

Questions and Concerns

This narrative is intended to accompany the Excel workbook submitted herewith. It describes a number of remaining questions and concerns about Olympic Water and Sewer, Inc.'s ("OWSI") water utility accounting and about UTC staff's review of OWSI's submissions. These include questions and concerns about various unexplained anomalies in OWSI's financial reports submitted to UTC and, in particular, questions and concerns about how certain shared expenses are allocated (i) between the water utility ("OWSI Water") and the sewer (wastewater) utility ("OWSI Sewer") and (ii) between OWSI and its parent company Port Ludlow Associates, LLC ("PLA") and PLA's other (non-utility) subsidiary companies and operations.

The data set forth below was taken directly from OWSI's annual submissions to the UTC, from OWSI's 2022 General Ledger, from other documents submitted to UTC by OWSI in support of its water rate increase request, and from written responses to data requests in this proceeding.

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1. Some Unexplained Anomalies in OWSI Annual Filings

		Olympic Water and Sewer UTC Filing Schedule 1					
		Income Statement Federal Income Tax					
Income Statement		Year	Year	Year	Year	Year	Year
		2017	2018	2019	2020	2021	2022
Operating Revenue		\$ 711,052	\$ 704,730	\$ 707,739	\$ 686,129	\$ 778,508	\$ 802,430
Other Revenue		\$ 22,202		\$ 70,600	\$ 100,661	\$ 102,621	\$ 10,147
Utility Operating Revenue	Total	\$ 733,254	\$ 704,730	\$ 778,339	\$ 786,790	\$ 881,129	\$ 812,577
Expenses							
Operating Expense Accounts		\$ 452,776	\$ 529,981	\$ 578,419	\$ 509,711	\$ 634,220	\$ 829,531
Depreciation Expense		\$ 67,161	\$ 68,509	\$ 63	\$ 98,548	\$ 167,510	\$ 110,417
Amortization Expense		\$ (5,795)	\$ (5,145)	\$ (3,993)	\$ (12,275)	\$ (12,475)	
Other Tax and License		\$ 65,017	\$ 70,478	\$ 66,656	\$ 56,356	\$ 5,700	\$ 30,434
	Federal Income Tax	\$ 52,214	\$ 65,177	\$ 43,370	\$ 26,265	\$ 29,400	\$ 39,986
Utility Operating Expense	Total	\$ 631,373	\$ 729,000	\$ 684,515	\$ 678,605	\$ 824,355	\$ 1,010,368
Utility Operating Income or (Loss)		\$ 101,881	\$ (24,270)	\$ 93,824	\$ 108,185	\$ 56,774	\$ (197,791)

The above is a compilation of Schedule 1 – Income Statements from the UTC Annual Filings submitted by OWSI. A review of the Depreciation Expense shows the following:

Year	Year	Year	Year	Year	Year
2017	2018	2019	2020	2021	2022
\$ 67,161	\$ 68,509	\$ 63	\$ 98,548	\$ 167,510	\$ 110,417

In 2017 and 2018 the amounts were about the same and then in 2019, it dropped down to \$63.00. Then it jumps up to \$98,548 in 2020, then increases again by 70% in 2021 to \$167,510, and then decreases in 2022 to \$110,417. It is unclear whether the \$63.00 figure shown for 2019 merely reflects a decimal placement error or has some other explanation. In any event, this unexplained anomaly does not seem to have been noticed by UTC Staff.

A review of the Amortization Expense shows another apparent anomaly for 2022, namely, \$0.00 amortization.

Year	Year	Year	Year	Year	Year
2017	2018	2019	2020	2021	2022
\$ (5,795)	\$ (5,145)	\$ (3,993)	\$ (12,275)	\$ (12,475)	

A review of the Other Tax and Licenses expenses again shows a strange variation, as shown below:

Year	Year	Year	Year	Year	Year
2017	2018	2019	2020	2021	2022
\$ 65,017	\$ 70,478	\$ 66,656	\$ 56,356	\$ 5,700	\$ 30,434

It is unclear what if any impact these anomalies may have on the determination of appropriate water rates. But they certainly do not instill confidence in the reliability of OWSI's accounting practices, nor in the quality of UTC staff's review of OWSI's financial submissions. UTC staff should thoroughly investigate OWSI's "books, accounts, practices, activities, property, and operations," as explicitly ordered by the Commissioners on June 16, 2023. We suggest that the investigation cover at least the past 5 years.

2. Federal Income Tax Expenses

Income tax rates:

1994-2017	First \$50,000	15%
	\$50,000 to \$75,000	25%
	\$75,000 to \$100,000	34%
	\$100,000 to \$335,000 (g)	39%
	\$335,000 to \$1,000,000	34%

2018-2021	None	21%
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Olympic Water and Sewer UTC Filing Schedule 1 Income Statement Federal Income Tax

Year	Year	Year	Year	Year	Year
2017	2018	2019	2020	2021	2022
\$ 52,214	\$ 65,177	\$ 43,370	\$ 26,265	\$ 29,400	\$ 39,986

The formula for figuring out the Federal Income Tax using the above charts is easy and very straight-forward for 2018-2022. The basic formula is as follows:

	Total Utility Operating Revenue	\$ 100.00
Minus	Expenses Before Taxes	<u>-\$ 80.00</u>
Equals	Net Income Before Taxes	=\$ 20.00
Multiplied	By the Federal Tax Rate	<u>X 21%</u>
Equals	Federal Tax Owed	=\$ 4.20

The computation for 2017 follows the same basic formula except it is broken down into five percentage categories.

The Federal Income Tax amounts as shown on the UTC Annual Filings raise significant questions as to how they were computed and if there was a co-mingling of Federal Taxes owed between OWSI Water and OWSI Sewer. We understand that OWSI files one combined Federal tax return covering both utility operations, and then OWSI's taxes are allocated between the Water and Sewer operations when OWSI Water submits financial reports to UTC. OWSI's annual submissions to UTC call into question how those allocations are made.

The chart below compares the OWSI Water Federal Tax filing on the UTC Annual Report to the computed tax filings based on Revenue and Expenses as filed on the UTC Annual Report. The results seem strange and are very disturbing.

Olympic Water and Sewer Annual UTC Filings							
	Year	Year	Year	Year	Year	Year	
	2017	2018	2019	2020	2021	2022	
OWSI Annual Filing Fed Income Tax	\$ 52,214	\$ 65,177	\$ 43,370	\$ 26,265	\$ 29,400	\$ 39,986	
Computed Tax Based on UTC Filing	\$ 43,179	\$ 8,544	\$ 28,811	\$ 28,225	\$ 14,267	\$ -	
Difference	\$ 9,035	\$ 56,633	\$ 14,559	\$ (1,960)	\$ 15,133	\$ 39,986	

For example, in 2018 OWSI Water reported \$65,177 in Federal Income Tax. For that amount of tax to be owed by OWSI Water it would have to have \$310,367 in net Income Before Taxes. To owe \$65,177 in taxes the computation would be as follows:

Net Income Before Federal Tax	\$310,367
Federal Tax Rate	<u>21%</u>
Federal Tax Owed	\$ 65,177

Going back to 2002, OWSI Water has never had \$300,000 net income before taxes. It appears that OWSI Water may have been paying part of the Federal Income Tax for OWSI Sewer, which regularly had net income before taxes exceeding \$400,000. OWSI's calculation of federal income tax attributable to OWSI Water should be investigated more carefully.

OWSI's 2018 Annual Report filed with the UTC shows a loss of (\$24,270) for OWSI Water. This is the same 2018 report that had the Federal income tax reported as \$65,177. Below is a comparison showing the 2018 Annual Report Filing and next to it a recomputed filing using the same revenue and expense items and the 21% Federal Income Tax rate.

	Federal Income	UTC	
	Tax Computation	Filing 2018	
Income Statement	Year	Year	
	2,018	2,018	
Operating Revenue	\$ 704,730	\$ 704,730	Operating Revenue
Other Revenue			Other Revenue
Utility Operating Revenue	\$ 704,730	\$ 704,730	Utility Operating Revenue
Expenses			Expenses
Operating Expense Accounts	\$ 529,981	\$ 529,981	Operating Expense Accounts
Depreciation Expense	\$ 68,509	\$ 68,509	Depreciation Expense
Amortization Expense	\$ (5,145)	\$ (5,145)	Amortization Expense
Other Tax and License	\$ 70,478	\$ 70,478	Other Tax and License
		\$ 65,177	Federal Income Tax
Interest Expense	\$ 220		
Expenses Before Taxes	\$ 664,043	\$ 729,000	Utility Operating Expense
Income or (Loss) Before Fed Tax	\$ 40,687	\$ (24,270)	Utility Operating Income or (Loss)
Federal Income Tax 21%	\$ (8,544)		
Interest Expense	\$ (220)	-220	
Net Income or (Loss)	\$ 31,923	\$ (24,490)	Net Income or (Loss)

As shown in the chart on the previous page, the apparent disparity between the amount of OWSI Water’s federal taxes shown in its annual report to UTC and the calculated amount of federal tax payable based on OWSI Water’s reported net income or loss has been significant for each year since 2017. There is no greater example of this than the 2022 UTC Annual Filing by OWSI Water.

In 2022 OWSI Water’s expenses reportedly increased by more than \$111,000, and as a result the utility showed a loss before taxes of (\$151,449). Presumably no income tax is owed in the event of such a loss. Further, we understand that net operating losses incurred in business pursuits can be carried forward indefinitely as a result of the Tax Cuts and Jobs Act. The bottom line for OWSI Water with its (\$151,449) Loss Before Taxes is that no Federal Income taxes would be owed for 2022, yet OWSI Water claims nearly \$40,000 in such taxes. Below is a copy of its 2022 Annual Report to UTC:

**SCHEDULE 1
INCOME STATEMENT**

(For the Calendar Year 2022)

Instructions

Do not leave fields blank - If a field is not applicable, enter 0.
Misc Revenue Accounts should not include Jobbing & Contract work. Include this revenue under the Other Income section.

Ln.	Account #	Account Name	Water	Other	Total Company
(L)	(a)	(b)	(c)	(d)	(c)+(d) = (e)
Revenues					
1	400	Operating Revenue	\$802,430.00		\$802,430.00
2	471	Misc. Revenue Accounts (specify in footnote)	\$0.00		
3	474	Other Revenue Accounts (specify in footnote)	\$10,147.00		\$10,147.00
4		<i>Utility Operating Revenue (add lines 1 thru 3)</i>	\$812,577.00		\$812,577.00
Expenses					
5	401	Operating Expense Accounts	\$829,531.00		\$829,531.00
6	403	Depreciation Expense	\$110,416.78		\$110,416.78
7	406	Amortization Expense	\$0.00		
8	408	Other Tax & License	\$30,434.00		\$30,434.00
9	409	Federal Income Taxes	\$39,985.84		\$39,985.84
10		<i>Utility Operating Expense (add lines 5 thru 9)</i>	\$1,010,367.62		\$1,010,367.62
11		<i>Utility Operating Income (Loss) (line 4 less line 10)</i>	-\$197,790.62		-\$197,790.62
Other Income and Deductions					
Other Income:					
12	414	Gain (Loss) From Disposition of Plant	\$0.00		
13	415	Merchandising, Jobbing and Contract Work	\$12,000.00		\$12,000.00
14	419	Interest & Dividend Income	\$0.00		
15	421	Nonutility Income	\$0.00		
16		<i>Total Other Income (add lines 12 thru 15)</i>	\$12,000.00		\$12,000.00
Other Deductions:					
17	416	Merchandising, Jobbing and Contract Work	\$0.00		
18	426	Miscellaneous Nonutility Expenses	\$0.00		
19	427	Interest Expense	\$5,644.26		\$5,644.26
21		<i>Total Other Deductions (add lines 17 thru 19)</i>	\$5,644.26		\$5,644.26
22		Net Income (Loss) (add lines 11 and 16, subtract line 21)	-\$191,434.88		-\$191,434.88
Schedule 1 Footnotes (add lines as needed):					
17	211	Other Revenue Accounts (specify in footnote)		\$	10,147.00
Prepaid hookups and ancillary charges					

In 2022 OWSI Water reported owing **\$39,985.54** in Federal Taxes on a loss of (\$154,449) before taxes. This was not an isolated filing but rather OWSI was consistent in reporting this tax expense. In the form that OWSI Water used to show the need for its rate increase (PFIS), the \$39,985.54 shows up in the first column. The UTC staff asked for a breakdown of revenue and expenses between OWSI Water and OWSI Sewer. In response, Ms. Smeland submitted the following spreadsheet for 2022.

Income Statement

Description	Water Company End of Year	Waste-Water Company End of Year
List	\$	\$
REVENUES		
OPERATING REVENUE	\$ 824,577	\$ 1,560,907
EXPENSES		
OPERATING EXPENSES	\$ 970,494	\$ 914,138
Operating Income before Taxes	(145,917)	646,769
Interest Expense	5,644	2,200
Fed Income Tax	39,986	135,359
TOTAL OPERATING EXPENSE	1,016,124	1,051,697
NET INCOME (LOSS)	(\$191,547)	\$509,210
NET OPERATING INCOME	(\$185,903)	\$511,410

This spreadsheet needs to be looked at in detail. First, under Federal Income Tax for OWSI water, it clearly shows the \$39,986 Federal Income Tax reported on the UTC Annual Report for 2022. Next, look at the Net Operating Income line for OWSI Water and OWSI Sewer. Water lost (\$185,903) while Sewer made \$511,410 after taxes. OWSI Sewer generates twice the revenue of OWSI Water yet has fewer operating expenses before tax than OWSI Water. The disparity between the two entities is enormous.

Looking again at the chart below it needs to be determined whether OWSI Water paid the amounts shown on the Annual UTC filings to the Internal Revenue Service.

Olympic Water and Sewer Annual UTC Filings							
	Year	Year	Year	Year	Year	Year	
	2017	2018	2019	2020	2021	2022	
OWSI Annual Filing Fed Income Tax	\$ 52,214	\$ 65,177	\$ 43,370	\$ 26,265	\$ 29,400	\$ 39,986	
Computed Tax Based on UTC Filing	\$ 43,179	\$ 8,544	\$ 28,811	\$ 28,225	\$ 14,267	\$ -	
Difference	\$ 9,035	\$ 56,633	\$ 14,559	\$ (1,960)	\$ 15,133	\$ 39,986	

Presumably the \$29,400 Federal Income Tax reported for 2021 would have been paid in 2022. There is no General Ledger entry for this amount in 2022.

One other important note. In reviewing the General Ledger for 2022 under Income Tax the following was the only entry found.

INCOME TAX EXPENSE							
GL	HMM	June	34564	United States Treasury	Refund		-39,900.00
	To	tal Account	4-0500-73C.00	- INCOME TAX EXPENSE	.00*	.00*	39,900.00-* 39,900.00-*

The General Ledger shows a United States Treasury Income Tax **REFUND** of \$39,900.

If one adds up all the differences on the above table it totals \$133,386 in more taxes being paid than was owed.

As part of its investigation that was ordered by the Commissioners on June 16, UTC staff should thoroughly investigate how OWSI calculated its federal income taxes and how those taxes were allocated between OWSI Water and OWSI Sewer.

3. Previously Undisclosed “Management Fee” Paid to PLA’s Investors

A purported “Management Fee” of 3% of total revenue is being paid by OWSI Water to the three principal investors (two in Hong Kong and one in San Francisco) in the parent company of PLA, which in turn is the parent company of OWSI. That payment is made regardless of whether OWSI Water is making money or losing money. There has been no description of what management services are being provided to OWSI in return for the payment. The payment appears to be a return on investment rather than a legitimate expense for services rendered.

For example, in 2022 when OWSI Water had a Net Loss of \$191,434.88 according to its Annual Report to UTC, the 3% “Management Fee” was paid each month, totaling \$27,247.89 for the year:

4 0500-6461		MANAGEMENT FEES									
1/31/2022	GL		ii	January	34284	PLA mgmt fee for revenue	e	1,740.63			
						Total 1-31-22	.00*	1,740.63*	.00*		1,740.63*
2/28/2022	GL		ii	February	34345	PLA management fee entry	y	2,345.46			
						Total 2-28-22	1,740.63*	2,345.46*	.00*		4,086.09*
3/31/2022	GL		ii	March	34422	Monthly Management fee entry		1,718.31			
						Total 3-31-22	4,086.09*	1,718.31*	.00*		5,804.40*
4/30/2022	GL		ii	April	34519	Management fee for revenue	e	2,279.85			
						Total 4-30-22	5,804.40*	2,279.85*	.00*		8,084.25*
5/31/2022	GL		ii	May	34598	Management fee entry		2,362.92			
						Total 5-31-22	8,084.25*	2,362.92*	.00*		10,447.17*
6/30/2022	GL		ii	June	34672	Monthly management fee entry		1,661.82			
						Total 6-30-22	10,447.17*	1,661.82*	.00*		12,108.99*
7/31/2022	GL		ii	July	34743	Monthly management fee entry		2,966.88			
						Total 7-31-22	12,108.99*	2,966.88*	.00*		15,075.87*
8/31/2022	GL		ii	August	34812	Management fee for revenue		2,881.56			
						Total 8-31-22	15,075.87*	2,881.56*	.00*		17,957.43*
9/30/2022	GL		ii	September	34897	Monthly Management fee		2,238.06			
						Total 9-30-22	17,957.43*	2,238.06*	.00*		20,195.49*
10-31-202	2 GL		ii	October	34967	Management fee for water rev		3,520.74			
						Total 10-31-22	20,195.49*	3,520.74*	.00*		23,716.23*
11-30-202	2 GL		ii	November	35032	Monthly management fee entry	y	1,599.15			
						Total 11-30-22	23,716.23*	1,599.15*	.00*		25,315.38*
12-31-202	2 GL		ii	December	35098	Management fee for revenue		1,932.51			
						Total 12-31-22	25,315.38*	1,932.51*	.00*		27,247.89*
Total Account 4-0500- 461.00 - MANAGEMENT FEE								.00*	27,247.89*	.00*	27,247.89*

It appears the so-called “Management Fee” was also paid on revenue received from the new treatment plant surcharge, against the directive of the UTC.

A review of the Affiliated Interest statements submitted with OWSI’s annual reports to UTC for the past 10 years shows that the purported “Management Fee” was not disclosed by OWSI Water or PLA. For example, the 2022 Affiliated Interest statement merely recites that:

**OLYMPIC WATER AND SEWER, INC.
AFFILIATED INTEREST TRANSACTIONS
JANUARY 1 – DECEMBER 31, 2022**

Port Ludlow Associates provided the following services to Water in OWSI in 2022:

- Senior Management, accounting, customer service and other general and administrative services at a cost of \$285,524. The method used for the G&A allocation is percentage based on actual payroll cost, utilities, equipment, postage, operating and office supplies used throughout each year. The percentage within each department of G&A is reviewed annually based on utilization of time and resources within the departments toward the water company. This percentage method is reviewed annually and has been in place for many years with minimal change.

The previously undisclosed “Management Fee” paid to investors in PLA’s parent company is separate and apart from, and in addition, to the G&A expenses paid to PLA for management services as reported in OWSI’s Affiliated Interest statements. The so-called “Management Fee” paid to investors in PLA’s parent company should be disallowed as an expense item and should be removed from any rate-setting calculations.

4. New Treatment Plant Loan Fee

On September 1, 2022, the Washington State Department of Health sent OWSI Water a statement for the amount owing on the new treatment plant loan.



Office of Drinking Water
PO Box 1099
Olympia WA 98504-1099

DWSRF LOAN PAYMENT INVOICE

Olympic Water and Sewer Inc
70 Breaker Lane
Port Hadlow, WA 98365-9766

Date: September 01, 2022
Invoice # 3090
Loan: DWL24062

CR 4-2022
PR OWSI

Due Date	Description	Amount
October 01, 2022	Principal	\$85,519.15
	Interest	\$18,814.21
	Loan Fee	→ \$21,100.00
	Late Fee	
	Total Amount Due	\$104,333.36

7-2022

- Payments were calculated using a loan balance of \$1,881,421.32 with an interest rate of 1.00%. Late fees are calculated based on contract terms.
- For questions, please email the finance team at dwsrfinvoicing@doh.wa.gov
- Please notify us of any changes to your contact information.
- **ACH/EFT Payments require notification of payment and the principal interest split amount be emailed to DOHFSOAGRevenue@DOH.WA.GOV**

70% - 73,033.36
30% - 31,300.00

RETURN THE BOTTOM PORTION ALONG WITH YOUR PAYMENT



MAIL PAYMENT TO:

MAKE ACH/EFT PAYMENT:

Department of Health
Office of Drinking Water
PO Box 1099
Olympia, WA 98504-1099

OR

Financial Inst: US BANK
60 Livingston Ave; St. Paul MN 55107-2292
Account Name: 3030-Dept of Health
ABA/Routing #: 123000848
Account #: 153910882452
Cage Code: 1FSD1

Organization: Olympic Water and Sewer Inc		
Loan Invoice #: DWL24062 / 3090		
0866 04011 (04R) GL 1314	Principal	\$85,519.15
04011 04012 (04R)	Interest	\$18,814.21
	Late Fee	
	Total Due	\$104,333.36

Included in that DWSRF Loan Payment Invoice was a \$21,100 “Loan Fee” charge. As can be seen by the handwritten note on the Invoice, the loan fee was categorized by OWSI as a bank fee and was treated as an expense. The loan fee was then entered into the General Ledger on December 31, 2022 as follows:

4	0500-6915		BANK CHARGES								
	5/11/2022	GL	HMM	May	34492	OWSI Deposit Books				-51.58	
						Total 5-31-22	.00*	.00*	51.58-*	51.58-*	
	12-31-202	2 GL	jj	DWSRF	35090	Loan fee assessed by DW	SRF	21,100.00			
						Total 12-31-22	51.58-*	21,100.00*	.00*	21,048.42*	
						Total Ac	count 4-05C 0-6915.00 - BANK CHARGES	.00*	21,100.00*	51.58-*	21,048.42*

In its written response to a data request submitted in this proceeding, OWSI stated that it would agree to the removal of this charge as an expense item “and recategorizing it as a Capital Asset.” We asked UTC Staff about this and received the following response:

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION STAFF
RESPONSES TO DATA REQUESTS

DATE PREPARED: September 6, 2023
DOCKET: UW-230132
REQUESTER: PLVC

WITNESS: Mike Young
RESPONDER: Mike Young
TELEPHONE: 360-664-1155

REQUEST NO. 26 (PLVC No. 2.16): In light of OWSI’s statement in ¶ f of its response to PLVC’s Data Request No. 1- 2 (see OWSI’s Response at page 4) that “OWSI would agree and not object to the removal of [\$21,000] from the Company’s Profit & Loss (P & L) Statement and recategorizing it as a Capital Asset,” do UTC staff intend to make any changes to their analysis or any changes to their recommendation to the Commissioners regarding the proposed rate increase? If so, please describe any such changes and explain the reasons for making them; if not, please explain why not.

RESPONSE:

If the company files a revised revenue requirement, staff would review that filing and would make an appropriate recommendation based on that filing.

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That response from UTC staff is puzzling. On June 16 the Commissioners ordered staff to “institute” a thorough investigation of OWSI’s “books, accounts, practices, activities, property, and operations.” Since OWSI has already agreed that the \$21,000 loan fee should be removed as an expense item, there is no good reason why staff should wait for a further filing from OWSI before making “an appropriate recommendation” based on removing the loan fee as an expense item.

5. Conflicting Income Statements

OWSI's parent company PLA is required to file affiliated interest Income Statements as part of the annual UTC filings. The following is the 2022 Income Statement

Port Ludlow Associates, LLC and Subsidiaries	
Consolidated Balance Sheet	
(in Thousands of Dollars)	
Year Ended December 31,	2022
Revenue	
Hospitality services	\$ 3,834
Marina operations	2,264
Golf course operations	1,217
Inventoried home and land sales	11,064
Utility operations	2,468
Rental property operations	421
Total Revenue	21,268
Costs and Expenses	
Hospitality services	3,705
Marina operations	1,365
Golf course operations	1,411
Inventoried home and land sales	11,234
Utility operations	1,201
Rental property operations	153
Marketing expenses	135
General, administrative, and other expenses	1,127
Total Costs and Expenses	20,330
Income before Depreciation, Interest Expense, Gain on Forgiveness of PPP Loan and Income Taxes	
	937
Depreciation	(708)
Interest expense	(85)
Gain on forgiveness of PPP Loan & ERTC costs	(31)
Income (Loss) before Income Tax Expense	113
Income Tax Expense	114
Net Income (Loss)	\$ 227

Please note the revenue of Utility Operations (water and sewer together) of \$2,468,000 and the Utility Operations expenses of \$1,201,000.

UTC staff asked for a breakdown of revenue and expenses between OWSI Water and OWSI Sewer. Ms. Smeland provided the following:

<i>Income Statement</i>			
Description	Water Company		Waste-Water Company
List	End of Year		End of Year
	\$		\$
REVENUES			
OPERATING REVENUE	\$ 824,577		\$ 1,560,907
EXPENSES			
OPERATING EXPENSES	\$ 970,494		\$ 914,138
Operating Income before Taxes	(145,917)		646,769
Interest Expense	5,644		2,200
Fed Income Tax	39,986		135,359
TOTAL OPERATING EXPENSE	1,016,124		1,051,697
NET INCOME (LOSS)	(\$191,547)		\$509,210
NET OPERATING INCOME	(\$185,903)		\$511,410

UTC 2022	OWSI
Annual	Income Stmt
Submission	Ms. Smeland
Utility Revenue	Utility Revenue
\$ 2,468,000	\$ 2,385,484
Utility Expense	Utility Expense
\$ 1,201,000	\$ 2,067,824
Income or (Loss)	Income or (Loss)
\$ 1,267,000	\$ 317,660

To make the comparison easier the totals from both documents appear to the left.

Comparing the two documents shows significantly different numbers.

The revenue difference can be explained by the absence of the surcharge of **\$83,688** from the OWSI Income Statement.

The difference of \$866,824 in the Utility Expense is much harder to explain.

The difference between the two submissions for Income or (Loss) is enormous - \$948,340.

Port Ludlow Associates is the parent company of the Port Ludlow Inn, West Harbor Homes, Olympic Water and Sewer, the Port Ludlow Marina, the Port Ludlow Golf Course, and a commercial rental property operation. Presumably each of the above entities (not sure about the rental property operation) has its own separate business license, pays its own taxes, and has dealings with Olympic Water and Sewer. They are affiliated interests with OWSI per WAC 480-110-545.

In the Annual Submissions to the UTC, OWSI lumps together revenues and expenses of these other operations, effectively masking how several of the above entities are losing money and are being subsidized by OWSI.

That does not give a true picture of the affiliated interests' finances, and it obscures what is the true financial picture of OWSI Water and the various other business operations of PLA. As has been discussed previously, PLA has charged the following to OWSI for 2022.

3% "Management Fee" for both Water and Sewer	\$ 74,040
General and Admin Fee for both Water and Sewer	<u>\$426,155</u>
OWSI Water and Sewer paid to PLA	\$500,165
	=====

Below is the revenue portion of the 2022 Income Statement provided by Port Ludlow Associates.

Port Ludlow Associates, LLC and Subsidiaries	
Consolidated Balance Sheet	
(in Thousands of Dollars)	
Year Ended December 31,	2022
Revenue	
Hospitality services	\$ 3,834
Marina operations	2,264
Golf course operations	1,217
Inventoried home and land sales	11,064
Utility operations	2,468
Rental property operations	421

The \$500,165 of revenue that Olympic Water and Sewer paid Port Ludlow Associates does not seem to be included in the revenue that PLA reported.

Such income statement inconsistencies should be included in UTC staff's investigation of OWSI's accounting practices that was ordered by the Commissioners on June 16.

6. Hours Worked Breakout and Allocators between Water and Sewer

The UTC has been told repeatedly about how much more employee time the new treatment facility is taking. The UTC Staff asked Olympic Water and Sewer to give a time breakout of employees between water and sewer for 2022. The following was submitted by Greg Rae, as Vice President of OWSI:

Report: Calculated Time Summary: Copy of Calculated Time Summary - \$ Split
Sorted By: Last Name Ascending; First Name Ascending
Filtered By: Employee Filter: All Employees; Counter Date: 01/01/2022-12/31/2022; Department in Water G&A,Sewer G&A
Date & Time: 03/09/2023 09:52a
Generated By: Gregory Rae
Company: Port Ludlow Associates LLC (90539)

Counter Date: 01/01/2022-12/31/2022			Olympic Water and Sewer Worked				
Employee ID	First Name	Last Name	Department	Regular Hours	Overtime Hours	Water Hours	Sewer Hours
10290	Enrique	Denkfranco	Water G&A	22.5	-	22.50	
10290	Enrique	Denkfranco	Sewer G&A	128.75	-		128.75
10273	John	Graham	Sewer G&A	71	-		71.00
10273	John	Graham	Water G&A	193	5	198.00	
2891	Michael	Graves	Water G&A	336	3.5	339.50	
2891	Michael	Graves	Sewer G&A	153.5	8.5		162.00
10223	Alexander	Jones	Sewer G&A	649.5	42.5		692.00
10223	Alexander	Jones	Water G&A	729	16	745.00	
10161	Dawson	Lawrence	Water G&A	252	1	253.00	
10161	Dawson	Lawrence	Sewer G&A	155	12.75		167.75
10147	Shae	Sill	Water G&A	950.83	9.25	960.08	
10147	Shae	Sill	Sewer G&A	977.95	68		1045.95
10120	Joseph	Spears	Sewer G&A	1022.25	58.75		1081.00
10120	Joseph	Spears	Water G&A	827.75	3.5	831.25	
10215	Rustin	Webb	Water G&A	488	3	491.00	
10215	Rustin	Webb	Sewer G&A	464.5	21		485.50
Total Hours						3840.33	3833.95

Statistically, it very close to 50%-50%, with only about 6 hours separating Water and Sewer employee hours for 2022. Couple this with OWSI Sewer having twice the revenue (\$1,516,907) versus OWSI Water (\$824,577) and it is easy to question why the allocator between Water and Sewer should be 67% Water and 33% Sewer.

Allocators, the ratios between OWSI Water and OWSI Sewer, have been a point of contention throughout the rate-setting process. Questions were asked of the UTC Staff and Olympic Water and Sewer to get the origin of the allocators and where they were written down. OWSI provided the following information:

Personnel: For personnel and employee payroll, OWSI employees track where they work and segregate their time between water and sewer services. The Vice President and Management time is split 50/50 between water and sewer. This 50/50 split has been consistent.

Invoices: Invoices for contracts, services, and purchases are reviewed by the Operations Manager and individually coded before input into Accounts Payable. With the exception of the noted items below, invoices are allocated based on where used except for the following:

- Uniforms are allocated 50/50 between water and sewer.
- Safety (i.e. PPE type) costs are allocated 50/50 between water and sewer.
- Locates and emergency phone line services are allocated 50/50 between water and sewer.
- Transportation costs are allocated 67% water and 33% sewer.
- Automobile insurance is allocated 67% water and 33% sewer.
- General Insurance is allocated 50/50 between water and sewer.

As further explanation, for personnel and employee time, employees track where they work and segregate their time between water and sewer services on Company timecards. For invoices, the Operations Manager codes invoiced amounts based on the services applicable to the invoice.

With respect to the other categories, the referenced 67%/33% split is based on where most of the work is done. As a general matter, OWSI typically has 4 to 6 employees working on water utility related activities and 1 to 2 employees working on sewer (WWTP) utility related activities. OWIS worked closely with Jim Ward (WUTC Staff) when he worked on OWSI's general rate case back in or around 2008. Mr. Ward and WUTC staff worked closely with the Controller, and they went through the split and allocation between water and sewer. At that time, the allocation was established at 74%/26% (with 74% attributable to water and 26% attributable to sewer). This split has been reviewed over the years. In 2019, the allocation was changed from 74%/26% to the current allocation of 67%/33% (with 67% attributable to water and 33% attributable to sewer).

The above is the closest explanation of the allocators between Water and Sewer but it still raises several questions.

Where is the original documentation from 2008? This has been requested several times from both the UTC Staff and OWSI but the documentation has never been produced. Ms. Smeland indicated that the split had been reviewed over the years and in 2019 it was changed to a 67%-33% split. Who reviewed the split? Was it approved by the UTC? Where are the underlying documents for changing the split?

After reviewing the 2022 Time Summary submitted by OWSI, a 50%-50% split appears to be more appropriate.

According to Ms. Smeland, "Transportation Costs are allocated 67% Water and 33% Sewer." In reviewing the documentation requested by the UTC Staff, this split does not seem to be applied to EOM (End of Month) gas transfers for January or June 2023. Please see below.

Accounting Date	Account	Debit	Credit	Jrn	Reference 1	Reference 2	Transaction Desc
1-31-22	1-0300-6720.00	60.15	.00	72	HMM	January EOM Gas Transfers	
1-31-22	1-0010-6720.00	513.51	.00	72	HMM	January EOM Gas Transfers	
1-31-22	4-0500-6720.00	1,017.86	.00	72	HMM	January EOM Gas Transfers	
1-31-22	4-0600-6720.00	339.29	.00	72	HMM	January EOM Gas Transfers	
1-31-22	1-0180-6720.00	242.65	.00	72	HMM	January EOM Gas Transfers	
1-31-22	1-0101-6720.00	25.39	.00	72	HMM	January EOM Gas Transfers	
1-31-22	4-0000-1115.00	.00	339.29	72	HMM	January EOM Gas Transfers	
1-31-22	4-0000-1115.50	.00	1,017.86	72	HMM	January EOM Gas Transfers	
1-31-22	1-0000-2005.00	1,357.14	.00	72	HMM	January EOM Gas Transfers	
1-31-22	1-0201-6415.00	.00	2,218.84	72	HMM	January EOM Gas Transfers	

Port Ludlow Associates has its own gas pump and all of the affiliated businesses use it including Olympic Water and Sewer. The January OWSI usage was \$1,357.14 and it was split between \$339.29 for Sewer and \$1,017.86 for Water. Not the 67%-33% as had been specified but rather 75%-25%. Below is the General Ledger entry.

4 0500-6720		COMPANY CAR OPERATING EXPENSE					
1/5/2022	INV	WHIJAS00	1313	29866	DISTILLED WATER, HEAD L	IGHT	5.65
1/12/2022	INV	JEFAUD00	4462ZLIJAN	29928	2001 MULTI GENERATOR		47.25
1/19/2022	INV	CHSINC00	267269	29958	OWSI FUEL		105.08
1/25/2022	INV	PETLOC01	20692	30026	OWSI REKEY		40.91
1/31/2022	GL	HMM	January	34226	EOM Gas Transfers		1,017.86
Total 1-31-22						.00*	1,216.75*

This same 75%-25% split also shows up again in the June EOM gas transfers. It is thought that all of the EOM gas transfers are being split using the wrong allocators. This reinforces the inaccuracies that have been found in the OWSI accounting and they seem to repeatedly favor the Sewer side.

Ms. Smeland also submitted the following:

The Vice President and Management time is split 50/50 between water and sewer. This 50/50 split has been consistent.

In reviewing the invoices submitted for cell phones this 50/50 split is not being done for Greg Rae and Jason White. Their cell phones and one other employee are being charged to OWSI Water costing \$289.25 and the rest of the employees are being charged to OWSI Sewer at a cost of \$190.71. See below.



PO BOX 489
NEWARK, NJ 07101-0489

00000686/4080/ 1.583/AB/42646140.1



PT LUDLOW ASSOCIATES LLC
70 BREAKER LN
PORT LUDLOW, WA 98365-9766

00000686
MSP 7

Row Labels	Sum of Total
1-0010-6503	328.37
1-0121-6503	56.85
1-0123-6503	93.45
1-0160-6503	0
1-0180-6503	36.6
1-0200-6503	25.57
1-0201-6503	-25.14
1-0220-6503	118.84
1-0300-6503	56.84
1-0303-6503	-7.56
1-0304-6503	56.85
4-0500-6503	289.25
4-0600-6503	190.71
Grand Total	1220.63

Manage Your Account	Account Number	Date Due
b2b.verizonwireless.com	864954114-00001	04/28/22
Change your address at http://sso.verizonenterprise.com	Invoice Number	9903533134

Quick Bill Summary

Mar 07 - Apr 06

Previous Balance <i>(see back for details)</i>	\$1,305.87
Payment -- Thank You	-\$1,305.87
Balance Forward	\$0.00
Monthly Charges	\$894.39
Equipment Charges	\$259.32
Surcharges and Other Charges & Credits	\$35.09
Taxes, Governmental Surcharges & Fees	\$31.83
Total Current Charges	\$1,220.63

The split for cell phones is not a 50%-50% split, nor is it a 67%-33% split. The result again favors the Sewer side.

The last item about the allocators is what is not being allocated between Water and Sewer but should be. For example, Olympic Water and Sewer has one building at 781 Walker Way in Port Ludlow. This is the main office where the ordering is done, time records are kept, vehicles are stored, uniforms are stored, and where the employees report each day. In 2022 the property tax on this parcel was \$1851.99 and OWSI Water paid the entire amount. The property tax should have been split, presumably 50%-50%.

Electricity, sewer, water, insect extermination, etc. should all be split 50%-50%.

The personal property tax at 781 Walker Way probably should not be 50%-50%. OWSI Water has equipment there just for use on the waterside and this should be charged to Water.

The computers at the site are used interchangeably between Water and Sewer and should be charged at 50%-50% as well as the software maintenance. Office supplies sometimes are split 50%-50% while other times are charged just to OWSI Water. Below is an example:



Order# 7366970744

Order placed: October 12, 2022

Accounting Information

PO
OWSI

Billing address

PORT LUDLOW ASSOCIATES LLC
70 BREAKER LN
PORT LUDLOW, WA 98365

Shipping address

PORT LUDLOW ASSOCIATES LLC
TRESSA BARBER
70 BREAKER LN
PORT LUDLOW, WA 98365

INVOICE PENDING on November 11, 2022

Item#	Item Description	Price	Quantity	Subtotal
461375	uni-ball VISION ELITE Rollerball Pens, Bold Point, Blue Ink, 12/Pack (61232)	\$39.69	1	\$39.69
470087	uni-ball Vision Elite Rollerball Pens, Bold Point, Black Ink, 4 Pack (67180)	\$12.09	3	\$36.27
Merchandise Total:				\$75.96
Tax:				\$6.91
Total:				\$82.87

Water

Sewer

4-0.500-6600 = 41.43
4-0.600-6600 = 41.44 *JW*

The very next invoice shows something different.



Order# 7366554337

Order placed: October 04, 2022

Accounting Information

PO
OWSI

Billing address

70 BREAKER LN
PORT LUDLOW, WA 98365

Shipping address

PORT LUDLOW ASSOCIATES LLC
TRESSA BARBER
70 BREAKER LN
PORT LUDLOW, WA 98365

INVOICE PENDING on October 06, 2022

Items(s) Shipped

Item#	Item Description	Price	Quantity	Subtotal
24523508	2023 House of Doolittle Economy 17" x 22" Monthly Desk Pad Calendar, White/Black (124-02-23)	\$6.99	6	\$41.94
Merchandise Total:				\$41.94
Tax:				\$3.82
Total:				\$45.76

4-0500-6600
JW

As can be seen by the handwritten account number only OWSI Water is being charged for the 6 desk pad calendars.

OWSI Water and OWSI are both required to have an answering service. It does not matter if OWSI Water receives the majority of the after-hours phone calls; OWSI Sewer still must have the answering service. Again this should be a 50%-50% split. In reviewing the invoices, sometimes they are split 50%-50% and other times it is all being charged to OWSI Water.



SECURITY SERVICES
NORTHWEST, INC.
250 Center Park Way
Sequim WA 98382
(800) 859-3463

Invoice

DATE	INVOICE #
12/1/2022	125847

BILL TO:

OLYMPIC WATER & SEWER
781 WALKER WAY
PORT LUDLOW WA 98365

P.O. NUMBER	TERMS	PROJECT
-------------	-------	---------

Due by 15th

QUANTITY	DESCRIPTION	RATE	AMOUNT
	ANSWERING SERVICE ACCOUNT NUMBER 0276		
	MONTHLY RATE (120 MONTHLY BASE CALLS) DECEMBER 2022	114.85	114.85
0	OVERAGE FEES (.95 PER CALL)	0.95	0.00

4-0500-6503
12-20-22

Mr Rehberger in his September 7, 2022 response wrote the following:

Invoices: Invoices for contracts, services, and purchases are reviewed by the Operations Manager and individually coded before input into Accounts Payable. With the exception of the noted items below, invoices are allocated based on where used except for the following:

- Uniforms are allocated 50/50 between water and sewer.
- Safety (i.e. PPE type) costs are allocated 50/50 between water and sewer.

- Locates and emergency phone line services are allocated 50/50 between water and sewer.
- Transportation costs are allocated 67% water and 33% sewer.
- Automobile insurance is allocated 67% water and 33% sewer.
- General Insurance is allocated 50/50 between water and sewer.

Locates are done by a third party to show where underground power or telephone transmission lines are located. Mr. Rehberger states that these are split 50%-50% between Water and Sewer.

Statement

Utilities Underground Location Center
 P.O. BOX 3701
 SEATTLE, WA 98124-3701
 (410) 712-0082

Statement Date: 1/6/2023
 Customer Number: 00-0166700

OLYMPIC WATER & SEWER INC
 ACCOUNTS PAYABLE
 70 BREAKER LANE
 Port Ludlow, WA 98365

Date	Reference	Description	Charge	Credit	Balance
10/31/2022	2100523-IN		25.80		25.80
12/31/2022	2120522-IN		14.19		14.19 ✓

4-0506-6050
 AM

PAST DUE - FINAL NOTICE

The following shows the general ledger entry:

4 -0506 Water Distribution - Maintenance									
4 0506-6050		0 PROF SER	VICES - M	ISCELLANEOUS					
1/31/2022	INV		UTIUND00	2010515	30070	OWSI NOTIFICATIONS		16.77	
						Total 1-31-22	.00*	16.77*	.00
3/30/2022	INV		UTIUND00	2030517	30380	OWSI EXCAVATION		29.67	
						Total 3-31-22	16.77*	29.67*	.00
4/30/2022	INV		UTIUND00	2040519	30646	OWSI NOTIFICATIONS		25.8	
						Total 4-30-22	46.44*	25.80*	.00
7/28/2022	INV		MISCOM00	1067255	31109	OWSI SVC PKG		563.4	
						Total 7-31-22	72.24*	563.40*	.00
8/15/2022	INV		UTIUND00	2070523	31255	OWSI NOTIFICATIONS		23.22	
						Total 8-31-22	635.64*	23.22*	.00
9/30/2022	INV		UTIUND00	2090523	31568	OWSI NOTIFICATIONS		30.96	
						Total 9-30-22	658.86*	30.96*	.00
12-30-202	2 INV		UTIUND00	2120522	32043	OWSI NOTIFICATIONS		14.19	
12-30-202	2 INV		UTIUND00	2100523-IN	32095	OWSI NOTIFICATIONS		25.8	
						Total 12-31-22	689.82*	39.99*	.00

Of course we realize that the amounts involved in some of these particular examples are quite small, perhaps even trivial. But our concern is with the apparent inconsistencies in how such expenses are allocated by the bookkeepers, as well as whether there is an adequate basis for utilizing the particular allocation method. Even if those allocation methods were “carefully considered” in 2008, that does not mean the same allocation methods are still appropriate in 2022 or 2023.

7. Adding Hours and Dollars Together

In reviewing the OWSI Water General Ledger, it was noted that there were several interesting entries in the WIP Contra Payroll Account.

WIP Contra Payroll					

JCC	HMM	###	Meter Replace 77 Martingale		-87.15
JCC	HMM	###	REv JC#6880/Mov To Oct	87.2	

2 JCC	HMM	###	Meter Replace 77 Martingale		-176.12
2 JCC	HMM	###	Meter Replacement 20 Camano Ln		-89.42
2 JCC	HMM	###	Meter Replace 77 Martingale		-87.15

The \$87.15 was entered and then removed from the September entry for 77 Martingale.

The \$87.15 was then entered again in October along with another entry for 77 Martingale for \$176.12.

The UTC Staff must have had some questions about these WIP Contra Payroll entries because they requested the backup documentation from Olympic Water and Sewer. One of backup documents sent supporting this general ledger entry is provided below.

JO#6882

Job Extra	Task Cat	Transaction Type	Units	Unit Cost	Amount	Transactn Date	Accounting Date
1-300-105	3-30-80-20 0	JC cost	.0000	.0000	176.12-	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	Ref 1 1094			Deb Acc 4-0000-1320.50		
1-500-105	3-30-80-20 0	JC cost	.0000	.0000	176.12	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	Ref 1 1094			Deb Acc 4-0000-1320.50		
1-500-105	3-01-14-35 0	JC cost	.0000	.0000	308.50-	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	Ref 1 1096			Deb Acc 4-0000-1320.50		
Description	Meter Replace 77 Martingale	General Ledger only Ref 1 1094	.0000	.0000	.53	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	General Ledger only Ref 1 1096	.0000	.0000	176.12	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	General Ledger only Ref 1 1096	.0000	.0000	485.15	10-04-22	10-31-22
Description	Meter Replace 77 Martingale	General Ledger only Ref 1 1094	.0000	.0000	176.12	10-04-22	10-31-22

ENTRY TOTALS

Number of entries	6
Total amount of entries	353.30

ADDITIONAL INFORMATION

IMPD -- Job 1-300-105, task 3-30-80-20, category 0 Other was posted to a future GL period for account 4-0000-1320.50.

POST ENTRIES TOTALS

Number of Entries	Posted 6	Rejected 0
Amount of Entries	353.30	.00

Entry	Amount
JC Direct Cost	308.50-
Total Cost	308.50-
General Ledger Only	661.80
Total Amount Posted	353.30

Job	Category	Cost Posted	Hours Posted
1-500-105 1* RABED METERS	Other	308.50-	
* Total *		308.50-	

GENERAL LEDGER RECAP

Account	Account Title	Debit	Credit
4-0000-1320.50	INVENTORY WIP - COMMERCIAL	308.50-	.00
4-0000-1760.50	WATER METER INSTALLATION	485.15	.00
4-0500-6998.00	WIP Contra Payroll	.00	176.12
4-0506-6260.00	R & H - MISCELLANEOUS	.00	.53
		176.65	176.65

Number of entries created: 6

GL POSTING SUMMARY REPORT

Entries from JC Enter direct costs 10-04-22			
	Posted	Rejected	
Number of entries	6	0	
Debit Amount	176.65	.00	
Credit Amount	176.65	.00	
POSTING TOTALS			
Number of entries	6	0	
Debit Amount	176.65	.00	
Credit Amount	176.65	.00	
Proof	.00		

All of the above entries are for 77 Martingale, and OWSI provided the methodology used for determining the amount to be charged to the WIP Contra Payroll Account as follows:

DATE: 9/29/2022

	Greg Sal	Jason Hrly	Hrly	Joseph Hrly	John Hrly	Alex Hrly	Shae Hrly	Total	
Hours	-	-	-	-	2.00	2.00	-	4.00	based on installation report
PYRL TAXES	-	-	-	-	4.53	6.34	-	10.88	ER payroll tax breakdown .1133
L&I INS	-	-	-	-	0.58	0.56	-	1.12	per 2016 ER L & I rate table
BENEFITS	-	-	-	-	5.06	5.06	-	10.12	ER med+dent+life+vac
Gross Pay	-	-	-	-	75.00	75.00	-	150.00	Hourly rate
Total	-	-	-	-	87.15	88.96	-	176.12	

Meter Install Monthly Entry for Payroll allocation to capitalized meter

The total column on the right side shows the dollar total of \$176.12 as was referenced on the previous page. What is alarming is how that total was arrived at.

In the first column in line 1 it clearly says “Hours” and at the end of line 1 is this note “based on the installation report”. The rest of the lines reference payroll taxes, L&I benefits, benefits, and gross pay.

In reading the table John worked 2 hours and Alex worked 2 hours. Payroll tax dollars, L&I dollars, benefit dollars, and gross pay dollars were all entered. The column for John and the column for Alex were then summed and the totals were entered. Please note the 2 hours on line 1 were added to the dollars in the next 4 lines for both employees and the total, \$176.12 was at the right.

Clearly, the number of hours should not have been included in adding up the number of dollars.

To see how that error was compounded, a relook at the General Ledger entry is necessary.

WIP Contra Payrol				

JCC	HMM	###	Meter Replace 77 Martingale	-87.15
JCC	HMM	###	REv JC#6880/Mov To Oct	87.2

2 JCC	HMM	###	Meter Replace 77 Martingale	-176.12
2 JCC	HMM	###	Meter Replacement 20 Camano Ln	-89.42
2 JCC	HMM	###	Meter Replace 77 Martingale	-87.15

The entry of \$176.12 was entered for October (Alex and John) and then Alex’s total, \$87.15 was entered again.

If this was an isolated error it could be overlooked, but adding the hours and dollars together is repeated over and over. The following is another example.

This was entered in the General Ledger for meter replacement at 381 Rainer Lane:

General Ledger				
10-31-22	JCC	381 Rainer Lane Met	6889	-534

This is the supporting table:

DATE: 9/27/2022

	Greg Sal	Jason Hrly	Hrly	Joseph Hrly	John Hrly	Alex Hrly	Shae Hrly	Total	
Hours	-	7.00	-	-	-	7.00	-	14.00	based on installation report
PYRL TAXES	-	36.39	-	-	-	-	-	36.39	ER payroll tax breakdown .1133
L&I INS	-	1.96	-	-	-	1.96	-	3.92	per 2016 ER L & I rate table
BENEFITS	-	38.08	-	-	-	-	-	55.79	ER med+dent+life+vac
Gross Pay	-	262.50	-	-	-	161.00	-	423.50	Hourly rate
Total	-	325.56	-	-	-	208.04	-	533.60	

This time we have Jason and Alex working together and each spent 7 hours on the meter replacement. Again the **hours** have been added to the **dollars** in the totals.

There are dozens and dozens of such entries where hours are added to dollars.

A review of the dollar entries raises additional questions.

	Jason	Alex	Total
Hours	7.00	7.00	14.00
PYRL Taxes	\$ 36.39		\$ 36.39
L&I INS	\$ 1.96	\$ 1.96	\$ 3.92
Benefits	\$ 17.71	\$ 38.08	\$ 55.79
Gross Pay	\$ 262.50	\$ 161.00	\$ 423.50
Total	\$ 325.56	\$ 208.04	\$ 533.60

It looks like Alex does not get charged any payroll tax. Jason, whose gross pay was \$100.00 more than Alex's, had less than half the benefits. Perhaps there is a good explanation for this. But it is not apparent.

These kinds of accounting issues call into question the overall reliability of OWSI's accounting practices.

8. Allocation of PLA’s G&A Management Fee

In 2022 PLA charged OWSI Water a “G&A management fee” of \$285,524 and charged OWSI Sewer a “G&A management fee” fee of \$140,631, for a total of \$426,155. One of the questions that should be asked is whether OWSI is overpaying PLA for the management services being provided. A second question is whether the 67%-33% split between Water and Sewer is appropriate.

In the supporting documentation submitted to the UTC Staff, Ms. Smeland provided the following in the “Contractual Accounting” Tab as transcribed for easier reading.

Type of Service	PLA Corp Expenses	Percent Allocated To OWSI	OWSI	OWSI Water 67%	OWSI Sewer 33%
OWSI Corporate and Officers	\$ 303,417	65%	\$ 197,221	\$ 132,138	\$ 65,083
Accounting	\$ 457,867	48%	\$ 217,487	\$ 145,716	\$ 71,771
IT	\$ 74,873	15%	\$ 11,231	\$ 7,525	\$ 3,706
HCV	\$ 10,787	2%	\$ 216	\$ 145	\$ 71
Totals	\$ 846,944	50%	\$ 426,155	\$ 285,524	\$ 140,631

It should be noted that the salary of Greg Rae, Vice President of OWSI, is part of the OWSI payroll and is not included in the above “management fee.”

The UTC Staff asked Olympic Water and Sewer for all written contracts and arrangements with PLA. None were provided, and none seem to exist.

Ms. Smeland's table indicated that 65% of PLA’s Corporate and Corporate Officers' time was spent on OWSI business. There was no accompanying backup documentation supporting that assertion, but nevertheless it was accepted by UTC Staff. The percentage increased from an unknown prior amount to 65%. This was in clear violation of WAC 480-110-545, “Affiliated Interests”:

WAC 480-110-545 Affiliated interests—Contracts or arrangements. Prior to the effective date of any contract or arrangement described in RCW 80.16.020, each water company must file a verified copy or a verified summary, if unwritten, of contracts or arrangements, except for transactions provided at tariff rates, with any affiliated interest. **Prior to the effective date of any modification or amendment, the company must file verified copies of the modifications or amendments to the contracts or arrangements. If the contract or arrangement is unwritten, the company must file a verified summary of any modification or amendment.**

The 65% allocation was not applied for before 2022, and by the WAC provision should be disallowed.

Since there are no approved written agreements between PLA and OWSI, to determine the percentage for PLA Corporate and Officers another method must be used. The most logical place to look would be the submitted Income Statement from Port Ludlow

Associates. The amounts have been taken from the Olympic Water and Sewer 2022 UTC Annual Filing and have been recast and percentages added.

Port Ludlow Associates 2022	Revenue	%	Expense	
Hospitality services	\$ 3,834,000	18%	\$ 3,705,000	18%
Marina Operations	\$ 2,264,000	11%	\$ 1,365,000	7%
Golf Course operations	\$ 1,217,000	6%	\$ 1,411,000	7%
Inventoried home and land sales	\$ 11,064,000	52%	\$ 11,234,000	55%
Utility operations	\$ 2,468,000	12%	\$ 1,201,000	6%
Rental property operations	\$ 421,000	2%	\$ 153,000	1%
Marketing			\$ 135,000	1%
General, Administrative and Other			\$ 1,127,000	6%
	\$ 21,268,000	100%	\$ 20,331,000	100%

Please note that depreciation, Federal Tax, and other expenses have been removed from the individual entities by Port Ludlow Associates.

OWSI utility operations account for only 12% of PLA's Revenues and only 6% of PLA's Expenses, but are being charged 65% of the Corporate and Officers' Expense. A quick look at the Golf Course and the Inventoried Homes shows that they are in an apparent loss situation. Hospitality services, when depreciation and taxes are added, most likely would be in a loss situation. Together, those three segments of PLA's business represent 76% of the Revenue and 80% of the expenses.

It is hard to believe that 65% of the Corporate and Officers' time is being spent on the OWSI utility business when three major business segments representing 80% of the expenses are losing money.

PLA's Corporate and Officers total expense is \$303,417, and OWSI is being charged for 65% of that expense while accounting for only 12% of the revenues and 6% of the expenses. That defies common sense. Ms. Smeland, in the spreadsheet, gives the following explanation:

Basis: 65% of the department is associated with OWSI due to filtration and increased duties

Ms. Smeland refers to filtration, presumably meaning the new water treatment facility. If this were 2020 or 2021, Ms. Smeland would have spent a lot of time with plans, bids, and contractors getting the new treatment plant built and online. But the water treatment facility was online and functioning in 2022, and her time spent on the treatment facility would be decreased.

Ms. Smeland also talks about increased duties but gives no description or documentation as to what she is referring to. In 2022, West Harbor Homes (Inventoried

Homes and Land Sales) was in the process of building new home sites in Olympic Terrace II Phase Two. Jefferson County was telling West Harbor Homes that they were not going to pay for ongoing road maintenance in new developments. Ms. Smeland was very much involved in the negotiations with the County. Lead managers at the Port Ludlow Inn (Hospitality Services) and Port Ludlow Golf Resort (Golf Course) had resigned, adding to further problems at both locations. With all those problems it is difficult to believe that Ms. Smeland spent the vast majority of her time on OWSI Water.

Regarding the 67-33 split between OWSI Water and OWSI Sewer, OWSI provided the following explanation in its written response to Public Counsel's Data Request No.1:

With respect to the other categories, the referenced 67%/33% split is based on where most of the work is done. As a general matter, OWSI typically has 4 to 6 employees working on water utility related activities and 1 to 2 employees working on sewer (WWTP) utility related activities. OWIS worked closely with Jim Ward (WUTC Staff) when he worked on OWSI's general rate case back in or around 2008. Mr. Ward and WUTC staff worked closely with the Controller, and they went through the split and allocation between water and sewer. At that time, allocation was established at 74%/26% (with 74% attributable to water and 26% attributable to sewer). This split has been reviewed over the years. In 2019, the allocation was changed from 74%/26% to the current allocation of 67%/33% (with 67% attributable to water and 33% attributable to sewer).

As to employee time, as shown above (page 17) the information provided by Mr. Rae based on employee time records shows that OWSI employee time was split almost exactly 50-50 between Water and Sewer operations. In the absence of actual management time records showing time spent on water issues versus sewer issues, using the split between employee time spent on water operations or sewer operations might be a reasonable way to allocate management time between the two kinds of utility operations. This would suggest that a 50-50 split would be more appropriate than a 67-33 split. Perhaps another way to allocate management time would be on the basis of comparing water revenues versus sewer revenues. As shown above (page 8), sewer revenues were about twice as much as water revenues in 2022, suggesting that a 33-67 split between water and sewer management expense would be more appropriate than a 67-33 split. In any event, the notion that Mr. Ward of UTC worked closely with PLA's controller fifteen years ago in 2008 and concluded at that time that a 74/26 split was appropriate should somehow justify the present 67/33 split, is less than persuasive.

This is yet another reason why UTC staff should comply with the Commissioners' June 16 Order by instituting a thorough investigation of OWSI's accounting practices and its methods for allocating shared expenses.

9. Conclusion

As indicated above and in prior communications to UTC staff and to OWSI, we lack confidence in the reliability of OWSI's accounting practices, and we submit (i) that OWSI has not been complying fully with its reporting requirements and has not provided sufficient justification for its requested water rate increase and (ii) that UTC staff have not adequately scrutinized OWSI's purported justification for the rate increase request. We assume it was largely for these reasons that in their June 16 Order the Commissioners explicitly ordered UTC staff to "institute an investigation of Olympic Water and Sewer, Inc.'s books, accounts, practices, activities, property, and operations."

The Order did not suggest that staff should merely respond to questions raised by ratepayers or by intervenor PLVC. We assume the Commissioners intended that UTC's professional staff would "institute" their own thorough investigation and then would issue a report concerning the results of their investigation, which might or might not call for a refund or rollback of the provisionally approved rate increase. We see no evidence yet that staff have complied with the June 16 Order by performing such an investigation.

If our concerns about OWSI's accounting practices, including how shared expenses are being allocated to the water utility, are unwarranted, or if there are simple explanations for the apparent anomalies or inconsistencies we have noted, we have no wish to impose unnecessary costs or burdens on either OWSI or UTC staff and would welcome any such explanations from OWSI or from UTC staff. We look forward to having a constructive and informative discussion with the parties about these issues.