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BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,
Complainant,

Docket TP-

v.

PUGET SOUND PILOTS,
Respondent.

**TESTIMONY OF
JESSICA NORRIS, CPA, SHANNON & ASSOCIATES
ON BEHALF OF PUGET SOUND PILOTS**

NOVEMBER 19, 2019

TESTIMONY OF JESSICA NORRIS, Exh. JN-1T i

Williams, Kastner & Gibbs PLLC
601 Union Street, Suite 4100
Seattle, Washington 98101-2380
(206) 628-6600

EXHIBIT LIST

Exhibit No.	Description	Page Referenced
JN-02	Puget Sound Pilot's Capitalization Policy, Page 11	2
JN-03	Note 10 to the Financial Statements	2
JN-04	Consolidated Financial Statements for the years ended December 31, 2018 and 2017	7
JN-05	Statement of Assets, Liabilities and Pilots' Equity	7

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TESTIMONY OF JESSICA NORRIS, Exh. JN-1T ii

Williams, Kastner & Gibbs PLLC
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Seattle, Washington 98101-2380
(206) 628-6600

1 **I. IDENTIFICATION OF WITNESS**

2 **Q: Please state your name, business and business address.**

3 **A:** My name is Jessica Norris. I am a CPA licensed in Washington for the past 13 years.
4 My business address is Shannon & Associates, LLP; 1851 Central Pl S, #225; Kent, WA
5 98030.

6 **Q: Please describe your relationship with the Puget Sound Pilots?**

7 **A:** For the past 12 years, I have served as the lead auditor in the audit of the financial
8 statements of the Puget Sound Pilots. This entails supervising the team at Shannon &
9 Associates in auditing the statements of assets, liabilities and pilot equity and its revenues
10 and expenses and changes in pilot equity and cash flows. This also has included
11 presentation of the audited financial statements to the Board of Pilotage Commissioners.

12 **II. PURPOSE OF YOUR TESTIMONY**

13 **Q: We understand from Weldon Burton's testimony in this matter that PSP does not**
14 **produce statements according to GAAP or (generally accepted accounting**
15 **principles). Is this true?**

16 **A:** Yes, the financials are special purpose and prepared on a modified accrual basis. Puget
17 Sound Pilots is a rather unique entity made up of sole proprietors and corporations who
18 band together as an association for administration, dispatch, expense consolidation
19 purposes and receive equal individual annual income distribution. PSP is taxed as a
20 partnership under federal law and each pilot member is responsible for his or her own tax
21 fillings and payments of tax.

22 **Q: Do you have any responsibility for individual pilot tax return filings?**

23 **A:** No. Our role is solely as auditor for the association. We do not file individual tax returns
24 for pilots.
25

1 **Q: Can you describe a little more specifically what the modified accrual basis of**
2 **reporting entails?**

3 **A:** Yes, modified accrual basis of accounting is non GAAP. The revenue of the entity is
4 recorded on an accrual basis – as it is earned. For instance, in the case of the pilots, the
5 day the job is completed. Expenses, in general, are recorded when actually paid and not
6 necessarily accrued in the period in which the expense is incurred. Depreciation has been
7 accounted for on a straight line basis over the estimated useful life of assets such as the
8 pilot boats owned by the entity that are capitalized in line with the entity’s capitalization
9 policy.

10 **Q: And, what is that capitalization policy?**

11 **A:** For income tax purposes anything under \$5,000 is expensed: page 11 of PSP’s financial
12 statement Exh. JN-02 , sets forth the details of that policy.

13 **Q: Does the modified accrual basis also entail consideration of unrecorded liabilities?**

14 **A:** No, the modified accrual basis of accounting does not record the expenses identified as
15 unrecorded liabilities. The notes to the financial statements however include information
16 to assist a reader of the financial statements to understand the financial condition of the
17 entity. As a result, Note 10 to the financial statements, Exh. JN-03, details these items as
18 they are material pieces of the Puget Sound Pilots’ financial operations results. For
19 instance, Callback Days (also known as comp days) are not included in the body of Exh.
20 JN-03 and their estimated value on the balance sheet as of December 31, 2018 was
21 \$6,927,172. I understand that other witnesses have described callback days as a unique
22 feature of the PSP pilots and will not elaborate on the reason for the generation of this
23 liability, but only point out here that Callback Days are a material and growing liability
24 for PSP’s financial statement disclosure purposes.

25
TESTIMONY OF JESSICA NORRIS, Exh. JN-1T 2

Williams, Kastner & Gibbs PLLC
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1 **Q: Is there any other reason for not booking accrued Callback Days as a liability of**
2 **PSP's financials?**

3 **A:** Yes, since expenses are booked on a cash basis when there are incurred, accruing fluid
4 total of Callback Day aggregate liabilities would actually be “apples to oranges” mixture
5 of accounting methods and would not contribute to the overall accuracy of the audited
6 financials.

7 **Q: Are there other unrecorded liabilities that merit reference at this point?**

8 **A:** Yes. A significant unrecorded liability is the pilots' pension which is noted in Note 6 to
9 the financial statements. As of the date of PSP's financial statements, the unfunded
10 portion of that liability had not been determined. However, I understand Mr. Steven
11 Diess of Independent Actuaries, Inc. will submit testimony on this issue.

12 **Q: Is there another material unrecorded liability you would note here?**

13 **A:** Yes. Aggregate earned time off payable is estimated as of December 31, 2018 at
14 \$982,764.

15 **Q: Is the amount due to buyout the retired pilots' ownership interest also shown as an**
16 **unrecorded liability?**

17 **A:** Yes, and as of December 31, 2018, that totaled \$3,736,439, as compared to 2017, when it
18 was \$3,083,739. As noted above, to fund this there are also new pilots buying in and the
19 variance between the amounts due to pilots buying out versus amounts coming in from
20 pilots buying in, is recorded in 2018 as a net cash outflow of \$246,363 (page 7 of the
21 audited financial statements line 13).

22 **Q: Is this, in your opinion, analogous to any other accounting principle?**

23 **A:** Yes. The buy in and buy out is actually equity or “contributed capital” and is not part of
24 the revenue sought to be recovered in regulated rates. Again, this relates solely to
25

1 transitions in PSP ownership with newly licensed pilots “buying in” and retiring pilots
2 receiving their capital contributions “buy out” after retirement.

3 **Q: Do other entities use this system?**

4 **A:** Yes, it is common in accounting and law partnerships for parties who make “partner” or
5 achieve equity status to account for those transitions accordingly on inception and
6 conclusion of their equity tenure.

7 **Q: You are not the witness for the actuarial viability of the PSP plan, are you?**

8 **A:** No, again that testimony is being offered instead by Mr. Diess. My role here was merely
9 to underscore in the financial statements that the pension plan is a pay-as-you-go plan and
10 has not been funded as a reserve account.

11 **Q: Does Shannon & Associates, and, particularly you, have any goal in mind in
12 preparing and producing financial statements for the PSP?**

13 **A:** Yes, our goal in conducting the audit is to issue an ultimate opinion on the financial
14 statements of the entity. This includes us providing assurance that there are no material
15 misstatements in the financials and that the statements present accurately in accordance
16 with the modified accrual basis of accounting. In addition, we are constantly providing
17 advice and feedback to our clients such as the pilots to help them evolve and improve the
18 financial statement reporting and financial controls environment in which they operate.

19 **Q: As part of that process, what do you endeavor to do?**

20 **A:** Well, for one thing, our goal is to continue to preserve and secure individual pilot
21 personal information. Because of the unique nature of the PSP and the individual pilot
22 reporting concerns, despite submitting aggregate financial data into the public record at
23 multiple state agencies, we strive to preserve personal information such as social security
24 numbers and other individually-identifiable expenses unique to the individual
25 Association members. We also strive to protect confidential information while also

1 striving to increase transparency and an understanding of information offered to allow
2 regulators such as the Board of Pilot Commissioners (“BPC”) and the UTC to
3 appropriately assess financial results of the PSP on a regular basis.

4 **Q: Does that seem sometimes a delicate balancing act?**

5 **A:** Yes, to the extent that we are trying to be protective of identifier information of
6 individual pilots, yet straightforward and transparent about presenting the financial
7 results of the Association to regulators.

8 **Q: Can you highlight any particular material developments and/or changes reflected in**
9 **the 2018 financial data?**

10 **A:** Yes. One important change that occurred in 2018 was the final administration and
11 winding up of the Pilot Technology Services entity, a former PSP subsidiary. That entity
12 handled the personal pilot units, or independent navigational systems, previously
13 purchased (and now leased) by PSP to aid in the most updated fashion navigation
14 services performed by the Pilots. PSP no longer has that entity nor owns any such
15 systems. Secondly, 2018 also saw the transition of the Grays Harbor Pilot retirement
16 expense and reporting which previously had been administered and funded by PSP, and
17 now, through legislation, is accounted for, funded and separately reported by the Port of
18 Grays Harbor.

19 **Q: Can you please elaborate in some detail regarding the reference in Senate Bill 6519**
20 **to the financial statement reporting and how the Grays Harbor pilot retirement**
21 **expenses for pilots employed prior to October 1, 2001 was handled and the**
22 **subsequent transition to Grays Harbor County to account for this funding?**

23 **A:** Beginning in 2001, the Port of Grays Harbor found it did not have sufficient resources to
24 pay for existing retirees receiving pension benefits. Moreover, some Grays Harbor Pilots
25 had previously served in the Puget Sound Pilotage District and thus could actually

1 receive part of their retirement benefits through PSP. To remedy this situation, the BPC
2 decided to establish a new pension charge line item in the Grays Harbor Pilotage District
3 tariff, which was set at \$101 per pilotage assignment. In addition, there was an additional
4 charge in the Puget Sound Pilotage District tariff for the Grays Harbor pilot pension
5 liability phase out. As part of the arrangement, an \$8.00 increase in the rate for each
6 length overall (LOA) category for each zone, was added to the previous Puget Sound
7 Pilotage District tariff. This revenue, along with the Grays Harbor pension charge, was
8 remitted to the Puget Sound Pilots, which then disbursed pension benefits to Grays
9 Harbor retirees. Again, after action by the legislature, this procedure/program was
10 discontinued in 2018.

11 **Q: Would you now please generally describe the audit process followed by Shannon &**
12 **Associates in compilation of the PSP results of operations?**

13 **A:** Yes. We use a risk-based audit approach which requires us to evaluate the financial
14 statements risks and then perform procedures that allow us to obtain sufficient evidence
15 about the amounts and disclosures included in the financial statements. The procedures
16 selected on a year-to-year basis depend on the audit team's judgment, including the
17 assessed level of risks for each corresponding area. Prior to our assessment of risk, we
18 perform a walkthrough of the processes at PSP's Seattle offices to make sure we
19 understand them. In doing this, we consider the internal control environment at PSP to
20 help us design our audit that helps achieve our objective or, in providing the overall
21 opinion in this case, that the financial statements are free from material misstatements.
22 Examples of some of the procedures we perform are testing that the rates set by the tariff
23 are the actual amounts being charged to the customer and that revenue is recorded in the
24 correct period as well as that the detail of jobs performed and associated charges are able
25 to be reconciled within an acceptable level to the financial statement revenue reported.

1 **Q: Do you do anything else in regard to the audit due diligence?**

2 **A:** Yes, we also send confirmations to a sample array of customers of PSP to validate the
3 aggregate amount owed as well as test and reconcile a variety of expense accounts
4 reflected in the general ledger.

5 **Q: Do you have an understanding about how “price outs” for regulated rate filings are**
6 **accomplished and how does that relate to the more familiar invoice auditing you**
7 **have been engaged in?**

8 **A:** Yes, generally, and as I understand, that is comparable to the process just described
9 where revenue is tested against tariff invoices submitted to and remitted by customers in
10 the audit or test year period to validate that billing of customers and revenue in the time
11 period accurately balance.

12 **Q: Have you provided the consolidated financial statements for the Puget Sound Pilots**
13 **as part of this filing?**

14 **A:** Yes, I have provided as Exh. JN-04 the Consolidated Financial Statements for the years
15 ended December 31, 2018 and 2017 and the Statement of assets, liabilities and pilots’
16 equity – modified accrual basis as of June 30, 2019 and the related statement of revenues,
17 expenses and pilots’ equity – modified accrual basis for the twelve months then ended in
18 accordance with the modified accrual basis of accounting as Exh. JN-05.

19 **Q: Does this now conclude your direct testimony?**

20 **A:** Yes.
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