



DISTRICT OF COLUMBIA WATER AND SEWER AUTHORITY

BOARD OF DIRECTORS

Finance and Budget Committee
Thursday, October 23, 2008

9:00 a.m.

MEETING MINUTES

COMMITTEE MEMBERS

Daniel M. Tangherlini, Acting Chairman
Timothy L. Firestine
Paivi Spoon

WASA STAFF

Jerry Johnson, General Manager
Olu Adebo, Acting Chief Financial Officer
Yvette Downs, Director Finance and Budget
Avis Russell, General Counsel
Linda R. Manley, Board Secretary
Bob Hunt, Treasury Manager

Presenters

Ms. Demoor, WASA's Financial Advisor

Call to Order

The Acting Chairman, Mr. Daniel M. Tangherlini called the meeting to order at 9:00 a.m.

September 2008 Financial Report

Ms. Yvette Downs, Director of Finance and Budget reported that DC WASA met its key financial objectives for fiscal year 2008. At the end of September, revenues (cash receipt basis) totaled \$346.3 million or 102.3 percent of budget. Operating expenditures (expenditure basis) totaled \$322.7 million or 94.7 percent of budget, and Capital Disbursements totaled \$303.4 million or 93.7 percent of budget. Ms. Downs also noted that the average daily balance of the 180-day operating reserve was \$128 million at year end, or \$9.5 million above the reserve requirement.

Ms. Downs highlighted the following: Residential, Commercial and Multi-Family receipts exceeded budget by approximately \$3.3 million due to collection of some past due balances and associated fees. Federal receipts were on budget. Together, the District Government and DC Housing Authority revenues were on budget. Metering Fee receipts were 4 percent over budget which may be attributable to the replacement of some 5/8" meters with 1" meters along with services for new developments. Wholesale receipts exceeded budget due to adjustments to the Potomac Interceptor rates in early FY 2008. Other Revenue was also slightly higher than budget, and DC WASA ended the fiscal year with PILOT/ROW at 97 percent of budget.

Next, Ms. Downs reviewed FY 2008 operating expenditures (including Debt Service, Right of Way and Payment In-Lieu of Taxes). Year-to-date spending is at 94.7 percent. Ms. Downs reported

that personnel services were at 94 percent of budget due to higher than budgeted vacancy rates; Contractual services were at 85 percent of budget due reflecting both the timing differences in product and service delivery and invoicing by vendors. Spending for legal services during the year was also lower than anticipated. Water purchases spending exceeded budget by approximately 9 percent due to chemical and other operating costs at the Washington Aqueduct. Chemicals and supplies are also over budget by about 14 percent due to increases in chemical costs (primarily methanol and certain polymers). Utilities, driven by higher electricity costs, exceeded budget by approximately 3 percent. Debt service is under due to the quick reaction of Treasury Office on auction market rate and debt refinancing. Payment in-lieu of taxes expenditure was on budget on a GAAP basis at the end of September. Consistent with the Board's directive, payment of the Payment In-Lieu of Taxes has been remitted at the FY 2007 level. Right of way fees were on budget, and fourth quarter payments were remitted in August 2008. Other operating highlights included accounts payable and accounts receivable year-to-date status and the quarterly grants report. Mr. Adebo reported that the numbers presented were projections and are subject to change when actual invoices are received

Acting Chairman Tangherlini asked for an explanation for the difference between the FY 2007 Payment In-Lieu of Taxes and what was accrued. Ms. Downs replied that the amount was in the area of \$600 – \$700 thousand. He also inquired if DC WASA was concerned with the electricity lock-in rates due to reduction in recent market conditions. Ms. Downs expressed no concern and stated that staff will continue to follow the lock-in strategy, as previously presented to the Committee, which has proven effective to date.

Mr. Firestine inquired about the status of DC WASA's investments, particularly retirement programs given current financial market conditions. In response, the Acting Chief Financial Officer, Olu Adebo, introduced the Treasury Manager, Mr. Robert Hunt who gave a presentation on DC WASA's finances including debt services, investment portfolio, and cash balances. Mr. Hunt stated that there has been some recent positive movement in the bond market and that he continues to closely monitor the situation. Mr. Firestine continued by inquiring whether the Treasury Manager was comfortable with some of DC WASA's investments, particularly Dexia Bank and American Beacon. Mr. Hunt answered in the affirmative and went on to explain that American Beacon was not exposed to the sub-prime mortgage issue and that they were relatively sound.

Continuing with the monthly financial report, Ms. Downs presented highlights of capital disbursements for FY 2008. Ms Downs informed the committee that year-to-date capital disbursements were at 94% of budget and that the largest yearly spending categories were wastewater, the Washington Aqueduct (primarily due to disbursements for the residuals building), and the water service area (mostly in the area of lead service line replacements and pumping facilities). In response to an inquiry from Acting Chairman Tangherlini, Ms. Downs affirmed that the spike in disbursement, as depicted in the graph on page seven of the report, reflects a transfer to the Washington Aqueduct for the residuals building.

Mr. Firestine asked for additional information on the reasons that overtime was 30% over budget. Mr. Adebo explained that this negative variance was primarily driven by escalation in fire hydrant activities in the department of Water Services, vacancies in the department of Wastewater Services, and other activities in the departments of wastewater and maintenance services. He further went on to inform the committee that the recent successful completion of a training program in Wastewater Services will hopefully help alleviate overtime usage in FY 2009. Additionally, the FY 2009 revised overtime budget proposal has been reviewed and revised to reflect present wage rates and other factors. Mr. Firestine further went on to inquire if overtime was monitored by employee and how overtime hours were allocated. The General Manager, Mr. Jerry Johnson,

responded that there was built-in overtime in some work schedules and other overtime assignments allocated by terms in union contracts. Mr. Johnson also informed the committee that because of constant monitoring, overtime has been kept low compared to the earlier years of the Authority and reduced as a percentage of personnel costs. Mr. Adebo added that the budget department sends out monthly overtime management reports that provide the necessary tools to help directors manage overtime cost, and that he follows up with meetings if there is a potential for negative variance. Mr. Tangherlini requested that a column showing overtime as a percentage of regular payroll be included in the overtime report. He also requested to see some of the overtime management reports.

Revised FY 2009 & Proposed FY 2010 Budget Transmittal

Mr. Johnson presented highlights of the Revised FY 2009 and Proposed FY 2010 budgets. In his opening statements he reminded the Committee that the budget document reflected management's plan of undertaking the Board's objectives in the ensuing financial year and beyond. He informed the Committee that the budget season had been a challenging one due to the present national and global economic situation and cost pressures. Mr. Johnson presented a revised FY 2009 operating budget of \$363.2 million and a FY 2010 budget of \$393.6 million. He informed the Committee that to support the FY 2010 budget, management has proposed a 10% increase in water and sewer rates, a monthly impervious surface area rate of \$2.20, 10.3% increase in Payment In Lieu of Taxes (PILOT) rate, and a 7.7% increase in Right of Way fees.

The lifetime capital budget totals \$6.4 billion, the 10 year capital disbursements, FY 2008 – 2018 total \$3.2 billion, and authority requests for the period total \$773 million. Mr. Johnson went on to highlight the major changes in personnel and non-personnel services in the proposed revised FY 2009 budget compared to the approved FY 2009 budget, and in the proposed FY 2010 budget compared to the FY 2009 revised budget stating that debt service and chemicals were the major drivers. In response to a question, Mr. Adebo clarified why ROW remained at \$5.1 million when earlier in the presentation it was said that the fee would increase by 7.7%. The increase is required for a variety of collections reasons, including projected consumption decreases, however the total expenditure remains unchanged. Mr. Adebo promised to provide a worksheet explaining the scenario. There were also discussions on the increase in contractual services compared to the approved budget. Ms Downs provided some clarifications and informed the Committee that some of the increase had to do with the reallocation of the Lead Abatement line into the contractual services line item along with some anticipated increases in contractual requirements on behalf of the DC Department of Environment MS4 stormwater activities. Ms. Spoon requested that management provide a pie chart from other jurisdictions' demonstrating their distribution of operating expenses as compared to DC WASA. Mr. Johnson agreed to provide that by the next meeting.

Mr. Johnson continued the presentation with highlights on the Capital Improvement Program (CIP) and changes in major program areas, including the digester project and the inclusion of several high priority water and sewer projects identified by recent consultant recommendations. Also, the federally mandated Blue Plains Total Nitrogen Project and the Long Term Control Plan continue to be major expenditure areas of the 10-year CIP at approximately \$1.6 billion out of the total \$3.2 billion planned disbursements. Staff responded to questions relating to cost drivers, revenues, retail rates, and fees in relation to the CIP. Discussions continued with sources of funding of the Long Term Control Plan, stormwater fees, and the digester project. Discussions on the digester project involved revenue opportunities for Renewable Energy Credits (RECs), generation of clean energy, and environmental benefits. Mr. Johnson highlighted the importance of staffing and financing needs drawing attention to the fact that in other jurisdictions some of the financing needs are subsidized by the state unlike DC where the ratepayer carries the entire burden. Mr. Johnson

concluded his presentation with a review of the budget calendar, and informed members of the Committee to channel all questions relating to the budget request to the Board Secretary, Ms. Linda Manley who will direct the questions to staff.

Update on banking services and bond underwriters

Mr. Adebo provided an update on banking services and advised that although Wachovia had been proposed to be selected for a new banking services contract, based on significant changes in the financial market since the RFP was issued, staff was recommending extending the current banking contract for a period of nine months, and re-issuing the RFP at a later date. He also noted that staff will ask Board to withdraw its pending action on the banking services fact sheet. After some more discussion the consensus was that a banking services provider would be selected between May and June of 2009, and if more time was needed, management should advise the Committee.

Mr. Adebo advised the Committee that management plans to use Morgan Stanley as the Senior Book runner (Underwriter) on its 2009 bond issuance. Both J. P. Morgan and Siebert, Brandford and Shank will co manage the deal. Mr. Adebo further stated that by having all three bankers on the deal, it ensures that if any one of the three became incapable or unable to perform by the time of the issuance, somebody else can step in. Also the choice of Morgan Stanley as the senior would augment DC WASA's rating upgrade plan, because of the team proposed by the firm.. In response to questions from Mr. Tangherlini and Mr. Firestine, Mr. Adebo stated that the strategy would not have an impact on the cost of issuance; merely on the allocation of the liability between the three underwriters.

Action Item:

Recommendation for renewal of contract for payroll service

The Committee indicated that this item would be recommended to the Board.

Recommendation of lease of office space at 810 First Street, NE

After some discussions and recommendations the Committee indicated that this item would be recommended to the Board. Acting Chairman Tangherlini requested that staff follow up with his office on the proposed lease rate.

Other Business:

Update on DC PILOT cost of service study

Although DC WASA has been notified that the cost of service study has been completed and is now under review by DC Chief Financial Officer's staff, no significant update has been received from the DC CFO's office since last month's report.

Financial Market Update

Mr. Hunt and the financial advisers gave an update on the status of DC WASA's banking service and bond underwriters. Mr. Hunt started by informing the committee that the bond-working group met once and DC WASA was on track to issue \$300 million of fixed rate bonds in January 2009. Mr. Tangherlini inquired if January 2009 was a reasonable date in light of current market volatility. Ms. Karen Demoors of PFM responded and informed the Committee that the municipal market was moving in a positive direction but was not in a position to say if the trend would hold through January 2009. Mr. Firestine inquired if the deals in the municipal market this week were primarily retail driven, to which Ms. Demoors replied in the affirmative indicating that the market was volatile and would build confidence when institutional investors return. Mr. Tangherlini further inquired if

there was a pressing operational need driving the January 2009 date or was there flexibility. Mr. Hunt indicated that the cash would be needed. Mr. Adebo also added that January or February was fine in order to accommodate vendor payments. Mr. Firestine inquired whom the liquidity facilitator was for the outstanding commercial paper issuance and if there were any issues with them in relation to present market conditions. Ms. Demoors responded that West LB was the facilitator and that they were recently downgraded after the German guarantee was removed from them in 2005. However, she stated that DC WASA was grandfathered into the prior credit rating. Mr. Firestine inquired of the status of the taxable commercial paper. He was informed that the taxable commercial paper is still outstanding. The discussion followed with Mr. Tangherlini inquiring whether the new federal treasury backing covered the taxable commercial paper. Mr. Adebo replied that he would check with the General Counsel and get back to him. Mr. Tangherlini continued by saying that since the January date of issue was formulated before the present state of the market it would be prudent to explore alternate plans and defer some spending while observing how the market levels out. Mr. Johnson informed the Committee that he was currently weighing several options in that regard.

Adjournment

The meeting was adjourned at 11:15 AM