Agenda Date: December 7, 2023
Item Number: A5

Docket: **UW-230132**
Company: Olympic Water and Sewer, Inc.

Staff: Mike Young, Regulatory Services
Jaclynn Simmons, Regulatory Services

Attachment 2: Staff Responses to PLVC "Questions and Concerns" Document

1. "Some Unexplained Anomalies in OWSI Annual Filings"

PLVC has identified several data entries contained in the income statements from OWSI's annual reports submitted to the Commission for the years 2017-2022 that it believes undermine the reliability of OWSI's accounting practices. However none of these alleged anomalies implicate any issue with the rates OWSI filed on February 24, 2023. Staff reviewed the model submitted by the company and determined that it matches almost exactly to the income statement provided in the company's filed 2022 annual report, as well as the company's general ledger. Because Staff sets rates through the examination of a test year (in this case, calendar year 2022), annual reports are not audited and not used in the rate setting process and are thus irrelevant to whether the rates are fair, just, reasonable, and sufficient.

2. "Federal Income Tax Expenses"

PLVC has also identified alleged inconsistencies between OWSI's reported income and federal income tax owed on its annual reports for the years 2017-2022. However, even if Staff accepted the annual report entries as inconsistent, they once again do not indicate that OWSI's revised rates are unreasonable as the annual reports are not used in Staff's review of rate filings. The water Excel model used to determine revenue requirement and rates automatically calculates an amount of federal income tax based on the revenues and expenses entered into the model. The model submitted by the company erroneously did not include any provision for federal income tax. The model staff used in its review did provide for federal income taxes, however, crucially, Staff's model resulted in higher rates than those proposed by the Company and subsequently accepted by Staff as fair, just, reasonable, and sufficient. Moreover, as previously stated in Staff's response to DR no. 23, federal income tax is a below the line expense and is not included in the rate calculation.

3. "Previously Undisclosed 'Management Fee' Paid to PLA's Investors"

PLVC has identified a management fee of 3% of total revenue paid annually by OWSI water to the three principle investors in OWSI's parent company, PLA, as an expense that should have been excluded from rates. The fee totaled $27,247.89 in 2022, the test year in this case. Staff did remove this management fee in its model, which, as noted above, generated higher rates than the company model. Staff's model was not used in its recommendation to the Commissioners. Staff thus concluded that the company's proposed rates were fair, just reasonable, and sufficient even including the management fee.

4. "New Treatment Plant Loan Fee"

OWSI included in the rate filing a loan fee of $21,000 billed by the State Department of Health as a one-time cost to the company, which it properly paid and recorded as an expense. PLVC represents that OWSI has agreed to remove this charge as an expense item and recategorize it as a capital asset. It is unclear what action PLVC expects Staff to take in response to this information. If the parties wish to agree to new rates with this expense removed or recategorized, the Company must submit a new/revised tariff filing. The Company has not indicated any intent to do so. Moreover, Staff does not believe that recategorization of the loan fee would have a material effect on rates, nor does it believe that the current categorization of the amount renders the rates unreasonable.

5. "Conflicting Income Statements"

PLVC has also identified alleged inconsistencies between the affiliated interest income statements filed with the Commission by OWSI's parent company, PLA, and OWSI's income statement. However, annual affiliated interest income statements are not used to determine reasonable rates. Rates are set on the audited income statement accounts of the regulated operation. The Company provided general ledger accounts from the water company, which Staff reviewed to verify the expense amounts entered into the model by the Company. Staff's model varied from the company model as a result of the general ledger review, but again, Staff's model generated higher rates than the company's submitted model and therefore Staff determined the Company's rates were reasonable as filed.

6. "Hours Worked Breakout and Allocators between Water and Sewer"

PLVC asserts that the methodology governing the allocation of expenses between OWSI's sewer and water sides established by Staff in 2008 may not be appropriate for the current rate case and highlights several general ledger entries it claims indicate that OWSI has failed to follow the agreed-upon allocation methodology. Staff has not seen any evidence calling into question the established allocation methodology and stands by the allocation split decided on in 2008 as reasonable. Staff reviewed the Company's general ledgers to ensure expenses are properly allocated. The individual expense items identified by PLVC as inconsistent with the allocation split do not yield the conclusion that the Company did not properly allocate any one category of expenses. Moreover, PLVC's claims that the allocation split was not strictly adhered to in the Company's filing, even if true, do not render the rates unreasonable. The items highlighted by PLVC implicate immaterial amounts and, as previously stated, Staff's model demonstrated that the Company is entitled to a higher revenue requirement than that contained in the Company's filing.

7. "Adding Hours and Dollars Together"

PLVC identified a data input error in OWSI's general ledger related to payroll accounts. This is a simple formula mistake that is not material to the rate calculation.

8. "Allocation of PLA's G&A Management Fee"

PLVC finally challenges the Company's inclusion in rates of a $285,524 "G&A management fee" paid to OWSI's parent company, PLA, for management and accounting services. The Company increased this accounting fee by $67,000 over the previous rate case amount. Staff used the prior amount of $218,000 in its original model based on the previous rate case which includes direct charged costs and allocated costs. Even despite this $67,000 reduction, Staff's model still yielded a higher revenue requirement than that contained in the Company's filing. Moreover, during Staff's subsequent review of the filing conducted after the June 16, 2023 suspension order, Staff determined that the general ledger supported the $285,524 fee. If Staff were to redo this rate case, it would include the entire amount as recoverable in rates.

9. Staff's Conclusion

Staff takes its job very seriously in determining whether rates are fair, just, reasonable, and sufficient, as it found in this case. Staff have a limited amount of time to conduct the audit, including its review of the Company's general ledger entries, balance sheet, rate base calculation, cost of capital, and rate design. In this case, Staff did not simply review the Company's submission but created its own model, which generated rates that were higher than those proposed by the company. Staff has reviewed company books in several past filings, and will continue to review the Company books in the future.