DISTRICT OF COLUMBIA
BOARD OF DIRECTORS

Audit Committee

Thursday, February 24, 2005
8:30 a.m.

BOARD MEMBER/S PRESENT	**WASA STAFF PRESENT**
Glenn S. Gerstell, Chairman	Jerry N. Johnson, General Manager
Anthony Griffin	Michael Hunter, Internal Auditor Director
David Lake	Linda Manley, Board Secretary

I. Call to Order

Mr. Gerstell called the meeting to order at approximately 9:10 a.m.

II. External Auditor's Presentation

On behalf of TCBA, Mr. Al Lucas expressed satisfaction with their working relationship with the Authority. He noted that the Authority's environment is one of continuous improvement, despite starting out at a very high standard. He also noted that the Authority has taken TCBA's management letter comments very seriously and have incorporated them into the organizations accomplishments. Mr. Lucas noted that the organization had overcome some serious accounting concerns as a result of the lead issue and has remained fiscally strong. He noted that the Authority is a financially healthy organization and that he believes that this is testimony to the operations and the staff.

TCBA's audit is related to the issuance of an opinion on the organization's financial statements. The Authority is responsible for preparing and providing these statements for review by the external auditors. The consultant team for this engagement included Kevin Bernard, Engagement Manager, Ralph Brazillio, Technical Advisory, and Barbara Hudlow, Quality Assurance.

Mr. Kevin Bernard stated that an unqualified opinion is the highest level of opinion that can be received. He noted that there were no qualifications or exceptions in the report.

Mr. Bernard also reported that the OMB A-133 audit has not been issued, but the fieldwork has been completed and the report is expected to be issued soon with no material weaknesses to report. Mr. Bernard noted that the Management Discussion & Analysis (MD&A) has been reviewed for consistency with the financial statements and that they found the statistical section and the introduction to be consistent with the financial statements. No significant accounting pronouncements were implemented in FY'04. Mr. Bernard noted that GASB 40, which was implemented in early 2003, was the last major implementation and that there were no new implementations this year.

Mr. Bernard reported that the residential, commercial, and multi-family revenues were up 7.6% - this is consistent with the rate increases and the effect for the one-time meter replacement program. The operating margin declined slightly (to 13.4% from 15.6%) due to a $9.7M non-recurring charges related to the lead program. Net assets increased by $28.7M despite total non-recurring charges of $15.9M. Mr. Bernard stated that the Board mandated that cash reserves equivalent to 180 days of operating and maintenance costs be placed on reserve (this would total $94.6M). That figure was exceeded by $53.6M. Mr. Bernard noted the following significant adjustments/non-recurring charges: 1.) The Lead Program ($9.7M); 2.) $3.8M write-off of receivables accrued to the Washington Aqueduct McMillan Plant and; 3.) The $2.4M write-off of interest accrued on the WSSC allocation of the A.S. McGaughan settlement. Mr. Bernard also noted that the environmental remediation accrual was a significant transaction that affected the composition of the Authority's balance sheet. The Authority issued $295M of variable rate option bonds consistent with the CIP funding program.

Two comments regarding the management letter related to recommendations for improvement of an internal control issue. Mr. Bernard noted that inadequate communication between Customer Service and the Finance Department in handling special billing procedures for Federal accounts resulted in the late payment of an account related to the McMillan plant. Management discovered this mistake during the reconciliation. However, TCBA recommended that communication between the two departments be strengthened so that errors are quickly identified and resolved. TCBA also recommended that the CIS system be upgraded to enable the Authority to improve in its reporting of cash collections and the allocation of cash collections. This would allow the CIS system to be used more efficiently and would allow management to focus on analyzing the data.

Six of the seven comments from the previous year have been resolved. Resolution of the last comment involves matching purchase orders and contracts. Although this comment has been open for a couple of years, management expects it to be resolved with the upgrade of the CIS system, which should take place over the next few months.

Mr. Bernard noted that it is TCBA's responsibility to express an opinion on the financial statements. TCBA provides reasonable, but not absolute assurance of detecting material misstatements. TCBA had to gain an understanding of the internal control policies and procedures in order to design effective and efficient audits and was required to review internal controls.
Mr. Bernard noted that no material illegal acts were identified during the audit.

Mr. Bernard noted that management undertakes material judgments and accounting estimates in the following areas: allowance for potentially uncollectible accounts, contingencies, and depreciation and obsolescence. The comprehensive annual report has been reviewed for consistency with the audited financial statements; the information is consistent. Mr. Bernard noted that TCBA is required to inform the Board of consultations with other accountants, whether discussions were held with TCBA prior to their being selected as the external auditors and any other matters of which the Board should be apprised. There were no disagreements between TCBA and Management regarding accounting and reporting. Mr. Bernard noted that TCBA was not aware of any consultations with other auditors and no major issues discussed as a condition of TCBA's retention.

III. Executive Session

This discussion included TCBA staff and the Committee members only for approximately half an hour.

IV. Review of Internal Audit Office Activities

1st Quarter FY2004 Audit Activity

Michael Hunter noted that the Internal Auditor's Office has conducted four exit conferences since the October 28, 2004 Audit Committee meeting. As with all engagements, audit observations were discussed and opportunities for improvement were presented. Two audit reports have been finalized and three are in draft status. The Internal Auditor's Office is currently conducting 5 audits. He also noted that the Internal Auditor's Office is fully staffed and has contract support for 500 hours for this fiscal year. As of the end of the calendar year, 300 hours had been used leaving 200 hours of contract hours available. To date, the Internal Auditor's Office has obtained no CPE credits, however, these requirements will be met by the end of the fiscal year. The Internal Auditor's Office continues to focus on the Board's strategic goals for 2003-2005 and has tried to map its audit processes to those Board initiatives. Mr. Hunter invited the members to review at their convenience, Attachment B, which includes a summary of the Internal Auditor's Office reports and projects for the 1st Qtr of FY'05.

Process Improvement

Mr. Hunter reported that his department continues to have its clients assess the internal audit functions through the client satisfaction survey, which allows the clients to provide feedback and evaluate the services rendered. In addition, his department continues to increase the awareness of the Internal Audit functions and that he has provided documentation of the Internal Auditor Office operations as well as offer guidance on how the Internal Auditor Office fits into the business process of the Authority. The Internal Auditor Office decreased its contracting hours from 3000 to 500 over the last few years. In doing so, the Internal Auditor Office has completed more assignments in-house, minimizing the use of contractors and thereby, reducing cost. The Internal Auditor Office continues to meet with various departments as a means of making management aware of the range of services that can be provided.

Mr. Hunter provided an explanation of the Internal Auditor Office's utilization of the audit plan hours. He recapped the 4 positions to show what resources are available for contracting, audit projects and initiatives. He noted that 4,100 office hours are allotted for audit projects. Based on research performed on other utility organizations, the Institute of Internal Auditors, and National Association of Local Government Auditors, the Internal Auditor Office's hours are consistent with other best practices groups. The total level of effort for auditors is 5,570 hours, of which 4,100 are dedicated to audit engagements.

V. Audit Committee Training – Status Updates

Mr. Griffin addressed the suggested timeframe for audit committee training. Mr. Hunter noted that last year, the Internal Auditor's Office attempted to secure training for the full Board and selected members of Management. However, the training was postponed indefinitely, pending the selection of the new Board members. Mr. Hunter noted that an organization and a facilitator had been selected to provide the training, and a curriculum had been established. He also noted that the facilitator had provided a self-assessment to be completed by the Audit Committee members so that the training could be specifically tailored to address the needs of the organization. Mr. Gerstell asked that Mr. Hunter continue to hold the training pending the appointments.

VI. Other Business

No other business discussed

VII. Adjournment

The meeting was adjourned at approximately 10:00 a.m.