

DISTRICT OF COLUMBIA WATER AND SEWER AUTHORITY

Board of Directors

*Joint Meeting of the Audit and
Finance and Budget Committee*

Thursday, February 27, 2014

10:30 a.m.

1. **Call to Order**Bradford Seamon, Co-Chairperson and
Robert Mallett, Co-Chairperson
2. **FY 2013 Financial Statements (Attachment 1)** Mark Kim
3. **External Auditor’s Report (Attachment 2)** KPMG
4. **Questions**
5. **Adjournment**Bradford Seamon, Co- Chairperson and Robert Mallett, Co-Chairperson



DC Water FY 2013 Financial Statement Audit

Exit Conference
February 27, 2014



Agenda

- Introductions
- Financial Statement Audit Results
 - Opinion on the Basic Financial Statements
 - Report on Internal Control over Financial Reporting (ICOFR) and on Compliance
- Auditors' Required Communications
- Restatement of FY 2012 and FY 2011 Financial Statements
- Significant Deficiencies in ICOFR
- Open Discussions/Questions

This is intended solely for the information and use of the Board of Directors and Management of the District of Columbia Water and Sewer Authority, and is not intended to be and should not be used by anyone other than these specified parties.

Financial Statement Audit Results

- Opinion on the Basic Financial Statements
 - Unmodified or “clean” opinion

- Report on Internal Control over Financial Reporting
 - No Material Weaknesses Identified
 - Significant Deficiencies Identified

- Report on Compliance with Laws, Regulations, Contracts and Grants
 - No instances of non-compliance noted

- Management Letter
 - Control deficiencies noted

Auditors' Required Communications

Responsibilities Under Auditing Standards Generally Accepted in the United States of America

- Conduct our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* which provide reasonable – not absolute – assurance about whether the basic financial statements are free of material misstatement, whether caused by error or fraud.

Scope of Independent Audit

- No significant changes to planned audit scope

Other Information in Documents Containing Audited Financial Statements

- Management's Discussion and Analysis (RSI)
- Introductory and Statistical Sections (CAFR Only)

- No matters came to our attention that cause us to believe such information is materially inconsistent with the basic financial statements
- Our responsibility relating to other information in documents containing the basic financial statements upon which we report:
 - Applied limited procedures, which consisted principally of inquiries of management
 - We did not audit this information and, accordingly, we express no opinion on it.

Auditors' Required Communications (continued)

Significant Accounting Policies

- Described in Note 2 of the basic financial statements
- DC Water - No longer reported as part of District reporting entity
- Implemented several new accounting standards that did not have a material impact on DC Water's financial statements in FY 2013

Significant Audit Differences and Adjustments

- Significant **corrected** audit adjustments/reclassifications to the basic financial statements and related notes for FY 2013 and FY 2012:
 - Components of Net Position
 - Unrecorded liabilities (FY 2013 only)
 - Reporting of Current Portion of Restrict Cash and Investments
 - Reporting of PILOT and ROW Fees
 - Gross vs. Net Reporting of Short-Term Debt Activity
 - Reporting of Accumulated Interest on Federal Appropriations
 - Reporting of Current and Long-term Components of Certain Liabilities
 - More Significant Changes to Note Disclosures:
 - Cash and Investments
 - Capital Assets /Purchased Capacity
 - Compensated Absences
 - Short-term Debt (Gross vs. Net)
 - audit ROCIP IBNR Liability Roll-Forward
- Uncorrected** differences noted for FY 2013:
- ROCIP Liability Calculation
 - IMA Operating Revenues Accrual
 - Retiree Health Savings Plan

Auditors' Required Communications (continued)

Quality of Accounting Principles

- We discussed quality of accounting principles as well as acceptability with management
 - Purchased Capacity (Washington Aqueduct)
 - IMA Wholesale Agreement Capital Contributions
 - Component unit status with District
 - Useful lives of capital assets

(as well as items requiring correction from prior slide)
- Accounting principles have been consistently applied
- Corrected basic financial statements and footnotes demonstrate clarity and completeness

Management Judgments and Accounting Estimates

- **Actuarial Self-Insurance Liabilities (Risk Management and ROCIP)**
- **Useful Lives of Capital Assets**

- We evaluated the key factors and assumptions used to develop these estimates and determined that the estimates are reasonable in relation to the DC Water basic financial statements taken as a whole

Significant and Unusual Transactions

- None identified

Auditors' Required Communications, continued

Major Issues Discussed with Management Prior to Retention

■ None

Disagreements with Management on Financial Accounting and Reporting Matters

■ None

Difficulties Encountered with Management in Performing the Audit

■ None

Consultation with Other Accountants

■ None that we are aware of relating to audit matters

Independence

■ We are independent with respect to the Authority

Restatement of FY 2012 and 2011 Financial Statements

- DC Water has historically issued comparative financial statements and desired to continue to do so in FY 2013
- FY 2012 financial statements required correction and were audited by another auditor
- KPMG could have taken responsibility for performing the audit of the corrections in the FY 2012 financial statements, but this would have required KPMG to do substantially more work than it would take the prior auditor if they would be willing to do so
- The prior auditor was willing to take responsibility for corrections in reissued FY 2012 and FY 2011 financial statements
- KPMG/Prior Auditor/DC Water management worked together to make necessary corrections in FY 2012 and FY 2011 financial statements
- Benefits to DC Water:
 - No reference to correction of errors in FY 2013 KPMG audit report or financial statements
 - No impact on GFOA Certificate of Achievement for Excellence in Financial Reporting for FY 2012 and FY 2011 financial statements
 - DC Water has corrected comparative financial statements for fiscal years 2013, 2012 and 2011 that all have unmodified opinions for use in subsequent bond official statements

Corrections of Errors Leading to Restatement

- Calculations of the Components of Net Position
- Reporting of Current Portion of Restricted Cash and Investments Associated with Current Liabilities
- Reporting of PILOT and ROW Fees as Operating vs. Non-operating
- Gross vs. Net Reporting of Short-Term Debt Activity
- Reporting of Current and Long-term Components of Certain Liabilities
- Reporting of Accumulated Interest on Federal Appropriations

Significant Deficiencies in Internal Control Over Financial Reporting

Significant Deficiencies in Internal Control Over Financial Reporting

2013-01

Improve Internal Controls over Financial Reporting

- Formal documentation of all significant accounting policies and procedures and GAAP compliance
- Provide additional technical training
- Improve management reviews

2013-02

Improve Year-End Accounts Payable and ROCIP Accrual Processes and Controls

- Improve year-end accounts payable accrual process and related controls
- Engage an actuary to estimate the ROCIP liability at fiscal year-end as is currently the practice related to the Authority's other self-insurance liabilities

2013-03

Improve Process for Estimating IMA Year-End Operating Cost Adjustments

- Establish methodology for greater precision in estimates
- Perform "look-back" analysis to continuously refine methodology

2013-04

Improve Design and Execution of Management Review Controls

- Unbilled accounts receivable analysis
- Legal representation letters
- Accounts payable accruals
- Draft financial statements
- Purchase orders
- Net position computations

2013-05

Improve General Information Technology Controls

- Access to programs and data
- Program changes
- Computer operations

Open Discussion/ Questions

Appendix

Categories for Reporting Control Findings

- **Material Weakness** is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.
- **Significant Deficiency** is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
- **Control Deficiency** exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.

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- Contact information
 - Jeff Steinhoff, Executive Director (jsteinhoff@kpmg.com)
 - Website: www.kpmginstitutes.com/government-institute/

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PRESENTATION TO JOINT AUDIT AND FINANCE & BUDGET COMMITTEES FY2013 FINANCIAL STATEMENTS

February 27, 2014





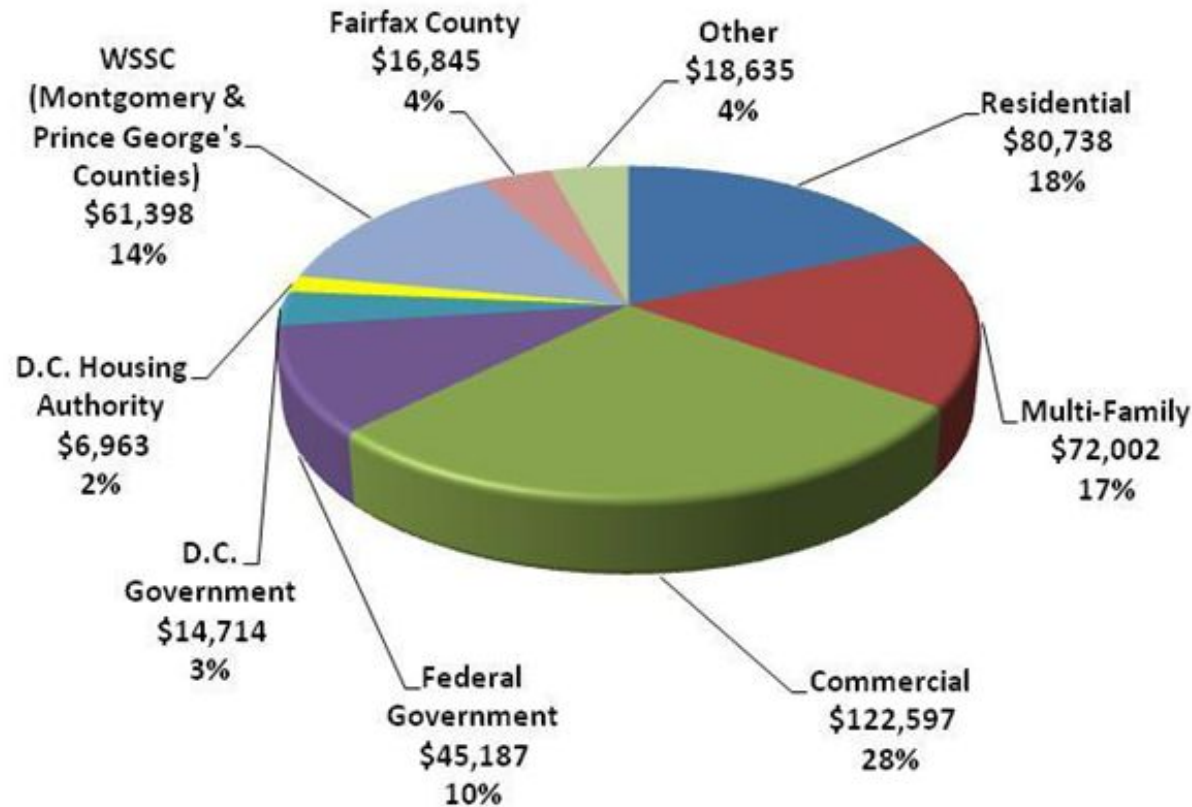
FY2013 Financial Overview

- The Authority's balance sheet remains strong and is growing
 - Total net position of \$1.2 billion (increase of \$81.9 million or 7.1%)
- Despite a challenging environment, the Authority posted financial results from operations generally in line with expectations and consistent with historical performance
 - Operating revenues decreased by \$1.5 million (0.3%) to \$439.1 million
 - Operating expenses increased by \$10.9 million (3.2%) to \$353.9 million
 - Total cash at fiscal-year end of \$277.5 million (vs. \$270.0 million in FY12)
 - Total long-term debt increased to \$2.1 billion (15.3% increase)
- The Authority maintained its credit ratings of Aa2/AA+/AA with a stable outlook from all three major rating agencies
 - Issued \$300 million of bonds in July 2013 to finance the Authority's \$3.8 billion capital improvement program



FY2013 Operating Revenues

- The Authority's operating revenues remain well diversified and stable





FY2013 Operating Revenues

- The Authority’s operating revenues decreased by \$1.5 million (or 0.3%) to \$439.1 million

| | FY 2013 | FY 2012 |
|--|-------------------|-------------------|
| Residential, commercial and multi-family customers | \$ 275,337 | \$ 256,846 |
| Federal government | 45,187 | 48,381 |
| District government and D.C. Housing Authority | 21,677 | 24,713 |
| Charges for wholesale wastewater treatment | 87,178 | 94,549 |
| Other | 9,700 | 16,077 |
| Total Operating Revenues | \$ 439,079 | \$ 440,566 |

- The reduction in revenue was due primarily to one-time adjustments and consumption declines greater than forecast



FY2013 Operating Expenses

- The Authority’s operating expenses increased by 3.2% (or \$10.9 million) to \$353.9 million

| | <u>FY 2013</u> | <u>FY 2012</u> |
|---|--------------------------|--------------------------|
| Personnel services | \$ 103,908 | \$ 97,784 |
| Contractual services | 68,417 | 64,939 |
| Chemicals, supplies and small equipment | 28,987 | 28,815 |
| Utilities and rent | 26,098 | 26,786 |
| Depreciation and amortization | 77,330 | 74,342 |
| Water purchases | 27,223 | 28,389 |
| Payment in lieu of taxes and right of way fee | 21,982 | 21,982 |
| Total Operating Expenses | <u>\$ 353,945</u> | <u>\$ 343,037</u> |

- Personnel and contractual services remain the primary drivers of the increase in operating expenses



Net Capital Assets

- The Authority’s net capital assets, including construction in progress and less depreciation, increased by \$574.5 million (or 15.5%) to \$4.3 billion

| | Fiscal Year | | |
|----------------------------------|---------------------|---------------------|---------------------|
| | 2013 | 2012 | 2011 |
| Wastewater treatment plant | \$ 1,945,920 | \$ 1,924,985 | \$ 1,839,010 |
| Wastewater collection facilities | 730,622 | 716,651 | 689,575 |
| Water distribution system | 920,150 | 897,077 | 863,474 |
| Purchased capacity | 326,290 | 319,840 | 307,593 |
| Capital equipment | 178,620 | 167,641 | 155,770 |
| Construction in progress | 1,381,652 | 807,430 | 485,497 |
| Less accumulated depreciation | (1,190,489) | (1,115,381) | (1,041,573) |
| Net capital assets | \$ 4,292,765 | \$ 3,718,243 | \$ 3,299,346 |



Change in Net Position

- The Authority’s net position increased by \$81.9 million (or 7.1%) to \$1.2 billion

| | Fiscal Year | | |
|---|---------------------------|---------------------------|---------------------------|
| | 2013 | 2012 | 2011 |
| Operating revenues | \$ 439,079 | \$ 440,566 | \$ 408,255 |
| Operating expenses | 353,945 | 343,037 | 341,273 |
| Net non-operating revenues (expenses) | <u>(61,555)</u> | <u>(71,146)</u> | <u>(69,585)</u> |
| Change in net position before Federal capital contributions | 23,579 | 26,383 | (2,603) |
| Contributions of capital from Federal government | <u>58,310</u> | <u>58,957</u> | <u>47,374</u> |
| Change in net position | 81,889 | 85,340 | 44,771 |
| Total net position - beginning of year | <u>1,145,489</u> | <u>1,060,149</u> | <u>1,015,378</u> |
| Total net position - end of year | <u>\$1,227,378</u> | <u>\$1,145,489</u> | <u>\$1,060,149</u> |



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