			47,657	3,305
3	FUEL AND POWER	1,755,680	1,819,430	2,274,868	1,922,043	2,511,238		$ 281,343	(47,403)	(133,570)			2,410,868	100,370
4	CHEMICALS	861,861	933,913	1,075,171	1,559,222	1,069,369		108,641	(122,525)	152,292			930,961	138,408
5	WASTE DISPOSAL	133,438	143,948	161,721	179,088	197,386			11,044	14,191			172,151	25,235
6	MANAGEMENT FEES	3,062,940	4,006,278	4,789,601	4,335,190	5,226,034			1,637,587	(82,402)			3,670,849	1,555,185
7	GROUP INSURANCE	1,386,004	1,543,022	1,596,405	1,714,550	2,034,757			(192,942)	62,438			2,165,261	(130,504)
8	PENSIONS	892,790	699,154	726,428	1,161,108	1,645,113			-	-		92,701	1,552,412	92,701
9	REGULATORY EXPENSE	58,000	292,095	508,129	543,384	379,918			184,634	-			195,284	184,634
10	INSURANCE OTHER THAN GROUP	657,000	530,011	559,655	583,492	485,904			77,786	86,205			321,913	163,991
11	CUSTOMER ACCOUNTING	572,893	585,288	704,362	738,845	857,278			6,023	10,780			840,475	16,803
12	UNCOLLECTIBLE EXPENSE	289,530	616,171	417,277	417,756	198,122			(52,168)	-			250,290	(52,168)
13	RENTS	38,286	38,043	30,037	11,336	8,706			-	270			8,436	270
14	GENERAL OFFICE EXPENSE	193,122	575,179	244,966	245,926	217,933			7,229	(7,509)			218,213	(280)
15	MISCELLANEOUS EXPENSE	1,661,970	1,798,639	1,931,046	2,018,623	2,005,675			69,276	(17,647)			1,954,046	51,629
16	OTHER MAINTENANCE EXPENSE	746,632	1,110,461	1,211,604	936,345	1,110,317			51,915	(84,283)			1,142,685	(32,368)
17	AFUDC	(28,791)	(193,631)	(110,499)	(463,690)	(204,000)							(204,000)	-
18	TOTAL	$ 16,680,568	$ 18,552,210	$ 20,820,447	$ 21,014,315	$ 23,475,011	$ 430,231	$ 389,984	$ 1,633,844	$ 606	$ 102,648	$ 325,086	$ 20,592,612	2,882,399
19	PERCENT CHANGE		11.22%	24.82%	0.93%	11.71%							23.45%	
20	CUMULATIVE CHANGE EXCLUDING AFUDC		12.19%	25.26%	28.54%	41.71%							24.46%	

A/ Company Exhibit No 2, Schedule 3, Page 1 of 1 plus amounts per TRA data request #1, dated 7/29/08.
B/ Terry Buckner work papers.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
PURCHASED WATER EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-PW

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS	B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
510100	PURCHASED WATER-OUTSIDE	**46,999**	**446**	**211**	**47,657**
	Total	**46,999**	**446**	**211**	**47,657**

A/ Per TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
WASTE DISPOSAL EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-WASTE

ACCOUNT #	DESCRIPTION	A/ 9/30/10 AMOUNTS	B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
511100	WASTE DISPOSAL	169,774	1,613	764	172,151
	Total	169,774	1,613	764	172,151

A/ TAWC response to Consumer Advocate 1st Discovery Request #31.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
GROUP INSURANCE EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-GI

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS	B/ INFLATION FACTOR	C/ GROWTH FACTOR	D/ ATTR YR AMOUNTS
504100	GROUP INSURANCE	948,465			1,118,530
505100	PBOP	1,032,278	9,807	4,645	1,046,730
	Total	**1,980,743**	**9,807**	**4,645**	**2,165,261**

A/ TAWC response to Consumer Advocate DR #64.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.
D/ Terry Buckner work paper E-GIA

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
OTHER INSURANCE EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-OI

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS	B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
557000	INSURANCE GENERAL LIABILITY	132,918	1,263	598	134,779
558000	INSURANCE WORKMAN'S COMP	145,291	1,380	654	147,325
559000	INSURANCE OTHER	39,259	373	177	39,809
	Total	317,468	3,016	1,429	321,913

A/ TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
CUSTOMER ACCOUNTING EXPENSE SUMMARY — **AMENDED E-CA**
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS		B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
520100	MATERIALS & SUPPLIES	1,215		12	5	1,232
575743	MISCELLANEOUS OPERATING EXPENSE	0		0	0	0
575000	MISCELLANEOUS OPERATING EXPENSE	(8)		(0)	(0)	(8)
575100	BANK SERVICE CHARGES	262,765		2,496	1,182	266,444
575200	COLLECTION AGENCIES	94,276		896	424	95,596
575320	ELECTRICITY	0		0	0	0
575500	JANITORIAL	0		0	0	0
575620	OFFICE & ADMINISTRATION SUPPLIES	7		0	0	7
575660	POSTAGE	348,144	D/	3,307	1,567	353,018
575740	TELEPHONE	0		0	0	0
575820	UNIFORMS	2,019		19	9	2,048
534000	CONTRACT SERV. MGMT FEE CUST. ACCT.	0		0	0	0
575420	FORMS	113,556		1,079	511	115,146
575743	CELL PHONE	6,896		66	31	6,992
	Total	828,871		7,874	3,730	840,475

A/ TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST TREND, one half of .89% billing growth.
D/ TAWC response to Consumer Advocate DR #50, plus normalizing adjustment of $3,809.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
GENERAL OFFICE EXPENSE SUMMARY **AMENDED E-GO**
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

ACCOUNT #	DESCRIPTION	A/ 9/30/10 AMOUNTS		B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
520100	MATERIALS & SUPPLIES	2,704		26	12	2,742
575670	RELOCATION EXPENSES	0		0	0	0
575002	COLLECTION AGENCIES	35		0	0	35
575100	BANK SERVICE CHARGES	51		0	0	52
575260	CREDIT LINE FEES	699		7	3	709
575280	DUES/MEMBERSHIPS DEDUCTIBLE	1,812	D/	17	8	1,837
575281	DUES/MEMBERSHIPS NON-DEDUCTIBLE	0		0	0	0
575320	ELECTRICITY	27,861		265	125	28,251
575340	EMPLOYEE EXPENSES	26,779		254	121	27,154
575351	MEALS & TRAVEL NON-DEDUCTIBLE	8,173		78	37	8,287
575881	MISC. CHARGES/SUBSCRIPTIONS	0		0	0	0
575480	HEAT - OIL/GAS	3,456		33	16	3,504
575500	JANITORIAL	5,432	E/	52	24	5,509
575620	OFFICE & ADMINISTRATION	18,136		172	82	18,390
575660	POSTAGE	3,119		30	14	3,163
575740	TELEPHONE	30,813		293	139	31,245
575780	TRASH REMOVAL	0		0	0	0
575830	WATER & WASTE WATER	7,567		72	34	7,673
575350	MEALS & TRAVEL DEDUCTIBLE	8,173		78	37	8,287
575342	EMPLOYEE EXPENSES CONF/REGISTR.	4,915		47	22	4,984
575741	CELL PHONE	38,835		369	175	39,379
575261	CREDIT LINE FEES	26,640		253	120	27,013
575880	MISC. CHARGES	0		0	0	0
	Total	**215,200**		**2,044**	**968**	**218,213**

A/ TAWC response to Consumer Advocate DR #51 and TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ Terry Buckner work paper R-CUST GROWTH, one half of .89% billing growth.
D/ TAWC response to Consumer Advocate DR #51, plus normalizing adjustments of ($969) and $889.
E/ TAWC response to Consumer Advocate DR #51, plus normalizing adjustment of $449.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
MISCELLANEOUS EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-MISC

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS		B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS	
504500	OTHER WELFARE EXPENSE	857		8	4	869	
504610	EMPLOYEE AWARDS	9,792		93	44	9,930	
504620	EMPLOYEE PHYSICAL EXAMS	3,393		32	15	3,441	
504660	TUITION AID	22,068		210	99	22,377	
504670	TRAINING	5,742		55	26	5,823	
507100	401 K	100,203		952	451	101,606	
508100	ESOP/508101-508102/508200	103,090		979	464	104,533	
520100	MATERIALS & SUPPLIES	117,618		1,117	529	119,264	
532000	CONTRACT SERVICES - ACC/AUDIT	71,574		680	322	72,576	
533000	CONTRACT SERVICES - LEGAL	47,111		448	212	47,770	
550002	LEASE FUEL	0		0	0	0	
531000	CONTRACT SERVICES - ENGINEERING	0		0	0	0	
535000	CONTRACT SERVICES - OTHER	320,168	E/	3,042	1,441	324,650	
535001	CONTRACT SERVICES - TEMP EMP	30,162		0	136	0	
536000	CONTRACT SERVICES - LAB TESTING	0		0	0	0	
550000	TRANSPORTATION	4,561		43	21	4,625	
550001	TRANSPORTATION LEASE COST	10,370		99	47	10,515	
550002	TRANSPORTATION LEASE FUEL	201,197		1,911	905	204,013	
550003	TRANSPORTATION LEASE MAINT	145,778		1,385	656	147,819	
550004	TRANSPORTATION EMPLOYEE REIMB.	(2,083)		(20)	(9)	(2,112)	
556000	INSURANCE VEHICLE	28,496		271	128	28,895	
575000	MISCELLANEOUS OPERATING EXP	149,322		1,419	672	189,412	D/
575030	ADVERTISING	9,277	F	88	42	9,407	
575220	COMMUNITY RELATIONS	10,815		103	49	10,967	
575240	COMPANY DUES/DEDUCTIBLE	16,017	G/	152	72	16,242	
575241	COMPANY DUES/NON-DEDUCTIBLE	0		0	0	0	
575242	COMPANY DUES/DEDUCTIBLE AWWA	18,117		172	82	18,371	
575270	DIRECTORS FEES	11,600		110	52	11,762	
575271	DIRECTORS EXPENSES	0		0	0	0	
575320	ELECTRICITY	69,061		656	311	70,028	
575480	HEAT - OIL/GAS	15,964		152	72	16,187	
575490	INJURIES & DAMAGES	100		1	0	101	

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
MISCELLANEOUS EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-MISC

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS		B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
575500	JANITORIAL	16,297	H/	155	73	16,526
575545	LAB SUPPLIES	33,523		318	151	33,993
575560	LOBBYING EXPENSES	340		0	2	0
575620	OFFICE & ADMINISTRATION	5,432		52	24	5,508
575625	OVERNIGHT SHIPPING	1,874		18	8	1,900
575680	RESEARCH & DEVELOPMENT	11,596		110	52	11,759
575740	TELEPHONE	40,638		386	183	41,207
575780	TRASH REMOVAL	4,793		46	22	4,860
575790	TRUSTEE FEES	2,770		26	12	2,808
575820	UNIFORMS	4,588		44	21	4,652
575998	PURCHASING CARD	25		0	0	26
575400	BUSINESS SERVICES PROJECT EXP.	134,872		1,281	607	136,760
575710	SECURITY SERVICE	145,428		1,382	654	147,464
575715	SOFTWARE LICENSES & SUPPORT	4,174		40	19	4,232
575460	GROUNDS KEEPING	0		0	0	0
575640	PENALTIES NON-DEDUCTIBLE	20,230		0	91	0
575741	CELL PHONE/575743	0		0	0	0
575275	DISCOUNTS AVAILABLE	(7,587)		(72)	(34)	(7,693)
575276	DISCOUNTS LOST	26		0	0	27
575130	BROCHURES AND HANDOUTS	936		9	4	949
	Total	1,940,324		17,951	8,731	1,954,046

A/ TAWC response to Consumer Advocate DR #52 and TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.
D/ TAWC response to Consumer Advocate DR #52, annual amortization (5Yrs) amount of Management Audit Expense of $38,000.
E/ TAWC response to Consumer Advocate DR #52, normalizing adjustment of $1,235.
F/ TAWC response to Consumer Advocate DR #52, normalizing adjustment of ($14,930).
G/ TAWC response to Consumer Advocate DR #52, normalizing adjustment of ($3,938).
H/ TAWC response to Consumer Advocate DR #52, normalizing adjustments of $898 and $449.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
OTHER MAINTENANCE EXPENSE SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 2011

AMENDED E-MAINT

ACCOUNT #	DESCRIPTION	A/ 12 MTD 9/30/10 AMOUNTS	B/ INFLATION FACTOR	C/ GROWTH FACTOR	ATTR YR AMOUNTS
620000	MAINTENANCE	533,879	5,072	2,402	541,353
635000	CONTRACT SERVICE - OTHER	13,553	129	61	13,743
675000	MISCELLANEOUS MAINTENANCE	88,215	838	397	89,450
675250	COMPUTER EQUIPMENT	134	1	1	136
675450	OFFICE EQUIPMENT	435	4	2	441
675650	PAVING	490,692	4,662	2,208	497,562
	Total	1,126,909	10,706	5,071	1,142,685

A/ TAWC Income Statements.
B/ Terry Buckner work paper E-GDP, .95% for 15 months growth.
C/ John Hughes work paper R-CUST GROWTH, one half of .89% billing growth.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
DEPRECIATION EXPENSE/NET PLANT IN SERVICE
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 31, 2011

AMENDED RB-PLANT

	Jan-11	Feb-11	Mar-11	Apr-11	May-11	Jun-11	Jul-11	Aug-11	Sep-11	Oct-11	Nov-11	Dec-11
304100 Struct & Imp SS	49,449	49,449	49,449	49,449	49,449	49,449	49,449	49,449	49,449	49,449	49,449	49,449
304200 Struct & Imp P	4,500,332	4,500,332	4,500,332	4,500,332	4,500,332	4,500,332	4,500,332	4,537,335	4,537,335	4,537,335	4,537,335	4,537,335
304300 Struct & Imp WT	7,267,400	7,274,900	7,276,400	7,300,400	7,302,400	7,316,400	7,318,400	7,322,100	7,349,050	7,386,350	7,420,350	7,510,508
304301 Struct & Imp WT Depr Pntng	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808	1,694,808
304310 Struct & Imp Treatment Handling	69,055	69,055	69,055	69,055	69,055	69,055	69,055	69,055	69,055	69,055	69,055	69,055
304400 Struct & Imp TD	517,881	517,881	517,881	517,881	517,881	517,881	517,881	517,881	517,881	517,881	517,881	517,881
304500 Struct & Imp AG	252,388	252,388	252,388	252,388	252,388	252,388	252,388	252,388	252,388	252,388	252,388	252,388
304600 Struct & Imp Offices	142,380	142,380	142,380	142,380	142,380	142,380	142,380	142,380	142,380	142,380	142,380	142,380
304700 Struct & Imp Store,Shop,Gar	312,642	312,642	312,642	312,642	312,642	312,642	312,642	312,642	312,642	312,642	312,642	312,642
304800 Struct & Imp Misc	654,998	654,998	654,998	654,998	654,998	654,998	654,998	654,998	654,998	654,998	654,998	654,998
306000 Lake, River & Other Intakes	489,123	489,123	489,123	489,123	489,123	489,123	489,123	489,123	489,123	489,123	489,123	489,123
309000 Supply Mains	603,834	603,834	603,834	603,834	603,834	603,834	603,834	603,834	603,834	603,834	603,834	603,834
310000 Power Generation Equip	227,422	227,422	227,422	227,422	227,422	227,422	227,422	227,422	227,422	227,422	227,422	227,422
311200 Pump Equip Electric	5,730,120	5,730,120	5,728,470	5,728,470	5,728,470	5,751,470	5,766,059	5,777,918	5,791,918	5,810,718	5,867,070	5,882,050
311300 Pump Equip Diesel	119,296	119,296	119,296	119,296	119,296	119,296	119,296	119,296	119,296	119,296	119,296	119,296
311500 Pump Equip Other	251,454	251,454	251,454	251,454	251,454	251,454	251,454	251,454	251,454	251,454	251,454	251,454
311520 Pumping Equipment SS	202,837	202,837	202,837	202,837	202,837	202,837	202,837	202,837	202,837	202,837	202,837	202,837
320100 WT Equip Non-Media	12,595,054	12,595,054	12,595,054	12,595,054	12,595,054	12,595,054	12,595,054	12,595,054	12,601,578	12,601,578	12,601,578	12,601,578
320200 WT Equip Filter Media	350,872	350,872	350,872	350,872	350,872	350,872	350,872	350,872	350,872	350,872	350,872	350,872
330000 Dist Reservoirs & Standpipes	6,669,924	6,669,924	6,669,924	6,669,924	6,669,924	6,669,924	6,669,924	6,669,924	6,669,924	6,844,924	6,844,924	6,844,924
330003 Dist Res & Stand Orig Repaint	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221	3,477,221
330100 Elevated Tanks & Standpipes	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254	1,900,254
330200 Ground Level Tanks	2,571	2,571	2,571	2,571	2,571	2,571	2,571	2,571	2,571	2,571	2,571	2,571
330300 Below Ground Tanks	18,648	18,648	18,648	18,648	18,648	18,648	18,648	18,648	18,648	18,648	18,648	18,648
330400 Clearwell	680,784	680,784	680,784	680,784	680,784	680,784	680,784	680,784	680,784	680,784	680,784	680,784
331001 TD Mains Not Classified by Siz	1,981,852	1,981,852	1,981,852	1,981,852	1,981,852	1,981,852	1,981,852	1,981,852	1,981,852	2,076,306	2,311,306	2,311,306
331100 TD Mains 4in & Less	5,455,492	5,449,869	5,448,307	5,458,565	5,454,565	5,452,715	5,447,365	5,446,365	5,470,204	5,451,954	5,426,599	5,414,334
331200 TD Mains 6in to 8in	1,458	1,458	1,458	1,458	1,458	1,458	1,458	1,458	1,458	1,458	1,458	1,458
331210 TD Mains 6in to 10in (TN)	65,988,214	66,102,955	66,236,461	66,477,147	66,543,573	66,805,351	67,085,282	67,371,827	67,582,508	67,854,542	68,225,487	68,511,321
331300 TD Mains 10in to 16in	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243	9,816,243
331350 TD Mains 12in & Grtr (TN)	25,676,273	25,674,273	25,674,273	25,922,673	25,982,652	26,163,300	26,428,300	26,428,300	26,443,845	26,500,964	26,555,840	26,631,076
331400 TD Mains 18in & Grtr	651,994	651,994	651,994	651,994	651,994	651,994	651,994	651,994	651,994	651,994	651,994	651,994
333000 Services	22,132,021	22,188,269	22,278,209	22,336,376	22,416,774	22,563,982	22,684,471	22,815,392	22,905,067	23,034,429	23,153,546	23,245,594
334100 Meters	4,695,346	4,716,346	4,761,346	4,804,958	4,832,758	4,891,258	4,918,654	4,946,054	5,017,254	5,057,654	5,105,154	5,179,154
334110 Meters Bronze Case	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588	3,668,588
334130 Meters Other	8,534	8,534	8,534	8,534	8,534	8,534	8,534	8,534	8,534	8,534	8,534	8,534
334131 Meters Other-Rem Rdr Unts	17,907	17,907	17,907	17,907	17,907	17,907	17,907	17,907	17,907	17,907	17,907	17,907
334200 Meter Installations	11,374,730	11,412,330	11,471,330	11,518,942	11,547,542	11,614,042	11,644,198	11,674,198	11,747,198	11,834,698	11,883,098	11,948,098
335000 Hydrants	8,242,019	8,269,954	8,289,045	8,324,780	8,350,580	8,431,180	8,479,830	8,505,169	8,547,819	8,574,319	8,589,673	8,621,773
339200 Other P/E SS	8,526	8,526	8,526	8,526	8,526	8,526	8,526	8,526	8,526	8,526	8,526	8,526
339600 Other P/E CPS	294,153	294,153	294,153	294,153	294,153	294,153	294,153	294,153	294,153	294,153	294,153	294,153
340100 Office Furniture & Equip	551,397	551,397	551,397	554,641	559,141	563,641	570,704	570,704	574,704	576,230	583,732	591,756
340200 Comp & Periph Equip	213,139	213,139	236,139	277,139	307,139	345,139	350,139	373,289	368,289	393,089	393,089	394,789
340210 Comp & Periph Mainframe	603,486	603,486	603,486	603,486	603,486	603,486	603,486	603,486	603,486	603,486	603,486	603,486
340220 Comp & Periph Personal	365,705	365,705	365,705	365,705	365,705	365,705	373,305	373,305	373,305	373,305	382,267	389,531
340230 Comp & Periph Other	284,736	284,736	284,736	284,736	284,736	284,736	284,736	284,736	284,736	284,736	284,736	284,736
340240 Comp & Periph Capital Lease	22,168	22,168	22,168	22,168	22,168	22,168	22,168	22,168	22,168	22,168	22,168	22,168
340300 Computer Software	430,569	430,569	430,569	430,569	430,569	430,569	430,569	430,569	430,569	434,569	434,305	437,561
340310 Comp Software Mainframe	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059	3,535,059
340320 Comp Software Personal	177,213	177,213	177,213	177,213	177,213	177,213	177,213	177,213	177,213	177,213	177,213	177,213
340330 Comp Software Other	14,222	14,222	14,222	14,222	14,222	14,222	14,222	14,222	14,222	14,222	14,222	14,222
340400 Data Handling Equipment	15,284	15,284	15,284	15,284	15,284	15,284	15,284	15,284	15,284	15,284	15,284	15,284
340500 Other Office Equipment	55,208	55,208	55,208	55,208	55,208	55,208	55,208	55,208	55,208	55,208	55,208	55,208
341100 Trans Equip Lt Duty Trks	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,224,479	1,261,579
341200 Trans Equip Hvy Duty Trks	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,127,023	1,361,823
341300 Trans Equip Autos	255,106	255,106	255,106	255,106	255,106	255,106	255,106	255,106	255,106	255,106	255,106	361,826
341400 Trans Equip Other	456,305	456,305	456,305	456,305	456,305	456,305	456,305	456,305	456,305	456,305	456,305	456,305
342000 Stores Equipment	43,392	43,392	43,392	43,392	43,392	43,392	43,392	43,392	43,392	43,392	43,392	43,392
343000 Tools,Shop,Garage Equip	1,273,050	1,273,050	1,273,050	1,273,050	1,280,250	1,287,290	1,293,290	1,302,290	1,312,850	1,322,694	1,338,694	1,360,894
344000 Laboratory Equipment	402,388	402,388	402,388	402,388	414,388	414,388	416,888	419,888	419,888	422,388	422,388	422,388
345000 Power Operated Equipment	287,053	287,053	287,053	287,053	287,053	287,053	287,053	287,053	287,053	287,053	287,053	287,053
346100 Comm Equip Non-Telephone	351,790	351,790	351,790	351,790	351,790	351,790	351,790	351,790	351,790	351,790	351,790	351,790
346190 Remote Control & Instrumentatl	174,974	174,974	174,974	174,974	174,974	174,974	174,974	174,974	174,974	174,974	174,974	174,974
346200 Comm Equip Telephone	90,325	90,325	90,325	90,325	90,325	90,325	90,325	90,325	90,325	90,325	90,325	90,325
347000 Misc Equipment	1,109,383	1,109,383	1,109,383	1,109,383	1,109,383	1,109,383	1,109,383	1,109,383	1,109,383	1,115,067	1,115,067	1,115,067
348000 Other Tangible Property	4,918	4,918	4,918	4,918	4,918	4,918	4,918	4,918	4,918	4,918	4,918	4,918
Land											250,000	250,000
Total	221,862,470	222,119,871	222,487,696	223,240,410	223,581,113	224,461,037	225,272,061	225,858,978	226,442,602	227,411,175	228,647,564	229,787,719
13 Month Average												224,823,729
											Land	672,433
											Total	225,496,162

A/ TRA Docket #08-00039, Consumer Advocate Exhibit, Charles W, King, Schedule 3.
B/ TAWC response to Consumer Advocate DR #59, page 2 of 2.

AMENDED RB-WORKING CAPITAL REQUIREMENT

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
WORKING CAPITAL REQUIREMENT SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 31, 2011

Item	Consumer Advocate Amount		H/ TAWC Amount	Difference
Prepaid Taxes	414,322	A/	284,235	130,087
Materials & Supplies	215,798	B/	254,110	(38,312)
Deferred Regulatory Expense	310,734	C/	630,897	(320,163)
Unamortized Debt Expense	460,842	D/	460,845	(3)
Other Deferred Debits	280,997	E/	280,983	14
Lead/Lag Study	714,285	F/	663,000	51,285
Total	$ 2,396,978		$ 2,574,070	$ (177,092)
Less:				
Incidental Collections	1,562,481	G/	1,562,812	(331)
Net Working Capital Requirement	$ 834,497		$ 1,011,258	$ (176,761)

A/ Terry Buckner work paper, RB-PREPAID TAXES.
B/ Terry Buckner work paper, RB-M&S.
C/ Terry Buckner work paper, RB-DEFERRED REGULATORY EXPENSE.
D/ Terry Buckner work paper, RB-UNAMORTIZED DEBT EXPENSE.
E/ Terry Buckner work paper, RB-OTHER DEFERRED DEBITS.
F/ Terry Buckner work paper, RB-CWC.
G/ Terry Buckner work paper, RB-INCIDENTAL COLLECTIONS.
H/ TAWC Exhibit No. 1, Schedule 3.

AMENDED RB-CWC

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
LEAD/LAG STUDY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 31, 2011

LINE NO.	DESCRIPTION	ATTRITION YEAR	LEAD/ LAG DAYS	DOLLAR DAYS
1	Revenues less private fire	$ 36,876,934	14.74	$ 543,566,007
2	Private Fire billed in advance	1,522,545	(45.63)	(69,473,728)
3	Total	$ 38,399,479	41.73	$ 474,092,279
4	Payroll Charged to Expense - Hourly	3,484,760	17.08	59,519,703
5	Payroll Charged to Expense - Salary	1,430,351	17.08	24,430,392
6	Purchased Water	47,657	36.44	1,736,621
7	Fuel and Power	2,410,868	28.04	67,600,739
8	Chemicals	930,961	23.64	22,007,918
9	Waste Disposal	172,151	73.61	12,672,035
10	AWWS Charges	3,670,849	(11.97)	(43,940,063)
11	Group Insurance	1,118,530	(13.63)	(15,245,564)
12	OPEBs	1,046,730	(1.63)	(1,706,170)
13	Pensions	1,552,412	(1.63)	(2,530,432)
14	Insurance Other Than Group	321,913	(40.00)	(12,876,520)
15	Rents	8,436	(33.42)	(281,931)
16	Maintenance Expense	1,142,685	21.74	24,841,872
17	Regulatory Expense	195,284	76.64	14,966,566
18	Uncollectibles	250,290	-	-
19	Other Operating and Maintenance Expenses	2,808,735	34.05	95,637,429
20	Depreciation	4,703,804	-	-
21	Payroll Taxes	386,405	15.79	6,101,335
22	Property Taxes	2,572,725	241.00	620,026,725
23	Franchise Taxes	391,255	37.50	14,672,063
24	Gross Receipts Tax	704,308	47.74	33,623,664
25	Utility Tax	71,766	267.00	19,161,522
26	Current Federal Income Tax	817,143	37.00	30,234,308
27	Current State Excise Tax	174,633	37.00	6,461,421
28	Deferred Income Taxes	789,324	-	-
29	Interest Expense	4,248,162	85.08	361,433,623
30	Preferred Dividends	69,010	45.63	3,148,926
31	Net Earnings	2,878,332		
	Total Operating Funds	$ 38,399,479	$ 34.94	$ 1,341,696,282
32	Net Lead (Lag) Days		6.790	
33	Average Daily Operating Expenses			$ 105,204
34	CWC Required for Operating Expenses			$ 714,285

Source: Consumer Advocate work papers, TAWC Exhibit 1, Schedule 3, Page 3 of 6.

OFFICE OF THE ATTORNEY GENERAL - STATE OF TENNESSEE
CONSUMER ADVOCATE AND PROTECTION DIVISION
ACCUMULATED DEFERRED INCOME TAX SUMMARY
TENNESSEE AMERICAN WATER COMPANY TRA DOCKET #10-00189
FOR THE ATTRITION YEAR ENDED DECEMBER 31, 2011

AMENDED RB-ADIT

		A/ Cap Repairs Change	B/ Temporary Difference Change	C/ Fin 48 Amount	Balance	
SEPTEMBER	2010			$ 2,068,329	$ 24,706,386	D/
OCTOBER		24,105	38,525	2,068,329	24,769,015	
NOVEMBER		24,105	38,525	2,068,329	24,831,645	
DECEMBER		24,105	38,525	2,068,329	24,894,274	
JANUARY	2011	24,105	41,672	2,068,329	24,960,051	
FEBRUARY		24,105	41,672	2,068,329	25,025,827	
MARCH		24,105	41,672	2,068,329	25,091,604	
APRIL		24,105	41,672	2,068,329	25,157,380	
MAY		24,105	41,672	2,068,329	25,223,157	
JUNE		24,105	41,672	2,068,329	25,288,933	
JULY		24,105	41,672	2,068,329	25,354,710	
AUGUST		24,105	41,672	2,068,329	25,420,486	
SEPTEMBER		24,105	41,672	2,068,329	25,486,263	
OCTOBER		24,105	41,672	2,068,329	25,552,039	
NOVEMBER		24,105	41,672	2,068,329	25,617,815	
DECEMBER		24,105	41,672	2,068,329	25,683,592	
AVERAGE ACC. DEF INCOME TAXES					$ 25,288,933	

A/ 2010-2011 amounts per TAWC response to TN-TRA-02-Q92g-ATTACHMENT, page 9 of 9.
B/ 2011 amounts per TN-TRA-02-Q92g-ATTACHMENT, page 4 of 9., 2010 per Consumer Advocate work paper RB-ADIT-1.
C/ TAWC exhibit MAM-14, Page 1 of 2,
D/ TAWC Trial Balance Sum of Deferred Income Taxes and Regulatory Assets.