



DISTRICT OF COLUMBIA WATER AND SEWER AUTHORITY

Board of Directors

Finance and Budget Committee

Thursday, June 27, 2013

11:00 a.m.

MEETING MINUTES

Committee Members in Attendance

Timothy L. Firestine, Committee Chairperson
James Patteson, Fairfax County
Adam Ortiz, Prince George's County
Bradford Seamon, Prince George's County
Alethia Nancoo, District of Columbia

DC Water Staff

George Hawkins, General Manager
Mark Kim, Chief Financial Officer
Gail Alexander-Reeves, Acting Director
Finance & Budget
Randy Hayman, General Counsel
Robert Hunt, Treasury and Debt Manager
Suzette Stona, Senior Financial Analyst
Linda Manley, Secretary to the Board

Other Presenters & Guests

Daniel Hartman, Public Financial Management (PFM)

Call to Order

Chairperson Timothy Firestine called the meeting to order at 11:00 a.m.

May 2013 Financial Report

Ms. Gail Alexander-Reeves, Acting Finance and Budget Director, reported that DC Water's financial performance remained strong with approximately 67 percent of the fiscal year completed. Ms. Reeves noted that in May, Mr. Mark Kim, Chief Financial Officer, reviewed the FY 2013 Year-End Projections in detail with the Committee, and that those assumptions remain unchanged.

Through the end of May 2013:

- revenues totaled \$311.7 million or 70 percent of the revised budget;
- operating expenditures were \$250.9 million or 57 percent of the budget; and
- Capital spending totaled \$340.1 million or 53 percent of budget.

Also last month, Mr. David McLaughlin, Director of Engineering & Technical Services, provided the Committee with a detailed review of the CIP and reported that although there had been delays in non-critical activities within the CIP, all critical path activities remain on track and on schedule for completion per the original baseline schedule.

Mr. Firestine asked for an explanation regarding the St. Elizabeth's account and basis for the reconciliation provided in Attachment 8 to this month's financial report. Ms. Suzette Stona, Senior Financial Analyst, explained that DC Municipal Government had disputed consumption on one account.

From October 2012 through September 2013, consumption for the account was estimated with a balance of \$4.1 million. The settlement resulted in two one-time adjustments of \$2.3 million and \$0.5 million. Going forward, there will be a revised estimate for revenue from the DC Government.

Mr. Robert Hunt, Treasury and Debt Manager, reviewed the 120-day Operating Reserve Analysis. For May, DC Water had an average daily operating reserve balance of \$172.4 million relative to the operating reserve objective of \$125.5 million. Included in the \$172.4 million balance is the DC PILOT reserve fund of \$14.5 million. On a daily basis year-to-date, there is approximately \$30 million dollars excess in the reserve. Total cash balances (including bond construction funds) were \$381.0 million on the last day of May.

Mr. Firestine asked about the balance of bond construction funds as of June 27, 2013 to which Mr. Hunt reported approximately \$22 million withdrawn in June and an additional \$10 million anticipated withdrawals.

Mr. Hunt then reviewed the monthly investment report with the Committee. The portfolio remains properly diversified in accordance with the Investment Policy. The overall yield-to-cost for May is 0.38%, consistent with the previous months. Mr. Hunt reviewed purchases for the month of May and year-to-date for June.

Revised FY 2014 Budget Proposal

Prior to presenting a revised FY 2014 budget proposal, Mr. Kim reviewed the FY 2013 projected cash surplus of \$40.3 million with the following recommendations for the Committee's action:

1. Increase the refund due to wholesale customers by \$3.9 million, resulting in a total refund amount of \$9.7 million;
2. Transfer \$7.9 million to the DC PILOT Reserve Fund, resulting in a balance of \$22.4 million;
3. Increase contribution to Rate Stabilization Fund by \$3.4 million, resulting in a balance of \$28.9 million;
4. Increase contribution to PAYGO by \$10 million, for a total contribution this year of \$34.5 million; and
5. Maintain working capital of \$16 million above the O&M Reserve required.

In response to Mr. Firestine's inquiry, Mr. Kim provided further explanation regarding the basis of each recommended action. Mr. Kim explained that DC Water does not have an established target allocation to PAYGO but that the Authority intends to recommend a Board-adopted policy in the Fall of 2013, concurrent with the FY 2015 budget proposal.

In presenting the Revised FY 2014 Budget, Mr. Hawkins briefed the Committee on the strategic basis for revising the FY 2014 budget. DC Water had performed a bottom-up review of operational funding needs and sought to establish a tighter budget as an operational target with working capital to meet emergency needs. In concert with the lower operating budget proposal, Mr. Hawkins noted the strategic decision to reduce IAC (Impervious Area Charge) rates as opposed to water and sewer rates.

Mr. James Patteson inquired if it would be more judicious to maintain IAC rates, despite lower capital spending in the current year, amid uncertainty of future capital spending. Mr. Hawkins affirmed that DC Water has sufficient funding coverage in the event of unexpected expenditures for the Long-Term Control Plan. Mr. Kim and Mr. Firestine concurred on adequate flexibility for unanticipated needs.

Mr. Kim further explained that in order to maintain an AA credit rating, DC Water's target debt service coverage needs to be 1.5 times the debt service of \$130.0 or \$50 million in excess revenues. A total of \$25 million is included in the variance between revenues and operating expenditures while the additional \$25.0 million is attributed to operating savings. Excess revenues would provide the flexibility needed to meet unanticipated expenditures. In response to Ms. Alethia Nancoo's inquiry regarding the rating agencies receptivity of the planned approach, Mr. Kim confirmed that the Revised FY 2014 Budget proposal was reviewed with the rating agencies and well received.

Ms. Nancoo and Mr. Firestine jointly summarized that revenues, with the exception of wholesale revenues, remain unchanged, while total O&M is lower and meets coverage requirements.

Mr. Firestine inquired on the impact of the proposed tighter budgeting approach on the development of FY 2015 budgets while ensuring the Authority obtains adequate Congressional authorization. Mr. Kim discussed establishing an appropriated fund for PAYGO in the FY 2015 budget proposal. Mr. Firestine reminded Mr. Kim that PAYGO is not expenditure and has not historically been approved by Congress as such. Mr. Kim noted that in previous years, the amount has been embedded in budget surpluses for individual line items and explained that the plan for DC Water was to provide more transparency by appropriately categorizing those expenditures in the budget.

In support of Mr. Kim's acknowledgement of Ms. Reeves for her extensive work in examining the budget for reductions, Ms. Nancoo applauded the DC Water Finance & Budget team for the effort in reducing and allocating conservatively, where appropriate.

Mr. Kim summarized the Revised FY 2014 operating budget proposal of \$441.7 million, revised revenue budget of \$467.2 million, and unchanged capital disbursement budget of \$620.2 million. CFO Kim highlighted the major areas of operational risk and asserted that the Revised FY 2014 Budget adequately manages those risks. Mr. Firestine re-emphasized his concern with instituting a PAYGO policy prior to approving a FY 2015 budget. Mr. Kim reassured the committee that the intention is to establish an appropriately conservative approved budget and set rates based on the revised FY 2015 budget.

With no further questions, the Committee recommended the Revised FY 2014 Budget Proposal and management's recommendation for the use of the FY 2013 excess cash surplus to the full Board for approval.

Bond Financing Update

Mr. Kim briefed the Committee on the upcoming bond financing, which is scheduled for a mid-July pricing. DC Water received certification from the DC Auditor on revenue sufficiency. In addition, the rating agencies affirmed the Authority's credit ratings with a stable outlook and all bond documents are ready for the Committee's approval. However, since there have been recent and significant changes in the bond market, management is advising the Board accordingly.

Mr. Daniel Hartman, Public Financial Management, reported on the recent fluctuations of the bond market. Despite the current volatility of the bond market, DC Water's current strategy to lock in favorable rates is still the appropriate strategy. In response to Ms. Nancoo's inquiry, Mr. Hartman confirmed the scheduled date for DC Water's bond pricing is July 23rd but that there is flexibility to price as soon as early July in order to capture opportunities in the market.

Mr. Kim asserted that the only potential changes to the bond documents would be timing or structure, which could potentially be accelerated or delayed. One structural change could be to take a portion of the fixed rate debt and to convert it to floating debt. DC Water would take the appropriate actions with the Committee and the full Board in the event of these changes.

Mr. Firestine asked if any questions or concerns were raised by the rating agencies. Mr. Kim reported that DC Water's presentation was very well received by the rating agencies and that any potential concerns were addressed.

Ms. Nancoo inquired about the flexibility in the resolution to accommodate accelerated or delayed bond pricing as well as the termination date of the authorization. Mr. Kim explained that the authorization does not limit the timing and that the amount includes a limit.

Ms. Nancoo also advised that the bond authorization be technically amended, for enforceability, where the Director of Finance and Budget is in fact the Acting Director of Finance and Budget.

With no further questions or comments, the Committee recommended moving the bond documents to the full Board for approval.

Action Items

- A. The Committee recommended the transfers to the FY 2013 Rate Stabilization Fund Transfer, DC PILOT Reserve Fund and PAYGO Capital Financing be moved to the Board for approval.
- B. The Committee recommended the Revised FY 2014 Operating Budget for the Board's approval.
- C. The Committee recommended the Bond Documents be moved to the Board for approval.

Agenda for July Committee Meeting

With no further changes, Chairperson Firestine approved the agenda for the July Committee meeting.

Follow-up Discussion – Selection of Legal Services

Mr. Randy Hayman, General Counsel, reviewed a revised RFP process for procuring legal services with the Committee. Mr. Hayman proposed advertising an RFP for general legal services in three areas: General Civil Litigation; Environmental Law; and Human Resources. According to Mr. Hayman, DC Water would select a pool of three firms for each of the above areas of the law, without guarantee of a minimum amount of work for each firm. For complex or specialized areas of the law, DC Water would solicit known firms to submit a proposal through a separate RFP process, consistent with existing procedures.

Mr. Hayman further clarified the modified RFP process explaining that that the modified RFP process targets firms with specialized experience while including the same selection criteria as the general RFP.

Mr. Adam Ortiz inquired about the delineation between competitive bidding for legal services and sole-source providers. Ms. Nancoo clarified that there was not dissatisfaction with the existing process but that, per her own suggestion, DC Water proposed this competitive process to provide more flexibility and transparency.

The Committee went into an executive session at 12:15 and convened into open session at 12:44 p.m.

Adjournment

Hearing no further business, Chairperson Firestine adjourned the meeting at 12:45 p.m.

Follow up Items

1. Provide the Committee with a status update on the concrete quality issues of the tunnel shaft.
(Mr. Firestine)
2. Provide the Committee with an explanation of the basis of the settlement for St. Elizabeth's account. **(Mr. Firestine)**