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April 12, 2012

IN RE:)
)
TENNESSEE WASTEWATER SYSTEMS, INC) Docket No. 11-00112
ESCROW ACCOUNT REVIEW)

**NOTICE OF FILING BY THE 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 hereby gives notice of its filing of the Limited Compliance Review Report of the Escrow Account for Tennessee Wastewater Systems, Inc. (the "Company") in this docket and would respectfully state as follows:

1. The present docket was opened by the Authority on July 14, 2011 to hear matters arising out of the review of the Company's Escrow Account for the period January 1, 2010 through December 31, 2010.
2. The Authority Staff ("Staff") completed its review of the escrow account on February 22, 2012.
3. The Staff's review revealed two findings. The Report is attached hereto as Exhibit A and is fully incorporated herein by this reference.

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

Respectfully Submitted:

A handwritten signature in cursive script, reading "Pat Murphy", written over a horizontal line.

Pat Murphy, Deputy Chief
Utilities Division
Tennessee Regulatory Authority

CERTIFICATE OF SERVICE

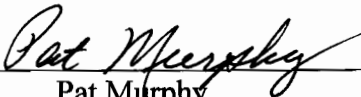
I hereby certify that on this 12th day of April 2012, a true and exact copy of the foregoing has been either hand-delivered or delivered via U.S. Mail, postage pre-paid, to the following persons:

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EXHIBIT A

COMPLIANCE REVIEW REPORT

OF

TENNESSEE WASTEWATER SYSTEMS, INC.

ESCROW ACCOUNT

DOCKET No. 11-00112

PREPARED BY THE

TENNESSEE REGULATORY AUTHORITY

THE UTILITIES DIVISION

April 2012

TENNESSEE WASTEWATER SYSTEMS, INC.
LIMITED COMPLIANCE REVIEW REPORT OF
ESCROW ACCOUNT
DOCKET NO. 11-00112

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I. INTRODUCTION

The objective of this limited scope escrow review is to determine whether the escrow account maintained by Tennessee Wastewater Systems Inc. ("Tennessee Wastewater" or "Company") was administered in accordance with the TRA's Wastewater Rules 1220-4-13-.07(8) and 1220-4-13-.07(9) during the twelve (12) months ended December 31, 2010. The rules require escrow funds to be maintained in a separate bank account. Documentation should support all monthly amounts placed into the escrow account and amounts withdrawn from the escrow account. Funds withdrawn should be used for non-routine equipment replacement, preventative maintenance and tank pumping. The Company is required to file an annual calendar year-end report detailing the balances and activity in the escrow account, monthly banks statements, and explanations and supporting documentation for all disbursements with its annual report to the Authority on April 1 of each year.

II. STAFF SUMMARY OF CONCLUSIONS

After reviewing the Company's escrow account and supporting documentation, Staff reports two (2) findings, which are detailed in Section VI. Finding #1 summarizes some withdrawals that were not appropriately reimbursed by a third party. These amounts are not monetarily material. Finding #2 cites areas where the Company failed to fully comply with the TRA Rules, which Staff considers material. The Staff also provides the Company's responses to the findings and Staff's recommendations in connection with the findings.

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:

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 Utilities Division of the TRA is responsible for auditing and/or reviewing energy, water and communications utilities under its jurisdiction to ensure that each company is abiding by Tennessee statute as well as the Rules and Regulations of the Authority. Paul Greene, Helen Trimble-Anthony and Darlene Standley of the Utilities Division conducted this limited compliance review.

IV. BACKGROUND INFORMATION ON ESCROW ACCOUNT

TRA Wastewater Regulations addresses the establishment of an escrow account for public wastewater utilities. TRA Rule 1220-4-13-.07(8) states:

“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. Upon the filing of an initial CCN application, a determination shall be made regarding the establishment of a reserve/escrow account. The Authority may review the financial condition of any public wastewater utility at any time to determine whether a reserve/escrow account balance is adequate or an account should be established.”¹

Additionally, TRA Rule 1220-4-13-.07(9) states:

“Reserve/escrow accounts established by the public wastewater utility to pay for non-routine operation and maintenance expenses shall meet the conditions as specified by the Authority. The public wastewater utility shall file bank statements and a report that details the expenses on all disbursements from the escrow account with its annual report or as the Authority may direct....”

The existing escrow account for Tennessee Wastewater was upheld pursuant to the Authority’s December 18, 2007 Order in Docket 07-00063. A majority of the panel found that non-routine operation and maintenance expenses should include equipment replacement, tank pumping and preventative maintenance not covered in the Company’s base rates.

¹ The Wastewater Rules were adopted by the TRA on March 6, 2006 and became effective on June 12, 2006.

At the July 14, 2011 Authority Conference, the Authority opened a docket for TRA Staff to review the escrow account approved by the Authority for Tennessee Wastewater to determine if it is being used as intended and whether the escrow funds are adequate to support the continued adequate service to the Company's customers. At the end of the review, Staff would issue a report with its findings, conclusions, and recommendations for the Authority's consideration. On October 7, 2011, the Staff issued its first data request, to which the Company responded on October 25, 2011 and November 14, 2011.

V. SCOPE OF AUDIT

In meeting the objective of the audit, the Staff:

- (1) Verified that escrow funds were maintained in a separate bank account;
- (2) Reviewed and verified all documentation supporting all amounts placed into the escrow account;
- (3) Reviewed and verified all documentation supporting all amounts withdrawn from the escrow account;
- (4) Verified expenditures were non-routine in nature in accordance with TRA orders; and
- (5) Verified accuracy of December 31, 2010 escrow account balance.

In reviewing the documentation Staff determined that some withdrawals were not reimbursed by third parties. Staff did determine, however, these withdrawals to be immaterial relative to the escrow balance. Additionally, Staff found the Company filed its 2010 escrow information after the date required by Authority rules.

VI. AUDIT FINDINGS AND RECOMMENDATIONS

Staff has reviewed all the information initially filed by the Company regarding activity in its escrow account during the period under review and the related responses to subsequent Data Requests. Based upon our review, Staff determines that the Company's escrow account meets the conditions as specified by the Authority for the twelve months ended December 31, 2010, with two (2) exceptions. The exceptions are discussed below.

FINDING #1

Exception

The Company failed to seek escrow reimbursement in some cases.

Discussion

Some expenses withdrawn from the escrow account should have been reimbursed to the escrow account by third parties. Expenses incurred by the Company that were caused by third parties, acts of God, or situations that may be covered by insurance are allowed to be withdrawn from escrow; however, the Company should bill the appropriate third party and deposit the funds recovered back into the escrow account. The Company stated that it will reverse the inappropriate withdrawals that were discovered.

Staff initially sampled seven (7) invoices which appeared to be withdrawals for which a third party should be billed. Two (2) of these should have been paid by the Company's affiliate due to faulty equipment or wiring error and one should have been billed to the developer who caused the damage. The Company stated in response to a Staff Data request that three (3) of the items would be reversed, but that the one item's cost was less than the \$1000 insurance deductible.

Due to the high percentage of escrow withdrawals which should have been billed to third parties, Staff extended its sample to include the entire population of all such invoices for charges we suspected should have been billed to third parties. As a result, Staff identified seven (7) additional withdrawals that were questionable. Staff sent a follow-up Data Request regarding the seven (7) additional items noted. The Company responded that five (5) of the items would be reversed. Three (3) items should have been billed to customers and two (2) items should have been billed to contractors. The remaining two items were draws due to flood damage and each exceeded the \$1,000 deductible identified in the first Data Request. The Company's response indicated that while the amounts exceeded \$1000, the Company's insurance did not cover flood damage.

The total dollar amount of the discrepancies identified is considered immaterial.

Company Response

TWSI does not carry flood insurance; therefore, repairs of the damage done to equipment from the great flood of 2010 were funded out of escrow. We have nothing additional to add to Finding #1.

Discussion and Recommendation based on Company Response

The Company response is unacceptable.

The TRA Data Request dated October 7, 2011 and the Company's October 25, 2001 response follows:

12. Explain TWWS' procedure to ensure that expenses paid out of escrow (subsequently billed to a customer, insurance company, builder, or developer and payment received) are reimbursed to the escrow account. Provide documentation to support to the reimbursement of escrow funds for the following:

- a. 812110 invoice to Electric Company (Electric Company broke line);
- b. 9122110 MVR for Oak Pt for \$150 plus the material charge from Adenus (owner was billed);
- c. 312/10 Southeast Environmental Engineering, LLC ("SEE") invoice for service on 2/19/10 (contractor was billed);
- d. 3/8/10 SEE invoice for service provided 11/28/09 - 12/1/09 (developer and/or builder was billed);
- e. 6/10/10 SEE invoice for service on 4/1/10 for storm damage (insurance reimbursement). If insurance company was not billed, explain why it was not;
- f. 912110 SEE invoice for service on 4/29/10 (recovery from Adenus Technologies since the damage was caused by "a wiring error at Adenus Technologies"). If Adenus Technologies was not billed, explain why it was not; and
- g. 9110110 SEE invoice for services provided 6/10/10, 6/14/10, 6/15/10 and 6/16/10 (recovery from Adenus Technologies since the repeated maintenance visits were due to a defective "Red Lion module" produced by Adenus Technologies). If Adenus Technologies was not billed, explain why it was not.

Answer:

- a. Line broken by electric company by fault of Adenus personnel; missed marking location. TNWW responsibility to cover cost of repair.

- b. Lid damage was not home owners responsibility.
- c. Charges will be reversed by TNWW in October 2011.
- d. Developer was contacted not billed. TNWW could not prove who was responsible for break in line. TNWW covered expense.
- e. Insurance deductible is \$1,000. \$153.08 would not be reimbursed. TNWW covered expense.
- f. Charges will be reversed by TNWW in October 2011.
- g. Charges will be reversed by TNWW in October 2011.

The TRA issued a follow-up Data Request and the Company responded November 14, 2011 response follows:

1. Provide documentation to support the billing, claim or other reimbursement requests for the charges related to the items listed below and provide documentation that the reimbursement amounts were deposited back into escrow. If reimbursement were not received, explain.

- a. 3/4110 - Jet grease at Riley's Market;
- b. 3/8110 - Robbie to the Rescue invoice 9076 and related Adenus personnel charges- Contractor "busted" line;
- c. 3/9/10 Robbie to the Rescue invoice 9078 and related Adenus personnel charges- Contractor needed sewer line lowered;
- d. 4/21110 - Grease trap pumped at Cindy's Catfish Riley's Market;
- e. 5/8/10 Replaced bi-oxide tanks and pump due to flood;
- f. 5/811 0 Replaced fence and repair bladder tank due to flood; and,
- g. 5115/10 - Grease trap pumped at Lance's Market.

Answer:

- a. Charges will be reversed by TNWW and we will bill the customer in November 2011.
- b. Charges will be reversed by TNWW in November 2011.

- b. Charges will be reversed by TNWW in November 2011.
- c. Charges will be reversed by TNWW in November 2011.
- d. Charges will be reversed by TNWW and we will bill the customer in November 2011.
- e. The Bi-oxide tanks are a part of the treatment of effluent at our Clarksville Subdivision. The flood in May 2010 destroyed tanks and pump.
- f. The fence around our drip field and bladder tank in control house was destroyed by May 2010 flood.
- g. Charges will be reversed by TNWW and we will bill the customer in November 2011.

Recommendation

The Company must provide evidence within thirty (30) days of the Authority Conference at which this report is considered, demonstrating that the questioned charges have been reversed and placed back into escrow. Additionally, the Company must provide written procedures the Company will follow regarding billing third parties who are responsible for damages and depositing recoveries from such billings back into the escrow account.

FINDING #2

Exception

The Company failed to file its 2010 escrow information timely.

Discussion

Staff sent a letter dated August 20, 2010 to the Company regarding Staff's review of the 2009 escrow activity and reminding the Company of items to be filed with the 2010 Annual Report. The following is selected text from this letter:

In future years, however, we request that the Company track the number of residential customers billed by each escrow rate monthly for 2010 on an Excel spreadsheet. In addition, the Company should begin to prepare an Excel spreadsheet showing the amount of commercial revenues billed each month individually for the three (3) commercial classes. As part of the Escrow information filed next year (April 1, 2011) the Company should provide the December 31, 2010 bank statement and the subsequent deposit slip and/or bank statement documenting that the year-end Escrow balances per the bank has been trued up to the year-end accrued escrow balance per books at December 31, 2010. Be sure to include copies of all invoices supporting Escrow withdrawals.

Staff sent a letter dated February 11, 2011 to all Companies to file their Annual Report by April 1, 2011. The following is selected text from this letter:

The 2010 annual report is due on **April 1, 2011.**

In addition, each utility that maintains a separate escrow account, established pursuant to TRA Rule 1220-4-13-.07(8), must file along with its annual report, a separate report detailing the monthly deposits to the escrow account and the amount and purpose of each disbursement from the escrow account during the period covered by the annual report. To support the reported amounts, copies of the monthly bank statements must be attached.

The Company failed to file its escrow information with the annual report pursuant to TRA Rule 1220-4-13-.07(8).²

² Pursuant to TRA rule 1220-4-13-.07(9), wastewater utilities with established escrow accounts shall "file bank statements and a report that details the expenses on all disbursements from the escrow account with its annual report or as the Authority may direct."

Company Response

TWSI will file its escrow information along with the annual report in future filings.