

March 30, 2011

**Via E-Mail and USPS**

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

filed electronically in docket office on 03/30/11

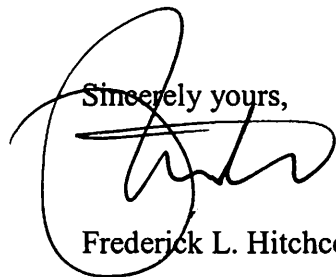
**Re: Petition of Tennessee American Water Company  
Docket No. 10-00189**

Dear Chairman Freeman:

Enclosed please find an original and five (5) copies of the City of Chattanooga's Supplement to Post Hearing Brief. Please file this electronically. I would appreciate you stamping the extra copy of the document as "filed," and returning it to me in the enclosed, self-addressed, stamped envelope.

With best regards, I am

Sincerely yours,



Frederick L. Hitchcock

FLH:pgh  
Enclosures

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cc: Mr. J. Richard Collier (w/encl.)  
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Ms. Monica Smith-Ashford (via email)  
Ms. Shilina Chatterjee Brown (via email)

**BEFORE THE TENNESSEE REGULATORY AUTHORITY  
NASHVILLE, TENNESSEE**

<b>IN RE:</b>	)	
	)	
<b>PETITION OF TENNESSEE</b>	)	<b>Docket No. 10-00189</b>
<b>AMERICAN WATER COMPANY TO</b>	)	
<b>CHANGE AND INCREASE CERTAIN</b>	)	
<b>RATES AND CHARGES.</b>	)	

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**CITY OF CHATTANOOGA’S SUPPLEMENT  
TO POST HEARING BRIEF**

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Tennessee American Water Company (“TAWC”) has questioned whether two statements at pages 30 and 31 of the post hearing brief filed by the City of Chattanooga (the “City”) were supported by the record. These statements addressed (1) the fact that purchasers of publicly traded stock in TAWC’s parent, American Water Works Company (“AWWC”)<sup>1</sup> are willing to accept a return on equity of less than half that sought by TAWC in this case and (2) that TAWC’s parent, which is the only source of TAWC’s capital, is deliberately diverting capital away from TAWC to other of its subsidiaries.

**1. Purchasers of AWWC Stock Are Willing to Accept a Return on Equity of Half that Sought by TAWC.**

On page 30 of its brief, the City stated that Mr. Miller “acknowledged, based on AWWC’s stock price, that investors in AWWC are willing to accept a rate of return of only about 5.5%.” City of Chattanooga’s Post Hearing Brief at 30; T. Vol. VI-B 135-137. TAWC asserts that Mr. Miller did not “acknowledge” the facts stated. However,

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<sup>1</sup> The NYSE symbol for AWWC is AWK.

the record indicates that Mr. Miller did acknowledge that the current return on equity accepted by purchasers of AWWC's stock is some 5.5 percent.

Mr. Hitchcock asked Mr. Miller to calculate the return on equity of American Water Works Company based on its stock price of \$27.55 per share and its annual earnings per share of \$1.53. Tr. Vol. VI-B, 135-136. Mr. Miller admitted that the calculated rate of return of 5.5% "is a rate of return on their [AWWC's] earnings per share at a point in time." Tr. Vol. VI-B, 136, Lines 11-12.

Mr. Miller admitted that TAWC obtains all of its equity capital from AWWC. Tr. Vol. VI-B, 131-132. Publicly available information, of which the TRA may take judicial notice,<sup>2</sup> establishes that AWWC is daily attracting investors at more than \$27.50 a share, for a return on equity of approximately 5.5%.

The market has established that TAWC, through its parent AWWC, can attract capital at a return on equity of approximately 5.5%. This is compelling evidence that should be given heavy weight by the TRA in rejecting TAWC's unreasonable demand for a return on equity more than twice as great.

**2. Mr. Miller Asserted That AWWC Was Justified In Depriving TAWC of Needed Capital By Sending It to Other Subsidiaries.**

On page 31 of its post hearing brief, the City stated that "Mr. Miller justified AWWC's decision to deprive TAWC of needed capital by asserting that it was reasonable to send capital to better performing subsidiaries." T. Vol. VI-B, 131-34. TAWC incorrectly asserts that the record does not support the City's statement that

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<sup>2</sup> Information concerning AWWC's earnings, stock prices, and shares traded daily is available from public filings with the Securities and Exchange Commission and from other public sources of which the TRA may take judicial notice. Tenn. R. Evid. 201.

AWWC was diverting capital that TAWC needed to other subsidiaries.

**A. TAWC Consistently Argued that TAWC Capital Needs Were Not Being Met.**

In its objection to the City's post hearing brief, TAWC inexplicably argues that AWWC had not deprived TAWC of needed capital, after arguing throughout these proceedings that TAWC's return on equity needed to be set at 11.5% in order to attract needed capital.<sup>3</sup>

In his opening statement, TAWC's attorney asserted that unless the TRA increased TAWC's rates to provide its requested return on equity, TAWC could not "attract the capital." Tr. Vol. I-A, 86-87. He continued, "[a]nd if they can't get the money, then they can't improve the infrastructure – they can't maintain the infrastructure." In his direct testimony, Mr. Watson stated "the Company's financial performance for 2008-2010 has not been adequate and the Company has had to limit capital investment until its financial performance improves." Mr. Watson then listed a whole series of "needed" and "necessary" investments that have been delayed, cancelled, or postponed. Watson Pre-Filed Direct Testimony at pp. 14-16.

**B. Mr. Miller Admitted that AWWC Was Sending Its Capital to Other Subsidiaries Where It Could Receive a Greater Return.**

During his cross-examination, Mr. Miller stated that AWWC's decisions regarding where to invest capital were based largely on a subsidiary's ROE.

Q: So if there's a decision that is made not to give capital to Tennessee American Water Company, that is a decision of its parent, American Water Works Company; correct?

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<sup>3</sup> As Mr. Miller has admitted, the only source for TAWC's capital is AWWC. M. Miller Rebuttal Testimony at p. 29, line 1-2.

A: It's the decision of the parent American Water Works Company and that's – but while they are the parent of Tennessee American, they're no different than any other investor. If American Water Works has options on where to invest its money and we go back to a schedule like Mr. McGehee sent me earlier, although it had achieved ROE's and it has an option to invest it in Pennsylvania American that earns 8 or 9 percent or whatever, and Tennessee American at 2 percent or zero, I mean, why would American Water Works, or any other prudent investor if capital is limited and there's not an unlimited source of capital to invest, why would American Water Works be different from any other prudent investor? They're going to invest their money where they can get the highest return. That's just Finance 101.

Tr. Vol. 6-B, 132.

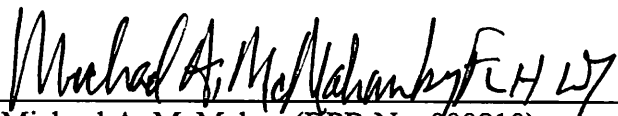
### **Conclusion**

TAWC has consistently argued that it cannot “attract” capital to fund needed capital improvements. TAWC's only source of capital is its parent, AWWC. As Mr. Miller acknowledged, AWWC is attracting its capital with a current return on equity of about 5.5%, less than half the return on equity that TAWC demands in this proceeding. As Mr. Miller has also acknowledged, instead of sending its capital to Tennessee, AWWC is sending it to other subsidiaries.

The return on equity that TAWC needs to attract capital is best measured by the market, which provides equity capital to TAWC's publicly-traded parent at a return on equity of about 5.5%. AWWC's decision not to make available needed capital to TAWC is a result of AWWC's desire to earn more, it is not a result of any requirement of the market.

Respectfully Submitted,

OFFICE OF THE CITY ATTORNEY

By:  *permission*

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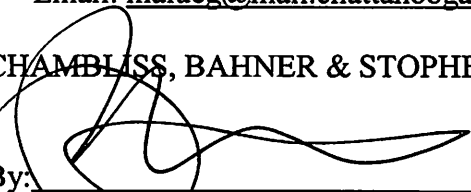
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### CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing pleading was emailed and was served upon the following person(s) via ☐ hand delivery or ☒ United States first class mail with proper postage applied thereon to ensure prompt delivery:

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This 30 day of March, 2011



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