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IN THE TENNESSEE PUBLIC UTILITY COMMISSION
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF TENNESSEE-AMERICAN WATER COMPANY REGARDING CHANGES TO THE QUALIFIED INFRASTRUCTURE INVESTMENT PROGRAM RIDER, THE ECONOMIC DEVELOPMENT INVESTMENT RIDER, AND THE SAFETY AND ENVIRONMENTAL COMPLIANCE RIDER AND IN SUPPORT OF THE CALCULATION OF THE 2019 CAPITAL RECOVERY RIDERS RECONCILIATION	)	DOCKET NO. 19-00031

DIRECT TESTIMONY

OF

DAVID N. DITTEMORE

September 26, 2019

IN THE TENNESSEE PUBLIC UTILITY COMMISSION
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF TENNESSEE-AMERICAN WATER COMPANY REGARDING CHANGES TO THE QUALIFIED INFRASTRUCTURE INVESTMENT PROGRAM RIDER, THE ECONOMIC DEVELOPMENT INVESTMENT RIDER, AND THE SAFETY AND ENVIRONMENTAL COMPLIANCE RIDER AND IN SUPPORT OF THE CALCULATION OF THE 2019 CAPITAL RECOVERY RIDERS RECONCILIATION	)	**DOCKET NO. 19-00031**

AFFIDAVIT

I, David N. Dittemore, on behalf of the Consumer Advocate Unit of the Attorney General's Office, hereby certify that the attached Direct Testimony represents my opinion in the above-referenced case and the opinion of the Consumer Advocate Unit.

David N. Dittemore
DAVID N. DITTEMORE

Sworn to and subscribed before me this 26th day of September, 2019.

Terra Allen
NOTARY PUBLIC

TERRA ALLEN STATE OF TENNESSEE NOTARY PUBLIC HICKMAN COUNTY

My commission expires: 9/28/2022

Q1. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION FOR THE RECORD.

A1. My name is David N. Dittemore. My business address is Office of the Tennessee Attorney General, War Memorial Building, 301 6th Ave. North, Nashville, TN 37243. I am a Financial Analyst employed by the Consumer Advocate Unit in the Financial Division of the Tennessee Attorney General's Office (Consumer Advocate).

Q2. PLEASE PROVIDE A SUMMARY OF YOUR BACKGROUND AND PROFESSIONAL EXPERIENCE.

A2. I received a Bachelor of Science Degree in Business Administration from the University of Central Missouri in 1982. I am a Certified Public Accountant licensed in the state of Oklahoma (#7562). I was previously employed by the Kansas Corporation Commission (KCC) in various capacities, including Managing Auditor, Chief Auditor, and Director of the Utilities Division. For approximately four years, I was self-employed as a Utility Regulatory Consultant representing primarily the KCC Staff in regulatory issues. I also participated in proceedings in Georgia and Vermont, evaluating issues involving electricity and telecommunications regulatory matters. Additionally, I performed a consulting engagement for Kansas Gas Service (KGS), my subsequent employer during this time frame. For eleven years I served as Manager and subsequently Director of Regulatory Affairs for KGS, the largest natural gas utility in Kansas serving approximately 625,000 customers. KGS is a division of One Gas, a natural gas utility serving approximately two million customers in Kansas, Oklahoma and Texas. I joined the Tennessee Attorney General's Office in September 2017 as a Financial Analyst. Overall, I have thirty years' experience in the field of public utility regulation. I have presented testimony as an expert witness on many occasions. Attached as Exhibit DND-1 is a detailed overview of my background.

Q3. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION (COMMISSION OR TPUC)?

A3. Yes, I have testified before the Commission on a number of occasions.

Q4. WHAT IS THE PURPOSE OF THIS DOCKET?

A4. The purpose of my testimony is to address the request of Tennessee American Water Company (TAWC) to implement a reconciliation associated with the three Capital Riders totaling ($436,646), translating to a reduction to the existing Capital Riders of (1.237%).

EXECUTIVE SUMMARY

Q5. PLEASE SUMMARIZE THE RECOMMENDATIONS YOU ARE SUPPORTING IN THIS CASE.

A5. My recommendations include sponsoring adjustments to the proposed reconciliation amount as well as identifying concerns with the methodology used to spread increases to TAWC customers. The appropriate reconciliation associated with the three Capital Riders is ($847,114), equating to a reconciliation factor of (2.4%). The adjustments comprising the difference in the reconciliation balance I am supporting compared with that of the Company include the following:

1. The Company has included lobbying as an Operating Expense for the purpose of determining excess earnings within the Earnings Test calculation. Thus, eligible expenses within the earnings test are overstated, and the appropriate level of excess earnings is understated; and

2. The Company has failed to gross-up the excess earnings for income taxes, thereby understating the excess earnings.

In addition to quantifying these adjustments, I will also provide comments on the following items:

a. The Commission should order the Company to track all costs associated with its outage beginning September 12th and record these costs in a below-the-line non-operating expense account, including costs associated with all civil litigation surrounding this incident. The purpose of this request is to ensure these costs do not factor into the Earnings Test calculation;

b. The Commission should cap the TAWC Capital Riders surcharge at the level adopted in this Docket, pending the outcome of the upcoming general investigation into the Capital Riders mechanism and a determination of the root cause of the September 12th outage;

c. The method used by the Company to determine its Repair Deduction component of Accumulated Deferred Income Taxes differs year to year, raising questions over the appropriate method for use in determining this important component of the Capital Riders calculation; and

d. The method used to apply the Capital Riders surcharge costs to customer bills results in significant disparities in the nominal amount charged to the various TAWC service areas.

Q6. WHAT SCHEDULES ARE YOU SPONSORING?

A6. In addition to my background referenced above, I am sponsoring Exhibits DND 2, 3, and 4, which set forth my adjustments to the Company's reconciliation proposal in this Docket. I am also including Attachments 1, 2, and 3, reflecting publicly available information provided to American Water Works investors.

Q7. WHAT IS YOUR RECOMMENDED RECONCILIATION AMOUNT AND HOW DOES IT COMPARE WITH THAT SUPPORTED BY TAWC?

A7. My recommended surcharge is (2.40%) as shown on Exhibit DND-3, which compares with the TAWC proposed surcharge of (1.237%). My recommendation is based upon a reconciliation amount of ($847,114) compared with the Company's proposed reconciliation of ($436,646), for a difference of ($410,468). This difference is comprised of the elimination of lobbying costs within the Earnings Test calculation ($100,335), the impact of tax savings on the Company's excess earnings ($299,148), and the application of interest to these changes to the reconciliation balance ($10,985).

RECOGNITION OF LOBBYING COSTS

Q8. PLEASE BEGIN WITH A DISCUSSION OF THE ADJUSTMENT YOU ARE SUPPORTING, RELATIVE TO LOBBYING COSTS INCURRED BY THE COMPANY?

A8. My first adjustment removes $100,335 directly related to lobbying activities from Operating Expenses in the computation of the Earnings Test.

Q9. WHAT IS THE EARNINGS TEST CALCULATION AS IT RELATES TO THE CAPITAL RIDERS SURCHARGE?

A9. The Earnings Test calculation is designed to flow back any TAWC earnings above its authorized rate of return (ROR) as authorized in its last rate case as a credit to the Capital Riders.

Q10. WHY SHOULD LOBBYING COSTS BE EXCLUDED FROM OPERATING EXPENSES WHEN EVALUATING THE EARNINGS TEST?

A10. There are two strong reasons to ensure that lobbying costs are removed from those expenses included within the Earnings Test calculation. First, lobbying costs are typically removed from revenue requirement determinations when establishing utility rates, both in Tennessee as well as throughout the country. Lobbying is generally done to promote shareholder interests and initiatives, often to the detriment of ratepayer interests. Lobbying costs are not eligible for inclusion in base rate cases and such costs should not be used to reduce the amount of excess earnings that would otherwise be credited to ratepayers. Second, the Company's accounting for lobbying costs does not comply with the NARUC Uniform System of Water Accounts for large utilities.

Q11. ACCORDING TO THE NARUC UNIFORM SYSTEM OF ACCOUNTS (USoA) FOR WATER UTILITIES, HOW SHOULD LOBBYING CHARGES BE RECORDED?

A11. Lobbying charges are properly recorded in Account 426, which is a non-operating expense account.[1]

Q12. IS THE COMPANY'S METHOD OF ACCOUNTING FOR LOBBYING CHARGES CONSISTENT WITH THAT PERSCRIBED IN THE (USoA)?

A12. No. The lobbying charges of TAWC are recorded as an operating expense, recorded to various accounts within the General and Administrative category of accounts[2]. It is important to note that the actual process of recording these charges by TAWC is inconsistent with standard ratemaking accounting to record lobbying charges below the line. Instead, the method used by the Company appears to be strategic, in order to reflect lower earnings and thus to minimize potential customer credits associated with excess earnings. If TAWC had complied with the NARUC Chart of Accounts for Water Utilities, it would not have included such costs as an Operating Expense, and excess earnings would be higher by $100,335. By including these lobbying charges incorrectly as an operating expense, the Company is effectively asserting that these costs should be

[1] *See e.g.,* Uniform System of Accounts for Water Utilities Operating in Illinois, Illinois Commerce Commission, publicly available at https://www.icc.illinois.gov/downloads/public/rl/USOAWater.doc (October 1998, Reprinted November 2002).

[2] *See* Response to Consumer Advocate Discovery Request No. 2-8.

recovered by its ratepayers by forgoing $100,335 in reduced operating expenses within the Earnings Test calculation.

Q13. PROVIDE A BREAKDOWN OF THE SOURCE OF TAWC LOBBYING CHARGES IN 2018.

A13. The Attachment to TAWC's Response to Consumer Advocate Request No. 2-8 provides a breakdown of lobbying charges. Of the approximately $100,000 identified total, only $16,000 is associated with internal Company employees, while the remainder is associated with external Governmental Affairs contractors and other miscellaneous costs.

Q14. DO YOU BELIEVE THE COMPANY'S RESPONSE INCLUDES ALL COSTS SURROUNDING TAWC'S LOBBYING EFFORTS?

A14. No, it is not clear if all of TAWC's lobbying efforts are included in what is identified here. This is my opinion and is based upon my experience as a regulator and as a utility employee; a significantly deeper dive into TAWC's record keeping, compared to the two rounds of discovery in this Docket, would be required to ensure all lobbying efforts are accounted for. I also suspect I have a broader definition of what should constitute lobbying efforts than does the Company, which has a financial incentive to define it narrowly for regulatory accounting purposes.

Q15. WHAT IS THE BASIS FOR YOUR OPINION?

A15. It is certainly no secret in the water industry that American Water Company, the parent company of TAWC, has been promoting "fair market legislation"[3] throughout its corporate footprint, including Tennessee. This, of course, is entirely appropriate for the

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[3] "Fair market" and "fair market value" are industry terms for the bills being promoted by utilities throughout the country. These should not be construed as an objective description.

company to do; our concern is only with the accounting. This effort is demonstrated within publicly available investor slide presentations (*See* Attachments 1, 2, and 3). It is obvious from the review of these slides that one of the Company's major, if not primary, growth initiatives is to acquire other water and wastewater systems and plans to use enabling fair market value legislation as the vehicle to achieve this corporate goal. The following tasks associated with promoting legislation should be charged to a non-operating expense account such as Account 426:

1. All executive and non-executive time spent formulating the draft legislation;
2. Developing and approving messaging and talking points to legislators and key staff members;
3. Reporting internally on the status and progress of the legislation to executives and upper management; and
4. Managing the efforts of contracted lobbyists.

I strongly believe the Company's identification of only $16,000 of internal labor and overhead expenses concerning this lobbying push is very minimal and likely does not include all appropriate time and expenses on the tasks described above, resulting in an understatement of the actual costs associated with this lobbying effort.

INCOME TAX IMPLICATIONS OF THE EARNINGS TEST ADJUSTMENT

Q16. PLEASE TURN TO YOUR NEXT ISSUE REGARDING THE IMPACT OF INCOME TAXES WITHIN THE DETERMINATION OF THE EARNINGS TEST. WHAT IS YOUR CONCERN WITH THE COMPANY'S METHOD FOR DETERMINING ITS EXCESS EARNINGS AS IT RELATES TO INCOME TAXES?

A16. The Company's computation of excess earnings fails to consider Income Tax Expense implications associated with its excess earnings. The Company has understated excess earnings by $299,148, as reflected on Exhibit DND-4.

Q17. IS THERE AN INCOME TAX COMPONENT THAT IS PART OF THE REVENUE REQUIREMENT DETERMINATION WITHIN THE CAPITAL RIDERS?

A17. Yes. The Company recovers the incremental Income Tax Expense associated with its Capital Riders revenue requirement in order to achieve its after-tax cost of equity. However, when it has excess earnings, it ignores the Income Tax implications of refunding these excess amounts back to ratepayers. This is a glaring inconsistency with the manner in which revenue requirements are determined and violates the basic accounting principle of matching.

Q18. IS THE DETERMINATION OF INCOME TAX EXPENSE, A BASIC FEATURE OF ALL REVENUE REQUIREMENT DETERMINATIONS INVOLVING UTILITIES, SUBJECT TO INCOME TAXES?

A18. Yes.

Q19. WHAT IS THE IMPLICATION ON THE EARNINGS TEST CALCULATION IF THE INCOME TAX EXPENSE COMPONENT IS IGNORED?

A19. If the Company's approach to ignore the Income Tax implications of excess earnings is adopted, this results in the Company retaining excess earnings associated with Income Tax expense savings. The revenue reduction associated with excess earnings results in a reduction in Income Tax expense. The Company would retain these savings, thus creating additional excess earnings. In short, the incomplete nature of the Company's calculation does not in fact return all excess earnings back to customers.

Q20. BY FAILING TO RECOGNIZE THE INCOME TAX EXPENSE COMPONENT OF THE EARNINGS TEST CALCULATION, IS THE COMPANY TRULY RETURNING ALL EXCESS EARNINGS TO RATEPAYERS?

A20. No, it is not. As demonstrated in Exhibit DND-4, the Company's method permits it to retain $299,148 in excess profits generated in 2018.

Q21. IS THE REFLECTION OF OVER-EARNINGS WITHOUT RECOGNITION OF THE IMPACT OF INCOME TAXES CONSISTENT WITH HOW THIS BALANCE WAS CALCULATED IN DOCKET NO. 18-00022?

A21. Yes. However, the oversight in Docket No. 18-00022 should not create a precedent that should be compounded in all subsequent dockets. Once this issue was identified in this Docket, the Company had the option to acknowledge the oversight in discovery, thus reducing the scope of litigation in this Docket. Instead, we find ourselves arguing about an issue that is simply an attempt by the Company to maximize earnings despite the lack of underlying logic in its position.

Q22. IS IT CONSISTENT OR APPROPRIATE FOR THE COMPANY TO INCLUDE THE TAX IMPACT OF THE CAPITAL RIDERS REVENUE DEFICIENCY WHILE IGNORING THE TAX IMPLICATIONS WITHIN THE EARNINGS TEST CALCULATION?

A22. No, it is inconsistent and inappropriate.

Q23. WHAT IS THE COMPANY'S RESPONSE TO YOUR CONCERNS OVER THE LACK OF A TAX GROSS-UP FEATURE OF THE EARNINGS TEST?

A23. In response to Consumer Advocate Request No. 2-4, the Company relies upon tariff language which it interprets as either not requiring or not permitting a tax gross-up associated with excess earnings.

Q24. WHAT IS YOUR RESPONSE TO THE COMPANY'S CLAIM THAT AN INCOME TAX FEATURE IS NOT INCLUDED WITHIN THE CAPITAL RIDERS TARIFF ASSOCIATED WITH THE EARNINGS TEST CALCULATION?

A24. The inclusion of an Income Tax expense component, whether positive or negative, is a standard component of revenue requirement calculations. That this issue is not identified in the tariff should not be construed as a specific determination by this Commission that any earnings test calculation need not be grossed-up for income taxes. The Income Tax expense implications of the earnings test is so basic that it need not be specifically identified within the tariff.

Q25. IS THE GROSS-UP FOR INCOME TAX EXPENSE APPLIED TO EXCESS EARNINGS CONSISTENT WITH THE TARIFF PROVISION GOVERNING THE CALCULATION OF EXCESS EARNINGS?

A25. Yes. The relevant paragraph within the tariff is as follows:

> If the earnings attained by the Company for the Annual Review Period exceed the earnings allowed for the Annual Review Period by applying the overall rate of return authorized in the Relevant Rate Order, then any such earnings difference shall constitute the Earnings Test Adjustment. If the earnings attained by the Company for the Annual Review Period by applying the overall rate of return authorized in the Relevant Rate Order, then no Earnings Test Adjustment shall be recognized.

The key phrase in the above passage is ". . . any such earnings difference . . . ." The phrase "earnings difference" necessarily includes the income tax gross-up. The recognition of Income Tax implications is a necessary component to quantify the "earnings difference" referenced in the tariff.

ACCOUNTING FOR THE OUTAGE EVENT BEGINNING SEPTEMBER 12

Q26. CAN YOU PROVIDE SOME BACKGROUND INFORMATION CONCERNING THE OUTAGE EXPERIENCED WITHIN THE COMPANY'S SERVICE TERRITORY?

A26. The TAWC system experienced a significant main break on September 12, 2019, resulting in a widespread service outage. Per reports[4], some 35,000 customers were directly affected. Published reports also indicate a civil suit has been filed, seeking to recover alleged damages incurred by customers as a result of the service outage.[5]

Q27. HOW IS THIS OUTAGE AND ITS COSTS RELATED TO THE CAPITAL RIDERS MECHANISM?

A27. In the current filing, the Company has experienced significant excess earnings. Even by the Company's own calculation, this amount is $745,142, and my testimony identifies $1,144,625 in excess earnings. In either case, this is substantial considering the number of customers served by the Company. The quantification of excess earnings is a function of the amount of revenue and expenses incurred by the Company. The question then

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[4] https://www.timesfreepress.com/news/breakingnews/story/2019/sep/14/work-repair-water-main-fixed-water-be-restored-soon/503586/

[5] https://www.timesfreepress.com/news/local/story/2019/sep/17/local-attorneys-file-class-action-lawsuit-filed-against-tennessee-american-water/503800/

becomes how the costs associated with the main break should be considered within the context of the earnings adjustment.

Q28. IF THE COMPANY IS OTHERWISE IN AN OVEREARNING SITUATION, WOULD INCURRING THESE COSTS ESSENTIALLY BE BORNE BY TAWC RATEPAYERS?

A28. Yes. If the Company is otherwise in an excess earnings situation, these costs would then reduce any over-earnings and result in funding by ratepayers resulting from the avoidance of a credit to the Capital Riders surcharge.

Q29. DO YOU BELIEVE THE COMMISSION SHOULD REQUIRE THE COMPANY TO TRACK ITS COSTS ASSOCIATED WITH THIS EVENT AS WELL AS COSTS ASSOCIATED WITH PROCESSING THE CIVIL CLAIM AND TO RECORD SUCH COSTS TO A NON-OPERATING EXPENSE ACCOUNT?

A29. Absolutely.

Q30. WHY IS THIS ACCOUNTING TREATMENT NECESSARY?

A30. Absent intervention by the Commission, these costs would be charged as an operating expense and not otherwise be separately identifiable. As such, it would be challenging to determine in hindsight what portion of its operating expenses may be associated with this event. Without adequate record-keeping, ratepayers may find themselves incurring these costs.

Q31. WHAT IS YOUR SPECIFIC ACCOUNTING RECOMMENDATION WITH RESPECT TO THE COSTS INCURRED RELATED TO THIS INCIDENT?

A31. The Commission should require the Company to track its incremental costs incurred as a result of the main break incident and the related class action lawsuit. These costs would include, but not necessarily be limited to, overtime pay and benefits for employees working on this situation, any third-party contractor costs incurred, incremental costs allocated or assigned from affiliates which are in any way related to this incident, as well as all legal costs incurred and any subsequent settlement or judgment in the litigation of the civil suit. These costs should be charged to a non-operating expense account.

SUSPENSION OF FURTHER CAPITAL RIDER SURCHARGE COSTS

Q32. WHAT IS YOUR RECOMMENDATION REGARDING FUTURE TAWC CAPITAL RIDERS SURCHARGE FILINGS?

A32. I recommend that upon resolution of the reconciliation in this Docket, all future TAWC Capital Riders surcharge filings should be suspended. The practical result of this recommendation is that the surcharges adopted in this Docket would continue to be charged until a Commission decision is rendered in the upcoming investigation into the TAWC Capital Riders surcharge pursuant to the Commission's decision in Docket No. 18-00120.

Q33. WHAT IS THE BASIS FOR YOUR RECOMMENDATION?

A33. There are two major factors supporting this recommendation. First, I believe significant modifications need to be made to the Capital Riders mechanism to ensure it is in the public interest. Suspending the current mechanism will encourage TAWC to cooperate in the expeditious resolution of that Docket. Moreover, this Commission should have the opportunity to determine the appropriate modifications to the Capital Riders prior to the Company submitting more filings based on the old method. Further, by the Company's own admission, it is earning in excess of its allowed rate of return. Rather than initiating a comprehensive rate filing, the Commission may address that issue through modification to the existing Capital Riders mechanism. As discussed in Docket Nos. 18-00022 and 18-00120, the Company's compensated Rate Base greatly exceeds its actual Rate Base. These two factors suggest there will be no undue harm to the Company from the suspension of further Capital Rider increases pending the resolution of the investigatory docket.

Second, another policy issue that should be considered before further increasing customer rates, is to evaluate whether the mechanism is truly providing benefits to customers in light of the recent customer outage. One component of the Capital Riders mechanism, the Qualified Infrastructure Investment Program Rider (QIIP), is designed to ensure system improvements are made which are necessary to maintain a quality system. I am not rendering an opinion on the Company's overall performance; however, with such a significant outage, the obvious question is whether ratepayers are truly realizing an appropriate level of service for their approximately $7 million in annual surcharge payments.

REPAIR DEDUCTION

Q34. WHAT IS THE REPAIR DEDUCTION AND HOW DOES IT IMPACT THE CAPITAL RIDERS CALCULATION?

A34. The Repair Deduction is an IRS tax deduction permitting a one-hundred percent write-off of qualifying costs on a utility's tax return related to certain system expenditures. This "expensing" for tax purposes is in contrast to the regulatory and financial accounting for these costs, which is to treat them as an asset. This difference in accounting applied for tax and regulatory purposes creates what is known as a book/tax timing difference, which produces a significant liability known as Accumulated Deferred Income Taxes. This liability represents funds that are provided by ratepayers to the Company for Income Tax costs which in theory would be paid to the IRS at some future (often distant) date. From a regulatory perspective, this liability represents customer supplied capital and as such is typically reflected as a reduction to Rate Base (as this portion of Rate Base is not financed by the Company and its shareholders but rather by ratepayers).

Q35. HAS THE COMPANY BEEN CONSISTENT IN ITS METHOD USED TO DETERMINE THE REPAIR DEDUCTION WITHIN THE CAPITAL RIDERS MECHANISM OVER TIME?

A35. No. The Repair Deduction first arose in Docket No. 18-00022. Prior to that time, the Company had ignored the impact of the Repair Deduction, to the benefit of shareholders and the detriment of ratepayers.[6] However, now that the Commission has ordered the consideration of the Repair Deduction within the ADIT computation, it is important to understand how these amounts were determined by the Company over the various Capital Riders filings. A review of the underlying support for the claimed Repair Deductions indicates the Company has utilized differing methods depending on the year. There has been no consistency in how the annual level of the Repair Deduction is determined on a year-to-year basis. This issue is somewhat complex because the Repair Deduction taken by the Company is not limited to qualifying Capital Riders investment; therefore, there is

[6] The Company testified that this Commission should not consider ADIT as an offset to Rate Base because the impact was "*de minimis*." *See* Rebuttal Testimony of Gary Verdouw, p. 20, lines 11-14, TPUC Docket No. 13–00130. The ADIT liability within the Capital Riders, which includes not only the Repair Deduction but Bonus Depreciation and Accelerated Tax Depreciation impacts, now totals approximately $9.8 million.

an assignment or allocation process that is required to arrive at the reasonable amount of Repair Deduction attributed to Capital Riders investment and to include within the surcharge calculation.

Q36. WHAT IS YOUR RECOMMENDATION REGARDING THE CALCULATION OF THE REPAIR DEDUCTION FOR PURPOSES OF COMPUTING THE CAPITAL RIDERS RECONCILIATION?

A36. I believe this is an issue that requires further study. Any modification to the amount of Repair Deduction assigned to Capital Riders investment necessarily modifies the remaining depreciable balance subject to accelerated tax depreciation. Therefore, any change to the Repair Deduction has implications on the more complicated tax depreciation analysis. For these reasons, I have not had an adequate opportunity to fully review this issue but wanted to identify it as a possible subject for consideration in future Capital Riders dockets.

Q37. DOES THIS TESTIMONY REPRESENT THE ENTIRETY OF THE MODIFICATIONS YOU BELIEVE TO BE NECESSARY TO ENSURE THE CAPITAL RIDERS MECHANISM IS IN THE PUBLIC INTEREST?

A37. No. I recommended several modifications to the Capital Riders mechanism in Docket No. 18-00120. I believe that absent meaningful changes to the current mechanism, ratepayers' interests are adversely impacted to the benefit of TAWC's shareholders. Because the Commission determined in Docket No. 18-00120 that an investigatory docket should be opened rather than addressing modifications within a Capital Riders tariff filing, I will not comment on further modifications that I believe are in the public interest at this time and will instead reserve my testimony for that docket. I am hopeful that the Company will work cooperatively with the Consumer Advocate and the Commission as we determine a way to ensure an appropriate streamlined mechanism and just and reasonable rates going forward.

Q38. DOES THIS CONCLUDE YOUR TESTIMONY AT THIS TIME?

A38. Yes. I reserve the right, however, to address any new information going forward provided by TAWC, including the filing of supplemental or rebuttal testimony.

Exhibit DND-1

David Dittemore

Experience

Areas of Specialization
Approximately thirty-years experience in evaluating and preparing regulatory analysis, including revenue requirements, mergers and acquisitions, utility accounting and finance issues and public policy aspects of utility regulation. Presented testimony on behalf of my employers and clients in natural gas, electric, telecommunication and transportation matters covering a variety of issues.

Tennessee Attorney General's Office; **Financial Analyst September, 2017 – Current**
Responsible for evaluation of utility proposals on behalf of the Attorney General's office including water, wastewater and natural gas utility filings. Prepare analysis and expert witness testimony documenting findings and recommendations.

Kansas Gas Service; **Director Regulatory Affairs 2014 – 2017; Manager Regulatory Affairs, 2007 - 2014**
Responsible for directing the regulatory activity of Kansas Gas Service (KGS), a division of ONE Gas, serving approximately 625,000 customers throughout central and eastern Kansas. In this capacity I have formulated strategic regulatory objectives for KGS, formulated strategic legislative options for KGS and led a Kansas inter-utility task force to discuss those options, participated in ONE Gas financial planning meetings, hired and trained new employees and provided recommendations on operational procedures designed to reduce regulatory risk. Responsible for the overall management and processing of base rate cases (2012 and 2016). I also played an active role, including leading negotiations on behalf of ONE Gas in its Separation application from its former parent, ONEOK, before the Kansas Corporation Commission. I have monitored regulatory earnings, and continually determine potential ratemaking outcomes in the event of a rate case filing. I ensure that all required regulatory filings, including surcharges are submitted on a timely and accurate basis. I also am responsible for monitoring all electric utility rate filings to evaluate competitive impacts from rate design proposals.

Strategic Regulatory Solutions; 2003 -2007
Principal; Serving clients regarding revenue requirement and regulatory policy issues in the natural gas, electric and telecommunication sectors

Williams Energy Marketing and Trading; 2000-2003
Manager Regulatory Affairs; Monitored and researched a variety of state and federal electric regulatory issues. Participated in due diligence efforts in targeting investor owned electric utilities for full requirement power contracts. Researched key state and federal rules to identify potential advantages/disadvantages of entering a given market.

MCI WorldCom; 1999 - 2000

Manager, Wholesale Billing Resolution; Manage a group of professionals responsible for resolving Wholesale Billing Disputes greater than $50K. During my tenure, completed disputes increased by over 100%, rising to $150M per year.

Kansas Corporation Commission; 1984- 1999

Utilities Division Director - 1997 - 1999; Responsible for managing employees with the goal of providing timely, quality recommendations to the Commission covering all aspects of natural gas, telecommunications and electric utility regulation; respond to legislative inquiries as requested; sponsor expert witness testimony before the Commission on selected key regulatory issues; provide testimony before the Kansas legislature on behalf of the KCC regarding proposed utility legislation; manage a budget in excess of $2 Million; recruit professional staff; monitor trends, current issues and new legislation in all three major industries; address personnel issues as necessary to ensure that the goals of the agency are being met; negotiate and reach agreement where possible with utility personnel on major issues pending before the Commission including mergers and acquisitions; consult with attorneys on a daily basis to ensure that Utilities Division objectives are being met.

Asst. Division Director - 1996 - 1997; Perform duties as assigned by Division Director.

Chief of Accounting 1990 - 1995; Responsible for the direct supervision of 9 employees within the accounting section; areas of responsibility included providing expert witness testimony on a variety of revenue requirement topics; hired and provided hands-on training for new employees; coordinated and managed consulting contracts on major staff projects such as merger requests and rate increase proposals;

Managing Regulatory Auditor, Senior Auditor, Regulatory Auditor 1984 - 1990; Performed audits and analysis as directed; provided expert witness testimony on numerous occasions before the KCC; trained and directed less experienced auditors on-site during regulatory reviews.

Amoco Production Company 1982 - 1984

Accountant Responsible for revenue reporting and royalty payments for natural gas liquids at several large processing plants.

<u>Education</u>

- B.S.B.A. (Accounting) Central Missouri State University
- Passed CPA exam; (Oklahoma certificate # 7562) – Not a license to practice

Tennessee Attorney General's Office - Consumer Advocate
Summary of TAWC Proposed Rider Charges
Docket 19-00031
As of 12/31/2018

Exhibit DND-2

Tennessee American Water Company Proposal
Reconciliation of the Calculation of Revenue Requirement

Line Number	Description	Qualified Infrastructure Investment Program QIIP Average YTD 12/31/2018 Actual	Budget	Variance	Economic Development Investment EDI Average YTD 12/31/2018 Actual	Budget	Variance	Safety and Environmental Compliance SEC Average YTD 12/31/2018 Actual	Budget	Variance	Total Average YTD 12/31/2018 Actual	Budget	Variance
1	Additions Subject to Rider:	$37,043,006	$34,471,184	$2,571,822	$1,285,890	$1,747,247	($461,357)	$25,776,252	$22,893,753	$2,882,499	$64,105,148	$59,112,183	$4,992,965
2	Plus: Cost of Removal less Salvage	4,572,046	5,315,317	(743,271)	933	1,262	(329)	2,927,298	2,676,731	250,568	7,500,278	7,993,310	(493,032)
3	Less: Contributions in Aid to Construction (CIAC)	2,293,497	493,440	1,800,058	31,700	3,845	27,855	0	0	0	2,325,198	497,284	1,827,913
4	Less: Deferred Income Taxes	5,828,886	281,920	5,546,966	190,955	26,904	164,051	3,824,037 (a)	532,977	3,291,060	9,843,878	841,801	9,002,076
5	Less: Accumulated Depreciation	1,681,625	1,849,125	(167,500)	37,852	42,678	(4,826)	1,409,092	1,142,221	266,871	3,128,569	3,034,023	94,546
6	Net Investment Supplied Additions:	$31,811,045	$37,162,017	($5,350,973)	$1,026,316	$1,675,082	($648,766)	$23,470,422	$23,895,285	($424,864)	$56,307,782	$62,732,385	($6,424,602)
7													
8	Pre-Tax Authorized Rate of Return:	8.45%	8.45%		8.45%	8.45%		8.45%	8.45%		8.45%	8.45%	
9	Pre-Tax Return on Additions:	$2,688,495	$3,140,730	($452,235)	$86,739	$141,569	($54,830)	$1,983,592	$2,019,499	($35,907)	$4,758,825	$5,301,798	($542,972)
10													
11	Depreciation Expense on Additions:	764,850	1,006,838	(241,988)	17,185	23,531	(6,346)	696,062	421,700	274,362	1,478,097	1,452,070	26,027
12													
13	Property and Franchise Taxes Associated:	448,094	441,677	6,417	17,370	23,590	(6,221)	322,199	288,397	33,802	787,662	753,665	33,997
14													
15	Revenues:	3,901,439	4,589,246	(687,807)	121,293	188,690	(67,397)	3,001,852	2,729,596	272,256	7,024,585	7,507,532	(482,948)
16													
17	Revenue Taxes	3.19%	3.19%		3.19%	3.19%		3.19%	3.19%		3.19%	3.19%	
18	Capital Riders Revenues with Revenue Taxes	4,030,038	4,740,516	(710,478)	125,291	194,910	(69,618)	3,100,799	2,819,569	281,230	7,256,128	7,754,994	(498,866)
19													
20	APP Revenue Reduction	(9,877)	(9,877)		(365)	(365)		(10,183)	(10,183)		(20,425)	(20,425)	
21													
22	Total Capital Riders Revenues with Revenue Taxes & APP	$4,020,160	$4,730,639	($710,478)	$124,927	$194,545	($69,618)	$3,090,615	$2,809,385	$281,230	$7,235,703	$7,734,569	($498,866)
23													
24													
25	Actual Capital Riders Revenues Billed		$4,284,542			$177,713			$2,752,446			$7,214,701	
26													
27	(Over)/Under Capital Riders Revenue Billings		446,096			16,833			56,939			519,868	
28	Budget to Actual Adjustment		(710,478)			(69,618)			281,230			(498,866)	
29	2017 Reconciliation Amount		547,960			(28,970)			(219,809)			299,181	
30	Earnings Test Adjustment		(442,512)			(18,354)			(284,276)			(745,142)	
31	Interest (Prime - 5.50%)		(4,371)			(2,753)			(4,563)			(11,687)	
32													
33	Reconciliation Amount		($163,305)			($102,863)			($170,478)			($436,646)	
34													
35	Authorized Capital Riders Revenues (9/12th)		$35,305,293			$35,305,293			$35,305,293			$35,305,293	
36													
37	Current Reconciliation Factor Percentage		-0.463%			-0.291%			-0.483%			-1.237%	
38													
39	2019 TCJA Savings Offset		0.463%			0.291%			0.483%			1.237%	
40													
41	Total Impact of 2019 Reconciliation Factor		0.000%			0.000%			0.000%			0.000%	

Explanation:
Tennessee American Water has been authorized 3 capital riders based on a 13-month average of in-service capital projects in the forecasted period. The revenue requirement for each rider is calculated similar to how total rate base is calculated by the Tennessee Public Utility Commission in a rate case. This table shows a comparison of the actual average over the reporting period to the proposed amount of each rider, and the total of the three.

*Taxes - From Docket #17-00124 which was approved on 4/9/2018.
Earnings Test - Calculation methodology from Docket #18-00022 and amount from Earnings Test workpaper

Tennessee Attorney General's Office - Consumer Advocate
Identification of Consumer Advocate Proposed Adjustments
Docket 19-00031
As of 12/31/2018

Exhibit DND-3

Line Number	Description	2018 Capital Rider Proposed by TAWC	To Remove Lobbying Costs from Operating Expenses	To Reflect the Income Tax Effect on the Earnings Test	Sum of CA Proposed Capital Rider Reconciliation
1	Additions Subject to Rider:	$64,105,148			$64,105,148
2	Plus: Cost of Removal less Salvage	7,500,278			$7,500,278
3	Less: Contributions in Aid to Construction (CIAC)	2,325,198			$2,325,198
4	Less: Deferred Income Taxes	9,843,878			$9,843,878
5	Less: Accumulated Depreciation	3,128,569			$3,128,569
6	Less: Retirements	0			$0
7	Net Investment Supplied Additions:	$56,307,782			$56,307,782
8					
9	Pre-Tax Authorized Rate of Return:	8.45%			8.45%
10	Pre-Tax Return on Additions:	$4,758,825			$4,758,825
11					
12	Depreciation Expense on Additions:	1,478,097			$1,478,097
13					
14	Property and Franchise Taxes Associated:	787,662			$787,662
15					
16	Revenues:	7,024,585			$7,024,585
17					
18	Revenue Taxes	3.19%			3.19%
19	Capital Riders Revenues with Revenue Taxes	7,256,128			7,256,128
20					
21	APP Revenue Reduction	(20,425)			(20,425)
22					
23	Total Capital Riders Revenues with Revenue Taxes & APP	$7,235,703			7,235,703
24					
25					
26	Actual Capital Riders Revenues Billed	$7,214,701			
27					
28	(Over)/Under Capital Riders Revenue Billings	519,868			519,868
29	Budget to Actual Adjustment	(498,866)			(498,866)
30	2017 Reconciliation Amount	299,181			299,181
31	Earnings Test Adjustment	(745,142)	(100,335)	(299,148)	(1,144,625)
32	Interest (Prime - 5.50%)	(11,687)		(10,985)	(22,672)
33					
34	Reconciliation Amount	($436,646)			(847,114)
35					
36	Authorized Capital Riders Revenues (9/12th)	$35,305,293			$35,305,293
37					
38	Current Reconciliation Factor Percentage	-1.237%			-2.40%
	Source:	TAWC Capital Rider Reconciliation File	CA Response 2-8	Exhibit DND-4	

Tennessee Attorney General's Office - Consumer Advocate
Calculation of Income Tax Effect on Earnings Test Adjustment
Docket 19-00031
As of 12/31/2018

Exhibit DND-4

Line No.	Item	Amount	%	Source
1	Excess Earnings Per Company	(745,142)		TAWC Capital Rider Reconciliation File
2	Plus: Lobbying Charged recorded as an Operating Expense	(100,335)		CA Response 2-8
3	Subtotal: Excess Earnings	(845,477)		Lines 1+2
4	Divided by Reciprocal Tax Rate (See Below)	73.865%		Line 12
5	Excess Earnings - Pre-Tax		(1,144,625)	Line 3/ Line 4
6	Additional Excess Earnings - Tax Gross-Up Calculation	(299,148)		Line 5 - Line 3
	Calculation of Tax Gross-Up Factor			
7	Tennessee State Tax		6.50%	
8	Reciprocal: Income Subject to Federal Tax (1-6.5%)	93.50%		1 - Line7
9	New Federal Tax Rate	21.00%		
10	Effective Federal Tax Rate		19.635%	Line 8 * Line 9
11	Composite Income Tax Rate		26.135%	Line 7 + Line 10
12	Reciprocal Tax Rate		73.865%	1 - Line 11

AMERICAN WATER

Highly *Fragmented* Water Industry Creates Opportunity

Industry opportunity

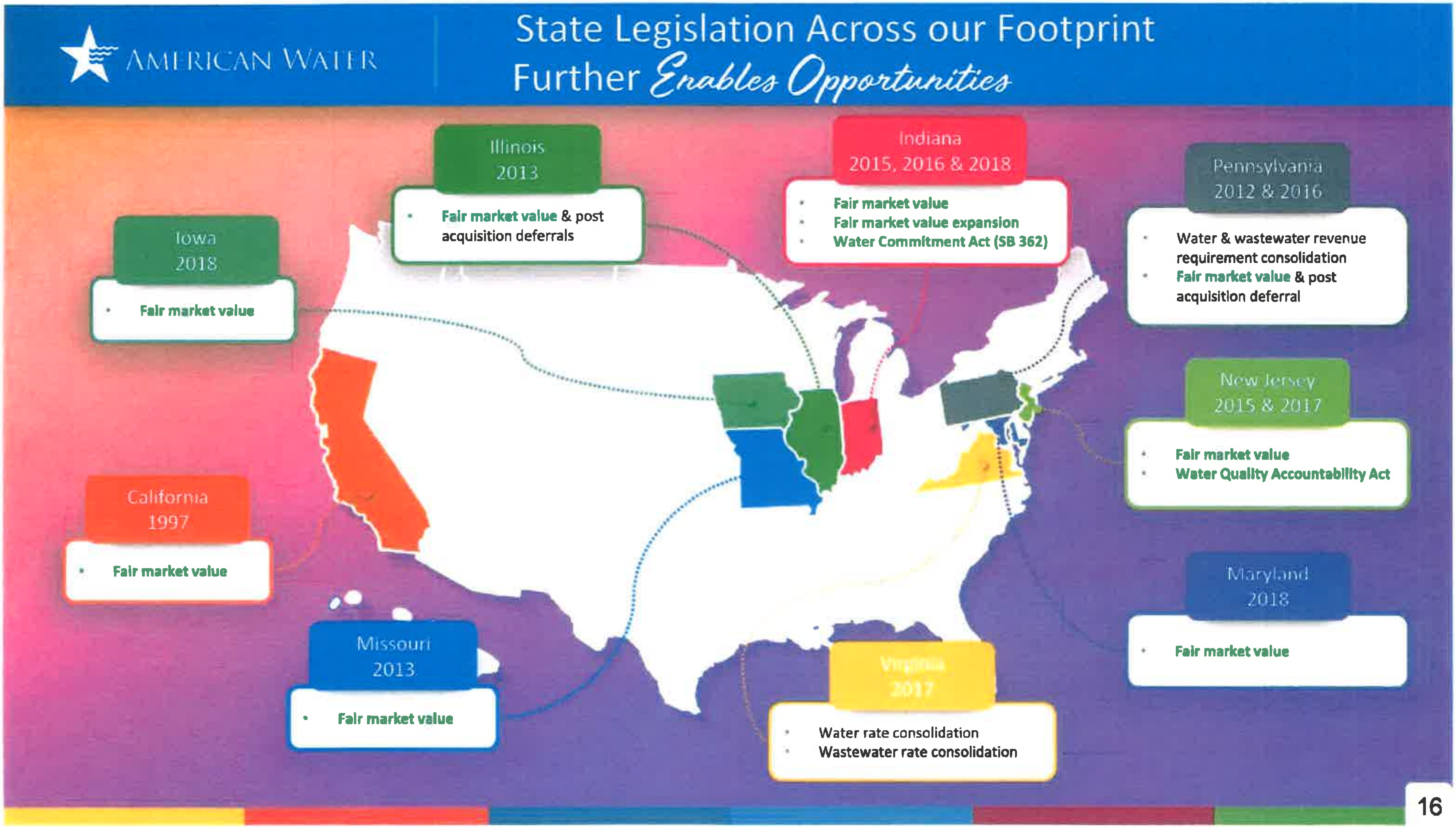
		Wastewater	
	Investor owned	**2%**	Investor owned
	Public & other	**98%**	Public & other

American Water footprint

- Ideal fit for industry consolidation opportunities
- Target 3K-30K customer connections per acquisition
- Wastewater focus (AWK customer connections mix – 94% water & 6% wastewater)

Water Utilities Source: EPA SDWIS Federal Reports Search
www3.epa.gov/enviro/facts/sdwis

Attachment 2




AMERICAN WATER
We actively pursue acquisitions using a Disciplined Approach
More than 50,000 Community Water & about 15,000 Wastewater Systems*
Regulatory & Legislative climate
Opportunities over 5 years ≈500,000
10,000 systems serving > 3,000 customers
American Water Acquisitions**
From 2015-2019
65*** closed deals in
10 states
≈110,000 Customer connections
17