DISTRICT OF COLUMBIA

WATER AND SEWER AUTHORITY

Board of Directors

Finance and Budget Committee

Thursday, July 28, 2016

11:00 a.m.

MEETING MINUTES

Committee Members	**DC Water Staff**
Timothy L. Firestine, Committee Chairperson	George Hawkins, CEO & General Manager
Matthew Brown	Mark Kim, Chief Financial Officer
Sara Motsch	Henderson Brown, General Counsel
Ana Harvey	Linda Manley, Board Secretary

Other Guests

Dan Hartman, Public Financial Management (PFM)
Eric Brown, Public Financial Management (PFM)
Eric Letsinger, Quantified Ventures
Jose Gaztambide, Quantified Ventures
David Goodman, Squire Patton Boggs

Call to Order

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

June 2016 Financial Report and Year End Projections

Mr. Mark Kim, CFO, reported that with 75 percent of the fiscal year completed, financials are on track with budgetary expectations and targeted performance metrics through this reporting period with the exception of capital disbursements.

Total revenues are at $430.5M or 74% of budget. Mr. Kim noted that projected year end revenues are expected to be within +/- 1% of budget due primarily to the federal government's share of the Water System Replacement Fee, which will not be paid until FY 2018. Since DC Water bills the federal government two years in advance, the projected FY 2016 revenue shortfall is a timing difference and the Authority will receive the revenue as part of the federal true-up process.

Operating expenses are below target at $343.2M or 63% of budget with savings primarily due to underspending in the contractual services, supplies and chemicals, and utilities categories relating to the reduction in Biosolid's hauling cost, alternative treatment process of digestion and lower electricity cost relating to the CHP, respectively.

Capital disbursements are at $426.3M or 78% of budget. Mr. Kim noted capital projects are projected to be slightly over budget by $15M or 2%, which will add pressure on the capital budget, but it is expected to be offset by underspending in the capital equipment category.

Mr. Kim briefly reviewed the performance of the investment portfolio which is currently earning 0.80%, noting that all investments are consistent with the Board adopted Investment Policy.

Mr. Firestine asked about the increased up-tick of the number of delinquent accounts. Mr. Kim responded that the Finance team and Customer Service closely monitors delinquencies and would report back to the Committee if any issues warrant further attention.

Rate Stabilization Fund Overview

Mr. Kim provided an overview of the Rate Stabilization Fund (RSF) policy. At the request of the DC Retail Water & Sewer Rates Committee, staff was asked to review the RSF policy to consider expanding its use not only to mitigate the impact of water and sewer rates, but also to consider other charges and fees, in particular the Clean River Impervious Area Charges. The Rates Committee also requested the Finance and Budget Committee to consider establishing a target reserve level for the RSF.

CFO Kim stated the purpose of the RSF policy was to assist in the mitigation of annual rate increases to avoid spikes and allow for gradual rate increases, and that the fund is governed by the Authority's Master Indenture, which only permits surplus funds to be used to contribute towards the RSF. He noted that according to the Master Indenture, the General Manager may determine the amount to transfer into the RSF.

Mr. Kim further explained that over $114M has been withdrawn from the fund between FY 2008 and FY 2015, primarily in anticipation of peak capital spending over that time period. In response to committee members' inquiries, he provided detailed annual contributions and withdrawals for FY 2008 – FY 2015. He further noted that the projected RSF balance is expected to increase to approximately $100M with no withdrawals over the next 10 years. Management's target end balance of $100M will help to maintain level rate increases through peak capital spending in the next 10-year period.

FY 2016 Projected Net Cash Surplus

Mr. Kim then made a formal recommendation to the Committee on the use of the FY 2016 projected net cash surplus of $13.4M. He stated that management's recommendation is to transfer $10M into PAYGO with the remaining $3.4M to be held in cash. The Committee accepted this recommendation.

Environmental Impact Bond Financing Overview

An overview of the Environmental Impact Bond (EIB) was jointly presently by Mr. Kim and Mr. Hartman of PFM. DC Water is structuring an EIB to finance the first project (Rock Creek Project A or "RC-A") in the DC Clean Rivers Project's Green Infrastructure (GI) Program. Mr. Kim explained that the investors will be repaid based upon the effectiveness of GI in managing the volume of stormwater runoff in RC-A. Mr. Kim also stated that the intended purpose of the EIB is to mitigate the financial risk of loss associated with a failure of green infrastructure to manage stormwater runoffs. As requested by the Committee at its meeting in June, Mr. Kim compared both the costs of issuance and true interest costs of the EIB with a traditional, tax-exempt bond financing. Mr. Kim concluded that the expected costs of issuance are significantly lower for the EIB than for a comparable traditional, tax exempt financing. He explained that the expected all-in-true interest cost (TIC) for the EIB is comparable to that of a traditional, tax-exempt financing.

Ms. Sara Motsch inquired as to how the success of the project is defined and who is measuring the success. In response, Mr. Hawkins, GM/CEO, stated that the success of the project is solely independent from that of financing of the project and that it is based on the performance level of GI. Mr. Hawkins also stated that DC Water's Clean River's team will monitor the program and will be able to measure and identify if the project is less successful. If the GI pilot captures less volume, then DC Water will have to use alternative methods. Mr. Brown inquired as to who controls the success factors. Mr. Kim replied, the success factors are controlled by the technical team and are monitored by a well-defined evaluation plan as stated in the Clean River's consent decree. The plan also requires a post-project evaluation to determine the efficacy of the program. Mr. Kim added that the structure and financing are very closely aligned to seek and to hedge any risk associated with the project. Mr. Brown asked if there were any other alternative methods of funding. Mr. Kim replied that DC Water can enter into a P3 (Private-Public-Partnership) deal to fund the GI. Mr. Brown then inquired about the advantage of procuring a performance contract as opposed to an Environmental Impact Bond. In response, Mr. Hartman stated that DC Water could have used a performance contract to achieve similar objectives but that the EIB was a novel financing solution in the form of a bond rather than a contract. In response to Mr. Firestine's inquiry, Mr. Kim explained that the Wholesale customers will pay their prorated share of DC Water's capital disbursements and the District rate payers would be responsible for the costs associated with the EIB.

Mr. Firestine then asked Mr. Kim and Mr. Hartman to provide an overview of the various financing scenarios in the presentation. Mr. Kim explained that the three EIB scenarios represented the expected range of initial interest rates that would be negotiated with the potential investor(s). In addition, Mr. Hartman stated that each of the three scenarios presented include figures for total debt service and the present value (PV) of total debt service in the expected case as well as if a contingent payment were due by one party.

Mr. Kim continued that the three traditional, tax-exempt scenarios were chosen to replicate certain aspects of the EIB such as a 5-year call, premium coupon and mandatory put. Mr. Kim noted that the comparisons between the EIB and traditional financing scenarios were not true "apple-to-apple" comparisons because they did not include the contingent feature of the EIB.

Mr. Firestine asked whether one of the traditional scenarios listed showed a lower all-in TIC than the EIB and why DC Water was not recommending that structure. Mr. Kim responded in the affirmative, but noted that there was additional risk associated with that particular scenario that was not associated with the EIB and that it did not achieve the risk transfer that was the primary purpose of the EIB."

Adjournment

Hearing no further business Chairperson Firestine adjourned the meeting at 12:33 pm.

Follow-up Items

1. Provide contributions and withdrawals schedule for the Rate Stabilization Fund. **(Chairman Brown)**