

September 18<sup>th</sup>, 2007

Dear Chairman Sidran, Commissioner Oshie, Commissioner Jones, and WUTC staff:

We are aware of and appreciate the amount of work that the UTC Staff has put into this rate case, and we thank you all. Many in our community have also worked hard and diligently on these issues and we would like to provide you a brief view from the consumer side of these converging and complicated issues. After waiting for the audit for over 60 days (with no information except that it was in process), and knowing that the Company was working with Staff on it, we received word in the late afternoon on August 23<sup>rd</sup> that the audit results were posted on the WUTC website. We hastened to the website. What was posted was not just an audit-- there was an entirely new rate design.

With the new rate design came the recommendation from staff that the normal regulatory review period be waived; that the matter be on the agenda for the Commissioner's Open Hearing the following Wednesday, August 29<sup>th</sup>, and go into effect on September 4<sup>th</sup> on a temporary basis with refund possibilities. The sale would follow 10 business days later. There were roughly 5 lengthy documents posted. We were stunned....why waive the review period when there was a completely new rate design? Shouldn't we have a 30 days review period? How could we get up to speed to testify in 6 days counting weekends? How can this process be "in the public interest"? We have worked really hard on this, but we can't work that fast!

The next afternoon, hundreds more pages were posted to the UTC website. We realize that it is not your normal process to the audit information, and we very much appreciate all you have done to accommodate our desire for a transparent process, but this was overwhelming. We met Saturday and Monday as a group and spent countless hours on our own trying to work our way through the generally not-well-marked documents to prepare for Wednesday's Hearing. We did not want the rates or sale to go into effect before we could intelligently comment on the audit & new rate design, to see if our issues had been addressed and if what was proposed was fair. Tuesday morning, as we preparing to leave that afternoon for the overnight trip to Olympia for the Hearing (and trying to fulfill our professional commitments as well), we received a phone call from Staff saying we were off the Agenda, and not to come. We were told that our new Hearing date would probably be the 12<sup>th</sup>, but maybe the 26<sup>th</sup>, and that the new effective date for rates and the sale would be September 15<sup>th</sup>. Somewhere in the next few days that changed to October 1<sup>st</sup>. Surely our community (the Public) should have a more even playing field than we have had!

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We fully support a thriving Rosario Resort and Rosario Utilities Company, as well as Olympus' efforts in seeking out Washington Water Services as a professional, experienced water utility management company. We also fully support the community's right to determine if it is in the public interest to own the utility.

Our goal has been 1) to bring out and get answers to underlying questions the Rosario Community has had regarding the Utility, and 2) to ensure fair water rates for both the Community and the Company.

Our Community's requests are:

- Raise the base rate to \$36/mo and Ready-to-serve to \$22/mo and change usage blocks to 0-8000, 8001-15,000, and 15,001+
- Make the rates fair for the Highlands, so that a customer using x gallons in the Highlands pays the same as someone using same x gallons in the  $\frac{3}{4}$  inch residential area
- Find that Olympus/Rosario Utilities acted imprudently, based on the following new evidence since the 2002 rate case:
  1. Olympus' claim that DOH forced them into this expensive choice has been denied by Steve Deem of DOH
  2. If Olympus had managed the Utility well, they would have finished the work necessary for the plant to operate at full capacity and thus have been able to sell more connections and offset cost-runs from building of plant
  3. The interest rate of 9.25% for plant loan not being re-negotiated when prime dropped to 4.75% in 2002 and then lower (this has been mitigated but not removed by staff for this rate case)
  4. **There have been no water connections available from the Utility since 2001—but there has been customer demand**
- To require that Olympus absorb the cost over-runs and the loan balance on the basis of lack of prudence as outlined above; or, at a minimum, to dis-allow the conversion of the cost overruns and loan balances from debt to equity which allows the company to earn a higher rate of return on these disputed items
- Find that the Staff evaluation that \$10000 per AF of additional water is a fair price for Rosario Utilities to charge Washington Water (and pass on to ratepayers) was incorrect and disallow it.

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Our goal has always been to bring out the underlying issues for resolution, to seek fairness for all parties, and to speak and act with integrity. We have made every effort to verify that what we say is truthful and accurate. To that end, we offer the following:

REGARDING THE SALE of 10 acre-feet of water @ \$10,000 per acre-foot from Olympus to itself (Rosario Utilities) and then to Washington Water:

In the website document “supplemental material Rosario Utilities and Washington Water meeting on August 20<sup>th</sup>, 2007” it states that “due to an interest in purchase of water rights by Eastsound, a study was undertaken to determine the avoided cost of providing water on Orcas Island,” and that it was “reviewed by Commission staff”. Staff confirmed that what they saw was entitled “Block Water Supply Valuation” by RH2 Engineering, Inc. We were able to read a copy of the study from another source.

The study was not done to determine the avoided cost of providing water on “Orcas Island”, but only for providing water through one method to Eastsound...so the Company’s statement is incorrect. Providing water to any other part of the Island would require a study specific to that part of the Island, as the water sources and availability on various parts of the Island differ.

Staff states that they determined that the price was fair. But Staff told us on the phone August 24<sup>th</sup>, that they were not given any supporting documentation to validate Olympus’ price for the water rights, but rather they had to go to the Company’s office, because it would not give them anything in writing. They were not allowed to see the whole 3 page study, only part of it. It is incomprehensible to us that Staff could determine that Olympus’ price is fair based on such a lack of documentation.

On page 1 of the RH2 study it says: “It is emphasized that (the) work has been done on a preliminary basis and is not intended as (an) appraisal. So how can Staff use it as a basis of determination of “fair price”—especially with no corroborating evidence?”

You may or may not know that Olympus and Eastsound Water Users Association have had negotiations over the past few years for additional water for Eastsound. Olympus has wanted \$10,000/AF for the water. EWUS hired WestWater Research to do an actual appraisal of Olympus’ water rights. WestWater Research is, and I quote from their corporate statement: “the premier transaction and asset valuation advisory company to the water sector. WWR specializes in water asset sales and acquisitions; water resource economics, water right and asset appraisals, and project finance services.”

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We were given permission from EWUA to obtain a memorandum from WestWater describing the work they did for Eastsound Water Users, including their methodology. They also discuss other approaches to appraising, such as the cost replacement/opportunity cost method RH2 used. And they discuss the RH2 study specifically.

They note that: “it is important that the analysis only consider projects that are likely to be pursued rather than hypothetical projects that have little chance of completion due to financial, political, or physical characteristics.” In fact, EWUA told us that they gave RH2 access to 4 different alternate water source studies, and RH2 chose to include in their report only the most expensive one-- raising the level of Purdue Lake by 23 feet. It is an option that EWUA has said they will not pursue because it is cost prohibitive and they have less expensive alternatives. If they never intend to pursue it, how can it be used to show “avoided cost”? Please see pages 3-6 of the WestWater study attached for an in-depth discussion of this. Using a hypothetical, cost prohibitive scenario to determine their valuation calls into question the whole foundation of the work RH2 did.

But a separate question poses itself—how does the cost for Eastsound hypothetically raising the level of Purdue Lake by 23 feet have any bearing on a sale of water from Olympus/Orcas Water Holdings to Olympus/Rosario Utilities to Washington Water? We don’t see any connection.

Olympus wants \$10,000 per acre-foot. The WestWater appraisal values the water rights at between \$1500 and \$2000 per acre-foot. This difference is stunning.

Olympus says in one of their discussions of this that they based their price on both the avoided cost and recent sales comparisons. We would like to know what these comps are. WestWater has looked at all the comps and none support Olympus’ value, let alone substantiate that their price is ‘under market value’, as Olympus also asserts without documentation.

So, Olympus has now sold 10AF from themselves to themselves (from their Orcas Water Holdings to their Rosario Utilities) for \$10,000 per acre-foot. This is not an arms-length/open market transaction, and based on the WestWater appraisal, the price is greatly inflated. Yet it will set a baseline for future water sales prices if it is allowed to go through. This is not in the public’s best interest.

As you have noted, Washington Water Services is a knowledgeable, professional, experienced water services company. Staff has stated that the sale of RU to WWS is in the public interest. Washington Water Services MUST know that they are grossly overpaying for the water rights. But they agreed to do it. Why?

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We can only conclude that they have reasons for doing so that we are not privy to. But grossly overpaying for water rights is clearly not in the public interest. On top of that, we understand that they can recover what they pay in a subsequent rate case—so overpaying does not harm them at all. But it harms the customers.

We have ask, especially in light of this situation, that the 283AFY shown in the March 2004 Six Year Comprehensive Water Plan be transferred back to Rosario Utilities/Washington Water at no cost.

It is unclear to us why these water rights should carry any value. Per the 6 year Comprehensive Water Plan dated March 2004, Rosario Utilities had 283 AFY. Within the past few years, by virtue of a paper transfer, these water rights were removed from RU to Olympus' newly created affiliate 'Orcas Water Holdings'. Subsequent to that, 183 AFY were transferred back to RU. Olympus now contends that it would be "prudent" of Washington Water to purchase an additional 10 AFY at the greatly inflated price of \$10,000 AF. Additionally Olympus, through Orcas Water Holdings, has issued a "demand note" to Rosario Utilities that \$100,000 be paid for the 10 acre feet of water, and if it isn't paid by January 1<sup>st</sup>, it will start accruing interest at 12% per year. This is outrageous. We ask the UTC to fulfill their responsibility and make sure this is made right for the public.

Thank you.

Sincerely,  
The Rosario Property Owners Board

**Please remember: There have been no water connections available from the Utility since 2001 (apart from the few overpriced ones that Rosario Resort sold earlier this year)—but there has been customer demand. How can this be? This is a UTC managed utility.**