



Agenda Date: 12/17/14

Agenda Item: 1C

STATE OF NEW JERSEY
Board of Public Utilities
44 South Clinton Avenue, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350
www.nj.gov/bpu/

AUDITS

IN THE MATTER OF A COMPREHENSIVE)
MANAGEMENT AUDIT OF NEW JERSEY AMERICAN)
WATER COMPANY PURSUANT TO N.J.S.A. 48:2-16.4)
AND N.J.A.C. 14:3-12.1) ORDER OF
IMPLEMENTATION
DOCKET NO. WA09070510

Parties of Record:

Michael Sgro, Esq., Vice President, General Counsel and Secretary, New Jersey American Water Company, Inc.

BY THE BOARD:¹

At its agenda meeting of July 29, 2009, the New Jersey Board of Public Utilities ("Board" or "BPU") authorized staff of the Audits Division ("Staff") to initiate a comprehensive management audit ("Audit") of New Jersey American Water Company ("NJAWC" or "Company"). NJAWC, the largest privately owned water utility in New Jersey, employs 912 employees and serves approximately 610,000 customers in New Jersey. This assignment included a comprehensive management audit of NJAWC's major organizational areas with an examination of executive management and corporate governance, organizational structure, human resources, strategic planning, system operations, customer service, external relations, support services, finance and cash management, accounting, property records and budgeting, affiliates cost allocations and relationships, and company contractor performance. The Board also authorized Staff to send a request for proposal ("RFP") to the five pre-approved management consulting firms under State Term Contract T2482.

In accordance with the RFP, bid proposals were submitted to the Board's Audits Division by September 11, 2009 by The Liberty Consulting Group ("Liberty"), NorthStar Consulting Group ("NorthStar"), PMC Management Consultants ("PMC") and Schumaker and Company ("Schumaker"). The fifth firm, Overland Consulting, advised Staff, in writing that, due to the ongoing audit of Public Service Electric and Gas Company, the firm decided not to bid on this project. The bid proposals were subsequently forwarded to the Evaluation Committee for

¹ President Richard S. Mroz and Commissioner Upendra J. Chivukula recused themselves due to a potential conflict of interest and as such took no part in the discussion or deliberation of this matter.

review and analysis. The Evaluation Committee consisted of staff members from the Audits Division (2), the Division of Water (2), and Counsel's Office (1).

At its November 10, 2009 agenda meeting, the Board approved the Evaluation Committee's recommendation of NorthStar to perform the audit at a not-to-exceed cost of \$444,825. The Board also authorized then President Fox to execute the Consulting Agreement with NorthStar.

The Audit began on January 12, 2010, and was conducted in three phases: 1) Orientation and Planning, 2) Technical Review, and 3) Report Development. The Orientation and Planning phase of the Audit was initiated on the Company's property with a comprehensive presentation by key management of the Company detailing its organization and operations. During the Technical Review phase, NorthStar conducted its principal investigation where 434 data requests were propounded on the Company and answered, 117 interviews with Company personnel were conducted and other technical review activities performed focused on substantive issues for each of the twelve audit areas. At the request of the Division of Rate Counsel ("Rate Counsel"), its consulting engineer, Howard J. Woods, Jr., P.E., met with representatives of Staff, NJAWC and NorthStar on May 12, 2010 to discuss issues of concern to Rate Counsel.

A comprehensive review of the twelve initial task reports of NorthStar ensued and detailed comments were received from across the Company and incorporated into the task reports. On August 19, 2010, NJAWC completed its factual review and verification of the twelve draft audit task reports and submitted its critique of any factual discrepancies to Staff and NorthStar.

On September 3, 2010, NJAWC advised NorthStar of certain areas of the draft audit reports it would like to discuss before the report was finalized. A meeting was held at the BPU in Newark, New Jersey on September 23, 2010, with Staff, NorthStar and NJAWC to review selected comments in an effort to move forward towards finalizing the report. On October 21, 2010, NorthStar sent a proposed final draft audit report to NJAWC for review. On November 5, 2010, NJAWC provided NorthStar with a markup of the final draft report containing all the proposed changes NJAWC recommended based on the September 23, 2010 meeting. On November 9 and 10, 2010, NJAWC identified to NorthStar those report sections containing what the Company considered to be confidential or otherwise sensitive business information.

On December 2, 2010, NJAWC provided NorthStar with another markup of the draft audit report, again showing the changes that it believed were warranted based on the discussions at the September 23, 2010 meeting between NorthStar and Staff. On December 8, 2010, NJAWC conducted a teleconference with NorthStar and Staff to review the markup of the draft audit report, including those findings and recommendations NJAWC still considered problematic.

At the Board meeting on February 10, 2011, NorthStar's Final Audit Report ("Final Report") was accepted "for filing purposes only," and interested parties were provided with the opportunity to file comments on the report. The Final Report consisted of fourteen (14) chapters including an executive summary. The Final Report contained 55 recommendations. NorthStar assigned a "priority ranking" for each of its recommendations based on what NorthStar determined was their importance to ratepayers. Out of the fifty-five recommendations, forty-four were ranked "A" or "B". According to NorthStar, recommendations ranked "A" or "B" when implemented should provide significant benefits to ratepayers in terms of reduced costs and/or improved service. NorthStar therefore suggested these priority recommendations be addressed by NJAWC as soon as practical.

Findings from the Audit are to be used by the Board to order the Company to adopt new and altered practices and procedures as the Board shall find necessary to promote efficient and adequate service to meet the public convenience and necessity pursuant to N.J.A.C. 14:3-12.4. By this Order, the Board determines whether to accept the conclusions of the Final Report and direct implementation of its recommendations.

GENERAL SUMMARY OF COMMENTS

By letter dated March 11, 2011, Rate Counsel indicated that it had reviewed NorthStar's Final Report and agreed with the majority of the conclusions and recommendations therein. Rate Counsel noted the Final Report identified substantial problems within NJAWC's organization that significantly impact how NJAWC carries out its statutory duty to provide safe, adequate and proper service to ratepayers at the lowest possible cost. In particular, Rate Counsel expressed serious concerns regarding what NorthStar reported about the financial relationship between NJAWC and American Water Works Service Company ("AWWSC" or the "Service Company"), which provides services to NJAWC pursuant to a Service Company Agreement approved by the Board on August 21, 1989 (Docket No. WE98030322). Rate Counsel's comments stated "[h]aving affiliates perform services for a regulated utility without competitive formal agreements or in compliance with its own procurement policy creates concerns about inherent conflicts of interest, procurement practices and cross—subsidization."²

Another area of concern to Rate Counsel was NorthStar's conclusion that the Company lacked "a strategic plan that includes consideration of rate effects and impacts on NJAWC ratepayers." Rate Counsel agreed with NorthStar's statements in its Executive Summary of the Final Report that it is problematic that the "mission statement" of American Water Works, Inc., and the strategic planning process of NJAWC do not directly address the cost of services to customers or the impact on ratepayers.³ Rate Counsel also felt that NorthStar raised the critical issue that "the effect on ratepayers (and by extension the timing and frequency of rates cases) may not be fully incorporated into NJAWC's decision-making process."⁴ NorthStar noted that "NJAWC is aware that rates will be increasing, but nowhere is there evidence of a focus on consideration of rate impacts in decision making, or a drive to mitigate rate impacts."⁵ Rate Counsel strongly believes that Company decision making regarding investments and operations must take into account the impact on ratepayers.

Rate Counsel found considerable merit in NorthStar's recommendation that NJAWC "[d]evelop effective service level agreements to cover services provided by affiliates to NJAWC."⁶ Rate Counsel commented that the Final Audit Report correctly noted that NJAWC has the highest water rates among the Class A water utilities in New Jersey. While several possible causes for this were suggested in the Audit, it has not gone unnoticed by Rate Counsel that the Audit identified several areas where affiliate relationships may not afford proper protection to New Jersey ratepayers.

This appears to be a significant issue with regard to the services provided by AWWSC. As commented by Rate Counsel, "NorthStar reported in its findings that NJAWC does not have effective service level agreements to ensure that it has control of the costs and quality of

² Rate Counsel's Comments, letter dated March 11, 2011, at 2.

³ Ibid.

⁴ Ibid.

⁵ Id. at 9

⁶ Id. at 6

services it receives from AWWSC. More alarming to Rate Counsel is the fact that NJAWC does not make effective challenges to AWWSC budgets or the costs of AWWSC services. Moreover, there are limited opportunities for NJAWC to "push back" on services or cost assignments from AWWSC. Rate Counsel generally concurs with the various recommendations NorthStar has made to reduce costs to NJAWC.⁷ Rate Counsel "finds considerable merit in NorthStar's recommendation that NJAWC [d]evelop effective service level agreements to cover services provided by affiliates to NJAWC."⁸ Rate Counsel "recommends that the Board adopt NorthStar's recommendations and order the Company to determine the value of services received from AWWSC, and optimize and control costs."⁹

In its reply, the Company expressed serious concerns with many of the findings, conclusions and recommendations in the Final Report, noting that it was unable to fact-check the document due to a lack of citation or attribution in the report. The Company felt that NorthStar's commentary in the report was unfair; that in many cases the findings were simply inaccurate; and that the Executive Summary of the report, in particular, was "highly critical and unfairly negative" in a way that is not reflective of the actual, substantive recommendations made by NorthStar.¹⁰ However, the Company stated that despite its serious concerns with the factual basis of the report and its "unfairly negative and unbalanced"¹¹ presentation, the Company elected to forego further comments on the specific findings and conclusions that were not tied to a specific recommendation.¹²

The Company responded to the specific recommendations made by NorthStar and provided further commentary on various statements made within the Final Report. The Company concurred with the majority of the 55 recommendations contained in the Final Report, and indicated that it had, in fact, already complied with or otherwise implemented several of the suggested measures and procedures, and had begun implementing many others. As summarized in the Audit Recommendation and the Party Position section of this Order, the Company ultimately agreed to implement, in whole or in part, 52 of the 55 recommendations.

Below is a detailed discussion of the comments filed by the Company and Rate Counsel as they relate to specific NorthStar recommendations. Additionally, the position of Staff is stated with respect to each of the audit recommendations that the Company did not initially agree to implement.

Section III - Executive Management and Corporate Governance

Recommendation III-1 Revise AWK's ("American Water Works Company") and NJAWC's long-term corporate objectives and strategies to make them more explicit relative to their responsibilities to meet the future needs of NJAWC ratepayers relative to the cost of water. (Refers to Findings III-1, VI-3, VI-6 and VI-7)

The Company conceptually accepted this recommendation in part as it applies to NJAWC, and rejected this recommendation as it applies to AWK stating that the companies are two separate corporate entities and as such, have separate corporate objectives and strategies.

⁷ Rate Counsel's Comments, March 11, 2011, at 6-7.

⁸ *Id.* at 6

⁹ *Id.* at 7

¹⁰ NJAWC Audit Report Response, Part 1 of 2, March 11, 2011, at 5.

¹¹ *Id.* at 4

¹² *Ibid.*

NorthStar found that the corporate level mission statement and associated strategies and goals are appropriate to both its regulated subsidiaries and its non-regulated operations. According to NorthStar, there is no conflict between regulated and unregulated operations at the mission/vision goal level.

Staff agrees with NorthStar's finding that NJAWC's mission of creating sustainable water solutions and its strategies made no mention of cost, even value of service, to the customers. Also none of the ten "Key Elements" supporting NJAWC's new strategic initiatives specifically address cost to the customer. Staff agrees with the Company that this recommendation should be implemented only as it applies to NJAWC. Rate Counsel did not take a position on this specific recommendation.

Recommendation III-2 Expand the number of KPIs [key performance indicators] to track performance and to address all NJAWC corporate goals. (Refers to Finding III-2)

NJAWC conceptually accepted this recommendation, stating that it is in the process of refining and aligning its goals, measures and targets across the business with corporate strategies and objectives.

Recommendation III-3 Expedite the requirement that all independent AWK board of directors ("BOD") members own a minimal number of AWK shares within a reasonable period of their joining the BOD. (Refers to Finding III-5)

NJAWC rejected this recommendation, stating that it does not apply to NJAWC and that this recommendation is not properly within the scope of the Audit as it recommends structural changes within the parent company that have no bearing on the operation or governance of the Company. NJAWC went on to state that the report fails to recognize that NJAWC and the parent company AWK (American Water) are two distinct and separate entities.

Staff agrees with NJAWC that this recommendation does not apply. Rate Counsel did not take a position on this specific recommendation.

Recommendation III-4 Add a member to AWK's Board of Directors who has extensive experience in operating a utility in New Jersey or extensive experience in New Jersey utility regulation who would represent the interests of NJAWC ratepayers. (Refers to Finding III-6)

NJAWC rejected this recommendation because the Company believes both its board and the AWK board are made up of members who have knowledge, experience and skills to provide high quality corporate governance. The Company also believes the recommendation is inconsistent with applicable securities laws and in conflict with a Board member's legal and fiduciary duties to the parent company shareholders.

NorthStar finds that none of the members of AWK's BOD has extensive utility regulatory or utility operating experience in New Jersey. Since NJAWC provides about 25 percent of AWK's operation revenues, Staff agrees with NorthStar that NJAWC ratepayers should have at least one member of the AWK BOD who is knowledgeable about operating a utility in New Jersey and can serve as an advocate, and Staff recommends that NorthStar's recommendation be taken into consideration.

Rate Counsel did not take a position on this specific recommendation.

Recommendation III-5 Consider adding a second member of senior management to the AWK BOD. (Refers to Finding III-6)

NJAWC accepts the concept of this recommendation, despite the fact that adding company management to the board of directors of a publicly traded company is contrary to best practices and in opposition to the direction most corporations are heading, and despite the fact that Company believes that this recommendation, directed as it is at AWK, is not properly within the scope of the Audit. The Company disagrees with the premise of NorthStar's finding III-6, relating to the composition of the AWK BOD, that only a person who has worked for a New Jersey utility can bring the appropriate perspective and experience to the AWK Board.

The CEO is the only member of senior management on the AWK BOD. Staff agrees with NorthStar that the BOD may benefit from having a second member of senior management in its membership to assure that it has the input from two members of senior management on strategic issues and can be useful in the planning for management succession. Rate Counsel did not take a position on this specific recommendation.

Recommendation III-6 Conduct the quarterly Business Performance Report meetings and the NJAWC quarterly Board of Directors Meeting simultaneously. (Refers to Finding III-8)

The Company rejected this recommendation. The Company states that it continually looks to conduct critical business meetings in the most efficient manner possible. However, the two meetings referred to in the above recommendation are each substantial time commitments in their own right. The meeting agendas are typically full with little commonality. The Company noted that implementation of this recommendation was a physical impossibility.

Staff agrees with the Company's position in terms of possible disruption to the business and difficulty in coordinating the schedules of such a large number of senior management on a regular basis. Rate Counsel did not take a position on this specific recommendation.

Recommendation III-7 Develop effective service level agreements to cover services provided by affiliates to NJAWC. (Refers to Findings III-9, IV-7, V-1, X-1 and XIII-6)

NJAWC conceptually accepted this recommendation. It is the Company's position that NJAWC has agreements with affiliates, and those agreements have been reviewed and approved by the BPU as required by statute. Those agreements include the BPU-approved agreement between NJAWC and AWWSC.¹³ NJAWC accepts the concept of using service measures and targets to track and measure whether appropriate value is received.

Rate Counsel found significant merit in NorthStar's recommendation that NJAWC develop effective service level agreements for services provided by affiliates to NJAWC. NorthStar notes that NJAWC has the highest water rates among the Class A water utilities in New Jersey. While several possible causes for this are suggested in the Audit, Rate Counsel believes that the Audit identified several areas where affiliate relationships may not afford proper protection to New Jersey ratepayers. This appears to be a significant issue with regard to the American Water Works Service Company ("AWWSC"). NorthStar in its findings reported that NJAWC did

¹³ The Service Company Agreement is the subject of a pending petition for reapproval by the Board, in Docket No. WO13050474.

not have effective service level agreements to ensure that it has control of the costs and quality of services it receives from AWWSC. Also, NorthStar found that NJAWC did not make effective challenges to AWWSC budgets or the costs of AWWSC services. Additionally, there are apparently limited opportunities for NJAWC to "push back" on services or cost assignments from AWWSC. Rate Counsel agrees with the various recommendations NorthStar has made to reduce costs. Rate Counsel recommends that the Board adopt NorthStar's recommendations and order the Company to determine the value of services received from AWWSC, and optimize and control costs.

NorthStar found that NJAWC did not have effective service level agreements ("SLAs") to ensure that the Company has control over costs and quality of services from affiliates like AWWSC. NorthStar also found that SLAs do not exist or are lacking in necessary detail for most support services being provided to NJAWC by AWWSC. Where an agreement does exist, the agreement for support services doesn't cover all of the services normally identified as support services.

The Company adopted a new Business and Accounting Manual in 2014 that the Company maintains reflects the many enhancements achieved by the business since 2010, as well as the benefits of the Company's new SAP system. The Company's current policies and practices are adequate, and the recovery of Service Company costs is always subject to Board scrutiny in base rate proceedings. Staff believes that no further action is required to achieve the objectives of this recommendation.

Section IV - Organization Structure

Recommendation IV-1 Develop a clear and consistent policy for defining the administrative and functional responsibilities of NJAWC and AWWSC officers and senior management. (Refers to Finding IV-2)

The Company disagrees with NorthStar's finding which states that AWK does not have a clear and consistent policy for defining the administrative and functional responsibilities of NJAWC and AWWSC officers and senior management. The Company states that it has undertaken a number of structural and organizational changes since 2010 that have enhanced the effectiveness of its management structure.

NorthStar found that while NJAWC is a separate legal entity, certain of its organizational resources and managerial positions of responsibility are integrated with AWWSC. Also, while most of the NJAWC senior management report administratively and functionally to the NJAWC president, some report only functionally to him and administratively to an AWWSC officer.

The Company has undertaken a number of structural and organizational changes since 2010 that the Company maintains have enhanced the effectiveness of its management structure. Staff has determined, based on its review of the additional information that the Company's current structure, policies and practices are adequate and no further action is required to achieve the objectives of this recommendation. Therefore, Staff supports the Company's position. Rate Counsel did not take a position on this specific recommendation.

Recommendation IV-2 Develop policies and procedures that address affiliate relationships covering topics that include:

- **Compliance with regulatory requirements**
- **Tariff transactions between affiliates**
- **Discriminatory practices among affiliated and non-affiliated companies**
- **Confidential information transfers between NJAWC and its affiliates**
- **Contracts for products and services between NJAWC and its affiliates**
(Refers to Findings IV-3 and VIII-17)

NJAWC conceptually accepts the general intent, but does not accept the exact wording or scope of the recommendation. Based on the Company's interpretation of the above recommendation, in most cases there are specific policies and procedures in place already that cover the activities described above.

Rate Counsel addressed this recommendation and agrees with NorthStar that the legal entitlement and nature of NJAWC's affiliate relationships are prescribed by N.J.S.A. 48:3-7 which mandates generally that contracts involving the expenditures of a sum exceeding twenty-five thousand dollars, made by any public utility and an affiliate owning, holding, controlling five percent or more of the capital stock of the utility shall be submitted to the Board for approval. To the extent affiliate relationships exist but the Board either has not approved an agreement, or the agreement has been deemed by NorthStar to be inadequate, Rate Counsel recommends that the Board order NJAWC to submit adequate affiliate agreements for review as soon as possible.

NorthStar found that NJAWC did not have policies and procedures that dealt with affiliate relationships or transactions. NorthStar identified nine agreements between NJAWC and its affiliates which may have required BPU approval but found the Company only had actual records of approvals or dates of approvals for only two of the nine contracts. N.J.S.A. 48:3-7.1 requires Board approval of certain contracts between a public utility and its parent or affiliates to ensure that the contracts conform to the law and that the prices charged are fair.

The Company has undertaken a number of structural and organizational changes since 2010 that the Company maintains have enhanced the effectiveness of its management structure. The Company also convened a Policy Review Project, which was made up of a team of business leaders from across the enterprise and led by the General Counsel for the Northeast Division of AWK, which includes NJAWC. The Policy Review Project team updated and streamlined many policy and practice documents, and the Company asserts that the improvements to the policy and practice review recommended by the Project team are embedded in the business. Staff agrees that based on these changes, the Company's current structure, policies and practices are adequate and no further action is required to achieve the objectives of this recommendation.

Recommendation IV-3 Obtain any required BPU approvals of all contract agreements between NJAWC and affiliate entities. (Refers to Finding IV-4)

NJAWC believes it has obtained timely BPU approval, as needed, for contracts between NJAWC and other affiliate entities. NJAWC believes it complies with all statutory and regulatory laws and rules relating to agreements with its affiliate entities.

NorthStar found a number of functions performed by AWWSC for the regulated business segments were not specifically identified within the contract agreement. The services are not specifically identified in the NJAWC/AWWSC contract and are provided as "such other services as Water Company and Service Company may agree."¹⁴ Rate Counsel agrees with NorthStar that the BPU has not approved provision of these additional services. Rate Counsel agrees that NorthStar's recommendation be implemented as written.

Subject to the Board's review of the Company's pending petition for approval of its Service Company Agreement in Docket No. WO13050474, Staff has concluded that no other agreements between NJAW and any affiliate require any further action by the Board. Staff believes that no further action is required for this recommendation at this time.

Recommendation IV-4 Obtain competitive bids for services provided by AWWSC. (Refers to Findings IV-5, IV-6, and XIII-7)

NJAWCC rejects this recommendation to the extent it calls for competitive bidding for the entire AWWSC contract, or alternatively for every function and service provided by the Service Company to be separately bid competitively. According to the Company, an attempt to competitively bid a majority of the AWWSC activities would not be feasible or cost-effective.

The Company asserts that it utilizes competitive bidding when appropriate and when required by statute, regulation or other governmental mandate.

NorthStar found that NJAWC did not obtain competitive bids for services provided by AWWSC, and NJAWC did not make effective challenges to AWWSC budgets or charges for services. Most of the service contracts between NJAWC and its affiliates did not have termination dates and no term limit was indicated. NorthStar determined that the services provided via AWWSC agreements were not competitive in terms of "market conditions" and a potential for "cross-subsidization" between NJAWC and its affiliates exists.

Rate Counsel agrees with NorthStar's recommendation that NJAWC obtain competitive bids for affiliate service activity. In addition Rate Counsel agrees with the approach but also thinks it is important to consider the size of NJAWC and evaluate the benefit of providing some of the services internally. Staff agrees with NJAWC that it would not be cost effective to obtain competitive bids for all service company activities. Staff recommends that the Company continues, as it claims to be currently doing, to utilize competitive bidding when appropriate or required by statute, regulation or other governmental mandate.

The Company has undertaken a number of structural and organizational changes since 2010 that the Company maintains have enhanced the effectiveness of its management structure. Staff has concluded that the Company's current structure, policies and practices are adequate to ensure that customers are receiving cost-effective service. All of the costs associated with the services provided by the AWWSC are subject to the ongoing review and approval of the Board in base rate proceedings. The Company currently utilizes competitive bidding effectively, where appropriate. Based on these changes, Staff has determined that no further action is required to achieve the objectives of this recommendation.

¹⁴ NorthStar's NJAW Final Audit Report, December 12, 2010, Findings and Conclusions IV-4.

Recommendation IV-5 Have the Internal Audit director report administratively to a senior officer other than the CFO and strengthen the Internal Audit function. (Refers to Findings IV-8, IV-9 and IV-10)

NJAWC partially accepts and partially rejects this recommendation, in part because the Company believes the recommendation fails to draw the distinction between NJAWC and the parent company.

NJAWC disagrees with NorthStar's finding IV-8 which states that the administrative reporting relationship of the AWK Internal Audit director to AWK's chief financial officer is not appropriate. The Company respectfully declined to make any changes to the existing reporting relationship.

NorthStar's concern was that the "Internal Audit function reports administratively to AWK's chief financial officer ("CFO") who performs the annual performance review of the Internal Audit director. The Internal Audit function is therefore not independent of its major audit focus areas of finance and accounting. A potential conflict of interest exists because the internal audit director cannot be expected to perform independent reviews of operations that report to the person responsible for performing his performance review."¹⁵

The Company has undertaken a number of structural and organizational changes since 2010 that the Company maintains have enhanced the effectiveness of its management structure, including the effectiveness of the Internal Audit function. Based on its review, Staff has determined that there is no basis for the Board to require the Company to change the administrative reporting relationship between the Internal Audit function and the CFO, so that portion of the recommendation is rejected. The Company's current structure, policies and practices appear to be adequate, and Staff has concluded that no further action is required to achieve the objectives of this recommendation.

Rate Counsel did not take a position on this specific recommendation.

Recommendation IV-6 Determine if NJAWC ratepayers have paid for the Sarbanes-Oxley Act of 2002 ("SOX") compliance and testing that was disallowed as a condition of the RWE Rate Order. (Refers to Finding IV-13)

NJAWC accepts this recommendation and believes the determination that customers have not paid any inappropriate SOX costs has been made in prior rate proceedings.

SOX is a piece of legislation created for the purpose of protecting investors from accounting fraud, specifically those that are related to shares sold by publicly traded companies. SOX mandates strict reforms with regards to how corporations make financial declarations. The law mandates increased vigilance with regards to disclosures related to the financial state of a company, particularly when it comes to earnings and profitability.

NorthStar found that "the initial development and implementation of the SOX compliance program were not part of the revenue requirements and thereby were not funded by ratepayers of NJAWC. NJAWC could not explain how the internal control and remediation initiatives were determined to be complete. Given the high level of urgency during 2009 to achieve year-one compliance, these costs appear to be initial internal control and remediation activities."¹⁶

¹⁵ NorthStar's NJAW Final Audit Report, December 12, 2010, Findings and Conclusions, IV-8.

¹⁶ Audit Report, December 12, 2010, Findings and Conclusions IV-13

The Company states that it has not sought recovery of any SOX startup costs in any rate proceeding or other proceeding. Consistent with the Board's Order,¹⁷ NJAWC represents that it will not request recovery of any of these costs from customers. NJAWC performed a review of all rate case documents and orders entered since the above captioned Board Order showing that the Company has not requested recovery of these costs, nor have any of these costs been included in the revenue requirement calculation supporting the rates charged to customers pursuant to the BPU Orders in its base rate proceedings.

Rate Counsel agrees with NorthStar that if it is determined that NJAWC customers paid for SOX compliance and testing expenses that were disallowed by the Board in the RWE divestiture proceeding, the Company should be directed by the Board to determine the exact amount of SOX expenses paid by customers and refund to customers any amounts improperly included in rates in Docket WR08050210 or any subsequent proceedings.

Board Staff agrees with Rate Counsel's position that if NorthStar's claim that NJAWC customers may have paid for SOX compliance and testing expenses that were disallowed by the Board in the RWE divestiture are determined to be true, the Company should be directed by the Board to determine the exact amount of SOX expenses paid by customers and refund to customers any amounts improperly included in rates in Docket WR08050210 or any subsequent rate proceeding.

Section V - Human Resources

Recommendation V-1 Continue to negotiate the elimination of substantial sick banks which have accrued under prior union employee benefits programs and replace them with short-term disability insurance. (Refers to Finding V-7)

The Company accepts this recommendation, but notes that it is required to bargain in good faith with its collective bargaining units. Good faith requires that the Company approach the negotiations without pre-judging any particular issue or outcome. In recent negotiations, the Company and two of its unions have agreed to replace sick banks with an alternative. This was done prior to the start of the Audit, and the Company intends to continue to approach the ongoing negotiations in good faith.

Rate Counsel did not take a position on this specific recommendation. Staff recognizes the Company's obligation to negotiate in good faith with its unions but supports NorthStar's recommendation to the extent that this would result in cost savings for ratepayers.

¹⁷ Board's Order in WM06050388, In the Matter of the Joint Petition of Thames Water Aqua Holdings on Behalf of Itself and its Parent Company, RWE, Thames Water Aqua US Holdings, Inc. Thames Water Holdings, Inc., American Water Works, Inc., Thames Water Holdings, Inc., E'Town Corporation, NJ-American Water Company, The Mount Holly Water Company, and Applied Wastewater Management, Inc. for Approval of a Proposed Transaction Involving, Among other Things, the Sale by Thames Aqua Holdings of Up to 100% of the Shares of the Common Stock of American Water Works Company, Inc. in One or More Public Offerings - Proposed Settlement and Stipulation, June 14, 2007.

Recommendation V-2 Continue steps to improve succession planning, professional development and performance review processes. (Refers to Finding V-9 and V-10)

The Company accepted this recommendation. Rate Counsel did not provide specific comments on this section. Staff supports NorthStar's recommendation as written.

Recommendation V-3 Develop and implement processes for determining appropriate staffing requirements, spans of control and layers of management. (Refers to Finding V-11)

The Company accepted this recommendation. Rate Counsel did not provide specific comments on this section. Staff supports NorthStar's recommendation as written.

Section VI - Strategic Planning

Recommendation VI-1 Continue the implementation of the Value Delivery Strategy ("VDS") process, including completing the risk and gap analysis, developing a prioritization process, building action plans and fully linking the VDS to the budgeting process, KPIs and performance goals for NJAWC. (Refers to Findings VI-1, VI-4, VI-5 and VI-8)

The Company accepted this recommendation. The Company reported that it began the development of its Value Delivery Strategy approximately six months or more prior to the commencement of the Audit. The Company represents that it has invested a significant amount of time and effort into the development and implementation of the VDS. This effort includes extensive stakeholder outreach, which commenced at the start of the process and will be repeated periodically in the future. The level of effort and cost involved in developing and implementing a successful corporate strategy is not "nominal" in any sense. The Company states it has a substantial process in place to ensure that the VDS is comprehensive, that all functions are involved, and that goals, objectives, measures and performance indicators are aligned throughout the organization and consistent with corporate goals and the needs of the business. A key element of the VDS is ensuring the delivery of high value water and wastewater service to customers.

Rate Counsel's comments on this issue agree with NorthStar's statement that "NJAWC is aware that rates will be increasing, but nowhere is there evidence of a focus on consideration of rate impacts in decision making, or a drive to mitigate rate impacts." ¹⁸ Rate Counsel finds this is a core issue with this Company, and it is paramount to customers that a focus on rates must be incorporated into every level of planning and operations throughout the organization. While there is no specific recommendation regarding this issue, Rate Counsel also believes this must be part of the recommendations regarding the VDS process and in particular, implementation of Recommendations 1, 3 and 5 on page VI- 17 of the Final Report. Staff supports NorthStar's recommendation as written.

Recommendation VI-2 Link New Jersey consumer and public education messages to align with VDS goals. (Refers to Finding VI-9)

The Company accepted this recommendation.

¹⁸ Rate Counsel's Comments, March 11, 2011, at 9.

Recommendation VI-3 Link employee engagement and training, and other human resources activities with the VDS goals. (Refers to Finding VI-10)

The Company accepted this recommendation.

Recommendation VI-4 Revise the AWK treatment of Business Development (BD) costs to an "as requested/fee" basis, and consider using non-AWK providers of training and other Business Development services. (Refers to Finding VI-11)

The Company conceptually accepted this recommendation.

The Company represents that it will investigate alternatives to its current approach of allocating Business Development ("BD") costs. The Company notes, however, that its current approach to allocating BD costs was selected because it is highly conservative and because much of the work associated with developing new business precedes a determination as to whether or not the ultimate customer is served by the regulated utility business or the nonregulated side of the business. The Company feels its existing approach provides customers with ample assurance that such costs are being fairly apportioned. NJAWC will continue to use outside vendors for training, education and other services when appropriate and cost effective, consistent with this part of the recommendation.

NorthStar found that AWK business development efforts are of minimal value to NJAWC ratepayers; therefore, Staff supports the Company's position. Rate Counsel did not provide specific comments on this section.

Recommendation VI-5 Modify the KPIs for NJAWC to reduce redundancies, focus on controllable activities and clearly link with the VDS process and develop action plans for achieving performance improvements. (Refers to Findings VI-12 and VI-13)

The Company conceptually accepted this recommendation.

The Company represents that it will continue the process of optimizing its key performance indicators to ensure success across the business. The Company states that part of the VDS process, which was begun in 2009, includes reducing redundancies, emphasizing activities that provide results, and aligning performance indicators with other aspects of the VDS. Action plans will be developed where appropriate and the effort involved is commensurate with achieving measureable performance improvements.

Recommendation VI-6 Install a process to ensure that SSC provides low-cost, efficient, competitive, and valuable support services to NJAWC (Refers to Finding VI-15)

The Company conceptually accepted this recommendation.

According to the Company, the Shared Services Center ("SSC") has a cost-effective process in place to help ensure that the SSC provides appropriate support services to the affiliates it serves, including NJAWC. The Company accepts the concept of this recommendation because the description of the desirable support services in the recommendation, -- "low-cost, efficient, competitive, and valuable"-- is a verbatim quote from the materials used by the SSC and provided to NorthStar at the conclusion of the audit process. The goals described in the recommendation are the goals the SSC aspires to as described in the SSC "vision statement"

NorthStar cites from. The Company asserts that such an aspiration should not be reduced to a legal requirement. Staff supports the Company's position. Rate Counsel did not provide specific comments on this section.

Recommendation VI-7 Implement the Business Transformation project within budget and on schedule. (Refers to Findings VI-16, V-2, VI-8, VIII-5, VIII-10, VIII-24, X-10 and XII-3)

The Company accepted this recommendation in concept to the extent it applies to NJAWC.

The Business Transformation ("BT") project is subject to the Capital Investment Management Committee policy. As such, the Company asserts that the BT project budget and timeline is scrutinized regularly, and any changes must meet the requirements of the policy. The project is currently in the "blueprint" stage, with considerable work ahead to finalize the business requirements and refine the project scope and timeline. Staff supports the Company's position. Rate Counsel did not provide specific comments on this section.

Section VII - System Operations

Recommendation VII-1 Take steps to improve the asset management systems, tools and processes. (Refers to Finding VII-1)

The Company accepts this recommendation and represents that it will continue to refine and improve its processes which relate to asset management. Staff supports NorthStar's recommendation as written. Rate Counsel did not provide specific comments on this section.

Recommendation VII-2 Revise the models which NJAWC uses to evaluate and prioritize projects and programs to give additional consideration to asset condition. (Refers to Finding VII-2)

The Company accepts the concept behind this recommendation. The Company believes that asset condition is a key component of its prioritization model, and NJAWC's model is balanced appropriately. However, if further weight needs to be given to asset condition, the Company will make the appropriate adjustments when necessary. Such adjustments are likely to be considered within the scope of an Enterprise Asset Management implementation, which is part of the scope of the Business Transformation Project, a large, high priority, enterprise-wide effort.

Staff supports the Company's position. Rate Counsel did not provide specific comments on this section.

Recommendation VII-3 Implement a computerized design tool that includes at a minimum: a compatible units feature; and interfaces with materials, Power Plant and graphical design and mapping software. (Refers to Finding VII-3)

The Company accepts the concept behind this recommendation. During the audit process, the Company was in the process of updating its design tools as part of the overall BT process. Additionally, the Company states that it has periodically upgraded its design tools when appropriate and cost-justified in the past without necessarily waiting for an enterprise-wide solution to be developed. The Company expects its design tool to continue to include appropriate features, including those described in this recommendation if appropriate. The Company believes this recommendation is already being met. The Company notes aspects of

recommendations that fall within the scope of the BT project should be considered part of that large, high priority, enterprise-wide effort.

Staff supports the Company's approach. Rate Counsel did not provide specific comments on this section.

Recommendation VII-4 Implement systems to enable NJAWC to capture and compare actual work units completed to those designed and budgeted. (Refers to Finding VII-4)

The Company conceptually accepted this recommendation. The ability to implement an integrated enterprise level system that captures and compares actual work units completed to those planned and budgeted is expected to be part of the BT project.

Staff supports the Company's approach. Rate Counsel did not provide specific comments on this section.

Recommendation VII-5 Benchmark detailed work performance metrics against other AWK companies and other water companies. (Refers to Finding VII-5)

The Company accepts this recommendation. The Company represents that adoption of BT will help to support this recommendation in the future as the ability to compare defined units of "work" and associated cost will be enhanced in detail and in definition.

Staff supports the Company's approach. Rate Counsel did not provide specific comments on this section.

Section VIII - Customer Service

Recommendation VIII-1 Perform an analysis of the relative costs of in-house versus outsourced call center operations for NJAWC. (Refers to Finding VIII-6)

The Company accepts this recommendation and will work with Staff to develop the appropriate analysis. The Company states that American Water Customer Service Center provides many functions besides call center services, and comparable comprehensive services may be difficult to benchmark in the marketplace.

Staff supports NorthStar's recommendation, and will work with the Company to develop the appropriate analysis. Rate Counsel did not provide specific comments on this section.

Recommendation VIII-2 Discontinue 24/7 operation of the call center. Determine the system/staff necessary to transition after hours' emergency calls to the local level. (Refers to Finding VIII-7)

The Company disagrees with NorthStar's assertion that operations of the call center 24 hours per day, seven days per week is unnecessary. The Company therefore rejects the first part of this recommendation. The Company conceptually accepts the second part of the recommendation and will review its systems and staff as part of its ongoing effort to optimize its operations and provide high-value, cost-effective service. The Company notes, however, that specifically studying one discrete issue such as transitioning emergency calls to the local level could generate costs substantially in excess of potential savings.

Rate Counsel generally supported the recommendations in this section. Rate Counsel specifically noted that the Final Report recommended further analysis of the continued operation of a 24/7 call center, and recommended that the Board "revisit" the economic analysis of the "costly proposition" that the Board's current meter testing requirements impose on water utilities and their ratepayers. Staff agrees with NorthStar's recommendation to determine the staff necessary to transition after hours' emergency calls to the local level.

Recommendation VIII-3 Determine whether call center staffing levels could be reduced while maintaining the overall average speed of answer (ASA) target and consider changing the ASA target. (Refers to Findings VIII-8 and VIII-9)

NJAWC accepted this recommendation.

Recommendation VIII-4 Shorten the window between meter read and billing. (Refers to Finding VIII-12)

The Company rejected this recommendation. The Company disagrees with NorthStar's finding that the window between meter read and billing is too long. The Company maintains that the window between the meter read and billing is approximately three days. The first day is required for quality control before the meter read data is transmitted, the second day is required for data to be transmitted. Data transmittal times are lengthy due to the requirements of current business systems and current information technology.

The Company maintains that the third day is required for quality control when the billing data is received. NJAWC asserts that it is not currently feasible to compress this time period further without the risk of increased billing errors, regardless of the level of effort or incremental cost expended. The Company notes that its current practice complies with all existing BPU regulations with regard to metering and billing.

Staff agrees with the Company's position. Rate Counsel did not provide specific comments on this recommendation.

Recommendation VIII-5 Implement a system that integrates the customer information system with the scheduling, monitoring and performance of new service work. (Refers to Finding VIII-16)

The Company accepts this recommendation. The Company expects this functionality to become available as part of the Customer Information System ("CIS") implementation phase of the BT project. A CIS implementation is a high priority for the business, and would entail a significant effort and cost even if it were not part of the existing BT project. Staff supports NorthStar's recommendation as written. Rate Counsel did not provide specific comments on this section.

Recommendation VIII-6 Take steps to improve non-pay disconnect performance. (Refers to Finding VIII-20)

The Company accepts this recommendation; however, it notes that the collections process performance (getting customers to pay on time), is related to many factors and not simply shut offs. In fact, with the approval of the BPU, NJAWC recommended and implemented a late fee for commercial and industrial customers who do not pay on time in its last rate case. Current regulations prohibit late fees for residential customers; however, this only provides a

disincentive for prompt payment encourages late payment behavior and imposes extra costs on the utility and its customers who pay on time due to the time and effort to track and process these customers through the collections process.

Staff supports NorthStar's recommendation as written. Rate Counsel did not provide specific comments on this section.

Recommendation VIII-7 Implement programs to track and increase the theft of service revenue recovered. (Refers to Finding VIII-23)

The Company accepted this recommendation. Staff agrees that NorthStar's recommendation should be implemented and a detailed action plan be included in NJAWC's implementation plan.

Section IX - External Relations

Recommendation IX-1 Assign administrative responsibility for the state external relations to the NJAWC president. (Refers to Finding IX-1)

The Company states that it will review the recommendation in the context of its overall organizational structure. NorthStar found that the state external affairs are managed administratively and functionally by the AWK senior vice president when all the work is actually performed for the NJAWC president.

Rate Counsel did not provide specific comments. Staff recommends that NorthStar's recommendation be implemented as written.

Recommendation IX-2 Take steps to improve communicating with customers including making better use of bill inserts. (Refers to Finding XI-2)

The Company accepted this recommendation.

Section X - Support Services

Recommendation X-1 Periodically benchmark IT costs against similar utilities. (Refers to Finding X-16)

The Company conceptually accepts this recommendation but notes that there is a limited universe of comparison companies of similar size and geographic reach. NJAWC represents that an appropriate benchmarking study would entail a substantial level of effort and associated costs and could not be done with existing resources. Staff supports the Company's position.

Rate Counsel did not provide specific comments on this section.

Recommendation X-2 Formalize the IT disaster recovery plan. (Refers to Finding X-17)

The Company accepted this recommendation.

Recommendation X-3 Conduct periodic reviews of records retention practices to ensure that policies are being adhered to. (Refers to Finding X-18)

The Company accepted this recommendation.

Section XI - Finance and Cash Management

Recommendation XI-1 Update the tax sharing agreement policies and procedures. (Refers to Finding XI-19)

The Company accepted this recommendation.

Section XII - Accounting, Property Records and Budgeting

Recommendation XII-1 Document the process for developing the five-year business plan. (Refers to Finding XII-8)

The Company accepted this recommendation.

Recommendation XII-2 Take steps to improve controls over the scope and cost of support provided NJAWC by AWWSC. (Refers to Finding XII-18)

NJAWC accepted this recommendation.

Section XIII - Affiliate Cost Allocations and Relationships

Recommendation XIII-1 Develop for NJAWC a monthly affiliate transaction financial report which lists and totals intercompany and affiliate transactions throughout AWK. The report should include product or service, cost quantity, and associate contract numbers as necessary. (Refers to Finding XIII-1)

The Company accepts the concept of this recommendation in that the report described therein is a report that can be run. However, the Company maintains that the specifics described above do not help to analyze company financial information. There are other separate affiliate transaction reports and other queries that can be run utilizing the AWWSC transaction database. The Company asserts that it already engages in the reporting and monitoring activities necessary to ensure compliance with appropriate corporate governance requirements, such as eliminating intercompany transactions on its financial statements.

NorthStar found that NJAWC could not provide the costs from 2007 through 2009 for a contract between Applied Water management and AWWSC to provide engineering services to NJAWC. Also NJAWC had financial records for eleven contracts but had only copies of five of the contracts. NJAWC did not have copies of the six contracts associated with services from NJAWC to its affiliates. While NJAWC included all of its transactions in its financial statements, it did not prepare separate intercompany or affiliate transaction reports.¹⁹

Rate Counsel agrees with NorthStar that a monthly affiliate report which lists and totals NJAWC intercompany and affiliate transactions throughout AWK should be developed. Rate Counsel also agrees with NorthStar's finding that these are critical issues for ratepayers that directly relate to ensuring that NJAWC has control of its costs and quality of services it receives from affiliates. Staff ate Counsel supports NorthStar's recommendation as written.

¹⁹ NorthStar's NJAW Final Audit Report, December 12, 2010, Findings and Conclusions XIII-1

Recommendation XIII-2 Expand the use of direct charging of AWWSC employee time where feasible. Use causal factors to justify cost allocations. (Refers to Findings XIII-2, XIII-3 and XIII-5)

The Company accepts the concept of using direct charging where feasible, while noting that NJAWC's total costs are unlikely to show a dramatic change. The Company represents that AWWSC uses appropriate factors to support and justify cost allocations, including (for example) causal factors and customer counts. Staff Rate Counsel supports NorthStar's recommendation as written.

Recommendation XIII-3 Assess the practice of applying two allocation factors for a single cost. If Tier 1 allocations are utilized, utilize them for the entire allocation of the cost. (Refers to Finding XIII-5)

The Company rejects this recommendation contending that it is based on a flawed interpretation of cost of service principles and an inaccurate finding. The Company believes that the way it charges costs is appropriate. The Company asserts that the above recommendation does not accurately describe the way costs are charged, and the associated sections of the report misconstrue the current AWWSC charging methodologies. NorthStar did not provide any analysis or discussion of a reasonable or appropriate alternative; rather, NorthStar recommends changes without consideration of the potential impact on the business or on customers, and without any attempt to assess the level or effort or costs associated with making such changes.

NorthStar in its findings pointed out that AWWSC utilized one set of drivers at the Tier 1 level and then switched the customer count as a driver at the Tier 2 allocation level. NorthStar is critical of the application of this allocation methodology, stating "the switch from Tier 1 drivers to customer count raises the question as to which driver is valid and underscores the fact that the allocation factors are not based on causal factors."²⁰ NorthStar recommends that NJAWC assess the practice of applying two allocation factors for a single cost. If Tier 1 allocations are utilized, they should be utilized for the entire allocation of cost.

Rate Counsel supported this recommendation, and provided specific comments on the Company's use of two allocation factors and the proportion of AWWSC expense that results from direct charging versus allocated charges. The Company informed Staff, that NJAWC assessed its application of cost-causative and allocation factors to costs in developing the current Business and Accounting Manual, which was updated and put into use in the second quarter of 2014. Staff will follow-up and examine the manual during the implementation review.

Recommendation XIII-4 Execute a lease for AWWSC's use of space at the Delran Water Treatment Plant. (Refers to Finding XIII-8)

The Company accepts this recommendation. NJAWC believes a lease exists although the records may have been mislaid. Since the completion of the audit, the Company has informed Staff that SSC no longer occupies any space in the Delran facility.

²⁰ Id. at XIII-5

Recommendation XIII-5 Discontinue counting customers that receive both water and wastewater service as two customers when determining allocation factors. (Refers to Finding XIII-9)

The Company at first rejected this recommendation then revisited its approach to customer counts as part of the development of the new Business and Accounting Manual. Effective in 2014, wastewater customers who are also water customers will no longer be counted as a completely separate, incremental customer. Customers receiving both water and wastewater service from the Company will count as 1.05 customers for the purpose of allocating costs on a "per customer" basis.

Staff agrees with the Company position.

Recommendation XIII-6 Complete documentation of affiliate contract files. (Refers to Finding XIII-13)

The Company accepted this recommendation.

Section XIV - Company Contractor Performance

Recommendation XIV-1 Modify the mark-out process and practices to ensure compliance with NJ regulations. (Refers to Findings XIV-1 and XIV-4)

The Company is currently a party to a docketed matter before the Board regarding the "One Call" regulations. Due to the pending nature of this matter, the Company believes that there are no modifications to make at this time. The Company conditionally accepts this recommendation, subject to the results of the ongoing proceeding before the Board and as otherwise described above.

NorthStar found that the "Company did not comply with certain provisions of the New Jersey one-call regulations. On October 15, 2007, certain amendments to the BPU's rules regarding Underground facilities: One-Call Damage Prevention System, N.J.A.C. 14:2 et seq., went into effect NJAWC sought a waiver of certain of the amendments and a stay of the effectiveness of the regulations."²¹

Rate Counsel commented that the first recommendation in this section was inappropriate because there was an "open Docket before the Board on the scope of the mark-out rule." Rate Counsel also believes that since the Company has petitioned the Board for relief from the rule, the Audit should not prejudge the action the Board may or may not take on the Company's petition.

Staff believes the Company should comply with all provisions of the New Jersey one-call regulations. Staff supports NorthStar's recommendation as written.

Recommendation XIV-2 Evaluate the actual costs of using the mark-out contractor versus using in-house resources. (Refers to Finding XIV-2)

The Company accepted this recommendation.

²¹ Id. at XIV-1

Recommendation XIV-3 Develop a program for inspecting mark-out work rather than relying on contractor self-inspection. (Refers to Finding XIV-3)

The Company accepts the concept of this recommendation. The Company will review its approach to inspecting mark-out work performed by contractors and make changes if appropriate.

Recommendation XIV-4 Collect and retain appropriate information on the mark-out work rather than relying on contractor self-inspection. (Refers to Finding XIV-4)

NJAWC accepted this recommendation. The Company believes it collects and retains the appropriate information required by the regulations, subject to the outcome of the "One Call" mark-out proceeding currently open before the Board. The Company also believes that it appropriately allocates resources and does not unreasonably rely on contractor inspections where appropriate.

Recommendation XIV-5 Develop a quality control and inspection process for main and service contractors. (Refers to Finding XIV-7)

The Company accepted this recommendation.

Recommendation XIV-6 Incorporate contractor work into the work management systems to identify the actual costs and resources required to do individual tasks. (Refers to Findings XIV-5 and XIV-6)

The Company conceptually accepted this recommendation. Currently, NJAWC maintains that it is not feasible to incorporate outside contractor work into the work management system. However, in the future the Company may revise business processes or systems, and upgrade information technology, to allow such integration to take place. Of course, such integration would need to be subject to appropriate safeguards regarding the integrity of the Company's systems and data, including customer data. At such time that it becomes feasible and practical to implement this recommendation, the Company expects that such a step will be part of a future work management system. Staff accepts the Company's position.

DISCUSSION AND FINDINGS

As noted above, there are fifty-five recommendations in NorthStar's Final Report for improvement of the management and operations of NJAWC. As also noted above, with respect to three of the recommendations -- III-3, III-6 and VIII-4 -- Staff agrees with the Company and does not recommend implementation by the Company at this time. Staff recommends implementation of the any of the remaining 52 recommendations, not already implemented subject to the specific modifications described above.

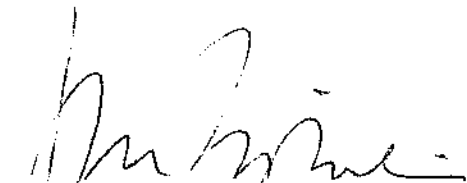
After review of the Final Report and the comments of the Company and Rate Counsel, and of the Staff's positions, the Board agrees with Staff's recommendations. Therefore, upon careful review of the Final Report recommendations and the comments received, the Board **HEREBY ORDERS** the Company to implement the 52 recommendations, as modified above not already implemented.

Specifically, the Board **HEREBY DIRECTS** NJAWC, with the assistance of the Division of Audits, to formulate detailed implementation plans for the 52 recommendations, as modified above, not already implemented, within 60 days from the date of this Order. NJAWC shall implement all recommendations as soon as possible but not later than one year from the date of this Order.

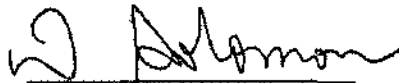
Furthermore, the Board **HEREBY DIRECTS** NJAWC to file quarterly reports with the Division of Audits, by the fifteenth day of the month following the conclusion of each calendar quarter, regarding the status of all recommendations. The Division of Audits shall monitor, evaluate, and modify, as necessary, the implementation of the recommendations. The recommendations of the Final Report shall not be dispositive of issues raised in any other proceedings before this Board.

DATED: 12/22/14

BOARD OF PUBLIC UTILITIES
BY:


JOSEPH L. FIORDALISO
COMMISSIONER

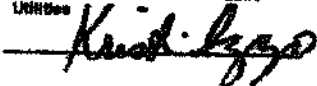

MARY-ANNA HOLDEN
COMMISSIONER


DIANNE SOLOMON
COMMISSIONER

ATTEST:

KRISTI IZZO
SECRETARY

I HEREBY CERTIFY that the within document is a true copy of the original in the files of the Board of Public Utilities



IN THE MATTER OF A COMPREHENSIVE MANAGEMENT AUDIT OF NEW JERSEY
AMERICAN WATER COMPANY PURSUANT TO N.J.S.A. 48:2-16.4, AND N.J.A.C. 14:3-12.1
Docket No. WA09070510

SERVICE LIST

Kristi Izzo, Secretary
Board of Public Utilities
44 South Clinton Street, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350

Henry Ogden, Esq.
Division of Rate Counsel
140 East Front Street, 4th Floor
Post Office Box 003
Trenton, N.J. 08625-0003

Debra F. Robinson, Esq.
Managing Attorney Water & Wastewater
Division of Rate Counsel
140 East Front Street, 4th Floor
Post Office Box 003
Trenton, N.J. 08625-0003

Maria Moran, Director
Board of Public Utilities
Division of Water
44 South Clinton Street, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350

Stefanie A. Brand, Esq., Director
Division of Rate Counsel
140 East Front Street, 4th Floor
Post Office Box 003
Trenton, N.J. 08625-0003

Rupal Patel
Board of Public Utilities
Division of Water
44 South Clinton Street, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350

Alex Moreau, DAG
Department of Law & Public Safety
Division of Law
124 Halsey Street
P.O. Box 45029
Newark, NJ 07101-45029

Caroline Vachier, DAG
Department of Law & Public Safety
Division of Law
124 Halsey Street
P.O. Box 45029
Newark, NJ 07101-45029

Babette Tenzer, DAG
Department of Law & Public Safety
Division of Law
124 Halsey Street
P.O. Box 45029
Newark, NJ 07101-45029

Michael Sgro, Esq.
New Jersey American Water Co.
1025 Laurel Oak Road
Voorhees, NJ 08043

Pasquale Salvemini
Board of Public Utilities
Division of Audits
44 South Clinton Street, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350

William J. Varley, President
New Jersey American Water Co.
1025 Laurel Oak Road
Voorhees, NJ 08043

Robert J. Brabston, Esq.
New Jersey American Water Co.
167 J.F.K. Parkway
Short Hills, New Jersey 07078

Frank Simpson
New Jersey American Water Co.
1025 Laurel Oak Road
Voorhees, NJ 08043

Howard J. Woods, Jr., P.E.
Howard J. Woods, Jr. & Assoc. LLC
138 Liberty Avenue
Newtown, PA 18940-1111

Robert J. Henkes
Henkes Consulting
7 Sunset Road
Old Greenwich, CT 06870