

**St. Lawrence Seaway Pilots' Association
Contract # GS-23F-0124M**

**Independent Accountant's Report on
Applying Agreed-Upon Procedures**

December 31, 2012

St. Lawrence Seaway Pilots' Association

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Independent Accountant's Report on
Applying Agreed-Upon Procedures

United States Coast Guard
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as "District 1" or the "Association") for the year ended December 31, 2012, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the St. Lawrence Seaway Pilots' Association, and is not intended to be and should not be used by anyone other than those specified parties.



Bethesda, Maryland
September 4, 2013

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results

I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the St. Lawrence Seaway Pilots' Association, as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on operating expenses. The procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on these expenses that were submitted by the pilot association and considered to be eligible for ratemaking purposes.

II. EVALUATION OF REPORTED EXPENSES

Procedure:

Obtain a listing of the expenses incurred by District 1 for the year ended December 31, 2012 and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
 - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
 - B. Federal Register final and interim rulings
 - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
 - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into group 1) general or 2) specific classes, and determine the methods of testing to be utilized.
3. Identify group one accounts to be selected for sampling.
 - A. These accounts will include:
 - i. Travel expense
 - ii. Member expenses
 - iii. Repair and maintenance expenses
 - iv. Insurance expense
 - v. Other operating expenses

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

- B. For group two accounts to be sampled, calculate planning materiality and performance materiality (PeM 75% of planning materiality) based on total submitted expenses and pilot compensation using industry guidelines.
 - i. Select all individually significant items in each group for testing. Items that are greater than 1/3 of PeM are considered individually significant.
 - ii. Using an accounting industry standard sampling form and assessing risk at high, determine remaining sample size to be selected from each group.
 - iii. Obtain supporting documentation from the Association for each transaction selected for testing.

- 4. For accounts not selected for sampling, perform the following procedures:
 - A. Pilot compensation
 - i. Review schedule provided by the District for appropriate classification
 - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2012

 - B. Depreciation expense
 - iii. Review schedule provided by the District for items that may not be eligible
 - iv. Select material fixed asset additions that are greater than 1/3 of PeM
 - v. Recalculate depreciation expense for each fixed asset addition selected for testing

 - C. Payroll (other than pilot compensation) and related expenses
 - i. Review payroll schedule provided by the District for the items that may not be eligible
 - ii. Agree to annual payroll summary register or haphazardly select 3 employees and agree to employee W-2 or other supporting documentation
 - iii. Recalculate estimated tax calculation and verify appropriate rates are being used

 - D. Legal expense
 - i. Review itemized detail for all invoices from the attorney shared by the three Districts
 - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger

 - E. Real estate taxes
 - i. Review tax bill for amount, location and tax period
 - ii. Recalculate tax expense based on taxable year

 - F. Utility expense
 - i. Review general ledger and verify there are no more than 12 monthly transactions during the year

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Summary of Agreed-Upon Procedures and Results - Continued

- ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
- G. Interest expense
- i. Obtain loan agreement or other documents that provide loan terms, including interest rate
 - ii. Recalculate interest expense based on the principal, interest rate and loan terms
- H. All other accounts not already tested
- i. Review general ledger activity and select any items that appear unusual
 - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

Results:

The "Total amount reported" column in the following table represents amounts provided by District 1 from their general ledger for the year ended December 31, 2012. The breakdown of amounts by area was provided by District 1 for information purposes only and was not subject to the procedures above. Exceptions are shown in the "Adjustments" column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 1. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

The following are the results of performing such procedures for the year ended December 31, 2012:

			District 1						Adjusted total amount reported
	Area 1	Area 2	Total amount reported	Area 1 adjustments	Area 2 adjustments	Total adjustments	Area 1 adjusted	Area 2 adjusted	
Pilot compensation									
Salaries (D1-12-01)	\$ 1,289,071	\$ 883,575	\$ 2,172,646	\$ 13,719	\$ 12,058	\$ 25,777	\$ 1,302,790	\$ 895,633	\$ 2,198,423
Employee benefits	85,445	58,841	144,286	-	-	-	85,445	58,841	144,286
Dues and subscriptions (D1-12-02)	2,400	1,800	4,200	12,762	11,218	23,980	15,162	13,018	28,180
Total pilot compensation	\$ 1,376,916	\$ 944,216	\$ 2,321,132	\$ 26,481	\$ 23,276	\$ 49,757	\$ 1,403,397	\$ 967,492	\$ 2,370,889
Operating expenses									
Other pilotage costs									
Pilot subsistence/Travel (D1-12-03)	227,199	\$ 137,315	\$ 364,514	\$ (887)	\$ (779)	\$ (1,666)	\$ 226,312	\$ 136,536	\$ 362,848
Payroll taxes (D1-12-01)	62,038	48,452	110,490	(13,719)	(12,058)	(25,777)	48,319	36,394	84,713
Other	596	549	1,145	-	-	-	596	549	1,145
Total other pilotage costs	289,833	186,316	476,149	(14,606)	(12,837)	(27,443)	275,227	173,479	448,706
Pilot boat and dispatch costs									
Pilot boat cost	108,539	95,405	203,944	-	-	-	108,539	95,405	203,944
Payroll taxes	13,429	11,804	25,233	-	-	-	13,429	11,804	25,233
Total pilot boat and dispatch costs	121,968	107,209	229,177	-	-	-	121,968	107,209	229,177
Administrative expenses									
Legal - general counsel	1,369	1,281	2,650	-	-	-	1,369	1,281	2,650
Legal - shared counsel (K&L Gates)	3,957	3,478	7,435	-	-	-	3,957	3,478	7,435
Insurance	21,907	18,998	40,905	-	-	-	21,907	18,998	40,905
Employee benefits	21,281	18,509	39,790	-	-	-	21,281	18,509	39,790
Other taxes	18,491	15,801	34,292	-	-	-	18,491	15,801	34,292
Travel	473	416	889	-	-	-	473	416	889
Depreciation/Auto leasing/Other	38,346	33,705	72,051	-	-	-	38,346	33,705	72,051
Interest	15,484	13,610	29,094	-	-	-	15,484	13,610	29,094
Dues and subscriptions (D1-12-02)	13,740	10,240	23,980	(13,740)	(10,240)	(23,980)	-	-	-
Utilities	4,549	3,897	8,446	-	-	-	4,549	3,897	8,446
Salaries	48,837	42,927	91,764	-	-	-	48,837	42,927	91,764
Accounting/Professional fees	4,683	4,317	9,000	-	-	-	4,683	4,317	9,000
Pilot training	26,353	21,961	48,314	-	-	-	26,353	21,961	48,314
Other	10,689	8,974	19,663	-	-	-	10,689	8,974	19,663
Total administrative expenses	230,159	198,114	428,273	(13,740)	(10,240)	(23,980)	216,419	187,874	404,293
Total operating expenses	\$ 641,960	\$ 491,639	\$ 1,133,599	\$ (28,346)	\$ (23,077)	\$ (51,423)	\$ 613,614	\$ 468,562	\$ 1,082,176
Total pilot compensation and operating expenses	\$ 2,018,876	\$ 1,435,855	\$ 3,454,731	\$ (1,865)	\$ 199	\$ (1,666)	\$ 2,017,011	\$ 1,436,054	\$ 3,453,065

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

III. VARIANCE ANALYSIS

Procedure:

Obtain a listing of the expenses incurred by District 1 for the years ended December 31, 2008 through December 31, 2012 and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2008 to 2012.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
 - A. Compute pilot compensation as a percentage of revenue;
 - B. Compute pilot boat expense as a percentage of revenue;
 - C. Compute health insurance per pilot;
 - D. Compute travel expense per pilot; and
 - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Conclude if any instances were identified that led us to believe 2012 expenses were overstated for ratemaking purposes.

Results:

No exceptions were noted as a result of performing such procedures.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

IV. INVESTMENT BASE CALCULATION

Procedure:

Prepare the Investment Base Calculation using information obtained from the audited financial statements of St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc., for the year ended December 31, 2012:

	Area 1	Area 2	District 1
Recognized assets			
Total current assets	\$ 532,237	\$ 467,833	\$ 1,000,070
Total current liabilities	61,808	54,329	116,137
Current notes payable	23,413	20,579	43,992
Total property and equipment (NET)	445,044	391,191	836,235
Land	11,727	10,308	22,035
Total other assets	-	-	-
Total recognized assets	927,159	814,966	1,742,125
Non-recognized assets			
Total investments and special funds	6,452	5,672	12,124
Total non-recognized assets	6,452	5,672	12,124
Total assets			
Total recognized assets	927,159	814,966	1,742,125
Total non-recognized assets	6,452	5,672	12,124
Total assets	\$ 933,611	\$ 820,638	\$ 1,754,249
Recognized sources of funds			
Total stockholders' equity	\$ 659,141	\$ 579,380	\$ 1,238,521
Long-term debt	262,785	230,986	493,771
Current notes payable	23,413	20,579	43,992
Advances from affiliated companies	-	-	-
Long-term obligations - capital leases	-	-	-
Total recognized sources	945,339	830,945	1,776,284
Non-recognized sources of funds			
Pension liability	-	-	-
Other non-current liabilities	-	-	-
Deferred federal income taxes	10,675	9,383	20,058
Other deferred credits	-	-	-
Total non-recognized sources	10,675	9,383	20,058
Total sources of funds			
Total recognized sources	945,339	830,945	1,776,284
Total non-recognized sources	10,675	9,383	20,058
Total sources of funds	\$ 956,014	\$ 840,328	\$ 1,796,342

Results:

No exceptions were noted as a result of performing such procedures.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as District 1), Lakes Pilots Association, Inc. (District 2) and Western Great Lakes Pilots Association, LLP (District 3) for the year ended December 31, 2012 and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilot Compensation, b) Other Pilotage Cost, c) Pilot Boat and Dispatch Cost and d) Administrative Expenses.
2. For each district, compare 2012 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
 - A. Pilot compensation and payroll taxes,
 - B. Travel expense/pilot subsistence,
 - C. Pilot boat and dispatch costs,
 - D. Cost associated with affiliated entities, and
 - E. Administrative expenses,
 - i. Legal, accounting and professional fees,
 - ii. Office rent, and
 - iii. Depreciation/auto leasing/other.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

Results:

The following are the results of performing such procedures for the year ended December 31, 2012:

	District 1		District 2		District 3		Total	
Total revenue	\$ 3,610,458		\$ 3,018,903		\$ 3,968,720		\$ 10,598,081	
	Adjusted amount	% of district revenue						
Pilot compensation								
Salaries	\$ 2,198,423	60.89%	\$ 1,334,438	44.20%	\$ 1,909,548	48.11%	\$ 5,442,409	51.35%
Employee benefits	144,286	4.00%	370,990	12.29%	404,866	10.20%	920,142	8.68%
Dues and subscriptions	28,180	0.78%	24,125	0.80%	33,880	0.85%	86,185	0.81%
Total pilot compensation	\$ 2,370,889	65.67%	\$ 1,729,553	57.29%	\$ 2,348,294	59.17%	\$ 6,448,736	60.85%
Operating expenses								
Other pilotage costs								
Pilot subsistence/Travel	\$ 362,848	10.05%	\$ 212,412	7.04%	\$ 357,169	9.00%	\$ 932,429	8.80%
License insurance	-	0.00%	15,420	0.51%	18,080	0.46%	33,500	0.32%
Payroll taxes	84,713	2.35%	105,546	3.50%	91,046	2.29%	281,305	2.65%
Other	1,145	0.03%	59,721	1.98%	5,867	0.15%	66,733	0.63%
Total other pilotage costs	448,706	12.41%	393,099	13.01%	472,162	11.89%	1,313,967	12.39%
Pilot boat and dispatching costs								
Pilot boat costs	203,944	5.65%	328,215	10.87%	534,566	13.47%	1,066,725	10.07%
Dispatching costs	-	0.00%	16,500	0.55%	167,261	4.21%	183,761	1.73%
Employee benefits	-	0.00%	111,812	3.70%	-	0.00%	111,812	1.06%
Payroll taxes	25,233	0.70%	18,531	0.61%	16,740	0.42%	60,504	0.57%
Total pilot boat and dispatch costs	229,177	6.35%	475,058	15.73%	718,567	18.11%	1,422,802	13.43%

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures And Results - Continued

	District 1		District 2		District 3		Total	
Administrative expenses								
Legal - general counsel	2,650	0.07%	5,136	0.17%	-	0.00%	7,786	0.07%
Legal - shared counsel (K&L Gates)	7,435	0.21%	6,759	0.22%	8,784	0.22%	22,978	0.22%
Legal - USCG litigation	-	0.00%	16,221	0.54%	-	0.00%	16,221	0.15%
Office rent	-	0.00%	65,688	2.18%	9,900	0.25%	75,588	0.71%
Insurance	40,905	1.13%	26,706	0.88%	13,203	0.33%	80,814	0.76%
Employee benefits	39,790	1.10%	41,130	1.36%	157,853	3.98%	238,773	2.25%
Payroll taxes	-	0.00%	10,359	0.34%	11,029	0.28%	21,388	0.20%
Other taxes	34,292	0.95%	31,365	1.04%	(1,674)	-0.04%	63,983	0.60%
Travel	889	0.02%	-	0.00%	-	0.00%	889	0.01%
Depreciation/Auto leasing/Other	72,051	2.00%	22,684	0.75%	35,637	0.90%	130,372	1.23%
Interest	29,094	0.81%	7,472	0.25%	5,494	0.14%	42,060	0.40%
Utilities	8,446	0.23%	34,793	1.15%	42,755	1.08%	85,994	0.81%
Salaries	91,764	2.54%	90,629	3.00%	110,210	2.78%	292,603	2.76%
Accounting/Professional fees	9,000	0.25%	29,410	0.97%	26,851	0.68%	65,261	0.62%
Pilot training	48,314	1.34%	-	0.00%	-	0.00%	48,314	0.46%
Other	19,663	0.54%	23,513	0.78%	8,204	0.21%	51,380	0.48%
Total administrative expenses	404,293	11.21%	411,865	13.63%	428,247	10.79%	1,244,405	11.74%
Total operating expenses	\$ 1,082,176	29.97%	\$ 1,280,022	42.39%	\$ 1,618,976	40.79%	\$ 3,981,174	37.57%
Total pilot compensation and operating expenses	\$ 3,453,065	95.64%	\$ 3,009,575	99.69%	\$ 3,967,270	99.96%	\$ 10,429,910	98.41%

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2012; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 13.3%, consisting of 10.4% for social security and 2.9% for Medicare, up to \$110,100. Compensation in excess of \$110,100 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at either \$250 or \$175 per day. Applicant pilots were paid at a rate of 70%, 80% or 90% of the standard pilot rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as fuel or taxi charges, are generally reimbursed at actual costs and require a receipt to be submitted. Mileage was computed using standard rates and per diem is calculated at \$44.25 per day based on submitted expense reports.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

District 3: Pilots were provided a per diem of \$59 'per available working day', or non-rest days. In addition, pilots were provided a hotel allowance of \$100 for each night's stay as documented on their expense report. Also, pilots were provided an allowance for transportation costs, such as taxi charges, for travel days as documented on their expense reports. The allowance was based on typical transportation costs incurred in each respective port area. Mileage was computed using standard rates. All other travel expenses incurred, such as fuel or tolls, were generally reimbursed at actual costs and require a receipt to be submitted.

Pilot Boat and Dispatch Costs

District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.

District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.

District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

Costs Associated with Affiliated Entities

District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.

District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.

District 3: This District did not enter into transactions with or make payments to affiliated entities.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

Administrative Expense

Legal, Accounting and Professional Fees:

District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2012, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The district also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

St. Lawrence Seaway Pilots' Association

Summary of Agreed-Upon Procedures and Results - Continued

VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

Procedure:

Recommend a list of general ledger accounts for use by each Association.

Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

St. Lawrence Seaway Pilots' Association

Summary of Findings and Recommendations

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D1-12-01

Finding Title: Payroll Taxes - Pilots

Condition:

The Association recorded excess payroll taxes for pilot compensation.

Criteria:

Federal Register, Vol. 70, No. 46, section 12091 dated March 10, 2005 allows for estimated Social Security and Medicare taxes to be recorded on behalf of the Association when these taxes are incurred by the pilots on their individual tax returns. Note: these estimates are based on taxes that would be incurred by the Association, not what the pilots incur on their own tax returns as a self-employed individual.

Effect:

Operating expenses are overstated.

Cause:

The pilots of the Association are self-employed, therefore they incur these payroll costs on their individual tax returns.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards. Estimates should be based on taxes that would be incurred by the Association and not based on individual self-employment rates.

Finding Number: D1-12-02

Finding Title: Dues and Subscriptions

Condition:

The Association incurred costs for dues and subscriptions that were classified as operating expenses.

St. Lawrence Seaway Pilots' Association

Summary of Findings and Recommendations - Continued

Criteria:

Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Pilot compensation is understated and expenses are overstated.

Cause:

The classifications of expenses in the Association's audited financial statements and trial balance are not tailored for ratemaking submission purposes.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D1-12-03

Finding Title: Travel Expenses

Condition:

Revenue was received for certain taxi expenses, therefore these specific charges are not considered necessary for ratemaking purposes.

Criteria:

Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Operating expenses are overstated.

Cause:

The Association received reimbursements for certain taxi expenses that should reduce travel expenses for purposes of this report.

St. Lawrence Seaway Pilots' Association

Summary of Findings and Recommendations - Continued

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

**Lakes Pilots Association, Inc.
Contract # GS-23F-0124M**

**Independent Accountant's Report on
Applying Agreed-Upon Procedures**

December 31, 2012

Lakes Pilots Association, Inc.

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Independent Accountant's Report on
Applying Agreed-Upon Procedures

United States Coast Guard
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the Lakes Pilots Association, Inc. (District 2 or the Association) for the year ended December 31, 2012, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the Lakes Pilots Association, Inc., and is not intended to be and should not be used by anyone other than those specified parties.



Bethesda, Maryland
September 4, 2013

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results

I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the Lakes Pilots Association, Inc., as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on operating expenses. The procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on these expenses that were submitted by the pilot association and considered to be eligible for ratemaking purposes.

II. EVALUATION OF REPORTED EXPENSES

Procedure:

Obtain a listing of the expenses submitted by District 2 for the year ended December 31, 2012 and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
 - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
 - B. Federal Register final and interim rulings
 - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
 - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into groups of 1) general or 2) specific classes, and determine the methods of testing to be utilized.
3. Identify group one accounts to be selected for sampling.
 - A. These accounts will include:
 - i. Travel expense
 - ii. Pilot boat and dispatch cost/repair and maintenance expenses
 - iii. Insurance expense
 - iv. Other operating expenses

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

- B. For group two accounts to be sampled, calculate planning materiality and performance materiality (PeM or 75% of planning materiality) based on total submitted expenses and pilot compensation using industry guidelines.
 - i. Select all individually significant items in each group for testing. Items that are greater than 1/3 of PeM are considered individually significant.
 - ii. Using an accounting industry standard sampling form and assessing risk at high, determine remaining sample size to be selected from each group.
 - iii. Obtain supporting documentation from the Association for each transaction selected for testing.

- 4. For accounts not selected for sampling, perform the following procedures:
 - A. Pilot compensation
 - i. Review schedule provided by the District for appropriate classification
 - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2012

 - B. Depreciation expense
 - i. Review schedule provided by the District for items that may not be eligible
 - ii. Select material fixed asset additions that are greater than 1/3 of PeM
 - iii. Recalculate depreciation expense for each fixed asset addition selected for testing

 - C. Payroll (other than pilot compensation) and related expenses
 - i. Review payroll schedule provided by the District for the items that may not be eligible
 - ii. Agree to annual payroll summary register or select three employees and agree to employee W-2
 - iii. Recalculate estimated tax calculation and verify appropriate rates are being used

 - D. Legal expense
 - i. Review itemized detail for all invoices from the attorney shared by the three Districts
 - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger

 - E. Real estate taxes
 - i. Review tax bill for amount, location and tax period
 - ii. Recalculate tax expense based on taxable year

 - F. Pilot subsistence
 - i. Determine that per diem does not exceed 200 days per pilot

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

- ii. Where per diem support can be obtained, haphazardly select 5 per diem transactions and agree to supporting expense reimbursement detail
- G. Utility expense
- i. Review general ledger and verify there are no more than 12 monthly transactions during the year
 - ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
- H. Rent expense
- i. Obtain signed lease agreement and recalculate the expense based on the terms of the lease
 - ii. For lease agreements with affiliated entities, CFR Part 404.5 (3) will be applied, stating that “in the absence of a comparable market, lease costs are recognized for ratemaking purposes to the extent that they conform to depreciation plus an allowance for return on investment.” In lieu of depreciation, actual annual expenses incurred in conjunction with purchase and maintenance of the land will be determined. Return on investment will be determined using the Moody’s Corporate Bond AAA index as of December 31, 2012, or 3.65%
- I. Interest expense
- i. Obtain loan agreement or other documents that provide loan terms, including interest rate
 - ii. Recalculate interest expense based on the principal, interest rate and loan terms
- J. All other accounts not already tested
- i. Review general ledger activity and select any items that appear unusual
 - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

Results:

The "Total amount reported" column in the following table represents amounts provided by District 2 from their general ledger for the year ended December 31, 2012. The breakdown of amounts by area was provided by District 2 for information purposes only and was not subject to the procedures above. Exceptions are shown in the "Adjustments" column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 2. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

The following are the results of performing such procedures for the year ended December 31, 2012:

			District 2						Adjusted total amount reported
	Area 4	Area 5	Total amount reported	Area 4 adjustments	Area 5 adjustments	Total adjustments	Area 4 adjusted	Area 5 adjusted	
Pilot compensation									
Salaries (D2-12-01)	\$ 531,793	\$ 797,689	\$ 1,329,482 *	\$ 1,982	\$ 2,974	\$ 4,956	\$ 533,775	\$ 800,663	\$ 1,334,438
Employee benefits	148,396	222,594	370,990	-	-	-	148,396	222,594	370,990
Dues and subscriptions	9,650	14,475	24,125	-	-	-	9,650	14,475	24,125
Total pilot compensation	\$ 689,839	\$ 1,034,758	\$ 1,724,597	\$ 1,982	\$ 2,974	\$ 4,956	\$ 691,821	\$ 1,037,732	\$ 1,729,553
Operating expenses									
Other pilotage costs									
Pilot subsistence/Travel (D2-12-01)	\$ 86,947	\$ 130,421	\$ 217,368	\$ (1,982)	\$ (2,974)	\$ (4,956)	\$ 84,965	\$ 127,447	\$ 212,412
License insurance	6,168	9,252	15,420	-	-	-	6,168	9,252	15,420
Payroll taxes	42,218	63,328	105,546	-	-	-	42,218	63,328	105,546
Other	23,888	35,833	59,721	-	-	-	23,888	35,833	59,721
Total other pilotage costs	159,221	238,834	398,055	(1,982)	(2,974)	(4,956)	157,239	235,860	393,099
Pilot boat and dispatch costs									
Pilot boat costs	131,285	196,930	328,215	-	-	-	131,285	196,930	328,215
Dispatch costs	6,600	9,900	16,500	-	-	-	6,600	9,900	16,500
Employee benefits (D2-12-02)	48,310	72,465	120,775	(3,585)	(5,378)	(8,963)	44,725	67,087	111,812
Payroll taxes	7,412	11,119	18,531	-	-	-	7,412	11,119	18,531
Total pilot boat and dispatch costs	193,607	290,414	484,021	(3,585)	(5,378)	(8,963)	190,022	285,036	475,058

*Includes \$40,000 of dividends that were not subject to the agreed-upon procedures in Section II

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

			District 2					Adjusted total amount reported	
	Area 4	Area 5	Total amount reported	Area 4 adjustments	Area 5 adjustments	Total adjustments	Area 4 adjusted		Area 5 adjusted
Administrative expenses									
Legal - general counsel	2,054	3,082	5,136	-	-	-	2,054	3,082	5,136
Legal - shared counsel (K&L Gates)	2,704	4,055	6,759	-	-	-	2,704	4,055	6,759
Legal - USCG litigation	6,488	9,733	16,221	-	-	-	6,488	9,733	16,221
Office rent	26,275	39,413	65,688	-	-	-	26,275	39,413	65,688
Insurance	10,682	16,024	26,706	-	-	-	10,682	16,024	26,706
Employee benefits	16,452	24,678	41,130	-	-	-	16,452	24,678	41,130
Payroll taxes	4,143	6,216	10,359	-	-	-	4,143	6,216	10,359
Other taxes	12,546	18,819	31,365	-	-	-	12,546	18,819	31,365
Depreciation/Auto leasing/Other	9,074	13,610	22,684	-	-	-	9,074	13,610	22,684
Interest	2,989	4,483	7,472	-	-	-	2,989	4,483	7,472
Utilities	13,917	20,876	34,793	-	-	-	13,917	20,876	34,793
Salaries	36,252	54,377	90,629	-	-	-	36,252	54,377	90,629
Accounting/Professional fees	11,764	17,646	29,410	-	-	-	11,764	17,646	29,410
Pilot training	-	-	-	-	-	-	-	-	-
Other	9,405	14,108	23,513	-	-	-	9,405	14,108	23,513
Total administrative expenses	<u>164,745</u>	<u>247,120</u>	<u>411,865</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>164,745</u>	<u>247,120</u>	<u>411,865</u>
Total operating expenses	<u>\$ 517,573</u>	<u>\$ 776,368</u>	<u>\$ 1,293,941</u>	<u>\$ (5,567)</u>	<u>\$ (8,352)</u>	<u>\$ (13,919)</u>	<u>\$ 512,006</u>	<u>\$ 768,016</u>	<u>\$ 1,280,022</u>
Total pilot compensation and operating expenses	<u>\$ 1,207,412</u>	<u>\$ 1,811,126</u>	<u>\$ 3,018,538</u>	<u>\$ (3,585)</u>	<u>\$ (5,378)</u>	<u>\$ (8,963)</u>	<u>\$ 1,203,827</u>	<u>\$ 1,805,748</u>	<u>\$ 3,009,575</u>

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

III. VARIANCE ANALYSIS

Procedure:

Obtain a listing of the expenses incurred by District 2 for the years ended December 31, 2008 through December 31, 2012 and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2008 to 2012.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
 - A. Compute pilot compensation as a percentage of revenue;
 - B. Compute pilot boat expense as a percentage of revenue;
 - C. Compute health insurance per pilot;
 - D. Compute travel expense per pilot; and
 - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Conclude if any instances were identified that led us to believe 2012 expenses were overstated for ratemaking purposes.

Results:

No exceptions were noted as a result of performing such procedures.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

IV. INVESTMENT BASE CALCULATION

Procedure:

Prepare the Investment Base Calculation using information obtained from the audited financial statements of Lakes Pilots Association, Inc. for the year ended December 31, 2012:

	Area 4	Area 5	District 2
Recognized assets			
Total current assets	\$ 498,456	\$ 747,683	\$ 1,246,139
Total current liabilities	494,410	741,614	1,236,024
Current notes payable	33,962	50,942	84,904
Total property and equipment (NET)	436,063	654,094	1,090,157
Land	-	-	-
Total other assets	60,418	90,627	151,045
Total recognized assets	534,488	801,733	1,336,221
Non-recognized assets			
Total investments and special funds	-	-	-
Total non-recognized assets	-	-	-
Total assets			
Total recognized assets	534,488	801,733	1,336,221
Total non-recognized assets	-	-	-
Total assets	\$ 534,488	\$ 801,733	\$ 1,336,221
Recognized sources of funds			
Total stockholders' equity	\$ 85,846	\$ 128,768	\$ 214,614
Long-term debt	414,681	622,022	1,036,703
Current notes payable	33,962	50,942	84,904
Advances from affiliated companies	-	-	-
Long-term obligations - capital leases	-	-	-
Total recognized sources	534,488	801,733	1,336,221
Non-recognized sources of funds			
Pension liability	-	-	-
Other non-current liabilities	-	-	-
Deferred federal income taxes	-	-	-
Other deferred credits	-	-	-
Total non-recognized sources	-	-	-
Total sources of funds			
Total recognized sources	534,488	801,733	1,336,221
Total non-recognized sources	-	-	-
Total sources of funds	\$ 534,488	\$ 801,733	\$ 1,336,221

Results:

No exceptions were noted as a result of performing such procedures.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as District 1), District 2 and Western Great Lakes Pilots Association, LLP (District 3) for the year ended December 31, 2012 and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilot Compensation, b) Other Pilotage Cost, c) Pilot Boat and Dispatch Cost and d) Administrative Expenses.
2. For each district, compare 2012 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
 - A. Pilot compensation and payroll taxes,
 - B. Travel expense/pilot subsistence,
 - C. Pilot boat and dispatch costs,
 - D. Cost associated with affiliated entities, and
 - E. Administrative expenses,
 - i. Legal, accounting and professional fees,
 - ii. Office rent, and
 - iii. Depreciation/auto leasing/other.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

Results:

The following are the results of performing such procedures December 31, 2012:

	District 1		District 2		District 3		Total	
Total revenue	\$ 3,610,458		\$ 3,018,903		\$ 3,968,720		\$ 10,598,081	
	Adjusted amount	% of district revenue						
Pilot compensation								
Salaries	\$ 2,198,423	60.89%	\$ 1,334,438	44.20%	\$ 1,909,548	48.11%	\$ 5,442,409	51.35%
Employee benefits	144,286	4.00%	370,990	12.29%	404,866	10.20%	920,142	8.68%
Dues and subscriptions	28,180	0.78%	24,125	0.80%	33,880	0.85%	86,185	0.81%
Total pilot compensation	\$ 2,370,889	65.67%	\$ 1,729,553	57.29%	\$ 2,348,294	59.17%	\$ 6,448,736	60.85%
Operating expenses								
Other pilotage costs								
Pilot subsistence/Travel	\$ 362,848	10.05%	\$ 212,412	7.04%	\$ 357,169	9.00%	\$ 932,429	8.80%
License insurance	-	0.00%	15,420	0.51%	18,080	0.46%	33,500	0.32%
Payroll taxes	84,713	2.35%	105,546	3.50%	91,046	2.29%	281,305	2.65%
Other	1,145	0.03%	59,721	1.98%	5,867	0.15%	66,733	0.63%
Total other pilotage costs	448,706	12.41%	393,099	13.01%	472,162	11.89%	1,313,967	12.39%
Pilot boat and dispatching costs								
Pilot boat costs	203,944	5.65%	328,215	10.87%	534,566	13.47%	1,066,725	10.07%
Dispatching costs	-	0.00%	16,500	0.55%	167,261	4.21%	183,761	1.73%
Employee benefits	-	0.00%	111,812	3.70%	-	0.00%	111,812	1.06%
Payroll taxes	25,233	0.70%	18,531	0.61%	16,740	0.42%	60,504	0.57%
Total pilot boat and dispatch costs	229,177	6.35%	475,058	15.73%	718,567	18.11%	1,422,802	13.43%

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

	District 1		District 2		District 3		Total	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
Administrative expenses								
Legal - general counsel	2,650	0.07%	5,136	0.17%	-	0.00%	7,786	0.07%
Legal - shared counsel (K&L Gates)	7,435	0.21%	6,759	0.22%	8,784	0.22%	22,978	0.22%
Legal - USCG litigation	-	0.00%	16,221	0.54%	-	0.00%	16,221	0.15%
Office rent	-	0.00%	65,688	2.18%	9,900	0.25%	75,588	0.71%
Insurance	40,905	1.13%	26,706	0.88%	13,203	0.33%	80,814	0.76%
Employee benefits	39,790	1.10%	41,130	1.36%	157,853	3.98%	238,773	2.25%
Payroll taxes	-	0.00%	10,359	0.34%	11,029	0.28%	21,388	0.20%
Other taxes	34,292	0.95%	31,365	1.04%	(1,674)	-0.04%	63,983	0.60%
Travel	889	0.02%	-	0.00%	-	0.00%	889	0.01%
Depreciation/Auto leasing/Other	72,051	2.00%	22,684	0.75%	35,637	0.90%	130,372	1.23%
Interest	29,094	0.81%	7,472	0.25%	5,494	0.14%	42,060	0.40%
Utilities	8,446	0.23%	34,793	1.15%	42,755	1.08%	85,994	0.81%
Salaries	91,764	2.54%	90,629	3.00%	110,210	2.78%	292,603	2.76%
Accounting/Professional fees	9,000	0.25%	29,410	0.97%	26,851	0.68%	65,261	0.62%
Pilot training	48,314	1.34%	-	0.00%	-	0.00%	48,314	0.46%
Other	19,663	0.54%	23,513	0.78%	8,204	0.21%	51,380	0.48%
Total administrative expenses	404,293	11.21%	411,865	13.63%	428,247	10.79%	1,244,405	11.74%
Total operating expenses	\$ 1,082,176	29.97%	\$ 1,280,022	42.39%	\$ 1,618,976	40.79%	\$ 3,981,174	37.57%
Total pilot compensation and operating expenses	\$ 3,453,065	95.64%	\$ 3,009,575	99.69%	\$ 3,967,270	99.96%	\$ 10,429,910	98.41%

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2012; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 13.3%, consisting of 10.4% for social security and 2.9% for Medicare, up to \$110,100. Compensation in excess of \$110,100 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at either \$250 or \$175 per day. Applicant pilots were paid at a rate of 70%, 80% or 90% of the standard pilot rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as fuel or taxi charges, are generally reimbursed at actual costs and require a receipt to be submitted. Mileage was computed using standard rates and per diem is calculated at \$44.25 per day based on submitted expense reports.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

District 3: Pilots were provided a per diem of \$59 'per available working day', or non-rest days. In addition, pilots were provided a hotel allowance of \$100 for each night's stay as documented on their expense report. Also, pilots were provided an allowance for transportation costs, such as taxi charges, for travel days as documented on their expense reports. The allowance was based on typical transportation costs incurred in each respective port area. Mileage was computed using standard rates. All other travel expenses incurred, such as fuel or tolls, were generally reimbursed at actual costs and require a receipt to be submitted.

Pilot Boat and Dispatch Costs

District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.

District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.

District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

Costs Associated with Affiliated Entities

District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.

District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.

District 3: This District did not enter into transactions with or make payments to affiliated entities.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

Administrative Expense

Legal, Accounting and Professional Fees:

District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2012, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The District also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

Lakes Pilots Association, Inc.

Summary of Agreed-Upon Procedures and Results - Continued

VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

Procedure:

Recommend a list of general ledger accounts for use by each Association.

Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

Lakes Pilots Association, Inc.

Summary of Findings and Recommendations

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D2-12-01

Finding Title: Pilot Subsistence/Travel

Condition:

The Association incurred travel costs for an event held by the American Pilots Association.

Criteria:

Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Pilot compensation is understated and operating expenses are overstated.

Cause:

The classifications of expenses in the Association's audited financial statements and trial balance are not tailored for ratemaking submission purposes.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D2-12-02

Finding Title: Employee Benefits

Condition:

The Association recorded and paid for cost in 2012 that will be incurred in 2013.

Criteria:

The scope of this report is that only 2012 expenses are allowable for ratemaking purposes.

Lakes Pilots Association, Inc.

Summary of Findings and Recommendations - Continued

Effect:

Operating expenses are overstated.

Cause:

Expenses to be incurred in 2013 were recorded and paid during 2012.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

**Western Great Lakes Pilots
Association, LLP
Contract # GS-23F-0124M**

**Independent Accountant's Report on
Applying Agreed-Upon Procedures**

December 31, 2012

Western Great Lakes Pilots Association, LLP

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Independent Accountant's Report on
Applying Agreed-Upon Procedures

United States Coast Guard
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the Western Great Lakes Pilots Association, LLP (District 3 or the Association) for the year ended December 31, 2012, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the Western Great Lakes Pilots Association, LLP, and is not intended to be and should not be used by anyone other than those specified parties.

CohnReznick LLP

Bethesda, Maryland
September 4, 2013

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results

I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the Western Great Lakes Pilots Association, LLP, as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on operating expenses. The procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on these expenses that were submitted by the pilot association and considered to be eligible for ratemaking purposes.

II. EVALUATION OF REPORTED EXPENSES

Procedure:

Obtain a listing of the expenses submitted by District 3 for the year ended December 31, 2012 and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
 - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
 - B. Federal Register final and interim rulings
 - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
 - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into groups of 1) general or 2) specific classes, and determine the methods of testing to be utilized.
3. Identify group one accounts to be selected for sampling.
 - A. These accounts will include:
 - i. Travel expense
 - ii. Pilot boat and dispatch cost/repair and maintenance expenses
 - iii. Insurance expense
 - iv. Other operating expenses

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

- B. For group two accounts to be sampled, calculate planning materiality and performance materiality (PeM or 75% of planning materiality) based on total submitted expenses and pilot compensation using industry guidelines.
 - i. Select all individually significant items in each group for testing. Items that are greater than 1/3 of PeM are considered individually significant.
 - ii. Using an accounting industry standard sampling form and assessing risk at high, determine remaining sample size to be selected from each group.
 - iii. Obtain supporting documentation from each Association for each transaction selected for testing.

- 4. For accounts not selected for sampling, perform the following procedures:
 - A. Pilot compensation
 - i. Review schedule provided by the District for appropriate classification
 - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2012

 - B. Depreciation expense
 - i. Review schedule provided by the District for items that may not be eligible
 - ii. Select material fixed asset additions that are greater than 1/3 of PeM
 - iii. Recalculate depreciation expense for each fixed asset addition selected for testing

 - C. Payroll (other than pilot compensation) and related expenses
 - i. Review payroll schedule provided by the District for the items that may not be eligible
 - ii. Agree to annual payroll summary register or haphazardly select three employees and agree to employee W-2
 - iii. Recalculate estimated tax calculation and verify appropriate rates are being used

 - D. Legal expense
 - i. Review itemized detail for all invoices from the attorney shared by the three Districts
 - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger

 - E. Real estate taxes
 - i. Review tax bill for amount, location and tax period
 - ii. Recalculate tax expense based on taxable year

 - F. Utility expense
 - i. Review general ledger and verify there are no more than 12 monthly transactions during the year

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

- ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
- G. Rent expense
 - i. Obtain signed lease agreement and recalculate the expense based on the terms of the lease
- H. Interest expense
 - i. Obtain loan statement and review for amount of interest expense incurred
- I. All other accounts not already tested
 - i. Review general ledger activity and select any items that appear unusual
 - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
- 5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

Results:

The "Total amount reported" column in the following table represents amounts provided by District 3 from their general ledger for the year ended December 31, 2012. The breakdown of amounts by area was provided by District 3 for information purposes only and was not subject to the procedures above. Exceptions are shown in the "Adjustments" column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 3. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

The following are the results of performing such procedures for the year ended December 31, 2012:

	District 3											
	Area 6	Area 7	Area 8	Total amount reported	Area 6 adjustments	Area 7 adjustments	Area 8 adjustments	Total adjustments	Area 6 adjusted	Area 7 adjusted	Area 8 adjusted	Adjusted total amount reported
Pilot compensation												
Salaries (D3-12-01), (D3-12-02)	\$ 978,991	\$ 419,568	\$ 599,382	\$ 1,997,941 *	\$ (43,313)	\$ (18,563)	\$ (26,517)	\$ (88,393)	\$ 935,678	\$ 401,005	\$ 572,865	\$ 1,909,548
Employee benefits	198,384	85,022	121,460	404,866	-	-	-	-	198,384	85,022	121,460	404,866
Dues and subscriptions	16,601	7,115	10,164	33,880	-	-	-	-	16,601	7,115	10,164	33,880
Total pilot compensation	\$ 1,193,976	\$ 511,705	\$ 731,006	\$ 2,436,687	\$ (43,313)	\$ (18,563)	\$ (26,517)	\$ (88,393)	\$ 1,150,663	\$ 493,142	\$ 704,489	\$ 2,348,294
Operating expenses												
Other pilotage costs												
Pilot subsistence/Travel (D3-12-02)	\$ 180,316	\$ 77,278	\$ 110,398	\$ 367,992	\$ (5,303)	\$ (2,273)	\$ (3,247)	\$ (10,823)	\$ 175,013	\$ 75,005	\$ 107,151	\$ 357,169
License insurance	8,859	3,797	5,424	18,080	-	-	-	-	8,859	3,797	5,424	18,080
Payroll taxes (D3-12-01)	-	-	-	-	44,613	19,120	27,314	91,046	44,613	19,120	27,313	91,046
Other	2,875	1,232	1,760	5,867	-	-	-	-	2,875	1,232	1,760	5,867
Total other pilotage costs	192,050	82,307	117,582	391,939	39,310	16,847	24,067	80,223	231,360	99,154	141,648	472,162
Pilot boat and dispatch costs												
Pilot boat costs	261,937	112,259	160,370	534,566	-	-	-	-	261,937	112,259	160,370	534,566
Dispatch costs	81,958	35,125	50,178	167,261	-	-	-	-	81,958	35,125	50,178	167,261
Payroll taxes	8,203	3,515	5,022	16,740	-	-	-	-	8,203	3,515	5,022	16,740
Total pilot boat and dispatch costs	352,098	150,899	215,570	718,567	-	-	-	-	352,098	150,899	215,570	718,567
Administrative expenses												
Legal - shared counsel (K&L Gates)	4,304	1,845	2,635	8,784	-	-	-	-	4,304	1,845	2,635	8,784
Office rent	4,851	2,079	2,970	9,900	-	-	-	-	4,851	2,079	2,970	9,900
Insurance	6,469	2,773	3,961	13,203	-	-	-	-	6,469	2,773	3,961	13,203
Employee benefits	77,348	33,149	47,356	157,854	-	-	-	-	77,348	33,149	47,356	157,853
Payroll taxes	5,404	2,316	3,309	11,029	-	-	-	-	5,404	2,316	3,309	11,029
Other taxes (D3-12-03)	941	403	576	1,920	(1,761)	(755)	(1,078)	(3,594)	(820)	(352)	(502)	(1,674)
Depreciation/Auto leasing/Other	17,462	7,484	10,691	35,637	-	-	-	-	17,462	7,484	10,691	35,637
Interest	2,692	1,154	1,648	5,494	-	-	-	-	2,692	1,154	1,648	5,494
Utilities	20,950	8,979	12,827	42,755	-	-	-	-	20,950	8,979	12,827	42,756
Salaries	54,003	23,144	33,063	110,210	-	-	-	-	54,003	23,144	33,063	110,210
Accounting/Professional fees	13,157	5,639	8,055	26,851	-	-	-	-	13,157	5,639	8,055	26,851
Pilot training	-	-	-	-	-	-	-	-	-	-	-	-
Other (D3-12-04)	4,657	1,996	2,851	9,504	(637)	(273)	(390)	(1,300)	4,020	1,723	2,461	8,204
Total administrative expenses	212,238	90,961	129,942	433,141	(2,398)	(1,028)	(1,468)	(4,894)	209,840	89,933	128,474	428,247
Total operating expenses	\$ 756,386	\$ 324,167	\$ 463,094	\$ 1,543,647	\$ 36,912	\$ 15,819	\$ 22,599	\$ 75,329	\$ 793,298	\$ 339,986	\$ 485,692	\$ 1,618,976
Total pilot compensation and operating expenses	\$ 1,950,362	\$ 835,872	\$ 1,194,100	\$ 3,980,334	\$ (6,401)	\$ (2,744)	\$ (3,918)	\$ (13,064)	\$ 1,943,961	\$ 833,128	\$ 1,190,181	\$ 3,967,270

* Includes \$1,053,525 of 2012 distributions that were not subject to the agreed-upon procedures in Section II

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

III. VARIANCE ANALYSIS

Procedure:

Obtain a listing of the expenses incurred by District 3 for the years ended December 31, 2008 through December 31, 2012 and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2008 to 2012.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
 - A. Compute pilot compensation as a percentage of revenue;
 - B. Compute pilot boat expense as a percentage of revenue;
 - C. Compute health insurance per pilot;
 - D. Compute travel expense per pilot; and
 - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Conclude if any instances were identified that led us to believe 2012 expenses were overstated for ratemaking purposes.

Results:

No exceptions were noted as a result of performing such procedures.

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

IV. INVESTMENT BASE CALCULATION

Procedure:

Prepare the Investment Base Calculation using information obtained from the audited financial statements of Western Great Lakes Pilots Association, LLP for the year ended December 31, 2012:

	Area 6	Area 7	Area 8	District 3
Recognized assets				
Total current assets	\$ 656,459	\$ 281,340	\$ 401,914	\$ 1,339,713
Total current liabilities	82,775	35,475	50,679	168,929
Current notes payable	7,730	3,313	4,733	15,775
Total property and equipment (NET)	19,611	8,405	12,007	40,022
Land	-	-	-	-
Total other assets	490	210	300	1,000
Total recognized assets	<u>601,515</u>	<u>257,793</u>	<u>368,275</u>	<u>1,227,581</u>
Non-recognized assets				
Total investments and special funds	-	-	-	-
Total non-recognized assets	-	-	-	-
Total assets				
Total recognized assets	601,515	257,793	368,275	1,227,581
Total non-recognized assets	-	-	-	-
Total assets	<u>\$ 601,515</u>	<u>\$ 257,793</u>	<u>\$ 368,275</u>	<u>\$ 1,227,581</u>
Recognized sources of funds				
Total stockholders' equity	\$ 586,300	\$ 251,271	\$ 358,959	\$ 1,196,530
Long-term debt	7,485	3,208	4,583	15,276
Current notes payable	7,730	3,313	4,733	15,775
Advances from affiliated companies	-	-	-	-
Long-term obligations - capital leases	-	-	-	-
Total recognized sources	<u>601,515</u>	<u>257,792</u>	<u>368,275</u>	<u>1,227,581</u>
Non-recognized sources of funds				
Pension liability	-	-	-	-
Other non-current liabilities	-	-	-	-
Deferred federal income taxes	-	-	-	-
Other deferred credits	-	-	-	-
Total non-recognized sources	-	-	-	-
Total sources of funds				
Total recognized sources	601,515	257,792	368,275	1,227,581
Total non-recognized sources	-	-	-	-
Total sources of funds	<u>\$ 601,515</u>	<u>\$ 257,792</u>	<u>\$ 368,275</u>	<u>\$ 1,227,581</u>

Results:

No exceptions were noted as a result of performing such procedures.

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as District 1), Lakes Pilots Association, Inc. (District 2) and District 3 for the year ended December 31, 2012 and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilotage Compensation (which includes pilot distributions and dividends), b) Other Pilotage Costs, c) Pilot Boat and Dispatch Costs, and d) Administrative Expenses.
2. For each District, compare 2012 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
 - A. Pilot compensation and payroll taxes,
 - B. Travel expense/pilot subsistence,
 - C. Pilot boat and dispatch costs,
 - D. Cost associated with affiliated entities, and
 - E. Administrative expenses,
 - i. Legal, accounting and professional fees,
 - ii. Office rent, and
 - iii. Depreciation/auto leasing/other.

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

Results:

The following are the results of performing such procedures for the year ended December 31, 2012:

	<u>District 1</u>		<u>District 2</u>		<u>District 3</u>		<u>Total</u>	
Total revenue	\$ 3,610,458		\$ 3,018,903		\$ 3,968,720		\$ 10,598,081	
	Adjusted amount	% of district revenue						
Pilot compensation								
Salaries	\$ 2,198,423	60.89%	\$ 1,334,438	44.20%	\$ 1,909,548	48.11%	\$ 5,442,409	51.35%
Employee benefits	144,286	4.00%	370,990	12.29%	404,866	10.20%	920,142	8.68%
Dues and subscriptions	28,180	0.78%	24,125	0.80%	33,880	0.85%	86,185	0.81%
Total pilot compensation	<u>\$ 2,370,889</u>	<u>65.67%</u>	<u>\$ 1,729,553</u>	<u>57.29%</u>	<u>\$ 2,348,294</u>	<u>59.17%</u>	<u>\$ 6,448,736</u>	<u>60.85%</u>
Operating expenses								
Other pilotage costs								
Pilot subsistence/Travel	\$ 362,848	10.05%	\$ 212,412	7.04%	\$ 357,169	9.00%	\$ 932,429	8.80%
License insurance	-	0.00%	15,420	0.51%	18,080	0.46%	33,500	0.32%
Payroll taxes	84,713	2.35%	105,546	3.50%	91,046	2.29%	281,305	2.65%
Other	1,145	0.03%	59,721	1.98%	5,867	0.15%	66,733	0.63%
Total other pilotage costs	<u>448,706</u>	<u>12.41%</u>	<u>393,099</u>	<u>13.01%</u>	<u>472,162</u>	<u>11.89%</u>	<u>1,313,967</u>	<u>12.39%</u>
Pilot boat and dispatching costs								
Pilot boat costs	203,944	5.65%	328,215	10.87%	534,566	13.47%	1,066,725	10.07%
Dispatching costs	-	0.00%	16,500	0.55%	167,261	4.21%	183,761	1.73%
Employee benefits	-	0.00%	111,812	3.70%	-	0.00%	111,812	1.06%
Payroll taxes	25,233	0.70%	18,531	0.61%	16,740	0.42%	60,504	0.57%
Total pilot boat and dispatch costs	<u>229,177</u>	<u>6.35%</u>	<u>475,058</u>	<u>15.73%</u>	<u>718,567</u>	<u>18.11%</u>	<u>1,422,802</u>	<u>13.43%</u>

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

	District 1		District 2		District 3		Total	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
Administrative expenses								
Legal - general counsel	2,650	0.07%	5,136	0.17%	-	0.00%	7,786	0.07%
Legal - shared counsel (K&L Gates)	7,435	0.21%	6,759	0.22%	8,784	0.22%	22,978	0.22%
Legal - USCG litigation	-	0.00%	16,221	0.54%	-	0.00%	16,221	0.15%
Office rent	-	0.00%	65,688	2.18%	9,900	0.25%	75,588	0.71%
Insurance	40,905	1.13%	26,706	0.88%	13,203	0.33%	80,814	0.76%
Employee benefits	39,790	1.10%	41,130	1.36%	157,853	3.98%	238,773	2.25%
Payroll taxes	-	0.00%	10,359	0.34%	11,029	0.28%	21,388	0.20%
Other taxes	34,292	0.95%	31,365	1.04%	(1,674)	-0.04%	63,983	0.60%
Travel	889	0.02%	-	0.00%	-	0.00%	889	0.01%
Depreciation/Auto leasing/Other	72,051	2.00%	22,684	0.75%	35,637	0.90%	130,372	1.23%
Interest	29,094	0.81%	7,472	0.25%	5,494	0.14%	42,060	0.40%
Utilities	8,446	0.23%	34,793	1.15%	42,755	1.08%	85,994	0.81%
Salaries	91,764	2.54%	90,629	3.00%	110,210	2.78%	292,603	2.76%
Accounting/Professional fees	9,000	0.25%	29,410	0.97%	26,851	0.68%	65,261	0.62%
Pilot training	48,314	1.34%	-	0.00%	-	0.00%	48,314	0.46%
Other	19,663	0.54%	23,513	0.78%	8,204	0.21%	51,380	0.48%
Total administrative expenses	404,293	11.21%	411,865	13.63%	428,247	10.79%	1,244,405	11.74%
Total operating expenses	\$ 1,082,176	29.97%	\$ 1,280,022	42.39%	\$ 1,618,976	40.79%	\$ 3,981,174	37.57%
Total pilot compensation and operating expenses	\$ 3,453,065	95.64%	\$ 3,009,575	99.69%	\$ 3,967,270	99.96%	\$ 10,429,910	98.41%

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2012; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 13.3%, consisting of 10.4% for social security and 2.9% for Medicare, up to \$110,100. Compensation in excess of \$110,100 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at either \$250 or \$175 per day. Applicant pilots were paid at a rate of 70%, 80% or 90% of the standard pilot rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as fuel or taxi charges, are generally reimbursed at actual costs and require a receipt to be submitted. Mileage was computed using standard rates and per diem is calculated at \$44.25 per day based on submitted expense reports.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

Western Great Lakes Pilots Association, LLP

Summary of Agreed-Upon Procedures and Results - Continued

District 3: Pilots were provided a per diem of \$59 'per available working day', or non-rest days. In addition, pilots were provided a hotel allowance of \$100 for each night's stay as documented on their expense report. Also, pilots were provided an allowance for transportation costs, such as taxi charges, for travel days as documented on their expense reports. The allowance was based on typical transportation costs incurred in each respective port area. Mileage was computed using standard rates. All other travel expenses incurred, such as fuel or tolls, were generally reimbursed at actual costs and require a receipt to be submitted.

Pilot Boat and Dispatch Costs

District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.

District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.

District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

Costs Associated with Affiliated Entities

District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.

District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.

District 3: This District did not enter into transactions with or make payments to affiliated entities.

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Summary of Agreed-Upon Procedures and Results - Continued

Administrative Expense

Legal, Accounting and Professional Fees:

District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2012, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The District also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

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Summary of Agreed-Upon Procedures and Results - Continued

VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

Procedure:

Recommend a list of general ledger accounts for use by each Association.

Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

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Summary of Findings and Recommendations

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D3-12-01

Finding Title: Payroll Taxes - Pilots

Condition:

The Association did not incur payroll taxes for pilot compensation as the pilots are responsible for these on their individual tax returns.

Criteria:

Federal Register, Vol. 70, No. 46, section 12091 dated March 10, 2005 allows for estimated Social Security and Medicare taxes to be recorded on behalf of the Association when these taxes are incurred by the pilots on their individual tax returns.

Effect:

Operating expenses are understated.

Cause:

The pilots of the Association are self-employed, therefore they incur these payroll costs on their individual tax returns.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D3-12-02

Finding Title: Pilot Subsistence/Travel

Condition:

The Association recorded costs in 2012 that were incurred in 2011 and incurred travel costs for an event held by the American Pilots Association.

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Summary of Findings and Recommendations - Continued

Criteria:

The scope of this report is that only 2012 expenses are allowable for ratemaking purposes. Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Pilot compensation is understated and operating expenses are overstated.

Cause:

Expenses incurred in 2011 were recorded during 2012. The classifications of expenses in the Association's audited financial statements and trial balance are not tailored for ratemaking submission purposes.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D3-12-03

Finding Title: Other Taxes

Condition:

The Association did not have appropriate documentation to support some costs.

Criteria:

Regulation 46 CFR 404.5(a)(8)(i) states that undocumented expenses are not recognized as reasonable for ratemaking purposes.

Effect:

Operating expenses are overstated.

Cause:

All costs must be documented and demonstrated that they are necessary and reasonable in order to be reimbursable.

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Summary of Findings and Recommendations - Continued

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D3-12-04

Finding Title: Other expense

Condition:

The Association incurred costs associated with political contributions.

Criteria:

Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Operating expenses are overstated.

Cause:

The classifications of expenses in the Association's audited financial statements and trial balance are not tailored for ratemaking submission purposes.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.