

BEFORE THE TENNESSEE REGULATORY AUTHORITY

Nashville, Tennessee

PETITION OF BERRY'S CHAPEL)	
UTILITY, INC. TO INCREASE)	
RATES AND CHARGES; TARIFF)	
TO RECOVER THE COST OF)	
FINANCIAL SECURITY;)	DOCKET NO. 14-00004
IMPLEMENTATION OF)	
PASS THROUGHs FOR)	
SLUDGE REMOVAL,)	
ELECTRICITY, CHEMICALS)	
AND PURCHASED WATER)	

**TESTIMONY
OF
MICHAEL KNOTTS**

**ON BEHALF OF BERRY'S CHAPEL UTILITY, INC.
d/b/a HARPETH WASTEWATER COOPERATIVE**

June 24, 2014

Q. Please state your name and your position with the Company.

A. My name is Michael Knotts, and I am the Chairman of the Board of Directors of Berry's Chapel Utility, Inc. d/b/a Harpeth Wastewater Cooperative. I also currently serve as the company President. My service is on a volunteer, uncompensated basis.

Q. Please tell us about your background.

A. I am a native of Nashville, TN and have been a customer of the utility since 2010. My family and I live in the Cottonwood subdivision, and I have observed the utility's operations and interaction with TRA since becoming a customer. I have submitted comments to the TRA Directors regarding the utility's rate case in docket #11-00198, and have also affixed my signature to a petition to the Consumer Advocate contained in that same docket.

Professionally, I serve as the Director of Government Affairs for the Tennessee Electric Cooperative Association, where my primary duties involve working with Federal, State, and local elected officials and government agencies on behalf of 23 cooperatively owned electric distribution companies. I also work extensively with the cooperatives' member-elected Boards of Directors through an education and training program that focuses on basic duties and responsibilities of elected directors, and other more advanced topics.

Electric cooperatives are private, non-profit corporations whose mission is to provide an essential utility service at the highest attainable level of quality and reliability while maintaining the lowest possible cost.

1 Because of their non-profit and self-governing nature, by statute, the
2 Tennessee Regulatory Authority does not regulate electric cooperatives.

3 I have volunteered my time and efforts to the reform of this troubled
4 utility because the mission and corporate structure of electric cooperatives
5 provides a useful model for Harpeth Wastewater, and I hope that my
6 background and experience will help guide the utility toward a more
7 sustainable business model.

8
9 **Q. What is the purpose of your testimony?**

10 A. To provide an overview and discussion of the change in the
11 company's governance, and update the Directors as to the new Board's
12 desires for this rate case.

13
14 **Q. Please explain the events leading up to the election of the new board of
15 directors.**

16 A. When the owners of Lynwood Utility re-formed the company into a
17 non-profit entity in 2010, the utility became subject to the obligations
18 prescribed by the Tennessee Nonprofit Corporation Act. Specifically, the Act
19 requires that non-profit corporations hold Annual Meetings and also elect
20 Directors to its governing board from within the membership of the
21 corporation. Acting in the capacity of Initial Director of the new non-profit
22 company, the previous owners of the Company failed to seriously solicit
23 membership, failed to ever schedule an annual meeting or allow for an
24 election of Directors. They also engaged in a protracted, and expensive,

1 dispute to declare itself a nonutility, which would have removed TRA's
2 regulatory jurisdiction over the actions of the utility. This effort failed
3 largely due to the failures listed above as well as legislative intervention, and
4 the utility remains subject to TRA regulation.

5 Discontented with this situation, a group of the utility's customers
6 acted under the rights afforded under the Tennessee Nonprofit Corporation
7 Act and organized additional customers to join the company as members.
8 These members then petitioned the utility to hold a specially called meeting
9 for the purpose of electing a new Board of Directors. A meeting was
10 scheduled for March 13, 2014.

11
12 **Q. What happened at the Special Meeting?**

13 A. Acting under the direction of state law and the company bylaws, a
14 quorum was established, a moderator elected, and Discussion was held.
15 This discussion included the opportunity for a representative of the Initial
16 Directors and their legal counsel to address the meeting. Representatives of
17 the Consumer Advocate Division of the Attorney General's Office were also
18 present at the meeting. After discussion, an election was held and five
19 customers of the utility were elected to serve as the Board of Directors for
20 the company. Also, members passed four resolutions to guide the new
21 Board in its oversight of the company.

22 During the course of the meeting, the representative of the Initial
23 Directors and their legal counsel expressed opposition to the actions being
24 considered (and eventually enacted). However, after subsequent discussion

1 with the newly elected Board the Initial Directors voluntarily resigned their
2 positions. All three Initial Directors recognized the newly-elected Board's
3 authority through a Resolution of Resignation that was signed by on April 3,
4 2014.

5
6 **Q. What resolutions were passed by the Members?**

7 A. The complete text of the resolutions are included with this testimony
8 as Appendix One. In summary, the members required the new Board to
9 take action to secure the assets of the corporation, change the company's
10 charter to require all future directors to be elected by the company's
11 membership, require the company to be operated under the seven
12 principles of a member-owned cooperative, make annual reports to the
13 company's members of the utility's financial condition, and immediately
14 begin a complete strategic review of the company's financial and
15 operational condition.

16
17 **Q. Please tell us the names and a brief biography of the new Board Members.**

18 A. Mike Knotts is a native of Middle Tennessee, and works as the
19 director of government affairs for the Tennessee Electric Cooperative
20 Association where he represents Tennessee's 23 electric cooperatives
21 before the state legislature and the U.S. Congress. He and his wife, Jen, have
22 four young sons and are members of Christ Presbyterian Church.

23 Steve Seger, his wife Jen, and their three children have lived in
24 Williamson County since 2000. He has over 14 years experience working

1 with utilities and cooperatives, and currently serves on the Board of
2 Directors of the Middle Tennessee Electric Membership Corporation. He is
3 also President of Crosstown, a logistics company.

4 Tom Moore is a Nashville native and attended Vanderbilt University.
5 He has 10 years of CIO experience and worked with the Association of
6 American Railroads, Baker Distributing Company, and the School Board of
7 Clay County, FL. Presently, he is the Director of Project Management Office
8 for Watsco, Inc. He and his wife, Susan, have five daughters and 11
9 grandchildren.

10 Bill Goodwin is an independent oilman, and has previously worked as
11 press secretary to U.S. Senator Bill Brock and also as a campaign consultant
12 and press secretary to Bob Dole for President in 1980. He and his wife,
13 Linda, have lived in Franklin for 15 years. Bill has three children and four
14 grandchildren.

15 James Savage has been a resident of the area for 19 years, where he
16 and his wife, Zuzu, have raised their daughter. A graduate of Syracuse
17 University, Tennessee State University, and Nashville State Technical
18 College, he is currently a software engineer for InStock Retail Services, Inc.
19 He has previously worked as the director of the Vanderbilt University
20 bookstore.

21
22 **Q. Please describe how the new Board has approached its responsibilities?**

23 **A.** Immediately upon assuming full control of the company after the
24 resignation of the Initial Directors, the Board began its strategic review of

1 the company. Each Board member received approximately 1000 pages of
2 information that was requested of the company's management consultant.
3 These documents included background information (charter, bylaws, and all
4 Board minutes), operational information (tariffs, overview of physical plant,
5 copies of permits, breakdowns of customers by class, profiles of company
6 employees), financial information (copies of all audit reports, complete
7 financial statements since company inception, copies of all
8 contracts/agreements with third party providers, tax returns, and detailed
9 information about assets and liabilities), and copies of all pending requests
10 before TRA, including this docket. Company employees and contractors
11 were interviewed to further investigate the current state of the company.

12 The Board also took immediate action to eliminate conflicts of
13 interest in the company operations. The company's officers were changed
14 to eliminate the conflict inherent in the situation we found which was that
15 of a previous owner, contractor to the company, and creditor to the
16 company simultaneously serving as President.

17 Additionally, the Board has developed a strategic path forward to
18 ensure future solvency. The objectives of these strategic actions are to first,
19 and always, continue to operate the utility's collection and treatment
20 systems in full compliance with the permits issued by the Tennessee
21 Department of Environment and Conservation. Then, the Board seeks to
22 fully develop the company's governance and ownership model into that of a
23 member-owned cooperative, restate the company financials based upon a
24 commonly accepted asset valuation method to more accurately reflect the

1 value of the company's plant, significantly lower the company's long term
2 debt liabilities, begin to prepare for future capital improvement and
3 replacement needs through a combination of cash savings and increased
4 credit worthiness, and implement an operating structure that provides the
5 highest level of value to the end-use customer over the long-term.

6 These actions are ongoing, and are highly interdependent upon
7 successful completion of each of the other items to be successful.
8 Stabilization of the rate base, including resolving the uncertainty of
9 revenues due to this outstanding rate increase request, is a central building
10 block to these efforts.

11 Lastly, I would remind the Directors that the Board's actions are being
12 taken without regard to any personal financial considerations outside of the
13 rates that we, like any customer of the utility, pay for sewer service. No
14 member of the Board is being compensated, nor does any member of the
15 Board have an ownership interest or other business relationship with the
16 company.

17
18 **Q. What else has the new Board done to educate itself about this rate case?**

19 **A.** The Board has held meetings with numerous third parties involved in
20 the rate case to provide deeper analysis and afford the opportunity for the
21 Board to ask detailed questions about the request. Participants in these
22 meetings have included Mr. Terry Buckner (the company's accountant and
23 author of the original rate request), our legal counsel, as well a meeting with
24 the entire staff of the Consumer Advocate Division of the Attorney General's

office.

While not specifically pertaining to this rate request, the Board also held a meeting with Mr. Jerry Kettles and Mr. Shiva Bozarth of the TRA's staff to seek their historical and institutional knowledge of the issues surrounding the utility. Their input and background was very valuable in our decision making process.

Q. What conclusion(s) has the new Board reached?

A. After three month review all of the relevant information, we agree with the assertion that the company's current revenue is insufficient to ensure that the utility will continue to be able to exist as an independent entity over the long term. At this time, the company is using its depreciation costs to cover expenses, and the company cannot survive doing that for much longer.

However, the Board believes that its ongoing cost containment efforts and operational evaluation are having, and will continue to have, a positive impact on the company's operational efficiency. For the time being, the Board believes the company's current cash flow is sufficient to ensure the base level of necessary expenditures to continue short-term operations of the utility, at least until the Board has a better idea of the success of our cost-containment efforts and the status of the company's debt obligations.

Therefore we wish to alter the request made in this docket to reflect the utility's two most urgent financial needs, which must be addressed now – financial security and capital improvements/replacements. At this time,

the Board has decided to hold off requesting additional revenue, which would allow us to stop the practice of monetizing depreciation and would provide revenue for debt payments.

Q. Please explain further.

A. Harpeth Wastewater is requesting that the TRA approve the following additions to its tariff. First, we wish to add a \$4 per month “Capital Improvement Surcharge” to each customer’s bill for a period of twenty-four months. It would appear as a separate line item and would include an expiration date in the verbiage, for those bills that are produced in-house by HWC (bills prepared by some of our customers’ water provider, the City of Franklin, may not have this ability due to the City’s technical limitations). These funds would be collected and deposited into an escrow account, the use of which would be reserved for improvements, repairs, and replacements of equipment that is deemed to be critical to the utility’s operations. The company’s use of this account will be subject to oversight by the TRA, similar to the arrangement as was approved in Docket #09-00056 for Cartwright Creek. LLC.

Second, we wish to add a \$1 per month “Financial Security Surcharge” to each customer’s bill for a period of up to 12 months. It would appear as a separate line item and would include the expiration date in the verbiage on those bills that are produced in-house by HWC (bills prepared by some of our customers’ water provider, the City of Franklin, may not have this ability due to the City’s technical limitations). These

1 funds would be collected and deposited into an escrow account, along with
2 the company's previously committed \$9,000, whose purpose is to satisfy
3 the TRA's financial security fund requirement.

4 Finally, we need approval for the four changes to our tariff as
5 detailed in Mr. Terry Buckner's direct testimony (in this docket) in the last
6 paragraph of page 9. These tariff changes will allow the company to charge
7 fees for late payment, disconnection, and reconnection, and to charge a fee
8 for handling new applications for service. These fees are comparable to
9 fees charged by other utilities in Williamson County and will not affect
10 existing customers who pay their bills on time. These fees are not expected
11 to have a material impact on the company's overall revenues, but to the
12 extent these fees may help the bottom line, the company's revenues will
13 still be inadequate to cover its costs, including depreciation and debt costs.

14 I would reiterate that in this revised request, the company is not
15 requesting any additional funds for operations, but only for a base level of
16 "savings" to ensure the entity's continued existence should a major repair
17 or replacement be required. Given the age of the utility's facilities, the
18 Board believes such an event is likely. It would be imprudent, if not
19 irresponsible, for the Board to ignore that possibility.

20 We believe this to be a modest and prudent request based on the
21 long-term health of the utility. The amount we ask for today is a greater
22 than 50% reduction in the company's original request, and is time limited
23 by 24 and 12 months, respectively. This phase-out of the surcharges will
24 bring the long-term effect of the request to near zero.

1

2 **Q. Are these the only rate changes the Board is requesting?**

3 A. Yes.

4

5 **Q. Have you communicated this reduced rate request to the members and to**
6 **those customers who are not yet members?**

7 A. A letter communicating this information was mailed to all customers of
8 record on June 24, 2014. A draft copy is included as Appendix Two.

9

10 **Q. What has been the reaction of customers to the news of a potential rate**
11 **increase?**

12 A. As a part of the transition process, the Board has been attempting to
13 communicate frequently with its customers about the company's changes.
14 A letter was mailed to all customers on April 17, 2014 to inform them of the
15 change in governance, as well as the change in the company's name. That
16 letter was filed in this docket, as well as docket #14-00048. Language has
17 been added to each customer's monthly bill (for the customers who receive
18 their bill from HWC rather than a third-party water provider) providing
19 basic information about the changes. Further, Board members have
20 appeared at the meetings of two of the three Homeowners Associations
21 that represent the majority of the company's customers (we continue to
22 seek an opportunity to meet with the third HOA, but thusfar have not
23 received a positive response to our requests). In these meetings, we have
24 attempted to be candid about the poor financial condition that the

1 company is currently in as well as the steps that will be required to remedy
2 it.

3 To paraphrase the reaction of a Board member of the Cottonwood
4 HOA, he understood that it was entirely possible that rates would need to
5 increase again “but if it is a group of my neighbors who have done their
6 homework and come to that conclusion, then I’m OK with that.”

7 His reaction, along with many others like it, is indicative of the
8 understanding that the customers now control the company, not an owner
9 with a profit or value-growth motive. Given that independent Directors
10 whose fiduciary duty is owed to the customers are making decisions, the
11 lingering suspicion by the customer base about the company’s motives
12 seems to have greatly diminished.

13 And the new Board members have a system of accountability that
14 the previous owners never subjected themselves to – if the customer base
15 decides that the Board is off course, then they will exercise their rights to
16 vote us out, and elect a different Board. This is the cooperative business
17 model in action.

18
19 **Q. Since the company is now a cooperative, do you believe continued**
20 **TRA regulation is needed to protect the interests of the customers?**

21 **A.** As instructed by the customers through the resolutions passed at the
22 Special Meeting, the company is now being operated under the seven
23 cooperative principles. The Board believes the cooperative business model
24 provides the greatest likelihood of long-term solvency for a utility as small

1 as Harpeth Wastewater because of the long track record of success of small
2 cooperative utilities all across America, the inherent accountability of
3 member-elected Directors, and the integral incentive to contain costs --
4 which therefore creates an environment in which a lowering of rates is
5 both desired and achievable, while all the while continuing to maintain
6 adherence to the operating permits issued to the utility by the State.

7 However, Tennessee statutes only recognize electric and phone
8 cooperatives as their own stand-alone cooperative entities. Other
9 cooperatives, like HWC, are non-profit corporations who have committed
10 to operative under cooperative principles. Upon the advice of our legal
11 counsel, therefore, there are some additional steps that need to be taken
12 by the company's Members to more fully complete the transition into a
13 cooperative model. The Board has scheduled an annual meeting on August
14 23, 2014 for the Members to hear reports on the finances and operations
15 of the utility, as well as conduct other business of the company.

16 Of course, the company cannot end TRA's jurisdiction of its activities
17 on its own. We believe that should the legislature take action to recognize
18 water and/or wastewater cooperatives in the same way as electric and
19 telephone cooperatives are recognized, that TRA regulation of HWC would
20 not be necessary. In fact, continued regulation of the company after the
21 enactment of such legislation would be duplicative because the customers
22 of the utility are already applying appropriate oversight through the
23 member-elected Board of Directors. Monopoly status is not a concern
24 since its members own all of the company's assets, and there is no distant

1 third-party in a position to take advantage of end-users. Further, continued
2 regulation could even be detrimental to the customer due to the high costs
3 of complying with a complex and inflexible regulatory process intended to
4 apply to large, for-profit companies that bear little to no resemblance to a
5 850 customer, member-owned, non-profit cooperative.

6
7 **Q. Does this conclude your testimony?**

8 **A. Yes.**

APPENDIX ONE**RESOLUTION**

WHEREAS, the members of Berry's Chapel Utility, Inc., so gathered in a specially called meeting on March 13, 2014, desire for the utility to respond to our wishes,

BE IT SO RESOLVED, that the members hereby instruct the Board of Directors to amend the Charter of the Corporation, filed with the State of Tennessee, to reflect a new registered agent. That person shall be a person whom the Board of Directors shall select, and shall entrust with the responsibility of serving as the registered agent.

FURTHER BE IT SO RESOLVED, the Board of Directors is empowered to add the following additional item to the Charter:

XX (Insert proper numbering here). The corporation shall be operated at all times in a manner consistent with the principles embodied by a member-owned cooperative, which were adopted by the International Cooperative Alliance in 1995. These principles include: voluntary and open membership, democratic member control, members economic participation, autonomy and independence, education, training, and information, cooperation among cooperatives, and concern for community.

FURTHER BE IT SO RESOLVED, the Board of Directors is empowered to add the following additional item to the Charter:

XX (Insert proper numbering here). The corporation held its first election of directors from within the membership on March 13, 2014 at special called meeting of the members. All directors henceforth shall be elected by the members, either at a special or annual meeting, excepting cases of vacancies of directors in which case the bylaws of the corporation shall describe a method of replacement until the next special or annual meeting of the members.

1
2 RESOLUTION

3
4 WHEREAS, the members of Berry's Chapel Utility, Inc., so gathered in a specially
5 called meeting on March 13, 2014, desire for the utility to respond to our wishes,

6
7 BE IT SO RESOLVED, that the members hereby authorize the Board of Directors
8 to take whatever actions are lawful and appropriate to secure the assets of the
9 corporation and change the corporate documents to reflect the election of directors.

1
2
3 RESOLUTION

4
5 WHEREAS, the members of Berry's Chapel Utility, Inc., so gathered in a specially
6 called meeting on March 13, 2014, desire for the utility to respond to our wishes,

7
8 BE IT SO RESOLVED, It is the intent of the membership of Berry's Chapel
9 Utility, Inc. to instruct the newly elected Board of Directors to conduct a strategic
10 review of the operations of the company over the next 30 days. This review should
11 include a review of the company bylaws, an inventory of all of the assets and
12 liabilities of the company, an inspection of all contracts and agreements entered into
13 by the previous management, and an evaluation of the operational efficiency of the
14 company. Upon completion of this review, a written summary of all actions taken
15 and any actions required by the members will be communicated to all members of
16 the corporation.
17
18

1 RESOLUTION

2

3 Resolution to instruct the Board of Directors to present an Annual Report
4 within 90 days of the Corporations fiscal year annually to the members in
5 written form or digitally.

6

1 APPENDIX TWO



Harpeth Wastewater Cooperative

www.harpethcoop.com (615) 764-0074 106 Mission Court Suite 203A Franklin, TN 37067

June 24, 2014

Name
4321 First Street
Anytown, State ZIP

Dear {Name},

It has been almost two months since we wrote to inform you that Berry's Chapel Utility, Inc., your sewer provider, has become the Harpeth Wastewater Cooperative. Since that time the customer-elected Board of Directors has been conducting a strategic review of the company. While the review is not fully complete, a number of new financial controls and cost containment efforts have gone into effect. Additionally, the company is working to eliminate and/or substantially reduce the long-term debts that are putting tremendous upward pressure on the rates the company must charge to recoup its costs. We believe these efforts, along with additional cost savings, will provide enough revenue to allow the utility to perform its basic mission of treating sewage and protecting the Harpeth River.

What has been most surprising to us, however, is the fact that the utility is operating with no cash savings or any ability to borrow funds for a significant capital expenditure. For instance, if a large piece of equipment at the sewer treatment plant were to fail, the company has no ability to replace that equipment and would be unable to perform its mission. This is a significant problem that requires immediate action.

The previous owners of the utility had requested from the Tennessee Regulatory Authority a rate increase of \$9 per customer, per month, that would be indefinite in nature. This week, we will be amending that request. We are asking for approval to collect a \$4 per month capital improvement fee, which will only be collected for 24 months and will be held in an escrow account to be used only for equipment replacement and repairs. Further, we are asking for a \$1 per month fee to provide for a state-mandated "financial security fund," which will only be collected for 12 months.

We take our two responsibilities to you very seriously: to provide a necessary service, and provide it at the lowest possible cost. This step is absolutely necessary to ensure that your sewer service can continue to operate. To read the full request or provide comments to us about this change, please visit our website at www.harpethcoop.com.

On behalf of the Board of Directors,

Mike Knotts
Chairman