

SOUTH CENTRAL CONNECTICUT REGIONAL WATER AUTHORITY

AUDIT-RISK COMMITTEE

SEPTEMBER 28, 2023

MEETING TRANSCRIPTION

[AUDIT-RISK COMMITTEE MEETING BEGINS AT 12:32 P.M.]

Catherine:

I would entertain a motion to approve the minutes from the May 25th meeting.

Suzanne:

I'll make that motion.

Mario:

Second.

Catherine:

So moved and seconded. Is there any discussion? All right, all in favor signify by saying, "Aye."

Committee:

Aye.

Catherine:

No objection. So the minutes are approved. The next item on the agenda is an audit presentation for 2023. Do we need to go into executive session for this?

David:

No.

Catherine:

Okay, great. For the 2023 audit and I'm going to turn this over to David Flint.

David Flint:

Good afternoon everyone. Can everyone hear me okay?

David:

Yes.

Rochelle:

Yes.

David Flint:

Great, thank you, Catherine. As Catherine said, my name's David Flint from CLA. With me today is Gabriel Epstein. He was the Director on the job. I'm going to try to share my screen here. Let me know when you can all see it.

Catherine:

We can see it.

David:

We can see it now, the bicycle.

David Flint:

All right, so on the agenda for today we are going to go through the audit scope reporting results, some really high level financial highlights, some required communications from us as your auditors, and then of course our contact information.

Under generally accepted auditing standards, we expressed an opinion on whether the basic financial statements fairly represent the financial position and results of operations and according with generally accepted accounting principles. Also under governmental auditing standards, we provided a report on internal control over financial reporting and in compliance with laws, regulations, contracts, and grants. More commonly referred to as the yellow book letter that we issue and that is included within the federal single audit report that you all have. It is the second opinion within that report.

We also completed a federal single audit under uniform guidance, which includes an opinion on compliance for the major federal program, which was the drinking water program, as well as provide a report on internal control over compliance with that major federal program. So onto the results. For the financial statements, we issued an unmodified opinion for the period ended May 31, 2023 and, of course, an unmodified opinion is the best opinion that can be given. Regarding that yellow book letter that I mentioned, we did not have any findings related to internal control over financial reporting. Also regarding compliance with laws, regulations, contracts, and grants, we did not note any instances of non-compliance.

For the federal single audit, we had that one major program that we audited. Its official name is Capitalization Grants for Drinking Water State Revolving Funds. This program includes both a grant and a loan portion, both of which are included as total program expenditures, which were \$1,966,000 for fiscal year 2023. We issued an unmodified opinion on the compliance requirements for this program, which as mentioned before, unmodified is the best opinion. We also had no internal control findings as it relates to compliance with this program.

I put this slide together to go through some of the changes we have had for fiscal year 2023. In 2023, we implemented GASB statement number 87, which has to do with leases. The Authority has significant leasing activity both as the lessee and the lessor and Gabriel and myself, we met with Rochelle at the beginning of the audit just to kind of go through all the leases and we were able to narrow down a pretty large population of leases to 47 contracts that we ultimately analyzed for this implementation.

You will see on your balance sheet there are four new line items that relate to the standard. You have a right to use lease asset, which is basically, a capital asset for the value of assets leased. You have a lease liability, which is the amount of lease payments payable over the contract period. We have a lease

receivable, which is a receivable for the leases that we are the lessor. Then the opposite to that lease receivable is a deferred inflow of resources.

Another change for the year is you will notice at the back of the financial statements at the end of the notes, we have added some condensed financial statements. If you remember from last year, the watershed fund is actually included within RWA's financial statements as a blended component unit. This is a requirement as part as GASB 84. So these condensed financial statements that we added just kind of break the two out and just show you what the watershed fund activity is by itself.

Along these lines, we have the well services entities. Those are included with the RWA activity as a whole. That same standard GASB 84 considers those entities and RWA as one. Then finally, I don't know if anybody noticed, but for the federal single audit, you were no longer considered a low risk auditee and I just wanted to bring that up because it is certainly not a negative for RWA. Basically the first criteria to be a low risk auditee is that you've had to have completed a federal single audit in each of the last two years and last year we did not need one simply just because the activity was not there. So we will not meet those low risk auditee criteria for 2023 and 2024. It doesn't really change anything for you guys, it just means that we have to audit a higher percentage of the activity in that program.

Just some very high level financial overview here. Looking at the statement of revenues, expenses, and changes in net position, net position increased \$31.4 million for the fiscal year, which is \$11 million better than 2022. When looking at operating revenues, water revenues increased seven and a half million, which was primarily due to the January 2022 rate increases. Of course, 2023 was the first year that experienced an entire year of those rates, but we also saw increased demand in the summer for fiscal year '23 just because of the weather. And of course, that was summer 2022 for fiscal year 2023.

Other operating revenues, you will see an increase of \$1.4 million. That was primarily due from revenues from well services and more specifically water systems, which was acquired in May 2022. So last year we really didn't have any activity for water systems, but this year we had a full year of activity which equated to about \$1.4 million. Total operating expenses increased by \$5.3 million year over year. Operating and maintenance lines specifically increased 2.8 million, which is primarily due to increased costs related to payroll, chemicals, outside services, things like that that just saw inflationary increases as we've all seen in day-to-day lives over the last year or two.

Expenses associated with water and other revenues increased \$1.4 million. Again, as mentioned on the previous slide, this had to do with well services, particularly water systems, which had a full year of activity, which equated to \$1.4 million in additional expense. Looking at the non-operating side of things, non-operating expenses decreased \$6.9 million year over year. This category, your financial statement is kind of net non-operating income and expenses. So really, that increase is due to an increase in interest income of \$6.4 million and that's a combination of two things. The interest to customers was halted during the pandemic and 2023 was the first full year that the interest was being charged again. And of course, what we have all seen in the market, much higher interest rates. So you're able to receive better interest income over the course of 2023.

Also in the non-operating section, you'll see \$490,000 of intergovernmental revenue. That is the grant revenue associated with that drinking water program that we tested for the federal single audit. If you remember, that was around \$2 million in total. The 490 is the grant, the rest of it was the additional loan taken out in 2023.

Catherine:

So is that essentially saying that nonoperational expenses are flat?

David Flint:

Yes. If you were to not consider the offset of all the additional interest income. Yes.

Catherine:

Okay, thank you.

David Flint:

Yes, I think that is a good way to look at it. All right. So looking at your statement of net position, just looking at the total net position categories here. As I said before, net position increased \$31.4 million for the fiscal year '23 and it is broken out into three categories. First, you have your net invested in capital assets, which increased \$11.1 million. That's due to two things, a reduction in capital related debt as well as an increase in capital assets. Any year you do not issue new bonds, you would expect the net investment and capital assets to increase.

Secondly, we have restricted net position, which increased \$15.3 million primarily due to an increase in restricted assets. You might see that restricted assets actually went down year over year, but included in restricted assets last year was \$30.1 million of bond proceeds that had not yet been spent. Those are actually included in the net investment and capital asset line and not the restricted line. Then of course, unrestricted is basically everything else that doesn't fit into those two categories.

Rochelle:

David, before you move on, Suzanne did you have a question?

Suzanne:

I have two quick questions. First, one's on the first bullet, and it was related to the fact that it's reduction. So if we were back in cycle of issuing debts, this would go away. This is not an improvement of a situation. This is a timing thing.

Rochelle:

Well, we paid a principal payment and we issued no additional debt other than a small DWSRF loan. So that is why that's a primary driver of that line.

Suzanne:

Right, but because we do not issue debt every single year, it is more of a timing issue than an improved situation.

Rochelle:

It is a combination because you are actually making principal payments every year on the debt that we do have. So it's both.

Suzanne:

So you would describe it as a partially improved situation on your patent?

David Flint:

Yes, so picture, if it was year one, let's say we had a \$100 million bond and we used that \$100 million bond to buy \$100 million in capital assets. You would have a \$100 million asset, a \$100 million liability, your net investment capital assets would be essentially zero. The next year you pay \$10 million on that bond. Now you have a \$100 million capital asset, you have a \$90 million bond, so you have a \$10 million increase in this category. Does that make sense?

Suzanne:

Yes, it does. And the second question is on the second bullet. Is this unspent bond proceeds meaning actual principle we've raised in bonds or premium?

Rochelle:

Last year, based on the timing of when we did our prior financing, there was about \$30.6 million of unspent by proceeds to the end of May of 2022. So that actually gets incorporated into net invested in capital assets and we of course use that money now for capital. I think the other key thing to mention actually what David also mentioned is, as long as your investments are going up, your assets are going up by more than your debt is going up, you're going to have a favorable impact.

Suzanne:

Right. But what I'm trying to see is did we borrow more than we need or it's just, no, we only spend so much from the borrowing and we cycle at the cash flow of the bond's revenue.

Rochelle:

Correct. Because we need that bond proceeds to last our 18-month period. A combination of debt plus internally generated costs.

Suzanne:

Lastly, none of this has to do with premiums that you are getting or is that also? What do you do with your premiums on your bonds?

David Flint:

The premiums are amortized over the life of the bond.

Suzanne:

They are, and you use them to pay off the debt service here?

Rochelle:

We actually get the premium and debt proceeds and then it is a non-cash accounting that happens subsequent to that.

Suzanne:

I'm not sure what that means.

Rochelle:

You put the premium as actually a liability on the books and it gets amortized over the life of the bond.

Suzanne:

How do you use it? Do you use it to pay off debt service and principal, or do you use it to expand your capital?

Rochelle:

So when we do the issuance we actually; it is a positive thing because when we do the issuance, we're actually getting the proceeds at par and we're getting the proceeds associated with premium. So the capital program.

Suzanne:

You spend it?

Rochelle:

Yes.

Suzanne:

We spend it, not you. We spend it. Okay, thank you.

David:

If I could.

Suzanne:

Yes.

David:

Just building on Suzanne's first comment, if we are in a little better position by millions of dollars we're talking about this year and we didn't issue bonds, does that mean that next year when we do go to issue bonds that we will be in a worse position or we'll still ...

Rochelle:

Not necessarily. There are multiple factors. Like I mentioned, as long as capital assets are going up by more than your debt is going up, that's favorable and we actually have pretty large principal payments every year that we are, in fact, by making those large principal payments, it's helping to bring down the debt. Even if we are issuing more than the principal payment, we're still paying off that older debt.

David:

So we are paying off more than we added up in order to get in that position.

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Rochelle:

Not in every year.

David:

Not every year. But we did this year.

Rochelle:

In fiscal '23 we definitely did because we had almost a \$23 million principal payment. Other than that small DWSRF we didn't issue any. So it cycled it. Any other questions?

Mario:

If I may, does this include the wealth services? I'm a little confused-

Rochelle:

Yes, all this includes the wealth services, all the net income from wealth services is all unrestricted because it's outside our general bonds.

David Flint:

The watershed fund is actually in here too for a small, I think it's like \$1.4 million.

Mario:

A follow-up. Although the requirements on the audit is that it all be combined in the single audit, you still maintain them as separate?

Rochelle:

We totally do. In fact, even in our financial reporting, it is the utility only and the only time it's combined is in our audit financials based on the requirements we have.

Mario:

Thank you. It is good to know that they're being audited too.

Rochelle:

Are there any other questions? Kevin, did you have a question?

Kevin:

No, thank you.

Rochelle:

Okay, David can go on.

David Flint:

Thank you. All right, so I guess this slide will help a little bit understand the debt side of that. So this is the schedule taken right out of the financial statements of the long-term liabilities. So total bonds payable were about \$512 million, which is a decrease of 21 and a half-million dollars year over year. Again, 21 and a half million dollars of payments on the bonds outstanding and no new bonds issued, which is what gets you to that \$512 million number.

The drinking water loans increased by \$117,000 and that's just the net activity between the pay downs of the old loans and the new loan that was taken out as part of that federal single audit program I spoke of. The net pension liability increased \$1.3 million due to relatively stagnant investment returns in 2023, which were less than what was anticipated, which were offset by RWA contributions that were \$2.3 million more than what the actuaries required you to contribute. I think that's important. So every year the actuaries give you an actuarially determined contribution and you guys put in an additional \$2.3 million above and beyond that amount to help the net position of the pension fund.

Rochelle:

Yes, so we are hoping the new chair will improve our success.

Mario:

I was pretty happy with the overall results of the last share.

David Flint:

You also have a net OPEB liability, which decreased one and a half million dollars, mainly due to differences between expected and actual experience. When it comes to various actuarial assumptions such as mortality, retirements, turnover, basically, the actuaries have these assumptions that they come up with these liabilities every year. The results were a little bit different than they expected and that primarily was the reason for the decrease in the liability year over year.

Catherine:

So fewer people died than expected, retired than expected.

Rochelle:

Actually, medical expenses that impacts this as the primary driver.

David Flint:

Then as mentioned earlier, we have a new line here, which is the lease payable and this is a result of GASB 87. The total lease liability at the end of the year was \$530,000. So that is my high level financial overview. Does anyone have any questions for myself, or Rochelle?

Catherine:

No. I do not know if this is the right time to ask this question, but we talked at one point about our overall liability and capital debt and what that would look like if interest rates stayed at the rate that they're at over a certain period of time. Is that something that the board has an appetite to look at just to understand how the debt can or will or won't decrease over time?

Rochelle:

We will actually be showing that as part of the 10-year Model and we can also include because our debt level, after a certain year based on our current debt actually goes down pretty significantly. But we actually display that as part of our 10-year Model. We will be doing that next month.

David:

But I do think that has been, if I may, I do think that's been an issue that we do need ... It's been festering, if you will, and it does need to come to the surface and this is the vehicle to do it, that's great. If not, we've talked about that they could come under the Strategic Planning Committee as well and they can be going together because the 10-year Model is really our strategic plan for 10 years in terms of finances.

Catherine:

Great.

Rochelle:

Are there any further questions?

David:

I have one and if I may, and you and I briefly talked about it and should have reminded you again. In the past we as a board have met privately with the auditors and they've usually been quick meetings pro forma, but even though they were pro forma, I'd like to get back to that practice again just for the purpose of them hearing from us or us hearing from them if there's anything. There's usually nothing. It is usually quick, but I liked that process. And quite frankly, the reason I'm bringing it up and I brought it up to you was because I received, outside of the meeting, I received communications from the audit firm asking for me to meet with them and I don't think that's my role as chair of the overall board or past chairman of the Audit Committee or whatever title I may have had at one time. I would rather see us as the five members do that.

Catherine:

I'm delighted to do that today if you ...

David:

Absolutely, I think this is appropriate, I do not know if this is the exact right time at this moment, but sometime today.

Larry:

Usually the auditor go through his report or her report.

David:

Right, which, and then you will meet with management. Okay. He's done. Now it's appropriate.

David Flint:

I plan on doing an executive session after this, so that'd be great.

Rochelle:

Okay. Do you have any further questions.

David:

Yeah, just one thing real quick. So you should have each received, we call it our governance communication. It is basically the four page letter from us. The only thing I really wanted to highlight in that is down in the bottom of page two, top of page three, circumstances that affect the form and content of the auditor's report. Just because we had a restatement as part of the GASB 87 implementation, we have an emphasis of matter in your audit opinion. That is basically just highlights that and that is discussed right here in that letter. That is the only thing from that letter that I kind of wanted to point out to you guys today.

Suzanne:

Can you just translate that into English?

Rochelle:

Do you want me to do that, David, or do you want to?

David Flint:

Yes, so the first part of your financial statement is our opinion. That is basically when we express our unmodified opinion, which again is their terminology for the best opinion. There are no issues. Included in that is an emphasis of matter. Something that we think is significant enough for us to point out within this opinion. And we're just saying that we implemented this standard and it had a change in some of the numbers that were reported in the fiscal year 2022 financial statements as we bring the liabilities and assets onto the books related to those leases.

Rochelle:

I think the reason it is emphasized, and David can correct me if you have a different view, but it was a pretty significant undertaking to be able to implement it and what was involved in. We did have to go back to fiscal '22 to make it comparable to fiscal '23.

Catherine:

I asked about this as well.

Rochelle:

Because of GASB 87, and David explained this a lot yesterday, there were significant changes in how these leases are reported, and so because of that, there were changes that had to be made to our fiscal '22. So there's a restatement in fiscal '22 audit and that's what he's talking about.

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Catherine:

He's just pointing out that that exists?

Rochelle:

Exactly.

Catherine:

Okay. Thank you.

David Flint:

Yes. Thank you, Catherine.

Catherine:

Did I get that right?

David:

You got that perfect.

Rochelle:

Is there anything else?

David Flint:

Not from me. Here is our contact information. If you ever need to reach out to us outside of the period of the audit, we're always happy to talk. If you have any questions, comments, or concerns. Other than that, I am ready for executive session.

Mario:

I entertain a motion to go into executive session for purposes of discussing confidential financial matters pursuant to Section 210(b)(5)(B).

David:

And inviting our auditors and the RPB member because they're part of the same ... they're also involved.

Suzanne:

Second.

Jennifer:

Is Tony staying?

David:

Yes, I think so. Because RPB is part of this and they will get it next week actually.

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[AUDIT-RISK COMMITTEE MEETS IN EXECUTIVE SESSION FROM 12:15 P.M. TO 1:13 P.M.]

Suzanne:

Before we conclude our meeting, a question came up, and this is something that actually was raised in prior months, is it possible to move this meeting to October instead of holding it in September, which might give greater time for our auditors to work? And our staff?

David:

And you guys, yes, too.

Rochelle:

Actually, the answer is actually no because we have an action we have to... Certain of our bonds have a 120-day labor requirement, so we actually have to file with our trustee the end of September and that does include the audited financials and some of the other [inaudible 00:00:53].

Suzanne:

So that's tomorrow.

Rochelle:

Correct.

Suzanne:

I knew there was a reason I could not recall what it was.

David:

We thought it might provide a little safety room there, a little easier, but okay.

Suzanne:

All right. Well-

David:

Rochelle, do we have to have this meeting before that date? And if this meeting was the first week of October.

Rochelle:

I guess that is if the board with it is comfortable that we would need all our filing requirements and then we would have everything.

David Flint:

So you want this meeting to be before you file?

Rochelle:

Ideally, I have to admit, I did actually file, but it was after we uploaded everything on the board pack.

Suzanne:

You did file.

David Flint:

Listen, this is totally up to you. Rochelle, I just thought you and your team would benefit from a week, even just a week more to close the year-end.

Rochelle:

I would agree we would benefit from that. I would agree with that.

Suzanne:

So think about it, Rochelle, and you do not get back to Catherine about if do we stick with the timeframe of getting it buttoned up for the report with more time for the meeting? Does that help in any way? Whatever might be helpful. We are present as a board to the fact that this is a big lift in a short period of time for your team and if there's ways to create capacity, we're open to it.

Rochelle:

And of course Chuck is here now.

David:

That'll help.

Rochelle:

I'll be better up here.

Mario:

We're going to push it out a week.

Catherine:

Anything to help the finance department. Unless there is any other thing that we need to cover, I would entertain a motion to adjourn as the Audit-Risk committee. All in favor?

Committee:

Aye.

Catherine:

All right so, it is unanimous so we are done.

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David:

Okay, thank you. All right.

David Flint:

Thank you so much guys.

Suzanne:

Thank you very much.

David:

Probably the [inaudible 00:03:11] team, you are welcome to stay but I'm sure you have other things [inaudible 00:03:15], so thank you.

David Flint:

Bye everybody.

Gabriel:

Thanks everyone.

[AUDIT-RISK COMMITTEE MEETING ADJOURNS AT 1:16 P.M.]