BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE
June 2, 2017

IN RE:	)	
	)	
PETITION OF TENNESSEE-AMERICAN WATER	)	
COMPANY REGARDING THE 2017 INVESTMENT	)	
AND RELATED EXPENSES UNDER THE QUALIFIED	)	**DOCKET NO.**
INFRASTRUCTURE INVESTMENT PROGRAM	)	**16-00126**
RIDER, THE ECONOMIC DEVELOPMENT	)	
INVESTMENT RIDER, AND THE SAFETY AND	)	
ENVIRONMENTAL COMPLIANCE RIDER	)	

ORDER APPROVING *PETITION*

This matter came before Vice Chairman Robin L. Morrison, Director Herbert H. Hilliard, and Director Kenneth C. Hill of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this docket, at a regularly scheduled Authority Conference held on March 13, 2017 for consideration of the *Petition* filed by Tennessee-American Water Company ("TAWC" or the "Company") on November 4, 2016.

BACKGROUND

TAWC provides residential, commercial, industrial and municipal water service to customers in Tennessee and North Georgia. TAWC is a wholly-owned subsidiary of American Water Works Company, Inc. On November 4, 2016, TAWC filed a *Petition* requesting Authority approval to increase the tariff percentage rates during the 2017 calendar year for the Qualified Infrastructure Investment Program Rider ("QIIP" or "QIIP Rider"), the Economic Development Investment Program Rider ("EDI" or "EDI Rider"), and the Safety and

Environmental Compliance Program Rider ("Safety Rider" or "SEC"). The QIIP, EDI and SEC (collectively, "Capital Riders") were previously approved by the Authority on April 14, 2014 in Docket No. 13-00130.[1]

On December 13, 2016, the Consumer Protection and Advocate Division of the Office of the Attorney General ("Consumer Advocate") filed its *Petition to Intervene.* On December 20, 2016, the Hearing Officer granted the Consumer Advocate's intervention.

PETITION

In accordance with the tariffs approved in TRA Docket No. 13-00130, on or before December 1 of each year, the Company shall submit to the Authority an annual filing that calculates the tariff Rider percentage rates for the upcoming calendar year.[2] In support of the *Petition*, the Company submitted the pre-filed testimony of Ms. Linda Bridwell and Mr. Brent E. O'Neill.

In pre-filed testimony, Ms. Bridwell submits the Capital Riders were calculated consistent with the modifications and clarifications ordered in TRA Docket Nos. 14-00121 and 15-00029, and the corrections made to the calculations in TRA Docket Nos. 15-00111 and 16-00022.[3] Per the prior directive of the Authority, new services, new meters and the alternative fuel vehicles costs have been removed from the EDI rider 2017 calculations and the cumulative amounts have been removed from the review periods of 2014, 2015 and 2016. Additionally, there are three new worksheets itemizing total additions, removals and retirements for 2014, 2015, 2016 and 2017 intended to provide a clear audit trail.[4]

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[1] *See In re: Petition of Tennessee-American Water Company for Approval of a Qualified Infrastructure Investment Program, an Economic Development Investment Rider, a Safety and Environmental Compliance Rider and Pass-Throughs for Purchased Power, Chemicals, Purchased Water, Wheeling Water Costs, Waste Disposal, and TRA Inspection Fee*, Docket No. 13-00130, *Order Approving Amended Petition* (January 27, 2016).
[2] *See Petition*, pp. 5-6 (November 4, 2016).
[3] Linda C. Bridwell, Pre-filed Direct Testimony, pp. 3-4 (November 4, 2016).
[4] *Id.* at 8-9.

Ms. Bridwell notes five changes and one update to the worksheets made to assist in review of this *Petition* and the supporting documentation: 1) The first worksheet or tab is a new "Workbook Info" which provides a description of each worksheet; 2) The tabs in the workbook are reorganized and color coded to facilitate the location of information; 3) all hard coded numbers are colored blue and a footnote is provided identifying where the source of the number can be found; 4) insertion of a "tie-point" throughout the worksheets which verifies the numbers are calculating correctly; 5) updated the historical average retirements, Contributions in Aid of Construction ("CIAC") and cost of removal for 2012-2015 in order to project these amounts by plant account; and 6) linked the 2015 Capital Expenditures to the worksheet in TRA Docket No. 16-00022 (copy included with filing).[5]

Ms. Bridwell explains the Capital Rider calculations utilize average end-of-month balances, beginning January 1, 2017 through December 31, 2017, reflective of only those qualified plant investments since the last rate case. These investments are reflective of plant retirements, depreciation and tax expense. TAWC used a 13-month average to calculate plant balances. The current approved pre-tax return is applied to the net amount of investment to determine the revenue requirement on the rate base portion. Annual depreciation is calculated next utilizing the latest approved depreciation rates and then property and franchise taxes are added. These components are then added together and grossed up to reflect Gross Receipts tax, Uncollectible expense and forfeited discounts to arrive at the final revenue requirement. No over or under-collections are reflected in this filing.[6] Any over or under-recovery would be included in the reconciliation filing which is due March 1st of the following year. The reconciliation filing

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[5] *Id.* at 9-10.
[6] *Id.* at 16-17.

will also include any variance from budgeted costs and actual costs and take into consideration the earned rate of return of the Company in comparison to the authorized rate of return.[7]

In summary, TAWC is proposing a QIIP Rider of 7.52% which will generate $3,539,145 revenue and represents a $1,394,019 and 2.96% increase from the previous year; an EDI Rider of 0.34% which will generate $161,282 revenue and represents a $114,026 and 0.24% increase from the previous year; and an SEC Rider of 6.09%, which will generate $2,868,066 revenue and represents a $174,222 and 0.37% increase from the previous year. The new surcharges in total are estimated to increase the average customer's bill $0.77 per month, or $9.24 per year.[8]

The Company asserts the Capital Riders are mutually beneficial to the ratepayers, the public and TAWC, and therefore, are in the public interest. Reducing the need for a rate case, minimizing rate shock to customers, providing for needed infrastructure, and providing opportunities for economic development and ensuring safe and reliable services are a few examples of such benefits. According to Ms. Bridwell, the Capital Riders provide an incentive for the Company to invest in the infrastructure necessary to provide safe and reliable service and spur economic development within its service territory because the investment can be recovered immediately and without the costs and time needed for a rate case. Ms. Bridwell also states she is not aware of any changes in market conditions or other factors that would affect whether the Riders remain in the public interest.[9]

The investment plan for determining the QIIP, EDI and SEC consists of 1) Recurring Projects and 2) Major Projects identified as investment projects ("IPs"). The Company provided a copy of its 2017 Strategic Capital Investment Plan with the testimony of Brent E. O'Neill, P.E.

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[7] *Id.* at 18-23.
[8] *Id.* at 25-27.
[9] *Id.* at 28-30.

Mr. O'Neill explains in pre-filed testimony that the Company's capital planning is flexible and can be adjusted to address the needs of TAWC and customers.

On a cumulative basis, TAWC is estimating it will exceed its 2014 to 2016 capital investment plan by 3.14%.[10] According to Mr. O'Neill, the QIIP allows the Company to replace aging infrastructure such as small diameter mains and mains with continuing leaks on a timely basis. The replacements are planned and proactive resulting in a more reliable and safe infrastructure, with less of a rate shock to customers. During 2017, TAWC plans on replacing 25,540 feet of main with an approximate cost of $2,620,255. In addition to better service, these scheduled replacements will result in fewer water leaks, reduction in the amount of water produced and less energy consumption.[11]

The majority of mains scheduled for replacement during 2017 are cast iron and galvanized material. While these types of mains represent 55.5% of main footage within the system, they experience 90.6% of all breaks. For this reason, the Company is focusing on cast iron and galvanized replacements for the next several decades until 706 miles of this material is removed. The Company does expect to expend more on main replacements during 2017 than in previous years. TAWC anticipates that all of the budgeted QIIP will occur during 2017. Mr. O'Neil submits that unexpected changes in infrastructure and changes in priorities sometimes occur resulting in project changes. When changes do occur, the Company's Management Committee reviews the needed changes and approves any movement from one capital item to another.[12]

The QIIP also includes unscheduled main replacements and/or restoration of existing mains. TAWC is proposing to spend $1,009,000 for unscheduled replacements in 2017. This

[10] Brent E. O'Neill P.E., Pre-Filed Direct Testimony, pp. 4-6 (November 4, 2016).
[11] *Id.* at 6-10.
[12] *Id.* at 12-14.

amount is similar to the three year average spending in 2013-2015 for unscheduled mains.[13] For 2017, the Company has budgeted for relocation of existing water mains, hydrants and/or valves which occur because of municipal or state agency projects. The Company has budgeted to replace hydrants and valves and small diameter pipe between the customer and the Company's distribution main. Based on the average cost of replacement, this will allow the Company to replace 175 services.[14]

The QIIP also includes $1,687,825 for replacement of approximately 9,978 meters during 2017. Meter replacement is necessary in order avoid service disruptions or inconveniences for meters that are at the end of their useful life. This budget is 87% above the five-year average between 2011 and 2015.[15] The large increase is due to the replacement of meters with Automatic Meter Reading ("AMR") meters. AMR meters allow the Company to read meters from the road rather than physically approaching each meter. The current plan allows TAWC to deploy these meters throughout its system through 2021.[16]

Tank rehabilitation/painting for the Mission Ridge Standpipe and South End Tank is included in the QIIP.[17] One Capital Investment Project for the Tennessee River Transmission main Crossing Project costing $2,001,711 is included in the QIIP. There are currently two river crossings: one concrete 30" main under the river installed in 1965 and one 16" under the Walnut Street Bridge installed in 1948. In 2016, the concrete main ruptured and a 24" High Density Polyethylene pipe was installed in the ruptured concrete pipe. While this overcame the rupture, it did permanently reduce the capacity of the main by approximately 34.5%. The new river

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[13] *Id.* at 14-15.
[14] *Id.* at 15-18.
[15] *Id.* at 19-20.
[16] *Id.* at 18-19.
[17] *Id.* at 20-21.

crossing will provide a third crossing, replace the lost capacity and provide a back-up for the existing 16" main for when it reaches its useful life of 70 to 80 years.[18]

The Company included $310,000 for new water mains associated with economic development. These EDI expenditures enhance the existing distribution system and allow the Company to respond quickly to future growth of the community. The planned expenditures will increase water capacity and pressure to the Northshore area, City of Chattanooga Stringers Ridge Park and the Valley View Industrial Park. The Company also plans on spending $74,000 on new hydrants and valves aimed at improving infrastructure in older areas including fire protection.[19]

The SEC Rider includes System Control and Data Acquisition ("SCADA") Equipment and Systems, Security Equipment and Systems and Process Plant Facilities and Equipment. SCADA monitors and controls treatment plants and network facilities. TAWC budgeted $175,000 for SCADA improvements in 2017. These improvements include replacement of the SCADA system at the Citico plant, Remote Terminal Units ("TRUs") at Suck Creek and security equipment and systems at the Company facilities. All of the projected expenditures ensure that the operation of the water system is meeting safety and environmental requirements.[20]

In supplemental testimony, Ms. Bridwell notifies the Authority of a change in its calculation from that in previous dockets. Normally, this filing would include all of the capital expenditure plan for 2016 that was included in TRA Docket No. 15-00111. However, this filing excludes $300,000 for the Retire Basin 1 project which is now scheduled for completion on December 31, 2020.[21] This testimony substantiates this change which is reflected in the previously filed workpapers.

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[18] *Id.* at 21-23.
[19] *Id.* at 24-26.
[20] *Id.* at 27-29.
[21] Linda C. Bridwell, Pre-Filed Supplemental Testimony, p. 3 (December 6, 2016).

POSITION OF THE CONSUMER ADVOCATE

Following discovery and exchanges of information with TAWC, Mr. Hal Novak submitted pre-filed testimony on behalf of the Consumer Advocate which addressed the calculations of TAWC's proposed Capital Riders. The Consumer Advocate reviewed the filing and found the proposed surcharges to be reasonable, although the testimony of Mr. Novak raised three issues: (1) A concern that an average of construction expenditures is used in prospective (budget) filings and actual plant additions are used in the reconciliation filings. They do not contend this is inconsistent with previous filings but rather assert that two different methods are used depending on the type of filing and this is a "haphazard way to manage this alternative regulation mechanism;"[22] (2) The Company modified this filing by converting the 2014 depreciation expense formulas to hard coded numbers which resulted in a different result. Mr. Novak estimates the total difference is $10,386; he points out, however, this would be cumulative (affecting all previous and future capital rider filings) and it would also affect the deferred tax calculation for 2014; and (3) the use of hard coded numbers without supporting documentation. The Consumer Advocate asserts this method causes a procedural and analytical delay in their review because a request for documentation has to be made and the Company has to respond.

REBUTTAL OF TAWC

Ms. Bridwell testified in pre-filed rebuttal testimony that the reconciliation dockets do not use forecasted construction expenditures but rather, the actual plant additions for each month are compared to the forecasted amounts.[23] . The basis of using the three-month average is the recognition that there is lag between construction expenditures and placing the assets in service.

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[22] William H. Novak, Pre-Filed Direct Testimony, p. 8 (February 1, 2017).
[23] Linda C. Bridwell, Pre-Filed Rebuttal Testimony, pp. 1-5 (February 13, 2017).

The current methodology, which was proposed and approved in TRA Docket No. 13-00130, was to recognize and account for this lag.[24]

Ms. Bridwell next addresses the Consumer Advocate's concern regarding the calculation of depreciation expense. She explains that the Company does not book depreciation by project or asset; rather the total value of all plant assets in a utility plant account is multiplied by the depreciation rate to determine the group asset depreciation amount. Therefore, TAWC developed a method to determine the actual depreciation expense based on the amount of actual plant additions for the Capital Riders Reconciliation in TRA Docket No. 15-00029. This methodology calculated 2014 actual depreciation expense based only on the amount of the actual monthly plant additions for the Capital Riders. The Company determined this method was hard to follow and did not produce any greater accuracy than taking the 13-month average of plant additions times the TRA approved depreciation rates.[25] Following up in TRA Docket No. 15-00111, the Company hard coded the 2014 depreciation amounts. In TRA Docket No. 16-00022, TAWC changed the methodology to calculate the actual 2015 depreciation expense based upon a 13-month average of plant additions times the approved depreciation rate.[26]

TAWC submits that restating the 2014 depreciation expense would not have enough material impact to justify the expense of doing so. Further, the Authority approved the 2014 depreciation expense calculation in TRA Docket No. 15-00022 and this expense methodology was utilized in TRA Docket Nos. 15-00111, 16-00022 and the instant docket. The Company asserts its willingness to make methodology changes on a prospective basis as needed changes are discovered.[27]

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[24] *Id.* at 5.
[25] *Id.* at 8-9.
[26] *Id.* at 9-10.
[27] *Id.* at 10.

Finally, Ms. Bridwell submitted that she attested to the numbers, calculations and financial information used to prepare the exhibits and is the appropriate witness to confirm the costs in this filing are accurate and reflect the Company's ledger.[28]

MARCH 13, 2017 HEARING AND APPEARANCES

A Hearing in this matter was held before the voting panel on March 13, 2017, as noticed by the Authority on March 3, 2017. Prior to the hearing, the parties gave notice to the Authority on February 24, 2017, that there were no outstanding disputes between the parties and the parties waived cross-examination of the respective expert witnesses and jointly requested the record in the docket, including the discovery, be made part of the evidentiary record.[29] Participating in the hearing were the following parties and their respective counsel:

> TAWC - Melvin J. Malone, Esq., Butler, Snow, O'Mara, Stevens & Cannada, PLLC, 1200 One Nashville Place, 150 Fourth Avenue North, Nashville, Tennessee 37219.
>
> Consumer Advocate – Daniel P. Whitaker, III, Esq., Office of the Attorney General, 425 Fifth Avenue North, Fourth Floor, John Sevier Building, P.O. Box 20207, Nashville, Tennessee 37202.

The voting panel heard testimony by Ms. Linda Bridwell on behalf of the Company. Mr. William H. Novak, the expert witness of the Consumer Advocate, was present. Ms. Bridwell represented that the Consumer Advocate had withdrawn its objections with respect to this docket and this specific *Petition*.[30] During the hearing, the public was given an opportunity to offer comment, but no member of the public sought to comment on the *Petition*. Following the conclusion of the testimony, the voting panel considered the *Petition*.

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[28] *Id.* at 14-16.
[29] *Joint Notice*, p. 1 (February 24, 2017).
[30] Transcript of Proceeding, p. 10 (March 13, 2017).

FINDINGS AND CONCLUSIONS

Upon review of the entire evidentiary record in this matter, and consistent with the agreement of parties, the panel unanimously found the capital expenditures as filed by the Company are reasonable. The Company is focusing on replacing mains, primarily cast iron and galvanized mains and needed tank rehabilitation/painting for the Mission Ridge Standpipe and South End Tank. The Company has also scheduled a Capital Investment Project to install a new Tennessee River crossing main to replace lost capacity and provide a back-up for the two current mains. In light of the evidentiary record, the panel concluded these projects are prudent and the type envisioned when these riders were established.

The panel unanimously approved QIIP surcharge of 7.52%, up from last year's surcharge of 4.56%. The new QIIP surcharge will generate $3,539,145 in annual revenues and represents a $1,394,019 increase from the previous year. The panel unanimously approved the SEC surcharge of 6.09%, up from last year's surcharge of 5.72%. The new SEC surcharge will generate $2,868,066 in annual revenues and represents a $174,222 increase from the previous year. For the EDI Rider, the panel unanimously approved a surcharge of 0.34%, up from last year's surcharge of 0.24%. The new SEC surcharge will generate $161,282 in annual revenues and represents a $114,026 increase from the previous year. In total, the new surcharges approved here are estimated to increase the average residential customer's bill $0.77 per month, or $9.24 per year.

Finally, the panel found that the Capital Riders continue to benefit both consumers and TAWC and remain in the public interest. The riders allow the utility timely recovery of investment related expenses to ensure safe and reliable drinking water and promote economic development, while benefitting consumers through reduced rate case and legal expenses that would otherwise result through expensive rate case proceedings. The panel voted unanimously to approve the *Petition*.

IT IS THEREFORE ORDERED THAT:

1. The *Petition* filed by Tennessee-American Water Company on November 4, 2016, is approved.

2. A Qualified Infrastructure Investment Rider of 7.52% resulting in annual revenues of $3,539.145 is approved.

3. An Economic Development Investment Rider of 0.34% resulting in annual revenues of $161,282 is approved.

4. A Safety and Environmental Compliance Rider of 6.09% resulting in annual revenues of $2,868,066 is approved.

Vice Chairman Robin L. Morrison, Director Herbert H. Hilliard and Director Kenneth C. Hill concur.

ATTEST:

Earl Taylor

Earl R. Taylor, Executive Director