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BEFORE THE TENNESSEE REGULATORY AUTHORITY

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NASHVILLE, TENNESSEE

November 8, 2006

IN RE:

**SHILOH FALLS UTILITIES, INC.
COMPLIANCE AUDIT**

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Docket No. 06-00177

**NOTICE OF FILING BY UTILITIES DIVISION OF THE TENNESSEE
REGULATORY AUTHORITY**


Pursuant to Tenn. Code Ann. §§ 65-4-104, 65-4-111 and 65-3-108, the Utilities Division of the Tennessee Regulatory Authority gives notice of its filing of the Shiloh Falls Utilities, Inc.'s Compliance Audit Report in this docket and would respectfully state as follows:

1. The present docket was opened by the Authority to hear matters arising out of the compliance audit of Shiloh Falls Utilities, Inc. (the "Company").
2. The compliance audit of the Company was conducted on-site on June 13 through June 15, 2006.
3. On August 18, 2006, the Utilities Division issued its preliminary compliance audit findings to the Company via e-mail. The Company responded on August 25, 2006 via e-mail. An additional Utilities Division request led to Company responses that were received on October 4 and October 9, 2006.

4. The preliminary compliance audit report was modified to reflect the Company's responses and a final compliance audit report (the "Report") resulted therefrom. The Report is attached hereto as Exhibit A and is fully incorporated herein by this reference. The Report contains the audit findings of the Utilities Division, the Company's responses thereto and the recommendations of the Utilities Division in connection therewith.

5. The Utilities Division hereby files its Report with the Tennessee Regulatory Authority for deposit as a public record and approval of the recommendations and findings contained therein.

Respectfully Submitted:



Ron Graham
Utilities Division of the
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

I hereby certify that on this 8th day of November, 2006, a true and exact copy of the foregoing has been either hand-delivered or delivered via U.S. Mail, postage pre-paid, to the following persons:

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Tennessee Regulatory Authority
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Ron Graham

COMPLIANCE AUDIT REPORT

OF

SHILOH FALLS UTILITIES, INC.

DOCKET NO. 06-00177

PREPARED BY

TENNESSEE REGULATORY AUTHORITY

UTILITIES DIVISION

November 2006

EXHIBIT A

COMPLIANCE AUDIT
SHILOH FALLS UTILITIES, INC.

DOCKET NO. 06-00177

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I. INTRODUCTION

The subject of this audit is Shiloh Falls Utilities, Inc.'s ("Company" or "Shiloh") compliance with the Rules and Regulations of the Tennessee Regulatory Authority ("TRA" or the "Authority") as they apply to wastewater utilities. At the direction of the Chief of the Utilities Division, the compliance audit was conducted by Butch Phillips and Ron Graham of the Utilities Division. The Company made its books and records available to the Compliance Audit Staff ("Staff") at 450 Church St., Savannah, Tennessee. The Staff's findings and recommendations resulting from the audit can be found in section V. of this report.

II. BACKGROUND

Shiloh is a small wastewater system located in Counce, Tennessee in Hardin County. It is owned in equal shares by Shackelford Development Company, Inc. and SPD Company, LLC. Both companies are owned by the Shackelford family. The Company currently has approximately 103 customers, which includes one small retail customer.

Shiloh was originally granted approval for a Certificate of Public Convenience and Necessity (CCN) in Tennessee Public Service Commission ("TPSC") Docket No. 95-03948. The last time this utility appeared before this agency was in Docket No. 02-00289. In that Docket, TRA Staff conducted a compliance audit of the Company's books and records. Staff issued its report containing five (5) findings on April 24, 2003. The matter came before the Authority on June 16, 2003, at which time the Directors approved and adopted the compliance audit report.

III. JURISDICTION OF THE TENNESSEE REGULATORY AUTHORITY

Tennessee Code Annotated (T.C.A.) gives jurisdiction and control over public utilities to the Tennessee Regulatory Authority. T.C.A. §65-4-104 states that:

The [A]uthority has general supervisory and regulatory power, jurisdiction, and control over all public utilities, and also over their property, property rights, facilities, and franchises, so far as may be necessary for the purpose of carrying out the provisions of this chapter.

Further, T.C.A. §65-4-105 grants the same power to the Authority with reference to all public utilities within its jurisdiction as chapters 3 and 5 of Title 65 of the T.C.A. have conferred on the Department of Transportation's oversight of the railroads or the Department of Safety's oversight of transportation companies. By virtue of T.C.A. §65-3-108, this power includes the right to audit:

The department is given full power to examine the books and papers of the companies, and to examine, under oath, the officers, agents, and employees of the companies and any other persons, to procure the necessary information to intelligently and justly discharge its duties and carry out the provisions of this chapter and chapter 5 of this title.

The TRA's Utilities Division is responsible for auditing those gas, electric, and water companies under its jurisdiction, to ensure that each company is abiding by Tennessee statute as well as the Rules and Regulations of the Authority.

IV. SCOPE OF AUDIT

The Staff examined Shiloh's books and records for the twelve months ended December 31, 2005, and conducted tests of accounts as it considered necessary to determine if the Company is complying with the Uniform System of Accounts (USOA) for Class C Wastewater utilities as well as TRA rules, regulations, and other directives of the Authority.

V. AUDIT FINDINGS

Staff audit resulted in three (3) findings. A discussion of those findings along with Staff's recommendations to remedy the findings and the Company's response to the findings are found below.

EXPLANATION OF FINDINGS

FINDING # 1:

Exception

The Company is delinquent in its customer billings.

Discussion

The Company via a data request response indicated that its customer billings are in arrears by several months. The Company also submitted a schedule indicating that the billings would be brought current during December 2006.

The Company, according to its data response, identified a billing problem approximately eighteen months ago. The cause of the problem was Shiloh's billing software and the billing software utilized by First Utility District, the water provider for the area. In addition, the Company reported that it has now obtained new billing software that reduces the time it takes to process customer bills from two days to two hours.

Staff believes that it is important for Shiloh to remain current with all billings to ensure that it receives sufficient revenue to pay for its operational expenses. By becoming lax in its billing process, the Company runs the risk of not collecting the revenue that it is entitled to and potentially, if enough bills become uncollectible, to experience net operational losses.

In its preliminary report issued to the Company, Staff recommended that Shiloh should bring customer billings current within sixty (60) days of the filing of this report and to subsequently provide written confirmation to the Authority that the billings are current.

Company Position

In response to the Staff's preliminary report, the Company disagreed with the recommendation and respectfully requested that Shiloh be allowed to continue with the billing schedule currently in place. The current schedule is to bill two months of service for November and December in order to get the Company caught up on its billing. The Company states that this schedule will fall within the proposed 60-day period

recommended by Staff and further, the Company states that it does not have a cash flow problem and has not experienced any loss of revenue from the delayed billings, other than those accounts which were a problem prior to the billing delays. The Company contends that its present schedule has no adverse effects on utility operations or its customer.

Staff Recommendation

The Company has committed to bring billing current by December 2006; this time period falls within the 60 days recommended by Staff in its preliminary report. Accordingly, Staff recommends that Company's proposed schedule to bring their billing current by December 31, 2006 be adopted by the Authority.

FINDING # 2:

Exception

The Company incorrectly recorded a capital expenditure as normal operational expense.

Discussion:

During a review of vendor invoices paid by the Company, Staff discovered that Shiloh recorded \$850 for major repairs to a lift station pump as a monthly expense. Uniform System of Accounts for Class "C" Wastewater Utilities sets a monetary level for capitalizing versus expensing for Class C wastewater utilities at \$150.00.

In its preliminary report issued to the Company, Staff recommended that Shiloh should reclassify this amount from a repair and maintenance expense to Utility Plant in Service (USOA Account No. 360) and depreciate over the extended life of the pump.

Company Position:

The Company agrees to comply with this recommendation and will request that its accountant reclassify this expenditure.

Staff Response

Staff is satisfied with the Company's response and therefore recommends that the Authority require Shiloh to reclassify the \$850 amount from repair and maintenance expense to Utility Plant in Service (USOA Account No. 360) and depreciate over the extended life of the pump.

FINDING # 3:

Exception:

The Company's tariff is not in compliance with TRA Rule 1220-4-1.

Discussion:

Staff discovered the following deficiencies during a review of the Company's tariff:

1. The Company could not produce a copy of the tariff page (First Revision Page No. 8) on file at the Authority which contains its sewer billing rates. A check of customer bills showed that the Company is billing customers consistent with the rates contained on this revised rate schedule.
2. The tariff does not conform to tariff specifications contained in TRA Rule 1220-4-1-.02, because there is no name and title of the issuing officer on each tariff sheet.
3. Tariff sheets in effect with an issue date of May 18, 2001 do not include an effective date. In addition these tariff sheets contain a business address that is not current and a telephone number that has been disconnected.
4. The "Application and Contract for Service" found in Shiloh's tariff is not the form currently used by the Company. The Company did not file the new service agreement with the Authority.
5. Tariff Sheet "Original Page No. 7" has not been revised to contain the current public contact information.
6. Tariff Sheet "Original Page No. 4" states that a customer's service may be terminated for non-payment of bill and in addition, penalties for non-payment. For environmental and health reasons, water service should be discontinued whenever sewer service is disconnected. This step also provides motivation for a customer to pay the outstanding sewer bill. The Company told the Staff during the on-site visit that the provider of water services, First Utility District of Hardin County, is unwilling to terminate water service for failure of a sewer customer to pay for sewer service. Pursuant to TRA Rule 1220-4-13-.14(2), after the effective date of this rule, a utility shall refuse new wastewater service to a customer unless the customer agrees to sign a "Subscription Service Contract" that would allow the utility to either install a water cutoff valve on the customer's premises for use by the utility or allow the utility to execute an agreement with the water provider to terminate water service.
7. There is no current map of the service territory included with the tariff or available from the Company during the on-site visit by Staff.

In its preliminary report issued to the Company, Staff recommended that Shiloh work with TRA Staff and file a revised tariff correcting the above deficiencies within sixty (60) days of the issuance of the compliance report.

Company Position:

The Company will comply with this recommendation and will instruct its attorney to contact the TRA Staff and begin the necessary revisions to its tariff.

Staff Recommendation:

Staff is satisfied with the Company's response and therefore recommends that the Authority order Shiloh to work with the TRA Staff and file a revised tariff correcting the above deficiencies within sixty (60) days.

VI. ESCROW DETERMINATION PURSUANT TO TRA RULE 1220-4-13-.07(8)

Issue: Authority determination whether a need exists for Shiloh to maintain an Escrow Account.

As stated in Rule 1220-4-13.07(8), “The requirement for a public wastewater utility to maintain a reserve/escrow account shall be determined by the Authority on a case by case basis. Within eighteen (18) months from the effective date of these rules, the Authority shall review the financial condition of any public wastewater utility holding a CCN to provide wastewater service as of the effective date of these rules to determine whether such wastewater utility shall establish or adjust the amount of a reserve/escrow account as described in this Chapter.” During the audit review, Staff noted that the Company does not currently maintain an escrow account for the purpose of non-routine or emergency system repairs.

In its preliminary report issued to the Company, Staff recommended that the Company not be required to maintain an escrow account based upon the owner’s assertions that any extensive or emergency repairs will be funded by the owner as needed.

Company Position

On March 18, 2005, in response to a TRA Staff data request in Docket No. 04-00434, Shiloh stated that “Extensive system repairs or operations necessitated by an emergency situation would be funded through capital investment from the owners of the utility company.” The Company maintains its position and agrees with the recommendation that it should not be required to implement an escrow account.

Discussion:

During 2002, Shiloh was fined \$15,000 by the Tennessee Department of Environment and Conservation (“TDEC”) for non-compliance with various TDEC regulations.¹ In 2002 and 2003, the owners, Shackelford Development and SPD Co., LLC, paid-in capital totaling \$553,018, to improve the wastewater system.² Shackelford Development and SPD Co., LLC, are also major developers of real estate located within the service territory of Shiloh and have a vested interest in seeing the utility survive financially. From 2002 through 2005, Shiloh reported repair and maintenance expenses of \$27,649.58.³ In addition, in Docket No. 05-00105, Shiloh provided a surety bond in the amount of \$35,000, as required by the Authority’s wastewater rules.

¹ See Authority Audit Report, Docket No. 02-00289, Page No. 5.

² See 2002 and 2003 Annual Reports, sheet F-4.

³ See data response dated October 9, 2006.

Recommendation

For the reasons set forth herein, Audit Staff opines that Shiloh and its owners are committed to fund and maintain the plant, thus ensuring continued adequate wastewater service to its customers. Accordingly, Audit Staff recommends that an escrow account is not necessary at this time.

VII. STAFF SUMMARY

The Company's customer billings are in arrears and it should make efforts to bring them current as soon as possible. The Staff has outlined in the report other material deficiencies (i. e. tariff deficiencies, misclassified expenditures, etc.) and will work with the utility to remedy these deficiencies. Shiloh has access to outside accounting personnel to assist in maintaining financial compliance.

In Docket No. 02-00289 the company was cited in several areas for various accounting and billing errors. Upon review of the Company's books and records the Audit Staff believes these prior issues have been corrected.

The Staff believes that an escrow for non-routine expenditures is not needed at this time. The Company has stated that the owners are committed to provide the necessary capital to properly maintain the utility's plant in service.