

Hello Neighbor,

Sadly, PSWID's attorney, Mr. John Gliege, passed away on February 21<sup>st</sup>. Our condolences to his family and friends on his passing.

A little over a year ago I prepared an analysis that pointed out seven errors in the water rate analysis that Economists.com's Mr. Dan Jackson prepared and provided to the board in October of 2008. At the time Mr. Jackson and Mr. Haney were rather abusive in their response to these errors and refused to address the merits of the actual issues. Basically they took the position that Mr. Jackson could not be questioned because of his experience and credentials. Their responses at the time can be viewed here:

- [http://www.paysonroundup.com/news/2009/feb/17/unfounded\\_accusations\\_waste\\_time\\_and\\_resources\\_wa/](http://www.paysonroundup.com/news/2009/feb/17/unfounded_accusations_waste_time_and_resources_wa/)
- [http://www.paysonroundup.com/news/2009/feb/17/attacks\\_against\\_consulting\\_firm\\_baseless/](http://www.paysonroundup.com/news/2009/feb/17/attacks_against_consulting_firm_baseless/)
- <http://www.waterforpinestrawberry.com/data%20pages/EconResponsetoSchwalm021009.pdf>

Over the course of time it has become clear that the Economists.com analysis was indeed in error. Of the seven errors, six have been confirmed and one is probable. Those errors were substantial and had they been addressed, the claim that the water companies could be purchased without a rate increase would have been shown to be false. There is every appearance that the board and Mr. Jackson avoided addressing the errors because if the public knew what the acquisition of the water system would really cost there might have been a backlash of public opinion. The board continued to say that Mr. Jackson was telling them that there would be no rate increase required, even after the amount being borrowed increased by \$2 million. What they did not say out loud was that Mr. Jackson had added hundreds of thousands of dollars a year in subsidies from property taxes and borrowed money to his rate analysis in order to close the gap.

The board purchased the water system without ever providing an honest assessment of the financial impact to the community. By actively avoiding addressing the issues that were brought up with the initial analysis, they ensured that a false picture of the financial commitment that they were making was presented to the community.

The PSWID board and Mr. Jackson owe the community an apology and an explanation.

What follows is the scorecard on the issues. The original analysis of the errors can be found here:

<http://www.waterforpinestrawberry.com/data%20pages/RateAnalysisWriteup.v3.pdf> .

1. Water transfers from Strawberry to Pine were being double counted.
  - a. Error: The water transferred to Pine from Strawberry is included in Strawberry's total water sold. That same water is also included in the Pine total water sold, so it has to be subtracted out of Strawberry's total to keep it from being double counted. Mr. Jackson did not make this adjustment in the numbers that he used

in his analysis. Over-stating the amount of water sold caused projected revenues to be higher.

- b. Jackson Response: “In fact, I believe it would be improper to include intra-company water transfers in the ratepayer water sales portion of the standardized ACC report. He then speculates, again with no supporting evidence, that \$39,051 of revenues should be eliminated to account for an alleged transfer payment for this water.”
  - c. Result: Pine and Strawberry were two separately regulated companies under the same holding company and it is basic regulatory knowledge that transfers between two companies of that nature would have to be accounted for so that one set of rate payers wouldn’t be subsidizing the others. This was clearly not an intra-company transfer. In addition, Mr. Jackson chose to ignore the fact that it was written in the Strawberry ACC reports that the transfers to Pine were included in the totals. Mr. Jackson used 97,881,236 gallons in the 2008 analysis and used 75,522,987 gallons in the September 2009 final version. **Error Confirmed.**
2. Removal of “Taxes Other Than Income” from Operations Budget needs to be balanced by reductions in Revenue
- a. Error: According to Brooke, the entry for “Taxes Other Than Income” was the sales taxes collected and that the sales taxes were included in the revenue numbers and this entry was there to subtract them out. Mr. Jackson included this entry in his 2003 rate analysis, but left it out of his 2008 analysis.
  - b. Jackson Response: “He erroneously adds Taxes Other Than Income to the forecast operating expense, even though as a public entity the District will not be required to pay taxes. He alleges that this offsets sales taxes that are supposedly in Brooke's sales figures. He provides no evidence to support this allegation, and there is nothing in any company data I have seen to substantiate this.”
  - c. Result: One has to wonder why if Mr. Jackson is so sure about it now that he included it in his 2003 analysis. I confirmed this several times with Brooke, however, I haven’t come across any additional data since the acquisition to definitively prove this one way or the other. **Error Unconfirmed, but Probable.**
3. Operations Cost Increases have an unexpected dip in 2011
- a. Error: The cost increases in the 2008 analysis go along at about 4% a year, with the exception of one year when they only go up 1.24%. In that year Mr. Jackson zeroed out the payments on water sharing agreements because a high capacity well was supposed to be on-line and water sharing agreements would no longer be used. Those water sharing agreements represent half of the water used in the system. The error is that Mr. Jackson does not increase the district’s electricity costs even though the amount of water that needs to be pumped from district wells doubles and that half of

Strawberry's water would now have to be pumped up the hill from Pine.

- b. Jackson Response: "Mr. Schwalm ignores the fact that due to the construction of a new well the District is forecast to cease purchasing water in 2011, a savings of approximately \$27,000 in 2011 alone. He implies that there is some sort of issue with our forecast because in 2011 operating expenses do not increase by approximately 4.0%, the same amount as prior years. When certain expenses increase by 4.0% and other expenses (i.e, water purchases) are eliminated, the net result is that total expenses will increase by less than 4.0%. This is a rather elementary point that should easily be noticed by someone who purports to be an expert in financial forecasting."
  - c. Result: One would think that an expert in rate analysis would know that electricity costs are going to increase when you pump twice as much water from district wells. In the 2009 follow-up analysis, instead of a \$27,000 dip, it is about \$9500. Clearly Mr. Jackson adjusted his thinking here to account for some increase in operations costs. **Error Confirmed.**
4. Salary and Wages are significantly understated in Operations Budget
- a. Error: The analysis used a Salary and Wages value of \$270,000 for a General Manager, a foreman, and three operators. The error identified was that the board was saying they were going to hire an operations company to run the water system, so the error was not accounting for the higher overhead costs of a contracted company. Also added an administrative assistant, for a total estimate of \$331,500.
  - b. Jackson Response: "He inflates forecast operating expenses for an "operations company" to be hired to run the acquired system. However, the District Board and General Manager have specifically stated that there are no plans to hire an operations company. The only conceivable need for such a company would be on an interim (90 day) basis while the District acquires its staff, and even this is not certain. Mr. Schwalm mistakes this potential temporary need for a permanent presence, and his five year expense projection is therefore overstated by hundreds of thousands of dollars."
  - c. Result: The district currently has a General Manager, foreman, four operators, a customer service manager, customer service representative, and two part time office positions. The operations budget prepared by Mr. Jones showed \$364,000, but it does not take into account such things as the operations staff over-time, Mr. Jones' time charges that have exceeded the budget for his position, or the two part-time workers. It is likely that the full costs will be in the neighborhood of \$446,000. The board has said that they want to convert the contract employees to staff, but even in doing

so it isn't likely that they can reduce the overall bill by a significant amount. **Error Confirmed.**

5. Strawberry and Pine Rate Tiers Merged Incorrectly
  - a. Error: The rate tiers for Pine and Strawberry overlap in their application to gallons of usage. Mr. Jackson used Pine's three rate tiers in his analysis when he should have used 4 to account for the overlap with Strawberry's rate tier.
  - b. Jackson Response: Mr. Jackson agreed that it was in error at the time.
  - c. Result: **Error Confirmed.**
6. Water Sale Percentages in the Rate Tiers Grossly Incorrect
  - a. Error: The analysis had the distribution of water sold between the rate tiers as 20%/20%/60% and for Strawberry 5%/5%/90%. Neither of them passes the make sense test. Using some assumptions about the distribution of users between weekenders, full timers and commercial users, I came up with an estimate of 65%/25%/10%.
  - b. Jackson Response: "This alleged discrepancy appears to be the result of several factors. The first is the fact that the model is attempting to graft together usage patterns and billings for Strawberry from three separate systems. Second, we believe that there may be some issues with the Strawberry volume data that has been supplied to us. A third possible reason why this is occurring is that there are a couple of very high volume customers in Strawberry's system that are skewing the averages (a school perhaps?). A fourth reason may be related to how Strawberry assesses its monthly bills."
  - c. Result: This error is driven in part by the fact that Mr. Jackson did not adjust the water totals to account for the transfers to Pine. Pine is the "high volume customer" that he cites as possibility number three. Based upon data that was provided by Brooke as part of the water system transfer, in 2007 the percentage of water sold in each of the tiers for Pine was 48%/29%/23% and for Strawberry 70%/30%. **Error Confirmed.**
7. Depreciation Should be included in Operations Budget
  - a. Error: Depreciation cost was not included as part of the operations budget in the October 2008 analysis. Mr. Jackson included depreciation costs in his 2003 rate analysis for Pine-Strawberry. Every other rate analysis and operational budget that I had seen for other water systems included depreciation. I spoke with the General Manager of Carefree Water Co. and he said that it was standard for depreciation to be included in public water company operations budgets and he provided me with his operations budget that demonstrated that.
  - b. Jackson Response: "I take issue with his claim that depreciation should be included in the analysis, which is a clear violation of the

nationally-recognized cash basis ratemaking methodology we employed for this analysis.” Mr. Haney also repeatedly denied that it was proper to include depreciation in operations budget.

- c. Result: Not sure why he clearly violated nationally-recognized methodology in his 2003 rate analysis. In the monthly statements of activity that PSWID is providing to Compass Bank, depreciation is being included in the operational expenses. **Error Confirmed.**

This email is from the group Water For Pine Strawberry. We will be sending out an email after each of the PSWID meetings with a summary of what the board did, additional facts that are relevant to what went on, and some commentary. Please forward this email to friends and neighbors that are interested in the local water issues. If you would like to be added to or removed from the list for these emails, please reply to [WaterForPineStrawberry@hotmail.com](mailto:WaterForPineStrawberry@hotmail.com). Emails on earlier meetings are available on our website: [www.WaterForPineStrawberry.com](http://www.WaterForPineStrawberry.com) .

Water For Pine Strawberry is a group of residents who are concerned about the communities water issues and how they can best be resolved. Visit our web site, [www.WaterForPineStrawberry.com](http://www.WaterForPineStrawberry.com), for more information. The website for PSWID is [www.pswid.org](http://www.pswid.org) .

Clarifications can be submitted by anyone who is explicitly named, implicitly identifiable, or a board member to items in this email. Clarifications will be posted on our website. We reserve the right to post a response. Clarifications must deal with the topics discussed in the email that relate to the individual or the board. They must be in family friendly language and be non-abusive. When the clarification is accepted, it will be posted to the website and notice of that posting will be added to the next email.