



DISTRICT OF COLUMBIA BOARD OF DIRECTORS

Audit Committee

**Thursday, May 25, 2006
8:00 am**

Meeting Minutes

COMMITTEE MEMBERS PRESENT

Anthony Griffin, Chairman
Kenneth Davis

WASA STAFF PRESENT

Michael Hunter, Director, Internal Audit
John Dunn, Chief Engineer
Webster Barnes, Principal Counsel
Linda Manley, Secretary to the Board

OTHER BOARD MEMBERS PRESENT

Paul Folkers

Mr. Griffin called the meeting to order at approximately 8:20 am.

Mr. Griffin pointed out that there are eight (8) recommendations from the Governance Study and that seven of the recommendations relate to the Sarbanes-Oxley Act that the committee should discuss. He also stated that he was generally supportive of the Governance Study recommendations, but thought that the Committee needed to discuss the relationship of the Internal Auditor with the Audit Committee, the Board, the General Manager and Staff.

Mr. Griffin reminded the Committee that the Sarbanes-Oxley Act was initiated in the past, not because of misbehavior on the part of the public sector, but rather the private sector. He also stated that many of the processes required by the Sarbanes-Oxley Act, have been practiced by the public sector for years.

Mr. Griffin stated that the Internal Auditor position should be a shared responsibility rather than reporting to the Board exclusively. He also initiated discussion of the prospect of the Auditor reporting to the Audit Committee and the Board and how that would effect availability to the General Manager in reviewing management practices in the organization. He asked the committee and Mr. Hunter for observations and discussion relative to this issue.

Mr. Hunter stated that as for his former employers —private industry and publicly traded companies, the relationship between the Executives and the Audit Committee was good. The Auditor reported to the Audit Committee of the Board and still had a strong relationship to the

CEO or other designated personnel. Mr. Hunter stated that he was not aware of any situations where there were two audit departments, one that reported to the Board and one that reported to the General Manager. Mr. Griffin stated that his organization is structured with two audit functions and discussed some of the pros and cons. Mr. Griffin also stated that he did not think WASA needed two audit departments and that he was not sure to what extent the Board should modify how they do business relative to the Governance Study recommendation.

Mr. Dunn stated that he had worked in three other public jurisdictions in Virginia and in all three cases, their organization charts have solid lines from the Internal Audit function to the Board with a dotted line to the General Manager. Mr. Dunn suggested that the purpose of the solid line relationship was to provide a formal track in the event of contention between the Auditor and the General Manager.

Mr. Griffin asked if the governing body appointed the auditor. Mr. Dunn said yes. Mr. Davis asked if the Board handled the Auditors raises and/or periodic promotions. Mr. Dunn could not offer any information with regards to the auditors' pay or raises. Mr. Davis asked if the Board managed the day-to-day activities or whether they provided a broad oversight. Mr. Dunn stated that the Board provided a broad oversight and a formal reporting.

Mr. Griffin noted that one of the considerations coming from Fairfax County is that the County Administrator/County Executive serves at the pleasure of the governing body so that if there were a disagreement the governing body would have the upper hand. Mr. Folkers stated that he agreed with Mr. Griffin's comments and discussed how the Montgomery County Audit function is organized. Mr. Folkers also stated that he thinks things at WASA have been working very well and that he does have an interest in Sarbanes-Oxley and what the Committee can do to see WASA move in that direction. Mr. Folkers stated that he does not think that the Committee needs to go so far as to have the Internal Audit report directly to the Audit Committee. However, there is a need for something more than is currently in place.

Mr. Griffin suggested that WASA could do something along the lines as Mr. Dunn had described, have a solid line from the Internal Audit function to the Board. The General Manager could recruit the Auditor (when it becomes necessary), and give the Board his recommendation. The Board would appoint the Auditor and delegate the day-to-day oversight. Also identify that the Auditor could go to the Chairman of the Board or the Chairman of the Audit Committee when there are issues with the General Manager. This would avoid the issue of having two audit functions.

After further discussion of the relationship between the Internal Auditor and the General Manager, it was suggested that the relationship should be such that the Board could make requests of the Auditor, as well as the General Manager. Mr. Griffin stated that this was the relationship WASA currently has.

Mr. Hunter stated that some of the provisions of Sarbanes-Oxley extend further than auditor independence, i.e., disclosure, sign offs, code of ethics, etc. There are a myriad of topics that can be explored and implemented into the organization across the board. This is where the audit function comes into play with this governance process. The internal audit profession has recently changed its mission to include governance. One of the recommendations addressed to the Board was about training. He discussed possibly partnering with other departments to bring relative information to the Board for disposition, i.e. best practices, governance practices, etc.

Mr. Griffin, acknowledged the above recommendation and pointed out that one of the suggestions in the governance recommendations is that WASA adopt a code of ethics. He then asked, if WASA has a code of ethics? Mr. Dunn said he had not seen a formal code of ethics. Mr. Webster Barnes responded that the Authority does not have a formal code of ethics. However, there are ethic provisions in the Authority's procurement and personnel policies.

Mr. Griffin stated that he thought there should be a code of ethics for every WASA employee as well as the Board. He stated that there are certainly enough models to use as a guide.

Mr. Griffin stated that there are seven items identified in the Governance Study recommendations for Sarbanes-Oxley, the Committee has discussed two and indicated support for the others.

Mr. Griffin indicated that he would be interested in some formal recommendation in terms of how the Committee might implement these—separate from a proposed code of ethics by the next meeting in July 2006. He would like to see progress on it so that by the end of the calendar year the Committee would have addressed all seven issues from the governance study.

The Committee needs to work out how and when the final recommendation, which is the independent benchmark, can be accomplished. He stated that the Governance Study was an independent benchmark of such, but we need to determine what kind of study or benchmark is needed. Mr. Griffin stated that staff needed to develop benchmarks against similar size utilities. Mr. Folkers and Mr. Davis concurred.

Mr. Hunter suggested tools utilized by the Institute of Internal Audit and outlined a few, discussing the problems with being compared to electric, gas and other utilities nationwide versus being compared to waste water treatment plants only. Mr. Griffin discussed using local utilities (Alexandria, Fairfax County, Montgomery County, Prince George's County, WSSC.) as a measure and maybe developing a support group to develop benchmarks with similar organizations.

Mr. Griffin stated that he thought there was a concurrence that Mr. Hunter come back with a work plan and/or recommendations on each of the seven Sarbanes-Oxley recommendations from the governance study and any further observations relative to the independent auditing benchmarking piece for our July meeting. Mr. Hunter reviewed the audit activity since the last meeting. The audit department has conducted four audits, which include:

- The Contract Administration Review –Goods and Services, large procurement side--contracts over \$100,000. Out of a population of \$230 million, which represents 109 contracts, sampled for detail review 45 contracts that amounted to over \$60 million. Primarily going to the COTR's to review the monitoring process in place to ensure that we are receiving proper service. Should be completing this review within the next couple of weeks.
- The Travel Process Review – First time review for WASA. Used 18 months worth of travel expenditures, close to \$2 million in travel. Very solid program. Used a new tool that we purchased, which is a Global Best Practice. We compare ourselves to 30,000 organizations travel process and we ranked very high. The only area that was not applicable was the individual corporate travel department—WASA employees do their own. Mr. Griffin had some questions relative to our travel policy. Mr. Hunter explained that we had a solid travel policy that was just revised June 2005.

- Change Order Process – This review was conducted utilizing the process employed during the Knowledge Management workshops, (one of the General Manager's initiatives). No significant issues were identified and the Report will be issued shortly.
- Several Consultant Overhead Reviews – One overhead rate was approved last month. Another Consultant is under review, we are waiting for the CPA's information in order to complete the approval.
- Compliance Assistance – Worked with the Procurement Department to develop a structured program. Developed a compliance manual based on the Davis Bacon Related Acts and other compliance laws; Created a review schedule, consisting of both on plant and off plant reviews; Conducted several on-site reviews, but will complete the on-site review schedule once we bring on our hired staff. Mr. Hunter stated that he felt this area was important for review, based on the value of WASA's contracts.

Mr. Hunter continued to discuss his Agenda Items:

- Inter-municipal Agreement (IMA) – Provided suggested audit protocol language to the Negotiating Team.
- Recruitment (Status) – Reviewed thirty-eight resumes and hope to have two positions filled sometime in June.
- Training and Development – Mr. Hunter discussed training for the Internal Audit Staff, as well as the Audit Committee. There was some discussion relative to the requirements and sources of the training. Mr. Griffin suggested that Mr. Hunter provide specific recommendations at the July meeting.

Mr. Griffin said there was no other business and asked if 8:00 am worked for the meeting start time. The Committee concurred. There was also discussion relative to adding Mr. Folkers to the Audit Committee.

Mr. Griffin restated the Committee's requests that Mr. Hunter present a work plan and recommendation for the eight Governance Study recommendations e.g., seven that relate to the Sarbanes-Oxley Act and the independent auditing issue, by the July meeting.

The meeting was at approximately 9:00 a.m.