



**DISTRICT OF COLUMBIA
WATER AND SEWER AUTHORITY**

BOARD OF DIRECTORS

*Joint Meeting of the
Finance & Budget
and Audit Committees*

Thursday, February 23, 2006

9:00 a.m.

MEETING MINUTES

BOARD MEMBERS

Glenn Gerstell
Paul E. Folkers
Anthony Griffin
Beverly Warfield

WASA STAFF

Jerry Johnson, General Manager
Olu Adebo, Acting Chief Financial Officer
Leonard Benson, Director
Engineering & Technical Services
Webster Barnes, Office of the Counsel
Linda Manley, Secretary to the Board

Paul Folkers called the meeting to order at 9:10 a.m.

Financial Overview

Olu Adebo, Acting Chief Financial Officer, referenced the detailed financial report provided to the Committee prior to the meeting. Mr. Adebo reported that at the end of January, with 33 percent of the fiscal year complete, financial performance is on track with budget. Revenues continue to exceed budget; operating expenditures are slightly below budget and capital disbursements are slightly below original projections. The operating reserve balance at the end of January totaled \$117.5 million, and is \$15.1 million in excess of the Board's policy requirement.

With the Committees' consent, Mr. Adebo continued with a report by exception and asked Board members to raise any questions or concerns pertaining to the written report.

Operating Expenditures

As discussed in previous reports to the Finance and Budget Committee, Mr. Adebo highlighted results and projections for chemicals and utilities, where we continue to experience spending pressures.

Utilities

Mr. Adebo reported that year-to-date utilities expenditures are at 30 percent of budget with 25 percent of the fiscal year completed. The key cost driver in this area is substantially higher than projected electricity costs.

Daily spot electric prices continue to exceed budget. Prices have averaged \$55/KWH and \$56/KWH in January and February, respectively, compared to a high of \$82/MWH in December. These average spot prices still exceed the budgeted amount for FY 2006. Staff continues to confer with our utility rate consultants and monitor futures pricing on a weekly basis, which continues to decline in recent weeks. However, Mr. Adebo noted that if prices continue for all of FY 2006 at the current highs experienced since the beginning of the fiscal year, we would exceed the revised budget.

Mr. Folkers asked whether staff have locked in any portion of our supply. Mr. Adebo responded that staff have not locked in any portion of the supply at this point. Based on available analysis at this point, actual prices have been historically less than the future pricing. As a result, staff is continuing to monitor the markets and finish the model to develop the ultimate scenario to decide the best pricing to lock in..

Mr. Folkers asked about personnel services expenditures, which are slightly ahead of budget at approximately 34 percent noting that in the past expenditures, have lagged due to vacant positions. Mr. Adebo explained that expenditures in the personnel services category were not straightlined and reflect disbursements for fringe benefits and health insurance. Staff expect that personnel services at year-end will remain within budget. Mr. Folkers asked about the current vacancy level. Mr. Adebo reported that there were 926 filled positions at the end of January; approximately 200 positions are currently vacant.

Chemicals and Supplies

In the chemicals and supplies category year-to-date expenditures total 33 percent of the budget with 33 percent of the year completed. Mr. Adebo reported that chemical prices are higher than anticipated, which could exceed the revised budget.

With the exception of the utilities and chemicals and supplies categories all remaining budget categories remain on track and we project that we will end the year within budget.

Capital Expenditures

Next, Mr. Adebo continued with a report on disbursement for the capital program. Mr. Adebo reported that first quarter capital disbursements totaled \$43.1 million, and year-to-date capital spending through January totaled \$58.4 million, or 24 percent of the revised disbursements annual budget.

Mr. Adebo reported that the Department of Engineering and Technical Services (DETS) has completed its first-quarter capital program review. As a result of their review, DETS has revised its capital program projections downward from \$239 to \$229 million. Management discussed their report with the Environmental Quality and Operations Committee at their meeting held in February.

Mr. Benson provided the Committees with a summary report of first quarter 2006 progresses and highlighted challenges associated with the egg digesters facility. WASA held a bid opening for the digester project on February 13, which resulted in no bids. Three contractors expressed interest

but were unable to procure a surety bond for the job, not because of the capabilities strength of the contractor but rather it dealt with the conditions of the bond. Mr. Benson explained that WASA's General Counsel is working with the surety to determine how WASA might resolve this issue. Mr. Johnson reported that staff is also exploring alternative project delivery methods in an effort to identify changes that may enable WASA and the contractor to resolve any surety bond issues.

Cost of Service Study

General Manager Johnson reported that last month staff began working with our rate consultants on a cost of service study, which will review and analyze the entire rate structure. The Authority's goal is to collect revenue based on fair and equitable rates and more specifically to design rate structures reasonably based on costs of rendering services. As previously discussed with the Committee, considerable work will go into reviewing the Stormwater and Combined Sewer Overflow rate structures. Mr. Johnson reported concerning his testimony last evening before the Council of the District of Columbia Committee on Public Works and the Environment. During the hearing, Mr. Johnson testified concerning the Stormwater rate approach, and the Council seemed receptive to WASA's strategy in this regard. Staff will continue to update the Committee as this study proceeds.

Mr. Johnson reported that several staff will visit Colorado to review the Denver impervious surface-based rate structure. WASA will consider the Denver rate structure model for possible implementation. WASA has already compiled much of the GIS data that would be necessary to support an impervious-based rate structure similar to Denver's.

Mr. Adebo reported that a more detailed update will be provided at the next meeting of the Retail Rates Committee.

Executive Session with WASA's External Auditors

Mr. Johnson introduced Mr. Albert Lucas, the engagement auditor and Mr. Ralph Bazilio, a partner Thompson, Cobb, and Bazilio & Associates (TCBA). Chairman Gerstell held an executive session to enable the TCBA to provide an independent briefing on WASA's FY 2005 audit results and management letter.

At the conclusion of the executive session, which lasted approximately 40 minutes, Chairman Gerstell reconvened the meeting and noted that the Committees are pleased that the Authority continues to receive clean audit opinions.

Mr. Johnson noted that around the region, there were concerns about credit card usages and associated controls. TCBA reviewed regional credit card usage where there are concerns, and reported favorably on their comparative review of WASA's credit card program.

FY 2005 Management Letter Comment

Olu Adebo reported that staff received the final management letter comments. The auditors noted two comments concerning the Intermunicipal Agreement and WASA's relationship with the Washington Suburban Sanitation Commission (WSSC).

First the auditor's commented that WASA is behind in sending out the operating settlement for FY 2004. Mr. Adebo reported that staff will complete the operating settlements for FY 2004 and 2005 in March.

The second audit comment concerns disputed delinquent WSSC receivables that total in excess of \$30 million. The auditors strongly expressed the need for both parties to resolve this matter before serious material financial implications result.

Grants Audit Results

The A-133 grants audit results was forwarded to the Board prior to the meeting. Mr. Adebo continued with a report concerning the status of WASA's A-133 grants audit. TCBA has completed the grant audit, which is crucial management of WASA's grants. This annual audit provides reasonable assurance that there was no area of noncompliance that could have a direct and material effect on a major federal program. The auditors issued a clean opinion, with no questioned costs or management letter comments on WASA's processes.

Annual Audit Contract Extension

Mr. Adebo asked the Committees to consider extension of the annual audit contract with TCBA authorized by the Board in May 2005. The contract includes one base year and three option years. This extension will exercise the first option year of the contract. While the amount for the audit contract is below the Board's review threshold, based on the Board's expression of interest we submit this request for Board review and consideration.

Chairman Gerstell asked how many years TCBA would serve in total if the Board grants the requested extension. Mr. Adebo responded that TCBA would serve for six years. Mr. Johnson explained that last year WASA's internal auditor, Michael Hunter, explored whether or not there should be limitations to the number of years that an audit firm provides service to the Authority. Mr. Hunter determined that current industry standard is to change the managing partner as opposed to changing the firm that provides the service. Staff followed Mr. Hunter's recommended action and changed the managing partner for the TCBA audit team in FY 2005.

Mr. Gerstell asked what criteria served as the basis for selecting the current audit firm. Mr. Adebo responded that WASA received seven proposals in response to our request for proposals from qualified firms on the GSA schedule. A selection committee, consisting of the CFO, Internal Auditor and Controller, evaluated the proposals and interviewed the top three firms. Management recommended the selection of TCBA for the external auditor work because the firm submitted the best proposal at the lowest bid. The Joint Finance and Budget and Audit Committees endorsed exercising option year one of the TCBA contract and the full Board will review this request at its March 2006 meeting.

WSSC Delinquent Accounts Receivable

Chairman Gerstell asked for an update on staff discussions with WSSC on their more than \$30 million delinquent accounts receivable since last month's meeting. Mr. Johnson responded that in light of statements from WASA's external auditors, and the serious financial implications to WASA, Mr. Adebo is scheduled to meet with WSSC's CFO, Tom Traber, on Monday, February 27 to try to continue our efforts to resolve the outstanding receivables issue.

Chairman Gerstell expressed concern that the matter has not been resolved more expeditiously and asked what steps staff had taken since last month to resolve the matter. Mr. Johnson reported that in addition to phone calls placed by himself and Mr. Adebo he has also held three meetings with WSSC representatives. In follow up to issues raised, staff researched issues raised during the meetings and followed up with phone calls to discuss issues raised. Mr. Griffin suggested that Chairman Gerstell arrange a meeting with WSSC's Board Chairman and appropriate representatives to further escalate the discussion. Mr. Gerstell agreed to contact WSSC's Board

Chairman and asked Mr. Johnson to follow up with WSSC representatives to try to arrange a meeting before February 27. This will provide staff with an opportunity to make one final attempt to stress the strong sense of urgency and to resolve this matter. This is essential although WASA did not receive any material audit findings; the most urgent audit issue raised is WSSC's unresolved debt, which WASA has carried since FY 2002.

Hearing no further business, Mr. Gerstell adjourned the meeting at 10:24 a.m.