PUGET SOUND PILOTS

SPECIAL-PURPOSE
FINANCIAL STATEMENTS AND
(MODIFIED ACCRUAL BASIS)

FOR THE YEARS ENDED
DECEMBER 31, 2019 AND 2018

PUGET SOUND PILOTS

TABLE OF CONTENTS

Shannon & Associates LLP
Certified Public Accountants
Management Consultants

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Puget Sound Pilots
Seattle, Washington

We have audited the accompanying special-purpose financial statements of Puget Sound Pilots (a voluntary association of sole proprietors and incorporated individuals), which comprise the special-purpose statements of assets, liabilities and pilots' equity - modified accrual basis as of December 31, 2019 and 2018, and the related special-purpose statements of revenues, expenses and changes in pilots' equity - modified accrual basis and cash flows - modified accrual basis for the years then ended, and the related notes to the special-purpose financial statements.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these special-purpose financial statements in accordance with the modified accrual basis of accounting as described in Note 1; this includes determining that the modified accrual basis of accounting is an acceptable basis for preparation of the special-purpose financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair preparation of special-purpose financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility
Our responsibility is to express an opinion on these special-purpose financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the special-purpose financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the special-purpose financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the special-purpose financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the special-purpose financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the special-purpose financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the special-purpose financial statements referred to above present fairly, in all material respects, the assets, liabilities, and pilots' equity of Puget Sound Pilots , as of December 31, 2019 and 2018, and its revenues, expenses and changes in pilots' equity, and cash flows for the years then ended, in accordance with the modified accrual basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the special-purpose financial statements, which describes the basis of accounting. The special-purpose financial statements are prepared on the modified accrual basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

Restriction on Use

This report is intended solely for the information and use of Puget Sound Pilots, the Washington State Board of Pilotage Commissioners, and the Utilities and Transportation Commission and is not intended and should not be used by anyone other than these specified parties.

Shannon & Associates, LLP

Kent, Washington
May 21, 2020

PUGET SOUND PILOTS
STATEMENTS OF ASSETS, LIABILITIES AND PILOTS' EQUITY - MODIFIED ACCRUAL BASIS
DECEMBER 31, 2019 AND 2018

ASSETS

		2019	2018	Increase (Decrease)
1.	**CURRENT ASSETS**			
2.	Cash in banks	$ 1,131,779	$ 1,495,202	$ (363,423)
3.	Accounts receivable, net of allowance for doubtful accounts of $5,500 at each year end	2,034,737	2,542,397	(507,660)
4.	Prepaid expenses	84,763	75,641	9,122
5.	**TOTAL CURRENT ASSETS**	3,251,279	4,113,240	(861,961)
6.	**PROPERTY, BOATS AND EQUIPMENT**			
7.	Total building, boats, furnishings, and equipment	9,887,515	10,159,007	(271,492)
8.	Less accumulated depreciation and amortization	8,888,429	9,122,378	(233,949)
9.	**NET PROPERTY, BOATS AND EQUIPMENT**	999,086	1,036,629	(37,543)
10.	**OTHER ASSETS**			
11.	Loan fees, net of accumulated amortization of $920 and $690 as of 2019 and 2018	230	460	(230)
12.	**TOTAL ASSETS**	$ 4,250,595	$ 5,150,329	$ (899,734)

The accompanying notes are an integral part of these special-purpose financial statements.

PUGET SOUND PILOTS
STATEMENTS OF ASSETS, LIABILITIES AND PILOTS' EQUITY - MODIFIED ACCRUAL BASIS
DECEMBER 31, 2019 AND 2018

LIABILITIES AND PILOTS' EQUITY

		2019	2018	Increase (Decrease)
13.	**CURRENT LIABILITIES**			
14.	Funds held in trust (See Note 3)	$ 122,815	$ 150,772	$ (27,957)
15.	Accrued taxes	34,427	38,163	(3,736)
16.	Retirement expense payable	426,243	393,599	32,644
17.	Line of credit	250,000	-	250,000
18.	Current portion of long-term liabilities	92,000	92,000	-
19.	**TOTAL CURRENT LIABILITIES**	925,485	674,534	250,951
20.	**LONG-TERM LIABILITIES, net of current portion**	22,997	114,997	(92,000)
21.	**TOTAL LIABILITIES**	948,482	789,531	158,951
22.	**PILOTS' EQUITY**			
23.	December distributions payable to pilots	989,644	1,481,341	(491,697)
24.	Reserved for operations	750,000	750,000	-
25.	Reserved for working capital account	40,993	356,444	(315,451)
26.	Remainder of pilots' equity	1,521,476	1,773,013	(251,537)
27.	**TOTAL PILOTS' EQUITY**	3,302,113	4,360,798	(1,058,685)
28.	**TOTAL LIABILITIES AND PILOTS' EQUITY**	$ 4,250,595	$ 5,150,329	$ (899,734)

The accompanying notes are an integral part of these special-purpose financial statements.

PUGET SOUND PILOTS
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN PILOTS' EQUITY - MODIFIED ACCRUAL BASIS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

	2019		2018	
	Amount	Percent	Amount	Percent
1. **PILOTAGE REVENUE**	$ 33,691,939	100.0 %	$ 33,996,799	100.0 %
2. **OPERATING EXPENSES**				
3. Seattle office operating expense and administrative overhead	11,857,741	35.2	10,252,297	30.2
4. Boat operating expense	1,913,854	5.7	1,679,687	4.9
5. Port Angeles station operating expense	494,663	1.5	538,388	1.6
6. **TOTAL OPERATING EXPENSES**	14,266,258	42.4	12,470,372	36.7
7. **TRANSPORTATION FEES PAID DIRECTLY TO PILOTS**	698,613	2.1	1,036,161	3.0
8. **NET INCOME FROM POOLED OPERATIONS**	18,727,068	55.6	20,490,266	60.3
9. **OTHER INCOME (EXPENSE)**				
10. Interest income and finance charges	2,096	0.0	(6,355)	(0.0)
11. Loss on asset disposal	(535)	(0.0)	-	-
12. **TOTAL OTHER INCOME (EXPENSE)**	1,561	(0.0)	(6,355)	(0.0)
13. **BALANCE OF REVENUE POOL BEFORE DEDUCTIONS OF INDIVIDUAL PILOTS' BUSINESS EXPENSES**	18,728,629	55.6 %	20,483,911	60.3 %
14. **LESS PER DETAIL BELOW**				
15. Buy-ins and buy-outs, net	(315,451)		(246,363)	
16. All other payments to pilots	(19,471,863)		(20,509,887)	
17. **TOTAL DETAIL**	(19,787,314)		(20,756,250)	
18. **NET DECREASE IN PILOTS' EQUITY**	(1,058,685)		(272,339)	
19. **BEGINNING PILOTS' EQUITY**	4,360,798		4,633,137	
20. **ENDING PILOTS' EQUITY**	$ 3,302,113		$ 4,360,798	

The accompanying notes are an integral part of these special-purpose financial statements.

PUGET SOUND PILOTS
STATEMENTS OF CASH FLOWS - MODIFIED ACCRUAL BASIS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

		2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES			
1.	Balance of revenue pool before deductions of individual pilots' business expenses	$ 18,728,629	$ 20,483,911
	Adjustments to reconcile balance of revenue pool to cash provided by operating activities:		
2.	Depreciation and amortization	157,800	162,429
3.	Loss on disposal of assets	535	-
4.	Decrease (increase) in net accounts receivable	507,660	(71,036)
5.	Decrease (increase) in prepaid expenses	(9,122)	5,000
6.	Increase (decrease) in funds held in trust (see Note 3)	(27,957)	72,697
7.	Decrease in accrued taxes	(3,736)	(512)
8.	Increase in retirement expense payable	32,644	16,094
9.	NET CASH PROVIDED BY OPERATING ACTIVITIES	19,386,453	20,668,583
CASH FLOWS FROM INVESTING ACTIVITIES			
10.	Purchase of property, boats, furnishings, and equipment	(120,562)	-
CASH FLOWS FROM FINANCING ACTIVITIES			
11.	Proceeds from line of credit	250,000	-
12.	Principal payments on notes payable	(92,000)	(92,000)
13.	Payments from buy-in and buy-outs, net	(315,451)	(246,363)
14.	Payments to members	(19,471,863)	(20,509,887)
15.	NET CASH USED IN FINANCING ACTIVITIES	(19,629,314)	(20,848,250)
16.	**NET DECREASE IN CASH**	(363,423)	(179,667)
17.	Cash at beginning of year	1,495,202	1,674,869
18.	Cash at end of year	$ 1,131,779	$ 1,495,202
Supplemental disclosure of cash flow information			
19.	Interest paid	$ 5,277	$ 8,203

The accompanying notes are an integral part of these special-purpose financial statements.

NOTE 1.--NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The Puget Sound Pilots (PSP) is a voluntary association of sole proprietors and incorporated individuals. As such, it is an organization made up of independent contractors who pool revenue and expenses and who operate together for administrative purposes in providing regulated pilotage services. They do so for the efficiency of the membership and also, for the benefit of their commercial customers. The association provides centralized dispatch and enables customers to streamline and consolidate pilotage service orders and communications with independent pilotage service providers ("pilots") in one place rather than relying upon direct contacts of individual pilots who may be providing services at remote locations, distant from those where the customer has pressing service needs and who is also aware of all of the safety and operating protocols of an experienced and established pilotage association.

Their abiding mission is to ensure against the loss of lives, loss of or damage to property and vessels, and to protect the marine environment by maintaining efficient and competent pilotage service on our State's inland waters within the Puget Sound Pilotage District. They pilot vessels under licenses issued by the U.S. Coast Guard and the State of Washington. Customers are international and domestic companies that pay prescribed rates to utilize pilotage services within Puget Sound. Their business is conducted in accordance with the Pilotage Act of the State of Washington and outlined in RCW 88.16. Pilotage revenues are dependent on the tariff set by the Washington State Board of Pilotage Commissioners ("Board") and the levels of maritime traffic on these waters. Recently the Washington State legislature enacted a bill (SB 6519) revising the procedure for marine pilotage tariffs and that was signed into law on March 15, 2018. That law transferred the function of marine pilotage rate setting from the Board of Pilotage Commissioners to the Washington Utilities and Transportation Commission ("Commission"), effective July 1, 2019.

The accompanying special-purpose financial statements have been prepared on the modified accrual basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. That basis differs from accounting principles generally accepted in the United States of America in that payments to vendors are recognized when paid instead of when goods or services are received. Also, payments to employees and the executive director for compensated absences (sick leave) are recognized when paid instead of when the leave is earned, and payments to pilots for compensated absences (vacation, callback and sick leave), retirement, major medical and redemption of member ownership interests (buy-outs) are recognized when paid rather than when the leave is earned or liability incurred. See Notes 6 and 10 for unrecorded liabilities.

NOTE 1.--NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

Pilotage revenue is recognized on the accrual basis of accounting when services are performed. Pilotage services are invoiced to their commercial customers in accordance with the tariff regulated by the Washington State Board of Pilotage Commissioners (WAC 363-116-300) (see above). The tariff is designed to cover current operating costs and liabilities and to provide fair, just and reasonable compensation for pilots. In 2019, the law transferred the function of the rate setting from the Washington State Board of Pilotage Commissioners to the Utilities and Transportation Commission. However, during 2019 there were no rate changes and the rates in place were those set by the Washington State Board of Pilotage Commissioners. The last tariff rate adjustment occurred in July 2015.

Pilot Distributable Revenue and Reimbursed Expenses

Puget Sound Pilots passes all revenue and expenses to the individual pilots monthly which is considered a distribution. Puget Sound Pilots is not in the business of retaining profits or providing a return on investment to the individual members (pilots). The objective is to optimize individual member monthly distributions by billing for all pilotage services on behalf of the members and maintaining efficient operations in which to minimize administrative expenses. As a result, each individual pilot receives a monthly distribution which is calculated as an equal share (based on duty days) of all billed revenue net of paid expenses.

In addition, each pilot is reimbursed for travel expenses that they personally incur. These reimbursements come in the form of TEC travel reimbursements as outlined in the tariff (pass through of direct charge to customer) as well as a Port Angeles reposition reimbursement ($163 per reposition assignment). During 2019, a trial was conducted for three months (February through April) to determine the reasonableness of the reimbursements being paid and to compare to the amounts that would have been reimbursed to pilots. This was done by suspending both travel reimbursements for February through April and having PSP as an organization pay all out of pocket travel costs. As a result, for year ended December 31, 2019 individual pilot reimbursement amounts were lower (in total) by $261,492. The results of the transportation trial were as follows:

Total assignments with TEC		1,519
TEC billed to customers	$	209,495
Actual TEC assignment expenses	$	240,292
Total repo assignments		319

NOTE 1.--NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and Cash Equivalents

Cash in banks for purposes of the statements of cash flows, includes checking accounts, money market accounts, and certificates of deposit.

Accounts Receivable and Credit Policies

Accounts receivable are customer obligations due under trade terms requiring payment within 30 days from the invoice date. Accounts receivable are stated at the amount billed to the customer.

Finance charges are accrued at 1.5% monthly if payment is not made within the normal payment terms. Accounts over 90 days were $4,115 and $68,008 at December 31, 2019 and 2018, respectively.

PSP establishes an allowance for uncollectible trade accounts receivable based on historical collection experience and management's evaluation of collectability of outstanding accounts receivable.

Property, Boats, and Equipment

Building, boats, furnishings and equipment (including software) are carried at cost. Depreciation and amortization of these assets is provided by the straight-line method over the assets' estimated useful lives which range from 3 to 39 years. Leasehold improvements are amortized over the shorter of the lease term or the assets useful life.

Effective January 1, 2014, PSP instituted a policy under which expenditures of $5,000 or more representing major improvements, replacements or extension of useful lives of property, boats, furnishings and equipment are capitalized. Expenditures for maintenance and repairs are charged to expense as incurred. Major boat and engine repairs are expensed as incurred. Upon sale or retirement of property, boats, furnishings and equipment, the cost and related accumulated depreciation are eliminated from the respective accounts and the resulting gain or loss is included in the results of operations. Depreciation and amortization for the years ended December 31, 2019 and 2018, was $157,800 and $162,429, respectively.

Other Assets

Loan fees are recorded at cost and amortized on the straight-line basis over the life of the loan.

NOTE 1.--NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

As a voluntary association of sole proprietors and incorporated individuals, the PSP files a US Partnership Return of Income, which is informational in nature. The income and expense of the PSP includes only items relating to the business of the PSP which pass on to the individual or corporate income tax returns of the pilots. Pilots are responsible for their own income, social security and Medicare taxes. Accordingly, no provision for federal income taxes is represented in the special-purpose financial statements.

Income Taxes (Continued)

PSP asserts on all filings with the Internal Revenue Service that it is a voluntary association of individual persons and corporations and is not a partnership for any purpose whatsoever, including taxation, per a 1954 IRS directive.

PSP measures and recognizes the implications of positions taken or expected to be taken in its tax returns on an ongoing basis in accordance with income tax guidance. PSP had no unrecognized tax benefits or liabilities and no adjustments to its financial position, results of operations or cash flows related to uncertain tax positions taken for the years ended December 31, 2019 and 2018. PSP is no longer subject to federal, state or local income tax examinations by tax authorities for years prior to 2016. If assessed, PSP recognizes penalties and interest associated with tax matters as part of operating expenses.

Use of Estimates

The preparation of special-purpose financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the special-purpose financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2.--PROPERTY, BOATS AND EQUIPMENT

Property, boats and equipment are summarized as follows:

	2019	2018
Port Angeles station building	$ 2,104,532	$ 2,104,532
Port Angeles station furnishings and equipment	150,684	153,542
Boat "Juan de Fuca"	3,221,448	3,229,434
Boat "Puget Sound"	3,639,784	3,718,327
Seattle office furnishings, furniture and equipment, including computers	771,067	857,513
Portable radio equipment	-	95,659
	9,887,515	10,159,007
Less accumulated depreciation and amortization	8,888,429	9,122,378
	$ 999,086	$ 1,036,629

NOTE 3.--FUNDS HELD IN TRUST - TRAINING SURCHARGE, SELF-INSURANCE LIABILITY PREMIUM AND GRAYS HARBOR PENSION

Funds held in trust at December 31, 2019 and 2018, consisted of the following:

	2019	2018
Pilotage Commission Trust - trainee surcharge	$ 108,095	$ 134,420
Pilotage Commission self-insurance premium	14,720	16,352
	$ 122,815	$ 150,772

Pilotage Commission Trust – Pilot Trainee Surcharge

PSP acts as a fiduciary agent for the Washington State Board of Pilotage Commissioners (Commission) and collects a training surcharge on behalf of the Commission. This fee is set by the Commission and is invoiced by PSP on a per trainee and per-assignment basis. The funds are scheduled to be transmitted by PSP to the Commission on a monthly basis.

Pilot Trainee surcharge detail for years ended December 31, 2019 and 2018, consisted of the following:

NOTE 3.--FUNDS HELD IN TRUST - TRAINING SURCHARGE, SELF-INSURANCE LIABILITY PREMIUM AND GRAYS HARBOR PENSION (Continued)

	2019	2018
Pilot Trainee surcharge billed to customers (excluded from Pilotage Revenue on Page 7)	$ 926,055	$ 777,105
Pilot Trainee surcharge collected from customers	952,725	732,285
Collected and due to Pilotage Commission at December 31, 2019 and 2018	70,725	70,380
Billed and uncollected amounts due to Pilotage Commission at December 31, 2019 and 2018	41,415	68,085

Pilotage Commission Trust – Self-insurance Liability Premium (SILA)

PSP acts as a fiduciary agent for the Washington State Board of Pilotage Commissioners (Commission) and collects a self-insurance liability account surcharge on behalf of the Commission. This fee was established as a result of the Washington legislative action in 2017.

In order to promptly comply with the provisions described in the Engrossed Senate bill 5096 Sec. 108, effective May 18, 2017, the Commission filed a new rule under emergency provisions. A public hearing was held at a future date in order to permanently adopt the rule, WAC 363-116-301 New Revenue Collection: Effective May 18, 2017 through June 30, 2021, Engrossed Senate Bill No. 5096 Section 108, the board of pilotage commissioners is appropriated $1,100,000 from the multimodal transportation account solely for self-insurance liability premium expenditures.

This appropriation requires three stipulated conditions: 1) The Puget Sound Pilots shall pay to the board, from its tariffs, $150,000 annually through July 1, 2020. 2) The board shall maintain the Puget Sound pilotage tariff at the rate which became effective on January 1, 2017. 3) A self-insurance premium surcharge of $16 shall be added to each Puget Sound pilotage assignment on all vessels requiring pilotage. The Puget Sound Pilots shall remit the total amount of such surcharge generated to the board by the 10th of each month. The surcharge is in effect from July 1, 2017 through June 30, 2021.

Self-insurance premium surcharge payable detail for years ended December 31, 2019 and 2018, consisted of the following:

NOTE 3.--FUNDS HELD IN TRUST - TRAINING SURCHARGE, SELF-INSURANCE LIABILITY PREMIUM AND GRAYS HARBOR PENSION (Continued)

	2019	2018
Self-insurance premium surcharge billed to customers (excluded from Pilotage Revenue on Page 7)	$ 112,000	$ 117,168
Self-insurance premium surcharge collected from customers	114,432	117,520
Collected and due to Pilotage Commission at December 31, 2019 and 2018	9,312	8,512
Billed and uncollected amounts due to Pilotage Commission at December 31, 2019 and 2018	5,406	7,840

Grays Harbor Pension

Following a public hearing on August 9, 2001, the Washington State Board of Pilotage Commissioners, by lawful motion, directed “that funds derived from the application of the Grays Harbor Pilotage District tariff (Pension Charge) for the purposes of offsetting a proportionate share of pension expenses will be remitted to Puget Sound Pilots for payment to retirees of the Grays Harbor Pilotage District and that Puget Sound Pilots will include reporting of the revenue and expenses in their annual audited Financial Statements.” On March 15, 2018, Washington Senate Bill SB6519 passed and amended RCW 53.08.390, Sec 2, 5(b) mandating that the Grays Harbor port district must include a charge in its pilotage tariff for Grays Harbor to cover costs associated with the pilot retirement agreement expenses for Grays Harbor pilots employed prior to October 1, 2001. This charge will be collected and accounted for by Port of Grays Harbor solely for the Grays Harbor pilot retirement agreement expenses. As a result, effective April 2018, an agreement was reached in which the Puget Sound Pilots would no longer pay the pension on behalf of Grays Harbor. There were no expenses paid by Puget Sound Pilots for Grays Harbor pilots in 2019.

2018 Grays Harbor Pilotage District Pension expense (included in Seattle Office Operating Expense and Administrative Overhead, Page 7)	$ 16,070

2018 Detail of Grays Harbor Pension Expense

Capt. J.M. Hoyne	$ 6,502
Capt. B. Watson	9,568

NOTE 4.--LONG-TERM LIABILITIES

Long-term liabilities at December 31, 2019 and 2018, consisted of the following:

	2019	2018
Dispatch software note payable to bank secured by PSP assets bearing interest at 1.50% plus the lender's cost of funds (total rate of 3.16% at both December 31, 2019 and 2018), monthly payments of $6,022 began May 1, 2016, maturing April 1, 2021.	$ 114,997	$ 206,997
Less current portion	(92,000)	(92,000)
Total long-term liabilities	$ 22,997	$ 114,997

Total interest expense on all borrowings was $5,277 and $8,203 for the years ended December 31, 2019 and 2018.

Estimated future maturities of notes payable are as follows:

Years ending December 31,	
2020	$ 92,000
2021	22,997
2022	-
Thereafter	-
	$ 114,997

NOTE 5.--LINE OF CREDIT

PSP has a line of credit with a bank in the amount of $500,000 that expires September 25, 2020. The line of credit bears interest at an annual rate equal to the 1-month LIBOR rate plus 1.35%. The interest rate was 3.04% at December 31, 2019. The balance outstanding at December 31, 2019 and 2018 was $250,000 and $0, respectively. Accounts, equipment, and other assets are security on the line. The agreement also requires PSP to provide periodic and annual financial statements prepared in accordance with generally accepted accounting principles. The bank has been provided with these special-purpose financial statements prepared in accordance with the modified accrual basis of accounting.

NOTE 6.--RETIREMENT PLANS AND UNRECORDED LIABILITY - PILOTS AND FORMER EXECUTIVE DIRECTOR

A retirement program, identified as Plan 1, was adopted in 1982 and most recently amended in August 2006. The program provides each retired pilot and a former executive director an annual income (paid monthly) of 1.50% of the average of the final three years Target Net Income, as established by the Pilotage Commission (or actual average net income for any year in which there is no target net income) multiplied by the number of years of service.

Pilots who retired between December 31, 1978, and December 31, 1981, participate in a retirement plan known as the "Retirement Agreement of 1978." Members who retired prior to that date participate in a smaller plan known as the "Trust Contract." Surviving spouses of members receive a benefit equal to 50% of the member's entitlement.

As part of an agreement with the Board, PSP was paying retirement benefits for the retirees of the Grays Harbor Bar Pilots for many years. That agreement was terminated in 2018, see also explanation in Note 3.

Retirement payments to eligible recipients are made from currently earned PSP income. There is no separate, segregated fund for satisfaction of future retirement income. As of December 31, 2019, and 2018, there were no assets earmarked for future benefits. For nearly four decades, from 1967-2006, the Board recognized the annual ongoing costs of the pilot retirement plans as allowed expenses in revenues generated by the pilotage tariff. The Board has thus historically taken and appears to continue to take the added cost of the retirement plans into account when setting the overall tariff and there is no expectation by management that this will change. An estimate of the unfunded retirement program liability as of December 31, 2019 and 2018, has not been quantified. See Note 10 for further discussion of unrecorded liabilities.

NOTE 7.--RETIREMENT PLANS - EMPLOYEES

The PSP union employee retirement plan is defined in the collective bargaining agreement between PSP and the Inland boatmen's Union of the Pacific (Union).

The Union sponsors a contributory 401(k) plan so that employees may contribute a portion of their pretax income into a retirement plan. All Union employees are eligible to participate upon commencing employment. PSP does not sponsor or contribute to the Union's 401(k) plan. See Note 11 for Union pension information.

The PSP non-union employee retirement plan is a 401(k) plan. The plan allows for elective deferrals and provides a safe harbor match and discretionary profit sharing contribution. PSP contributions to the Plan for 2019 and 2018 were $31,353 and $29,535, respectively.

NOTE 8.--LEASES

Port Angeles Station

A building serving as a boarding and boat station is constructed on tidelands leased from the State of Washington. PSP has a lease with the State of Washington Department of Natural Resources that expires June 2021. The lease contains an 8-year renewal option. Rent expense related to this lease for 2019 and 2018 was $4,548 and $4,362, respectively.

Seattle Office

During 2019, the dispatching and management headquarters moved locations. The Seattle office was under a lease that expired October 2019. The new lease is for seven years ending November 2026 and has a five-year extension option. Both leases have annual increases in rental rate per square foot. Rent is expensed as incurred and not amortized ratably over the lease term. At the lease inception PSP incurred prepaid rent paid in the amount of $49,449. Based on the accounting policy (see Note 1), the full amount paid was expensed in 2019. Rent expense related to the Seattle location for 2019 and 2018 was $138,324 and $106,633, respectively.

PSP obtained an operating lease for PPU's in 2018. The lease is for 53 units for a period of 36 months effective July 1, 2018. Rent expense related to this lease for 2019 and 2018 was $339,108 and $198,826, respectively.

The following is a schedule of future minimum lease payments for non-cancelable operating leases with a term greater than one year as of December 31, 2019:

Years ending December 31,	
2020	$ 452,805
2021	258,309
2022	116,870
2023	120,369
2024	123,984
Thereafter	247,993
	$1,320,330

Total Leases

Total rent expense for all leases including parking, which is on a month-to-month agreement, was $548,151 and $331,086 for 2019 and 2018, respectively.

NOTE 9.--CONCENTRATIONS

PSP maintains cash balances in certain financial institutions that may, at times, exceed limits insured by the FDIC. PSP does not believe that it is exposed to significant credit risk on cash and cash equivalents as deposits are maintained in high quality financial institutions and PSP has not experienced any losses in such accounts.

NOTE 9.--CONCENTRATIONS (Continued)

One customer accounted for approximately 13% of accounts receivable at December 31, 2018. There were no accounts receivable concentrations at December 31, 2019.

PSP derives its income from services performed within Puget Sound waters. Any disruption of ship travel within this region may significantly affect revenues and services.

NOTE 10.--UNRECORDED LIABILITIES

As noted in Note 1, these special-purpose financial statements are prepared on the modified accrual basis of accounting. This method of accounting and reporting permits PSP to present these special-purpose financial statements without recording the related liability for goods and services received but not paid, employee services earned but not paid, and the various pilot services earned but not paid. Thus, PSP is on a "pay-as-you-go" basis for most liabilities.

The following are unrecorded liabilities at December 31, 2019 and 2018:

Individual pilots earn respite time in paid days for working engagements during the two-week off part of their two-week on (duty)/two-week off (respite) watch periods. In addition, members earn 1.4 days of vacation for each watch period worked. Whenever the volume of shipping requires, members on respite or vacation may be called back to perform assignments during their off duty (respite) period and be credited with a callback day (also known as a "comp day"). For years ended December 31, 2019 and 2018 total callback days outstanding were 3,481 and 3,143, respectively. The estimated value of those days was approximately $7,052,506 and $6,927,172, respectively.

Only a minor portion of the accumulated callback day total is ever either used by pilots moving ships or "burned" by pilots prior to active retirement. Many pilots "burn" accumulated callback days immediately prior to retirement which is the only component of accumulated callback days historically funded by the tariff at the Board of Pilotage Commissioners. For years ended December 31, 2019 and 2018 total callback days "burned" by pilots prior to retirement were 364 and 160, respectively. The estimated value of those days was approximately $737,464 and $352,640, respectively.

Historically, funds to pay the cost to PSP of these callback days while pilots are "burning" them have been provided by the tariff. Management has no reason to believe that this will change in the future. In addition, the value of a callback day is directly related to the earnings of an active pilot (balance of pilotage revenue pooled per pilot). If those earnings adjust up or down, the value of the callback day - and the amount of the unrecorded liability associated with it – adjusts up or down by the same amount.

NOTE 10.--UNRECORDED LIABILITIES (Continued)

PSP's major medical plan provides for a continuation of full-share distributions for up to six watches to pilots who, due to illness or injury, are physically unable to pilot. During 2019 and 2018, 7.5 and 15.4 monthly payments, respectively, were made to different pilots under this operating rule. An estimate of the liability for major medical as of December 31, 2019 and 2018, has not been determined.

As pilots retire, PSP buys their membership out over a period of six years. As of December 31, 2019, and 2018, the amount due to retired pilots under the membership buyout is approximately $4,355,105 and $3,736,439, respectively.

Redemption of pilot membership interest for pilots being paid out as of December 31, 2019, due for each of the next five years and in the aggregate, are as follows:

Years ended December 31,	
2020	$1,305,049
2021	1,004,505
2022	767,181
2023	727,113
2024	396,129
Thereafter	155,128
	$4,355,105

Annual unpaid vacation value at December 31, 2019, was approximately $903,393 and approximately $982,764 at December 31, 2018.

All Union employees earn vacation and sick leave in accordance with the Union contract. Employees are entitled to 6 days of sick leave per year and may only carry forward a maximum of 90 days.

The Executive Director earns vacation and sick leave in accordance with their contract. Unused sick leave may carryover from one year to another and may accrue up to a maximum of 90 days. An estimate of the liability for employee and Executive Director compensated absences as of December 31, 2019 and 2018, has not been determined.

NOTE 11.--COMMITMENTS AND CONTINGENCIES

Effective January 1, 2018 a collective bargaining agreement between the Puget Sound Pilots (PSP) and the Inlandboatmen's Union of the Pacific was contracted effective January 1, 2018 through June 30, 2021.

PSP contributes to the Union's Trust, the purpose of which is to provide for hospital, medical, dental, vision care, time loss and life insurance benefits for all Union employees. Contributions to the Trust were $272,526 and $258,150 for the years ended December 31, 2019 and 2018, respectively, and are recorded on the cash basis in the accompanying special-purpose financial statements.

NOTE 11.--COMMITMENTS AND CONTINGENCIES (Continued)

PSP also contributes to the Union's Trust, the purpose of which is to provide pensions and annuities for the benefit of employees who qualify under the provisions of the Union's retirement plan (Inlandboatmen's Union of the Pacific National Pension Plan) and to provide benefits to the beneficiaries of the employees. Contributions to the trust were $124,791 and $121,026 for the years ended December 31, 2019 and 2018, respectively, and are recorded on the cash basis in the accompanying special-purpose financial statements. Contributions include supplemental contributions under the Rehabilitation Plan adopted by the Union not to exceed 6.05% per year.

Under the terms of the Union contract, PSP makes "defined contributions" and not "defined benefits." PSP does not consent to the existence or maintenance of any funding deficiency. Accordingly, PSP's liability is limited to the making of contributions as prescribed by the agreement.

NOTE 12.--SUBSEQUENT EVENTS

Subsequent to year end, physical and economic conditions worldwide have been impacted by the COVID-19 pandemic. There are uncertainties surrounding COVID- 19's impact on the economy as a whole and on businesses. There is also uncertainty regarding the positive impact of any federal government relief efforts through the date of this report. Accordingly, the impact of the global pandemic on the operations and financial plans or future results of the Association as a going concern is unknown.

Management has evaluated subsequent events through May 21, 2020, the date which the financial statements were available to be issued.