



**DISTRICT OF COLUMBIA
WATER AND SEWER AUTHORITY**

BOARD OF DIRECTORS

Finance & Budget Committee

Friday, December 19, 2008

8:30 AM.

MEETING MINUTES

COMMITTEE MEMBER

Dan Tangherlini

WASA STAFF

Jerry Johnson, General Manager
Olu Adebó, Acting Chief Financial Officer
Yvette Downs, Director Budget & Finance
Avis Russell, General Counsel
Linda Manley, Board Secretary

OTHER BOARD MEMBERS IN ATTENDANCE

David J. Bardin
Joseph Cotruvo
Paivi Spoon

Presenters

Ms. Faye Boatright, Executive Director Morgan Stanley (Lead Underwriters)
Mr. Richard Weis, Executive Director Morgan Stanley (Lead Underwriters)

Call to Order

Committee Chairman Daniel M. Tangherlini called the meeting to order at 8.35 a.m. The Chairman asked Ms. Yvette Downs, Director, Finance & Budget, to provide highlights from the November FY 2008 Financial Report and to focus on high level issues or changes from the last month.

November 2008 Financial Report

The November 2008 report notes that operating revenues totaled \$62.5 million; operating expenditures were at \$52.2 million and capital disbursements totaled \$53.0 million. The actual average daily balance for the 180—day Operating Reserve was \$122.2 million, or \$3.6 million over the Board-approved FY 2008 reserve requirement of \$118.6 million. Ms. Downs reported that there were no major changes and invited questions relating to the November financial report. No questions or issues were raised by the Committee members.

Bond Financing Update

Mr. Olu Adebo, Chief Financial Officer, reported that management and the new Chairman met with the three rating agencies in December. Mr. Adebo reported that he found the rating agencies receptive to DC WASA's discussion on the rating upgrade and schedule. Management anticipates issuance of approximately \$300 million in bond financing toward the latter part of January 2009. Mr. Johnson informed the Committee that two of the rating agencies committed to sending their responses before the end of next week, with the third response shortly after.

In response to Chairman Tangherlini's inquiry about an update on the status of the bond market, Mr. Johnson invited Ms. Faye Boatright, and Mr. Richard Weiss, from Morgan Stanley & Co., WASA's lead underwriters, to provide the Committee with an update on the bond market. Ms. Boatright reported that highly rated essential credits such as water and sewer credits have been performing well in the market, while lower-rated credits have not fared as well.

In response to a question by Mr. Bardin concerning recent water and sewer pricings. Ms. Boatright distributed to the Committee a Municipal Market Update presentation provided by Morgan Stanley, which highlighted the following recent and successful bond issuances:

- New York City Municipal Water Finance Authority bond issuance of about \$325.6 million with a yield of 6.125% over 30 years, and
- The State of Wisconsin's Clean Water Revenue bond issuance of \$92.2 million with a yield of 5.27% yield over 20 years.

She stated that highly rated essential issuers like DC WASA have had access to the market at fairly favorable rates.

Mr. Johnson reported that during the week, management did two roll-overs of its commercial paper in \$10 million tranches at interest rates of 0.65% and 0.73% through January 2009 compared to 2.15% in October 2008. Chairman Tangherlini requested an update of the bond issuance and market conditions at the January 2009 Board meeting in order to have everyone's view on the matter.

Review of Revised FY 2009 and Proposed FY 2010 Budgets

Mr. Johnson provided an overview of the budget process including the calendar, and a summary of the revised and proposed budget requests, which are the same level as the original presentation.

Operating budget request

- Revised FY 2009 operating budget is at the same level of the approved \$363.2 million, however there are reallocations between various line items.
- Proposed FY 2010 operating budget totals \$393.6 million, and increase of \$30.4 million above the Revised FY 2009 operating budget
- Proposed FY 2010 retail Water and Sewer rate increase of 10.0 percent

- Proposed FY 2010 monthly Impervious Area Charge (IAC) adjustment to \$2.20 per ERU (Assumes IAC implementation in April 2009 of \$1.24 per ERU monthly)
- Proposed FY 2010 PILOT fee increase of 10.3 percent and ROW fee of 7.7 percent

Capital budget request

- Lifetime budget totals \$6.4 billion
- FY 08 – 2017 Capital Disbursement budget totals \$3.2 billion
- Capital Authority request totals \$773.3 million

Chairman Tangherlini asked General Manager Johnson for clarification on the steps needed to be taken by the various Board committees on the budget proposals in the event that the proposal is recommended by the Finance and Budget Committee but not by the Retail Rates Committee given the proposed FY 2010 Water and Sewer rate increase of 10%. Mr. Johnson responded that appropriate adjustments would have to be made or agreement obtained from the Finance and Budget Committee. Mr. Johnson further explained that the budget action that will be requested at the January 2009 Board meeting will not serve as an approval for the rates but rather Board authorization for the General Manager to advertise the rates and proceed with the public rates proposal participation process. The FY 2010 water and sewer rates will not be approved until the August/September 2009 timeframe.

In response to Chairman's Tangherlini's comment on different scenarios for lower percentage rate increases, depending on the outcome of the public hearings, Mr. Johnson advised that since water and sewer rates are primarily driven by capital projects, the Authority would have to look at its capital program over the next few years for reduction in anticipated disbursements. Additional discussion focused on the digester project, which is estimated at a lifetime cost of approximately \$400 million inclusive of \$100 million increase in the capital budget proposal. Chairman Tangherlini asked for the debt service cost associated with the digester project in FY 2010. Mr. Adebo responded that associated debt service costs totaled \$438,000 with 0.2% rate impact in FY 2010. Mr. Adebo explained that based on the operating cost savings from the various elements of the Digester project, by FY 2014, management expects operating cost savings at Blue Plains which has been included in the 10-year financial plan. The Digester project is project to have positive financial returns as well as positive biosolids management impacts and environmental benefits.

Mr. Adebo also stated that the major driver for the water and sewer rate increases in the 10 year projection is the Total Nitrogen capital project, a regulatory requirement, with a lifetime cost of over \$900 million for which no payback period has been identified. Mr. Bardin added that the Environmental Protection Agency (EPA) has yet to provide the Environmental Quality and Operations Committee with the benefits associated with the Total Nitrogen project. Mr. Bardin continued with a discussion about the possibility of a stimulus package or other assistance from the United States Congress or determining if EPA needs the project to be completed as quickly as originally anticipated. Chairman Tangherlini's asked about the debt service cost associated with the TN project, to which Mr. Adebo responded that the debt service cost associated with the TN project for the District's share in FY 2010 is \$650,000. Mr. Adebo explained that the suburban jurisdictions raise their share of the Total Nitrogen project cost separately. Mr. Johnson added that

Virginia, through the State Legislature, had set aside some funds to assist with the upgrade of facilities involved in total nitrogen removal and Maryland implemented the 'flush tax' which has been set up to assist the ratepayers but there are no such outside funding sources available in the District.

Mr. Bardin requested for an explanation of the cost drivers of the increase of \$14.0 million (or 16.7%) in debt service between the revised FY 2009 and proposed FY 2010. Chairman Tangherlini expanded the request asking that the debt service cost associated with each capital project be provided in order to determine which projects can be further delayed or pushed back depending on prioritization. Mr. Johnson noted that 50% of the capital projects are driven by regulatory issues with permit timeframes and adverse associated penalties for default.

Mr. Johnson reminded the Committee that due to major disinvestment in the utility operations incurred by the District as the operator in years prior to the establishment of DC WASA, there are some infrastructures in bad shape. In addition to the projects included in the proposed capital budget, there are over \$1.0 billion of identifiable deficiencies in the system that need to be addressed and are neither currently funded nor programmed in the \$6.4 billion lifetime budget request currently before the Board for consideration.

Chairman Tangherlini inquired about the increase in personnel service costs between revised FY 2009 and proposed FY 2010 budgets and if management is considering elimination of pay increases or freezing pay. Mr. Johnson stated that the increase includes the union contract increases, increased insurance costs and merit pay increases. He also noted that the majority of employees are covered by a labor agreement which extends through FY 2011. In that agreement annual pay increases are locked in at 3.8% for FY 2010 and 4% for FY 2011. The non-union employees are merit-based with no step increases. The budget for merit increases assumes an average of 5% for all employees who receive merit-based pay.

Mr. Bardin asked about the increasing PILOT budget for FY 2010, given the Board's request to freeze payment at the FY 2007 level pending the receipt of the independent report from the Office of the District Chief Financial Officer (DC CFO). Mr. Johnson responded that since it is an anticipated expense, there is the need to ensure it is duly budgeted for at the rate of spending required by the agreement in anticipation that payment will eventually be remitted at some agreed upon amount.

The Committee consensus was to forward management's budget proposal to the Board for action. Chairman Tangherlini requested that management explore two alternative operating budget scenarios of an overall operating budget (inclusive of debt service) of \$386 million and \$378 million for FY 2010 and provide the resultant increase for water and sewer rates and the impact on the capital program.

Other Business

Hearing no further business, Chairman Tangherlini adjourned the meeting at 9.35 a.m.