

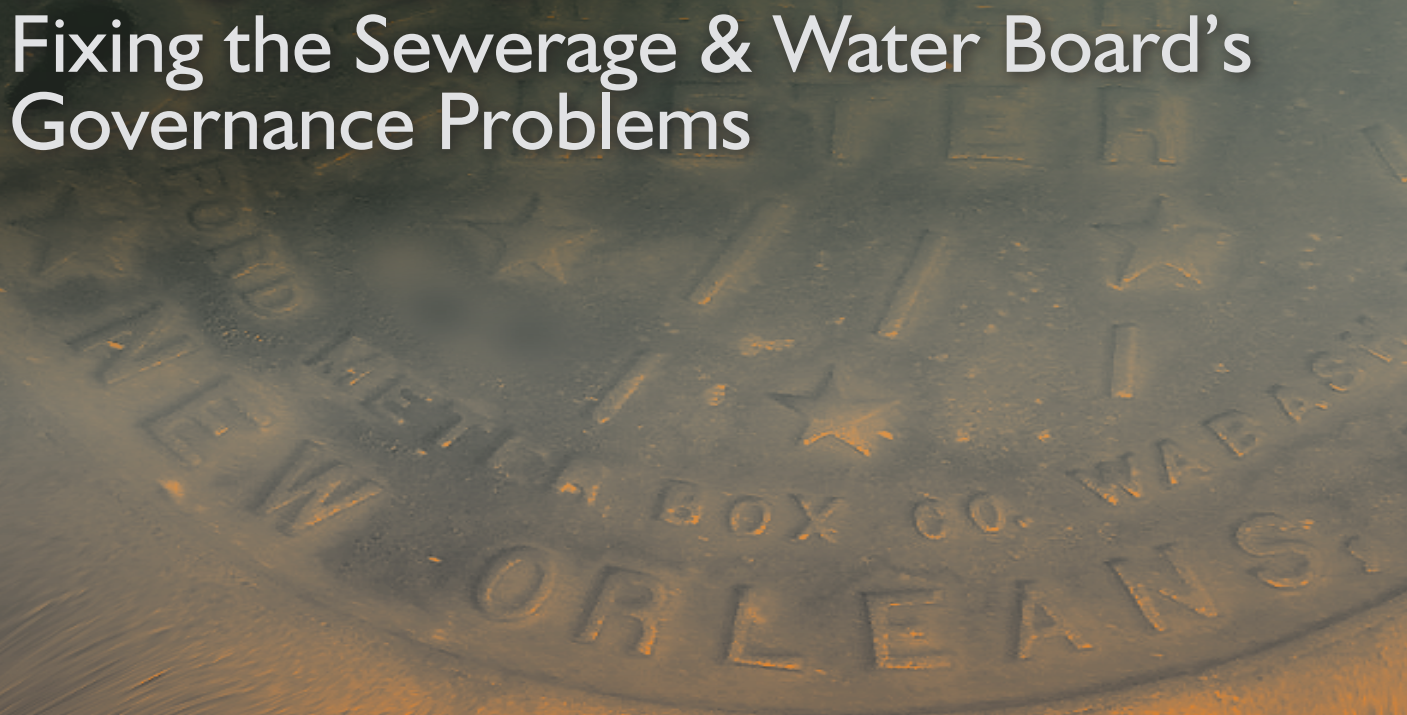


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A Report from the Bureau  
of Governmental Research

# MAKING THE WATERWORKS WORK

Fixing the Sewerage & Water Board's  
Governance Problems



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## MAKING THE WATERWORKS WORK

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## EXECUTIVE SUMMARY

Today, more than a century after it was born, the Sewerage & Water Board of New Orleans (S&WB) faces unprecedented challenges. The water system suffers from widespread leakage. The sewage collection system and treatment facilities do not yet meet federal standards. The S&WB's aging power plant has suffered two major outages since Hurricane Katrina, one of which prompted a boil-water order last year. The drainage system needs significant investments to address aging equipment and expand capacity.

The S&WB has mapped out a 10-year, \$3.5 billion capital program to address some, but not all, of its infrastructure needs. The lion's share of the funding for the program will come from the federal government. However, the S&WB is expected to ask the public to finance approximately \$1 billion of those improvements and to provide additional funding to improve current operations and cover new operating costs. This would require rate increases that nearly double the current sewer and water rates over a 10-year period, as well as tax increases and/or a new drainage fee.

It will be a tough sell. The agency's failing infrastructure and its customer service problems have sapped the confidence of the customer base that the agency must now convince to help finance its recovery.

Restoring that confidence begins with addressing the root causes of the S&WB's current predicament. In this study, BGR focuses on one factor that has significantly harmed the S&WB's performance: its governance structure. The study discusses how the S&WB's governance has contributed to the entity's problems. It presents options for reform and makes recommendations.

Underlying the S&WB's current infrastructure woes is a history of chronic underfunding. Since 1967, when the finances of the S&WB's three systems were first separated, rate increases have been sporadic, with substantial increases following long periods with little or no adjustment.

Two elements of the S&WB's governance structure have contributed to its erratic pattern of rate increases. To begin with, there is a basic misalignment in respon-

sibilities and powers. While the S&WB is responsible for constructing, operating and maintaining its systems, it lacks control over its financial destiny. The final say in the funding arena belongs to the City Council, which has no responsibility for the operations of the S&WB and plenty of political pressure to keep rates low. Over the past few decades, the City Council has on multiple occasions delayed or killed rate increases, despite the S&WB's pressing needs.

The other factor that has historically stymied regular rate increases is the presence of four elected officials – the mayor and three members of the City Council – on the board. The elected officials, leery of voters' ire, have on multiple occasions over the years objected to new rate and tax proposals at the board level. Their objections have discouraged proposals from coming forward or foreshadowed the outcome of a council vote, short-circuiting the process before it even begins. Rarely have the other members of the S&WB acted in concerted opposition to the elected ones.

There are two basic options for addressing the misalignment between responsibilities and powers that has hurt the S&WB's performance. One is to consolidate the S&WB into city government, transferring responsibility for the systems to the entity that controls the purse strings. The other is to make the S&WB more autonomous by increasing its authority over its funding sources.

BGR carefully considered the advantages and disadvantages of consolidation, but ultimately decided against that route. While consolidation would address the misalignment between responsibilities and powers, it would not address the second major governance problem: the undue influence of politics in the process of setting the S&WB's rates and taxes. Given the magnitude of the systemic problems at City Hall, the role elected officials have played in holding the S&WB back and the city's poor track record on funding the infrastructure it already controls, consolidation is clearly not the optimum solution.

Instead of consolidation, BGR is recommending a significant increase in the S&WB's autonomy. This would be accomplished through changes to both the board's composition and the rate-making process.

To reduce the role of politics in decision-making, BGR proposes removing elected officials from the board. This would eliminate the ability of officials to hinder the proper funding of the S&WB by opposing rate increases at the board level.

To better align powers with responsibilities, BGR proposes giving the S&WB limited authority to raise rates by reasonable amounts without the consent of the City Council. The maximum annual increase would be tied to an appropriate index or other measure. For larger increases, the S&WB would still have to obtain the City Council's consent. This would reduce the temptation for the S&WB to raise revenues rather than ferret out waste and inefficiencies. It would also provide a regulatory check on monopoly pricing.

Along the same lines, BGR also recommends allowing the S&WB to make limited upward adjustments to drainage fees if and when they are imposed. As with rates, City Council approval should be required for large increases.

The shift in control over funding should come with adequate public safeguards. The S&WB should develop its revenue requirements in the context of long-term strategic capital and financial plans, and devise its rates using a standard methodology.

Both the S&WB's lack of control over its funding and its board structure are unusual among sewer and water authorities. BGR took an in-depth look at the governance structure of 10 well-regarded independent utilities. Seven of them are composed exclusively of appointees. Only three have an *ex officio* member in addition to appointees, and in all three cases it is the mayor. No members of the local governing body (e.g., a city council) sit on any of the 10 boards.

BGR gathered information on 37 independent water utilities nationwide and found that all but four of them have full control over their rates. Two of the four are regulated by a state public service commission, and the local governing body has the final word on rate changes for the other two. To the extent that an independent entity controls its own funding sources, it can make decisions based on the objective needs of its systems, rather than the political currents.

BGR is aware that its proposal to give the S&WB partial control of its rates differs from the standard practice for independent utilities. It is also aware that giving the S&WB partial control would go only so far in rectifying the misalignment between powers and responsibilities. Limited rate and fee increases would not, for example, provide the S&WB with adequate resources to address the massive and immediate needs of its systems. Partial rate-making authority would, however, provide it with a mechanism for funding increases in operating costs as well as maintenance and capital repairs on an ongoing basis once the major needs are addressed. In that regard, we note that the changes that BGR is proposing would take time to implement and should not interfere with the important task of addressing immediate infrastructure needs.

Going forward, rate-making in New Orleans would benefit from a more comprehensive regulatory process. As part of that process, the City Council's Utility Committee should receive and review the S&WB's strategic and financial plans and reports, and monitor the S&WB's performance on a regular basis. This would keep the City Council informed of the needs, condition and performance of the S&WB and provide a better context for dealing with its funding requests.

Finally, it should be noted that responsibility for New Orleans' drainage system is currently divided between the city's Department of Public Works and the S&WB. This arrangement is unusual and ineffective. BGR recommends transferring responsibility for the maintenance and repair of the subsurface drainage from Public Works to the S&WB. The latter has the necessary expertise as well as responsibility for the more complex components of the local drainage system. BGR notes that the S&WB would need additional funding to discharge its expanded responsibilities.

### Addressing Other Governance Problems

The misalignment between responsibilities and powers and the presence of elected officials on the board are the S&WB's two most serious governance problems. But there is significant room for improvement in other areas, including board structure and responsibilities.

*Changing the Board's Size.* With 13 members, the

board is too large. Reducing the size to nine members by removing the elected officials would make it less unwieldy and – given the weak attendance history of elected officials demonstrated in this report – make it easier to achieve quorums.

*Reducing Members' Terms.* The nine-year terms of appointed S&WB members are too long. Reducing the terms to four years would allow for re-evaluation of their performance in the context of a reappointment process. Imposing term limits would help guard against the entrenchment of individual board members.

*Setting Qualifications Based on Experience.* The S&WB's members currently have a mix of relevant backgrounds, but this is not required by law. Formally establishing experience requirements for some members would help to ensure that the board has the necessary mix of expertise in the future.

*Reducing the Board's Involvement in Contracting.* The board is too involved in the review and approval of contracts. It should focus its role in contracting primarily on broad policy issues and oversight, and limit its review of individual contracts to extraordinary matters, such as significant privatizations. This would allow professional management to make good business decisions for the utility, free of the preferences of board members.

*Evaluating Top Management.* The board has not been evaluating top management on a regular basis. Doing so should become an annual priority for the S&WB board of directors. The evaluation should include a review measuring performance against objectives set in strategic and financial plans.

## Recommendations

To better align the S&WB's responsibilities with funding authority and improve the City Council's decision making:

- The State Legislature should amend state law to authorize the S&WB to increase water and sewerage rates annually by an amount tied to a suitable index or other measure, without City Council approval. State law and the city charter

should be amended to allow limited increases for drainage fees.

- The City Council should consider requests for larger increases using a formal review process, which at a minimum should provide for independent analysis of the requests, appropriate opportunities for public comment and clear timelines. The City Council should also adopt a formal process for considering S&WB requests to levy taxes and fees.
- The City Council should develop a comprehensive, ongoing process for regulating the S&WB, which includes reviewing the S&WB's strategic and financial plans and reports, and regularly monitoring the S&WB's performance.

To increase the effectiveness of the S&WB board of directors:

- The State Legislature should amend state law to remove the mayor and City Council members from the board, reducing it from 13 members to nine. The City Council should initiate a corresponding charter amendment.
- The State Legislature should further amend state law to:
  - Reduce the terms of board members from nine years to four years and stagger the new terms.
  - Limit members to three consecutive terms.
  - Require that seven of the nine members of the board have extensive experience in one or more of the following areas: finance, accounting, business administration, engineering, law, information technology or public health.
- The S&WB's board should limit its role in the agency's contracting primarily to broad issues of policy and oversight. It should

establish appropriate policies and goals to guide management's contracting processes, and set goals for the Disadvantaged Business Enterprise (DBE) program. It should monitor management's performance toward those goals and adherence to board policies. It should restrict its review of individual contracts to extraordinary ones, such as significant privatizations.

- The S&WB board should also establish an annual process for evaluating the performance of the executive management, including but not limited to measuring performance against objectives identified in strategic or financial plans adopted by the board.

To improve the upkeep of local drainage:

- The city should transfer responsibility for the maintenance and repair of its subsurface drainage from the Department of Public Works to the S&WB.
- The city and the S&WB should develop a new funding source for subsurface drainage.

## INTRODUCTION

After its establishment in 1899, the Sewerage & Water Board (S&WB) quickly became a jewel in New Orleans' municipal crown. The water and sewerage systems significantly improved the health of a city that had been mired in unsanitary conditions. The inventions of drainage engineer A. Baldwin Wood opened large swaths of the city to development, made the city's system an international model and inspired young engineers to flock to the S&WB. The innovation, scope and quality of the sewerage, water and drainage works built in those early years led Mayor Martin Behrman in 1914 to declare them "enduring monuments to the courage, determination and infinite resourcefulness" of New Orleans.<sup>1</sup> For decades thereafter, those monuments were well maintained.

Today, however, the S&WB's sewerage and water systems are in a deplorable state. The water system suffers from widespread leakage; 75% of the water treated by the S&WB passes through the system unbilled, and leaks are far and away the main cause.<sup>2</sup> The leaks undermine the streets and drive up costs. The sewage collection system and treatment facilities do not yet meet federal standards; they remain subject to a federal consent decree mandating more than \$220 million of upgrades and repairs by 2015.<sup>3</sup> The S&WB's aging power plant has suffered two major outages since Hurricane Katrina, one of which prompted a boil-water order in November 2010.<sup>4</sup> While the drainage system is not crumbling, the S&WB is seeking significant investment to address aging equipment and expand the system's capacity.

The S&WB has mapped out a 10-year, \$3.5 billion capital program to address some, but not all, of its infrastructure needs. The lion's share of the funding for the program will come from the federal government. However, the S&WB is expected to ask the city's residents and businesses to finance approximately \$1 billion of those improvements and to provide additional funding to improve current operations and cover new operating costs. This would require rate increases that nearly double the current sewer and water rates over a 10-year period, as well as tax increases and/or a new drainage fee.

It will be a tough sell. The agency's failing infrastructure and its customer service problems have sapped the confidence of the customer base that the agency must now convince to help finance its recovery.

Restoring that confidence begins with addressing the root causes of the S&WB's current predicament. In this study, BGR focuses on one factor that has significantly harmed the S&WB's performance: its governance structure. The study discusses how the S&WB's governance has contributed to the entity's problems. It also presents options for reform and makes recommendations.

## THE S&WB

The S&WB is a board established in state law to construct, control, maintain and operate the sewerage and water systems and part of the local drainage system for the City of New Orleans. With respect to drainage, the S&WB is responsible for pipes 36 inches or larger in diameter, drainage canals and pumping stations.<sup>5</sup> The City of New Orleans, through its Department of Public Works (Public Works), is responsible for the rest of the local drainage system, including more than 85,000 catch basins and the nearly 1,600 miles of smaller drainage pipes underneath streets, sidewalks and other rights of way. This part of the drainage system is referred to as the "subsurface drainage."<sup>6</sup> Public Works is responsible for more than 80% of all drainage lines (including canals) in New Orleans.<sup>7</sup>

Although the S&WB was created by state law, it is a municipal agency.<sup>8</sup> In relation to city government, it is one of 10 "unattached" boards and commissions placed under the executive branch by New Orleans' home rule charter, meaning it is not attached to a specific department of the city government.<sup>9</sup>

The S&WB is governed by a 13-member board of directors. Four elected officials – the mayor and three City Council members – serve in an ex officio capacity. The board also includes two members of the Board of Liquidation, City Debt, each of whom is appointed by the mayor on the recommendation of that board.<sup>10</sup> Seven citizen members are appointed by the mayor with the advice and consent of the City Council.

The S&WB receives no funding from the city government. Local funding for the water and sewerage systems comes primarily from user charges. Property taxes (which currently total 16.43 mills) provide most of the local support for the drainage system.

The finances of the water, sewerage and drainage systems are maintained separately. However, the S&WB operates all of the systems on a consolidated basis. In 2011, the S&WB adopted an operating budget of \$185.7 million and a capital budget of \$1.3 billion. Most of the capital budget came from federal funding.

The S&WB has significant, but not complete, independence from city government.

It has sole responsibility for and control over its management and operations. The city government cannot order the S&WB to take specific actions, nor can it impose specific financial burdens.<sup>11</sup>

However, the S&WB has limited control over its funding. It does not have taxing authority; taxes for its benefit are levied by the City Council. It must obtain the approval of the City Council and the Board of Liquidation before issuing bonds or (with the limited exception described in the next paragraph) raising sewer and water rates. The Board of Liquidation generally limits its review to the fiscal soundness of a proposed bond issue or rate increase. The City Council has no guidelines for its review. The Board of Liquidation and City Council cannot modify the rates proposed by the S&WB; they can only accept or reject the S&WB's proposed schedules.<sup>12</sup>

State law allows the S&WB to override the City Council and raise rates unilaterally when necessary to meet its existing debt service obligations (but not to support new debt). If the S&WB does not exercise that authority, the Board of Liquidation can compel it to do so.<sup>13</sup>

The City Council and Board of Liquidation were not always involved in rate setting. Until 1954, the S&WB set its own rates without even a public hearing.<sup>14</sup> However, rates were capped by state law and could not be used to support debt. In 1954, voters eliminated the cap. At the same time, they added requirements for public hearings and Board of Liquidation approval of rate adjustments.

In 1958, voters authorized the S&WB to issue revenue bonds with the approval of the Board of Liquidation and the City Council. They also added a requirement for City Council approval of rate increases.

## HOW GOVERNANCE CONTRIBUTES TO THE S&WB'S PROBLEMS

Underlying the S&WB's current infrastructure woes is a history of chronic underfunding. Since 1967, when the finances of the S&WB's three systems were first separated, rate increases have been sporadic, with substantial increases following long periods with little or no adjustment. For example, for a 20-year period from early 1987 to late 2007, water rates increased only twice. For a 14-year period running from early 1986 to early 2000, sewerage rates did not change at all, and customer charges declined relative to inflation. These long periods of inactivity were preceded and followed by multiple years of double-digit increases. The drainage system has not gained a new revenue source since 1982, and 10 years later it actually lost one of the taxes that supported it.

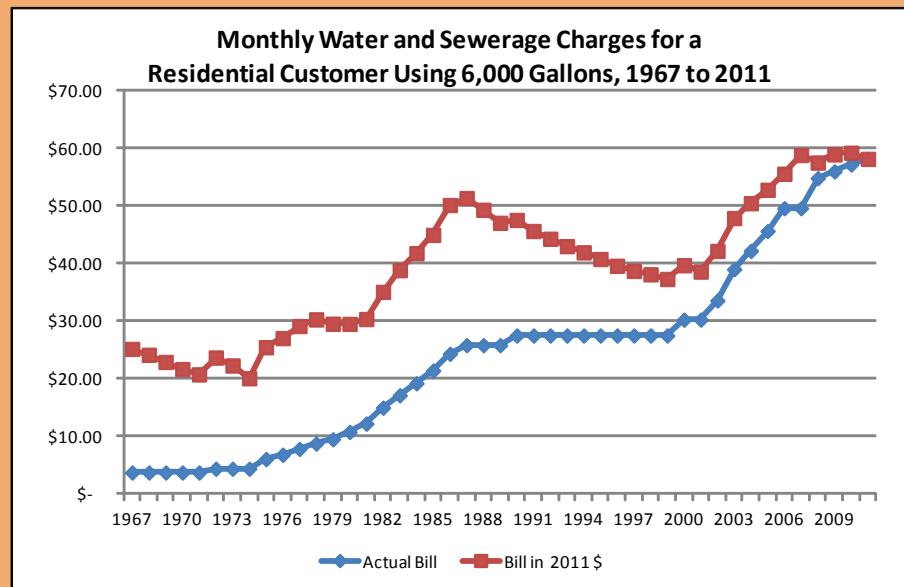
The S&WB's management coped with the stagnation in water and sewerage rates in the late 1980s and the 1990s – and their decline relative to inflation – by cutting operating costs, deferring system maintenance, funding some capital projects on a pay-as-you-go basis and deferring others. The deferred maintenance and capital investment increased the ultimate costs of repairing the systems and pushed the day of reckoning into the future.

New Orleans' approach to rate increases – long periods of inactivity followed by periods of substantial increases – flies in the face of best

practices. The recommended approach is to impose gradual increases at levels that are sufficient to keep up with operating costs and fund the regular investment needed to sustain the systems over time.<sup>15</sup> Ideally, the costs paid by customers are matched to the benefits they receive from the system improvements, without overburdening one generation of ratepayers.<sup>16</sup>

Two elements of the S&WB's governance structure have contributed to its erratic pattern of rate increases. To begin with, there is a basic misalignment in responsibilities and powers. While the S&WB is responsible for constructing, operating and maintaining its systems, it lacks control over its financial destiny. The final say in the funding arena belongs to the City Council, which has no responsibility for the operations of the S&WB and plenty of political pressure to keep rates low. As discussed below, the City Council has on multiple occasions delayed or killed rate increases, despite the S&WB's pressing needs.

The other factor that has stymied regular rate increases



*Note: Water charges are based on a 5/8" meter and water consumption of 6,000 gallons per month. Sewerage charges are based on a 5/8" meter and 85% of the monthly water consumption. The amounts do not include other charges on the bill, such as the city's sanitation service charge. The total water and sewerage charges are based on rates in effect on September 1 of each year.*

*Source: BGR calculations based on water and sewerage system rate schedules as published in various public notices, official statements, rate studies and other S&WB documents. The calculations of the water and sewerage bill in 2011 dollars were made using a web-based program provided by the U.S. Bureau of Labor Statistics.*



is the presence of four elected officials on the board. The elected officials, leery of voters' ire, have on multiple occasions objected to new rate and tax proposals at the board level. Their objections have discouraged proposals from coming forward or foreshadowed the outcome of a council vote, short-circuiting the process before it even begins. Rarely have the other members acted in concerted opposition to the elected ones.

Together, the requirement for council approval and the presence of elected officials on the board have contributed to an irregular, crisis-driven approach to rate-making.

### A Short History of Rate Proposals

*Sewerage Rates.* The history of sewerage rates helps to illustrate the reactive and reluctant approach that the City Council and the S&WB have taken to rate increases. A separate sewer rate was first established in 1967. In 1971, facing rising costs due to inflation and more stringent federal regulations for treatment, the S&WB sought a 72% rate increase. The City Council balked and negotiated a 19% increase instead. This was enough to satisfy the existing bond obligations for the next few years, but not enough to leverage federal funds needed for major upgrades at the treatment plants.

The S&WB returned to the council the next year with another large rate hike proposal. In addition to rising costs, it now faced increased pressure from the U.S. Environmental Protection Agency (EPA) to address pollution violations resulting from the discharge of raw sewage into the Mississippi River.<sup>17</sup> The council again delayed action, and the EPA threatened to ask federal agencies to withhold funds from the city. The City Council responded by giving the S&WB \$2.4 million to match federal funds needed to expand its East Bank sewerage treatment plant. While the investment enabled the S&WB to begin addressing the EPA's concerns, it was insufficient to fund all the improvements needed to bring the S&WB into compliance with EPA regulations or to meet debt service and other expenses.

The S&WB tried in vain for the next two years to win council approval for a rate hike. During that period, the EPA imposed even more stringent federal treatment regulations, and projected operating costs for the expanded treatment plant rose dramatically. When the

council refused to act, the S&WB, acting unilaterally, nearly doubled its rates. Two weeks later, in November 1974, the council relented and approved the new rate schedule.

There were no increases for the next five years. In 1979, the S&WB proposed a five-year series of sewerage rate increases to leverage federal funds for capital improvements. Two months later, the council approved that increase, noting that the risk of losing the federal funds left it with no alternative.<sup>18</sup> Midway through that series of increases, the S&WB's advisors determined that the new rates were inadequate to produce the revenue needed to meet bond covenants. In response, the S&WB and the City Council enacted another series of annual rate increases that extended through 1986.

Rates were not raised again for 14 years, largely because elected officials on the S&WB exerted pressure to hold rates down. In the interim, the EPA filed a lawsuit alleging environmental violations relating to the sewerage system. It added the City of New Orleans as a party to the lawsuit primarily on the basis that the city, including the mayor and the City Council, had failed to authorize increases to pay for needed repairs and could continue to do so. Only after the S&WB, the city and the EPA entered into a consent decree in 1998 did the S&WB request a rate increase for the sewerage system. Even under the pressure of that decree, the City Council initially delayed taking action in order to protect a revenue-raising measure that the city was sending to voters. Ultimately, it took nearly 18 months for the City Council to approve the first of what would be annual increases over a seven-year period ending in 2006. The S&WB has not requested an increase since then.

*Water Rates.* On three occasions in the 1970s, the City Council shot down the water rate increases needed to avoid default on the S&WB's debt. The denials forced the S&WB to exercise its legal authority to raise rates unilaterally to meet its existing debt service obligations.<sup>19</sup>

Two of the rejected rate increases also included funding to support the issuance of \$31 million of water revenue bonds approved by voters in 1975.<sup>20</sup> The council rejected the requests, despite that approval. In a contemporary report, BGR noted that the S&WB had sent

the City Council a dozen varying rate proposals. The council, however, had failed to approve any of them. BGR cited numerous reasons for the failure, including disagreements over the rate structure, the council's desire to seek federal funds and the council members' concerns about voter reaction. In 1978, the council approved a 22% increase, enough to allow the issuance of \$6 million of the \$31 million in bonds. Not until 1980 did the City Council approve the larger rate increase needed to support the rest of the bonds – a 70% total increase over five years.<sup>21</sup> After the last of those increases went into effect in 1984, the City Council approved another five-year series of rate increases to meet rising costs and fund additional system improvements.

The S&WB itself delayed implementation of two of the five water rate increases approved by the City Council in 1984. The pressure for delay came from the elected officials on the board, who argued that citizens caught in the city's economic downturn at that time should not bear higher water rates. It took an acrimonious 6-4 vote in 1990, led by the board's appointed members with all three council members in opposition, to implement the fourth increase.<sup>22</sup> The S&WB did not put the fifth and final increase into effect until 2002, approximately 18 years after the council's original approval. The long stretch without raises occurred despite rising operating costs, the advancing age and deterioration of the system, and warnings from the board's financial consultants that additional increases were needed.

The S&WB did not submit a request for a new rate increase until 2005. That request, for a series of increases over five years, was derailed by Hurricane Katrina. When the board voted to resubmit the request to the City Council in 2007, neither the mayor nor the three council members attended the meeting. The council approved the increases later that year.

*Drainage Funds.* Recent efforts to increase drainage system revenue have also met with resistance. In 1998, the City Council deferred indefinitely a request from the S&WB for a drainage service fee.<sup>23</sup> It deferred the request in the hope of improving the chances of passing a separate property service fee for the benefit of the city and public schools (which was roundly defeated). It also cited concerns about the structure of the drainage fee.<sup>24</sup> Eventually, the proposal died due

to the council's failure to act.

In 2010, the S&WB asked the City Council to roll forward the millage rates for the drainage property taxes. All four elected officials were absent from that hastily called meeting. Shortly afterwards, the mayor announced his opposition to the increase.<sup>25</sup> The council rejected the requested roll-forward, despite pressing capital and operating needs, while at the same time approving a roll-forward of general city taxes.

\* \* \*

To summarize, two aspects of the S&WB's governance structure have contributed to the erratic funding pattern that has undermined the adequacy of capital investment at the S&WB. One is the misalignment between responsibilities and powers, which has too often encouraged the City Council to take the easy road rather than address the need for rate increases. The other is the presence of elected officials, and the political considerations that accompany them, on the S&WB.

In the following sections, BGR first discusses the options for addressing the misalignment between responsibilities and powers. It then discusses the advantages and disadvantages of eliminating elected officials from the board. Finally, it suggests other governance changes to improve the board's structure and operations.

## REALIGNING RESPONSIBILITIES AND POWERS

There are two basic options for addressing the misalignment between responsibilities and powers that has hurt the S&WB's performance. One is to consolidate the S&WB into city government, transferring responsibility for the systems to the entity that controls the purse strings. The other is to make the S&WB more autonomous by increasing its authority over its funding sources.

### Consolidation

In the U.S., most water and wastewater utilities are departments of the city or county government. A 2005 survey of 202 utilities providing water or wastewater services found that approximately two-thirds of them were

part of a local government. Another 30% were stand-alone public entities.<sup>26</sup> The remainder took other forms, such as privately owned utilities and cooperatives.

While departmental utilities are still the most common form, independent water agencies have grown in popularity in recent decades. One driver has been a growing preference for special districts. A recent analysis found that the number of special water districts tripled between 1962 and 2002.<sup>27</sup>

Both the departmental and stand-alone structures offer advantages and disadvantages. In some cases, they are two sides of the same coin.

*Independent Utilities.* Independent public utilities have the advantage of a limited mission and the ability to focus exclusively on their business. Those with appointed boards are better positioned than departmental utilities to operate in a businesslike manner, free of political distractions and interference. And, when board terms are staggered, independent utilities enjoy a continuity that encourages a long-term view. This facilitates the development and execution of a capital investment strategy over a long period of time.

By contrast, a utility that is part of a city government must compete with other departments and needs for management's attention and resources. It is also subject to disruption from election cycles and changes in the city's administration.

To the extent that an independent entity controls its own funding sources, it can make decisions based on the objective needs of its systems, rather than the political currents. This positions it to better protect its substantial physical assets through adequate investment. Independence in the funding arena is a key reason for creating a stand-alone utility. Control of funding does, however, carry some risks, specifically the temptation to raise revenue rather than to ferret out waste and inefficiencies.

Disadvantages include the potential duplication of administrative costs. In addition, when the independent entity is an appointed body, the voters lose their ability to influence decisions. While this is necessary to keep politics out of the decision-making process, it also

eliminates a check on waste and inefficiency. Finally, placing responsibility for underground utilities in a separate entity complicates the coordination of infrastructure work with local street repair and reconstruction.

*Departmental Utilities.* The departmental approach generally offers several advantages over independent public utilities:

- It places responsibility for streets and subsurface infrastructure in one entity. This makes it easier to coordinate the maintenance and repair of subsurface infrastructure with other public works functions, especially street projects. Benefits include less disruption of the public right of way, better preservation of streets and cost savings from better coordination of work.<sup>28</sup>
- It facilitates coordination of infrastructure plans with land use plans, providing public officials with a comprehensive understanding of capital needs and opening the way for a more holistic development strategy.
- It eliminates redundancy in local government administration. The utility can use existing administrative and support services provided by the local government.
- It allows for better management of infrastructure emergencies and more efficient deployment of field crews and engineering staff.

The departmental approach also presents a number of risks and disadvantages. A major disadvantage is that departmental utilities must operate within a political environment. They typically must seek approval from elected officials for system funding<sup>29</sup> and are vulnerable to political interference in hiring or contracting decisions. They are also exposed to whatever dysfunction exists in the administrative departments that serve them. Along these lines, a common problem area is information technology.

The departmental structure provides local governments with opportunities to tap into utility funds for unrelated purposes. While segregated enterprise funds provide a strong degree of protection, they are not untouchable. Officials can inappropriately access them by overcharg-

ing the utility department for general and administrative services or by authorizing spending of utility department revenue on services and projects only loosely related to the utility's mission.<sup>30</sup>

Departmental utilities are also subject to the vagaries of the election cycle and the disruption that can accompany the arrival of a new administration and the turnover of department heads. The disruption can derail an infrastructure investment strategy and the implementation of crucial reforms.<sup>31</sup>

*Analyzing the New Orleans Situation.* Consolidating the S&WB into city government would offer three significant benefits. First, consolidation would force elected officials to accept responsibility for the system. The success or failure of the sewerage, water and drainage systems would find a clear focal point: the administration and the City Council.

Second, it would also allow for improved coordination of infrastructure work. Good coordination is very important in a city plagued by extensive deterioration of its street network and subsurface drainage infrastructure.

Third, consolidation would unify the local drainage system, ending the strange division of responsibility that exists in New Orleans.<sup>32</sup> This would allow for comprehensive drainage planning and unified operations. However, it would not solve a root cause of much of the street flooding in New Orleans: inadequate funding for maintenance.

Other advantages commonly associated with consolidation, such as significant gains in efficiency through work force reductions at the crew level, are unlikely to materialize. Public Works, the S&WB's counterpart at City Hall, has approximately 25 employees in functions relating to streets and drainage.<sup>33</sup> Prior to Hurricane Katrina, it had 102.<sup>34</sup> Only four of the remaining employees are engineers, and only 11 work as part of field operations crews. The small number of engineers and other workers and the scale of the post-Katrina reductions suggest that there is not substantial room for further reductions in Public Works' size.

Prior to Katrina, the S&WB had approximately 1,200 employees.<sup>35</sup> As of March 2011, it employed 957. Ad-

ditional study is needed to determine whether opportunities for further staff reductions exist at the S&WB.

There are a number of additional factors that call into question the wisdom of a consolidation.

First, even in smoothly-running organizations, consolidations can strain operational and managerial resources. They become far more difficult to pull off when the organization is struggling.

The current administration has inherited deeply ingrained problems at City Hall. The troubled state of the city's financial management, technology and personnel management systems are prime examples.<sup>36</sup> The dramatic shortcomings in those systems could seriously complicate the full integration of the S&WB's systems and personnel. In addition, folding an entity as large as the S&WB into City Hall could unnecessarily hinder the city's efforts to get its own house in order. The S&WB has nearly 1,000 employees and an operating budget approaching \$200 million; the city has approximately 4,500 city staff and an operating budget of \$800 million.<sup>37</sup>

The operational problems and risks associated with consolidation could be mitigated by making the S&WB a separate operating unit with its own financial, billing and other information technology systems. However, the underlying weaknesses in the merger partner remain a negative factor.

Second, the City of New Orleans has a poor track record when it comes to funding the infrastructure it already controls. Years of inadequate investment have led to the deterioration of many streets. Public Works estimates that it would cost \$1.4 billion to reconstruct poor and failing streets in the city; 30% of that amount is for the related subsurface drainage infrastructure.<sup>38</sup> The city continues to underfund road and drainage maintenance. In 2011, it budgeted a mere \$3.9 million for those purposes. This is about one-tenth of what Public Works has said is needed for regular maintenance. Furthermore, as of May 2011, the city had a backlog of approximately 2,000 work orders for drainage maintenance and repair. The condition of the streets and drains under the city's control, along with the miniscule funds allocated from year-to-year for maintenance, indicate that infrastructure

has not been a high priority of the city for many years.

Third, while folding the S&WB into City Hall would address the current misalignment between responsibilities and authority, it would not address the S&WB's other major governance problem: the undue influence of politics on the process of setting the S&WB's rates and taxes. After consolidation, the city's elected officials would have even greater control over funding decisions for the sewer, water and drainage systems. The political pressures that have affected decision-making by elected officials in the past would remain.

In short, consolidation is a radical institutional change that provides only a partial solution to the S&WB's problems. For that reason, BGR does not consider it the best solution to the S&WB's governance problems.

*Transferring City Drainage Responsibility to S&WB.* Although consolidating the S&WB into city government poses problems, it would make sense to transfer responsibility for maintaining and repairing subsurface drainage from the city to the S&WB, provided a new funding source is found. The S&WB performed this work on behalf of the city until 1997, when funding for it ran out. Neither the city nor the S&WB has available funds today, as state law specifically excludes the city's subsurface drainage from expenditures of the S&WB's drainage tax revenue.<sup>39</sup>

Transferring responsibility for the function would restore the unified approach to managing the local drainage network and enable the S&WB to address drainage needs comprehensively. Its crews could manage the flow of storm water from the catch basins to the pumping stations. The shift would also clarify for the public who is responsible for local drainage problems. One drawback is that it would increase the challenge of coordinating the S&WB's underground pipe repairs with the city's street projects.

### **Increasing the S&WB's Independence**

The S&WB's control over its three major local funding sources – water and sewerage rates and drainage taxes – is limited. Currently, the S&WB can propose changes in water and sewerage rates, but those changes cannot take effect without the approval of the Board

of Liquidation and the City Council. The S&WB lacks taxing authority; taxes are levied on its behalf by the City Council, with the approval of voters. Imposing drainage fees would require the approval of the City Council, the Board of Liquidation and possibly voters. In this section, BGR discusses options for increasing the S&WB's autonomy over each of these sources.

If the S&WB remains a stand-alone entity, the problems caused by the disconnection between the S&WB's responsibilities and the City Council's control of rates can be addressed in a number of ways. Options include:

- Giving the S&WB full or limited control of its water and sewerage rates.
- Improving the City Council's rate approval process.
- Transferring approval authority for water and sewerage rates from the City Council to the state's Public Service Commission.

*Giving the S&WB Control of Water and Sewerage Rates.* The S&WB's lack of control over its funding is unusual among sewer and water authorities. BGR gathered information on 37 other independent water utilities nationwide and found that all but four of them have full control over their rates. Two of the four are regulated by a state public service commission, and the local governing body has the final word on rate changes for the other two. In San Antonio, the city council has approval authority; in Little Rock, Ark., the Little Rock and North Little Rock city councils have the power to disapprove rate changes within a specified period of time.<sup>40</sup>

Sixteen of the 33 utilities with full control of their rates have totally appointed boards. Another four have appointed boards with one ex officio member. In 11 other cases, the public elects all or a majority of the board members. The remaining two boards are comprised solely of elected officials.

Giving a utility control of its rates allows it to set them based on the objective needs of the system, rather than political factors. However, there are downsides to this approach. Giving the system's management the sole authority to raise rates can decrease its incentive to con-

control costs and implement reforms. When the board is appointed, the public has no direct recourse or ability to influence the management decisions that drive rates. Chief among these is the adequacy or extravagance of its capital program. In some cases, 50% to 75% of a water utility's revenue requirements are related to capital projects.<sup>41</sup>

There are ways of ensuring that the public's interests and concerns are heard and that rate increases do not substitute for effective management of expenses. One safeguard is to require the utility to set rates within parameters and processes established in city or state law. For example, Denver's city charter directs its independent water utility to set rates "as low as good service will permit." It further provides that rates may generate sufficient revenue to pay for operations, maintenance, reserves, debt service and system improvements, and that rates be uniform, fair and equitable.<sup>42</sup>

A key safeguard is to set rates in the context of a rational, long-term strategic plan that takes affordability into account.<sup>43</sup> As noted earlier, the major driver of a water utility's revenue requirements is its projected capital needs. Once revenue requirements are determined, the utility should set its rates using a standard methodology.<sup>44</sup>

Another safeguard is to establish a ratepayer advisory committee with representatives of the various classes of ratepayers. Such committees review rate proposals and provide comments to the agency's board of directors. In Denver, for example, the water board has established a 10-member Citizens Advisory Committee to enhance public input on rate proposals, plans and other policy matters.

An alternative to granting a utility full control is to give it the power to increase rates annually by an amount tied to the percentage change in a specified index. Larger increases would require the approval of another entity, such as a public service commission or the local governing body. A number of departmental utilities have this type of authority. BGR did not find any example of an independent water utility with partial rate-making authority.

There are several types of index-based adjustments. Locally, Jefferson Parish uses the change in the broad Consumer Price Index (CPI) to adjust both the monthly

service charge (based on meter size) and the usage fee (based on volume).<sup>45</sup> Miami-Dade County, Fla., adjusts rates based on the change in the portion of the CPI specific to water and sewer services, which tends to rise more rapidly than average consumer prices.<sup>46</sup> Last year, Houston switched from a CPI-based adjustment to one based on the Producer Price Index.<sup>47</sup> Florida's Public Service Commission allows water and wastewater utilities to make adjustments for major categories of operating costs based on a price index tied to the national gross domestic product.<sup>48</sup>

Some jurisdictions allow utilities to adjust rates by passing on increases in certain expenses, such as the cost of electric power.<sup>49</sup> Thirty-six states allow private water systems to do this.<sup>50</sup> BGR came across just one public system, Miami-Dade County, that can pass through increases in the cost of electrical power.<sup>51</sup>

Allowing a limited annual increase based on an index would help to stabilize the S&WB's funding over time. Revenue stability and continuity in rates are some of the essential criteria for a sound rate structure for any utility.<sup>52</sup> Limited rate-making power would not, however, meet the immediate need for larger rate increases to fund critical capital improvements.

*Improving the Council's Rate Approval Process.* The City Council's control of water and sewerage rates has been a serious impediment to steady, rational funding for the systems. Political expediency has too often trumped rational decision making. However, having a third party sign off on rate increases can provide a valuable counterforce to unnecessary increases and exert pressure against waste and extravagance. It also provides a regulatory check on the monopoly pricing of the utility's services. Eliminating the City Council's approval over rates would eliminate this check on the powers of an unelected body.

An alternative to giving the S&WB greater control of its rates would be to improve the City Council's rate approval process. Currently, the council has no formal process in place. In recent years, it has hired a consultant at the S&WB's expense to review proposals for rate increases. But it has no timeline, standards or other policies and procedures to guide it in assessing them. Nor does the City Council regularly review the

condition of the S&WB and the systems for which it is responsible. Thus, it lacks the context that a regulator would normally have.

Rate-making in New Orleans would benefit from a more comprehensive regulatory process. If such a process were implemented, the City Council's Utility Committee would receive and review the S&WB's strategic and financial plans and reports, and monitor the S&WB's performance on a regular basis. This would keep the City Council informed of the needs, condition and performance of the S&WB and provide a better context for dealing with its financial needs.

The City Council's review of rate proposals would also benefit from the adoption of a formal process. That process should incorporate the current practice of obtaining an independent analysis, provide for a formal structure, including hearings, for receiving public comments, and establish clear timelines for review and approval. Such a process would promote more informed, objective consideration of S&WB's requests and prevent the extraordinary delays that have characterized rate-making in the past.

*Public Service Commission Oversight.* Another possibility is to move the approval process for water and sewerage rates from the City Council to the Louisiana Public Service Commission (LPSC).

Currently, 13 state public service commissions regulate some or all municipal water utilities. Six of them also regulate municipal wastewater utilities.<sup>53</sup> The Louisiana constitution allows the LPSC to regulate municipal water and wastewater utilities, but only with voter approval.<sup>54</sup> It does not currently do so.

Only one of the 13 commissions is an elected body (Mississippi); the rest are appointed, providing greater insulation from political considerations.<sup>55</sup> In Louisiana, the public service commissioners are elected on a district basis.

Transferring rate approval authority to the LPSC offers a number of advantages. Unlike the City Council, the LPSC focuses exclusively on utility regulation and brings to the table substantial experience in regulating water and wastewater companies. Although it currently regulates private companies of smaller size and scope

than the S&WB, its staff and regulatory framework could be expanded to handle the S&WB's water and sewerage systems.

The transfer could also dilute the influence of city politics in the regulation of water and sewerage rates. Three of the five LPSC commissioners do not represent any part of Orleans Parish, allowing them to decide issues relative to the S&WB without political pressure. The other two commissioners represent districts that extend well beyond the boundaries of Orleans Parish.

However, while turning responsibility for rate approval over to the LPSC would create a more promising environment for objective decision making, it would not guarantee it. If commissioners from outside of New Orleans made a practice of deferring to their colleagues representing the city, the problem with political decision making could remain.

Transferring rate approval authority to the LPSC has a number of potential downsides. First, without changes to the S&WB's taxing and fee authority or an expansion of the LPSC's powers, it would result in a bifurcated regulatory structure for the S&WB. Since the LPSC does not have regulatory authority over local drainage systems, responsibility for funding decisions relating to the S&WB's drainage system would remain with the City Council. (See discussion below.) Dealing with two regulatory bodies could increase the S&WB's costs, while creating new holes in the oversight. Neither regulator would be evaluating the S&WB as a whole.

Another disadvantage is that the shift in regulation from New Orleans to Baton Rouge would make it more difficult for citizens and businesses to voice their concerns in the water and sewerage rate-making process. Convincing voters to shift control over their water and sewerage rates from their local council members to a Baton Rouge-based body would be a daunting task.

\* \* \*

A more practical solution to the rate-making problem would be to give the S&WB partial control over water and sewerage rates and to establish a formal process for the City Council's consideration of larger rate increases. The S&WB's authority to raise rates could be

limited by reference to an appropriate index, take the form of pass-through adjustments for specific cost factors, or combine the two approaches.

Greater rate control should come with adequate public safeguards. The S&WB should develop its revenue requirements in the context of long-term strategic, capital and financial plans, and devise its rates using a standard methodology.

BGR is aware that its proposal to give the S&WB partial control of its rates differs from the standard practice for independent utilities. It is also aware that giving the S&WB partial control would go only so far in rectifying the misalignment between powers and responsibilities. Limited rate and fee increases would not, for example, provide the S&WB with adequate resources to address the massive and immediate funding needs facing it. Partial rate-making authority would, however, provide it with a mechanism for funding ordinary maintenance, operations and capital repairs on an ongoing basis once the major needs are addressed. In that regard, we note that the changes that BGR is proposing would take time to implement and should not interfere with the important task of addressing immediate funding needs.

*Other Limitations on the S&WB's Funding.* Unlike its sewer and water systems, the S&WB's drainage system is funded by taxes. The S&WB cannot raise or impose taxes without the cooperation of the City Council. It cannot seek voter approval for a new tax unless the City Council calls an election for that purpose. While the S&WB can propose a roll-forward in millage rates, the power to roll forward resides with the City Council.

Options for increasing the S&WB's control over drainage funding include making the S&WB its own taxing authority. As the taxing authority, the S&WB could seek voter approval for new property taxes without going through the City Council. It could also roll forward such taxes.<sup>56</sup> The State Legislature could give the S&WB the necessary power by establishing a parish-wide taxing district for drainage, and designating the S&WB as its governing body and taxing authority.

However, placing taxing authority in the hands of the S&WB would further fragment local control over the city's limited taxing capacity. The S&WB could tap that

capacity without considering the broader government funding needs in the city. Furthermore, it is unusual for water utilities to have taxing authority at all. Only eight of the 37 independent utilities reviewed by BGR have the power to tax. None of those imposed taxes for drainage. BGR notes that only five of the 37 independent utilities reviewed provide any drainage services. Three of them fund drainage through their sewerage rates, while the other two impose a separate fee.

Another funding option is the imposition of a drainage fee. That funding mechanism has a significant advantage over a property tax. If carefully structured, it would spread the cost across a broader base of property owners, including those who are exempt from property taxation.<sup>57</sup>

Currently, state law allows the S&WB to impose a drainage fee, but requires the approval of both the City Council and the Board of Liquidation.<sup>58</sup> The city's charter gives the council the right to impose fees.<sup>59</sup> Changes to both state law and the charter would be needed to allow the S&WB to act on its own without the cooperation of the City Council.

State law also requires voter approval to impose a drainage fee. However, the city's home rule charter authorizes the City Council to impose certain fees and service charges without voter consent. The charter provision might trump the statutory requirement for voter approval, but the issue has not been considered by the courts. The matter is further complicated by ambiguities in the scope of the charter provision.

Allowing the S&WB to impose drainage fees without the consent of the City Council and voters would substantially expand the S&WB's control over its drainage funding. However, as with water and sewerage rates, full control could create a disincentive to control costs and make reforms. An alternative would be to allow the S&WB to make limited upward adjustments once a fee has been imposed, and require council approval for larger increases. This would require a charter amendment. If the City Council retains any authority over fees, it should establish a formal process for considering fee requests.



## ELIMINATING ELECTED OFFICIALS FROM THE S&WB

Reforming the rate-making process would help to address one of the major governance problems that has contributed to the underfunding of the S&WB. However, the second governance problem – the presence of elected officials on the S&WB board of directors – must also be addressed.

BGR took an in-depth look at the governance structure of 10 well-regarded independent utilities. Seven of them are composed exclusively of appointees. Only three have an ex officio member, and in all three cases it is the mayor. No members of the local governing body (e.g., a city council) sit on any of the 10 boards. All of the other members are appointed.

Appointments are made by the mayor, the city council or other local governing body, or, most commonly, by the mayor with council approval. Usually, the officials make the appointments without assistance from special nominating entities. One exception is Washington, D.C., which includes five members recommended by suburban jurisdictions and appointed by Washington’s mayor.<sup>60</sup> The other is El Paso, Texas, which relies on a selection committee consisting of the board and additional members appointed by the city council.<sup>61</sup>

In New Orleans, the board consists of the mayor, three council members, two members of the Board of Liquidation appointed by the mayor on the recommendation of that board, and seven citizen members appointed by the mayor with the advice and consent of the City Council. Prior to this year, two of the three council members had to be the council members at large. Recent changes in state law and the city charter have reduced the required number of council members at large to one.

Louisiana law requires that a citizen be appointed from each of the five council districts. The other two are appointed from the city at large. Each citizen member must be a registered voter in the area from which he is appointed and a resident of the area for at least two years prior to appointment.<sup>62</sup>

In making appointments, the mayor and the City Coun-

cil must also follow a general directive to consider the demographic diversity of the city’s population, so that the composition of the boards, commissions or other entities acting on the city’s behalf reflects the diversity of its population.<sup>63</sup> The directive is set forth in the city code.

Earlier in this report, BGR identified the role of politics as a key impediment to responsible stewardship of the S&WB. Elected officials have at times over the years hindered the proper funding of the organization by opposing rate increases at the board level. At other times, they have shirked their responsibilities by not participating in key funding decisions.

There are other problems with having elected officials serve on the S&WB. First, they can exert disproportionate influence. It is difficult for some citizen appointees to act independently when the person who appointed them also sits on the board. In addition, the mayor, as the S&WB’s president, also controls all appointments to the board’s four standing committees (finance, operations, infrastructure and executive). The mayor’s power to assign and reassign committee members is significant because the committees per-

### NOTE ON METHODOLOGY

BGR selected the 10 utilities based on interviews with industry experts and other research. Each utility has a Standard & Poor’s bond rating of AA- or higher.<sup>64</sup> Each is a stand-alone utility governed by a board of directors. BGR obtained data on those utilities through a review of their enabling legislation, official statements for recent bond issues, their websites and other materials, and interviews with staff. The utilities are located in Birmingham, Ala.; Boston; Chapel Hill, N.C.; Denver; Des Moines, Iowa; El Paso, Texas; Jacksonville, Fla.; Louisville, Ky.; San Antonio; and Washington, D.C.<sup>65</sup>

form much of the board's work.<sup>66</sup>

Second, the political relationships among the elected officials can work against good governance. For example, a council member may hesitate to disagree with the mayor on an S&WB issue if he is seeking the mayor's support on an unrelated matter. Alternatively, when elected officials vote as a bloc, they can exert disproportionate influence. Both cases inhibit robust discussion of important issues affecting the board.

Third, there is the ever-present risk of elected members raising money from agency contractors to fund their campaigns. At the least, the presence of elected officials on the board (which approves all contracts and most change orders) raises the perception of pay-to-play political influence in the agency's contracting decisions.

Fourth, elected officials on the S&WB generally have poor attendance records. Several best practice guidelines for corporate governance indicate that board members should attend at least 75% of meetings of the board and the committees on which they sit.<sup>67</sup> In the period from January 2007 to June 2011, only two council members achieved that level of attendance at the monthly board meetings. Attendance rates for other elected officials ranged between 38% and 63%. At the committee level, attendance was even worse, with attendance rates of 12% to 50% logged by the three council members serving on the S&WB's busiest committees (finance and operations, and infrastructure) during the four-and-a-half year period reviewed.<sup>68</sup>

The attendance problem has not gone unnoticed by the elected officials themselves. This year the legislature amended state law to allow the mayor, if he is unable to attend a meeting, to send an unclassified member of his administration in his place.<sup>69</sup> The year before, the law was changed to require only one at-large council member, rather than both, to serve on the S&WB. This move was designed to give the council more flexibility in selecting members who are interested in the S&WB and can make the necessary time commitment.

Having elected officials on the board offers certain advantages. In a situation like New Orleans, where the council has the final say on rates, it gives some members of the body a detailed knowledge of the system and

its needs. With their place at the table, they can keep pressure on the agency to seek cost savings and other efficiencies. Their presence on the board also provides the public with a more direct voice in the utility.

Overall, however, the officials' presence on the S&WB's board undermines the advantages of the board's separation from city government. Removing the four elected officials from the S&WB and making it an all-appointed board would reduce the potential for politically driven decisions. The mayor and council would continue their roles in appointing the board members.

## OTHER GOVERNANCE CHANGES

BGR has identified the misalignment between responsibilities and powers and the presence of elected officials on the board as the S&WB's two most serious governance problems. This is not to say that they are the only ones.

There is significant room for improvement in other areas, including board structure and responsibilities. In this section, BGR discusses a number of possible structural reforms, including changing the size of the board and the length of terms, imposing term limits and requiring some citizen members to have experience in relevant areas. It also discusses problem areas in the board's operations, including its role in contracting and its oversight of management.

Addressing the problems in these areas is important regardless of whether the S&WB's rate-making authority is increased. It becomes imperative if the powers of the S&WB are expanded.

### Addressing Problems in Board Structure

*Changing the Board's Size.* Removing elected officials from the board would reduce the board's size from 13 to nine members. The reduction in size could improve the board's general effectiveness. At 13 members, the board is nearly twice the median size (seven members) of the 10 boards reviewed. Those boards range in size from three to 11 members, with most consisting of either five or seven members. The two largest include representatives of suburban jurisdictions served by the

systems. The S&WB's board is also significantly larger than the average public company board.<sup>70</sup>

A board should be large enough to bring together sufficient experience and expertise to handle the workload, reach consensus and carry out its role effectively. If the board is too large, it can become unwieldy. It is easier for some directors to avoid pulling their own weight, and it is more difficult to reach consensus. On the other hand, if a board is too small, members may suffer from "groupthink" and forget their responsibility to be constructive skeptics.<sup>71</sup>

At the S&WB, there has not been a board meeting in the past four-and-a-half years that all 13 members attended, undermining the vision of the board's broad representation.<sup>72</sup> The highest attendance was 11 members, and the average was 8.2 members. The board also had recurring trouble reaching a quorum of seven members. There were five times – once each year – when it could not reach a quorum and had to defer its business actions until the next month. In at least one other case, it lost its quorum when a member left the meeting prior to the consideration of committee reports.

Reducing the board from 13 to nine members by removing the elected officials would make the board less unwieldy and, given the weak attendance history of elected officials, make it easier to achieve quorums.<sup>73</sup>

*Reducing Members' Terms.* Appointed members of the S&WB serve nine-year terms and have no term limits.<sup>74</sup> The four elected officials are obviously limited by their terms in office. The two seats for the Board of Liquidation tend to turn over more often than once every nine years, as that board follows a policy of asking the mayor to appoint its two most junior appointed members to the S&WB.

Under the city charter, the appointing authority may remove a member of a board only for reasonable cause set forth in writing.<sup>75</sup> The charter also gives the appointee the right to request a public hearing before the City Council. It then takes a majority vote of the council to remove the appointee.

Appointed board members at other public water utilities have significantly shorter terms than the S&WB's.

For the 10 boards that BGR reviewed, the terms of appointed members range from three to six years; the median is 4 years.

Shorter terms allow for regular evaluation of individual board members, usually as part of a reappointment process. Nine-year terms are too long to permit regular evaluation of members' performance.

While the S&WB's lengthy terms may offer some political protection for appointees, they also provide the opportunity for a board member to become entrenched and politically powerful. This is exemplified by the case of Benjamin Edwards, who served approximately 20 years on the board until he resigned in 2009 after his indictment on federal charges of taking kickbacks from S&WB contractors.<sup>76</sup> Mr. Edwards ultimately pled guilty and was sentenced to 22 years in federal prison in 2010.

The terms of appointed S&WB members should be reduced from nine years to four years to allow for reevaluation of their performance in the context of a reappointment process. The new four-year terms should be staggered to establish some continuity in board membership and insulation from election-cycle politics. All of the 10 boards reviewed by BGR have staggered terms. The S&WB's terms are not currently staggered, and state law is silent on the matter.

Formal term limits would provide additional protection against an individual appointee becoming too entrenched. Four of the 10 boards reviewed are subject to legal limits of two consecutive terms, while another two follow an unofficial practice of a two-term or three-term limit.<sup>77</sup> The limits add up to eight years in three cases and 12 years in the other three.

Downsides to term limits are that they can unnecessarily deprive citizens of the services of a good board member and strip the utility's board of its institutional knowledge. New members have a steep learning curve in the highly technical world of water utilities. On balance, however, it would be advantageous to have some limit. A limit of three consecutive terms would guard against entrenchment of individual members while giving members ample time to learn and guide the utility.

*Setting Qualifications Based on Experience.* At present, appointees to the S&WB do not have to meet any experience or expertise requirements. Attempts in 2008 and 2010 to impose professional qualifications on five of the seven citizen members and establish a nominating committee process failed in the State Legislature.<sup>78</sup>

Best practices in corporate governance indicate that a board should have a mix of relevant expertise. The desired skills should be carefully articulated and considered when making appointments.<sup>79</sup> In the context of public water utilities, board members should be appointed based on their qualifications, not on their political connections.

Only two of the 10 boards that BGR reviewed are subject to experience requirements. In one case, the requirements, which apply to two of three board members, are spelled out in state law. In the other, the by-laws stipulate the desired areas of expertise for appointed board members: engineering, financial management, general business management, environmental or health, consumer or citizen advocacy and communications, public administration or education. Despite the lack of legal requirements for the other boards reviewed, all or some of their members have professional backgrounds or other relevant experience.

While the law governing the S&WB does not require specific experience, the majority of its current appointed members have relevant experience. Among them are two accountants, an architect, an engineer and an attorney with engineering experience.

Formally establishing experience requirements for some members in statute would help to ensure that the board continues to have the necessary mix of expertise. The requirement should be crafted broadly to provide the mayor with sufficient flexibility to tap the best talent available at a given time. Rather than dictating a specific set of qualifications, the law should require that most of the nine appointed members have extensive experience in one or more of the following areas: finance, accounting, business administration, engineering, law, information technology or public health. The mayor would have the flexibility to appoint multiple members from a single category. The other members would not be subject to those requirements.

## Addressing Problems in Board Operations

The current board has a number of operational problems that should be addressed. These include excessive involvement in contracting and the absence of any formal process to evaluate the S&WB's top management.

*Reducing the Board's Involvement in Contracting.* The board, through its committees, spends a disproportionate amount of time evaluating and approving contract-related matters, leaving little time for financial and other important issues. A board of directors should focus primarily on setting policy and strategy; hiring, compensating and holding management accountable; approving budgets and business plans; approving material transactions outside of the ordinary course of business; providing oversight of the compliance with laws, regulations and board policies; and setting and enforcing a high standard for ethical conduct.<sup>80</sup> It should play only an oversight role in day-to-day operations, including most contracts. This allows professional management to make good business decisions, free of the preferences of board members.

The S&WB's two busiest committees by far are its finance and operations committees.<sup>81</sup> Both spend most of their time reviewing and approving matters related to contracts. The finance committee reviews and approves all advertisements for bids, requests for proposals, contracts, contract amendments and significant bid change orders.<sup>82</sup> It also hears all bid appeals. The operations committee also reviews contracts, but focuses on the contractor's use of subcontractors identified through the agency's Disadvantaged Business Enterprise (DBE) program.<sup>83</sup>

The volume of contracting matters eats up valuable time that would be better spent delving into financial matters, such as budgets and audits, or operational matters, such as customer service. In July 2011, for example, the finance committee spent two hours reviewing and approving contracts, then lost its quorum before it could consider any financial items on the agenda. At its worst, the micromanagement of contracts provides board members, whether elected or appointed, with an opportunity to corrupt contracting decisions.

Other boards' involvement in contracting decisions varies widely. Some boards approve all contracts above

a relatively low threshold, such as \$40,000.<sup>84</sup> In other cases, the threshold is set at a much higher level. In Washington, D.C., board approval is required only for contracts of \$1 million or more and contract modifications of \$500,000 or more.<sup>85</sup> In Louisville, board approval is required for initial contracts valued at more than \$1.5 million and any change orders greater than \$250,000.<sup>86</sup> In Jacksonville, the board has delegated most contracting authority to the staff.

The board should focus its role in contracting primarily on broad issues of policy and oversight. Rather than delving into the specifics of every contract, it should establish appropriate policies and goals to guide management's contracting processes, devise appropriate goals for the DBE program, and monitor management's performance and adherence to board policies. It should restrict its review to extraordinary contracts, such as significant privatizations.

*Evaluating Top Management.* Another problem with the board's operation is its failure to evaluate the executive management on a regular basis.<sup>87</sup> In recent years, the board has not performed any formal evaluations of management. Its executive committee, which is responsible for personnel matters, held no meetings from 2007 to 2010 and had not done any evaluation through June 2011. Those familiar with the board's operations in the years prior to Hurricane Katrina told BGR they could not recall any formal management review during that period.

Best practices call for an annual evaluation of top management by the board of directors. This evaluation is based in part on certain performance objectives established by the board in accordance with its strategic plan. A committee of the board may perform the review.

Almost all of the 10 boards reviewed require an annual evaluation of their chief executive officers. In at least two cases, the board limits the executive's contract to a one-year term and evaluates his performance in the context of an annual contract renewal.

Evaluating top management should become an annual priority for the S&WB's board of directors. The evaluation should include a review measuring performance against objectives set forth in strategic and financial plans.

## CONCLUSION AND RECOMMENDATIONS

The chronic underfunding of the S&WB over the past several decades has created a monstrous problem. The history of water and sewerage rates reflects long periods of stagnation, followed by spikes in rates to avoid crises. The failure of certain fee and tax proposals for drainage has led to the erosion of drainage revenue. The underfunding of the three systems has contributed to the buildup of billions of dollars in capital needs. According to the S&WB, the city's residents will have to provide \$1 billion to help meet those needs over the next decade.

Two key governance problems have contributed to the erratic, crisis-driven approach to funding the water, sewerage and major drainage systems.

One is the misalignment between responsibilities and powers. The S&WB must build, operate and maintain the systems, but it does not control its financial destiny. The City Council has the final say in funding matters, and over the years it has often bowed to political pressure to keep rates low.

The other governance problem is the intrusion of political pressure into the S&WB from elected officials on the board. Their opposition to rate and tax increases has discouraged the board from making new proposals.

BGR considered addressing the misalignment between responsibilities and powers by folding the S&WB into city government, but ultimately decided against that route. While consolidation would address the misalignment between responsibilities and powers, it would not address the second major governance problem: the undue influence of politics in the process of setting the S&WB's rates and taxes. Given the magnitude of the systemic problems at City Hall, the role elected officials have played in holding the S&WB back and the city's poor track record on funding the infrastructure it already controls, consolidation is clearly not the optimum solution.

It would make sense, however, to transfer the responsibility for maintaining and repairing the city's subsurface drainage infrastructure to the S&WB. The current division of responsibility between Public Works and the S&WB is unusual and ineffective. Placing respon-

sibility for the entire drainage system with the S&WB would allow it to oversee all essential local drainage infrastructure, although a new source of funding for maintenance and repair would still be needed.

Addressing the misalignment between powers and responsibilities should begin with making the S&WB a more independent entity. This approach would provide greater insulation from city politics and help to keep the board focused on the needs of its systems.

To function effectively, the S&WB should be given the flexibility to increase its water and sewerage rates each year by a limited amount tied to an appropriate index or other measure. This would provide the S&WB with a mechanism for keeping up with increases in operating costs and funding maintenance and capital repairs on an ongoing basis. But larger increases, such as those now needed to begin addressing capital needs, should continue to go through the City Council for approval. This would provide a check on the power of the appointed board. However, the council should not take a political or undisciplined approach; rather, it should establish a more comprehensive regulatory approach and adopt a formal process to guide its analysis, review and approval of the S&WB's rate requests.

BGR considered whether the S&WB should have the power to levy taxes and to impose fees to support the drainage systems. It decided against making a recommendation to place taxing authority in the hands of the S&WB at this time. While making the S&WB its own taxing authority would better align responsibilities and powers, it would further complicate much needed efforts to prioritize the community's needs and bring coordinated tax propositions to voters.

With respect to drainage fees, BGR concluded that the power to impose them should remain with the City Council. However, the S&WB should have the power to make limited increases to fees, if and when they are imposed. As in the case of rate approvals, the council should develop a good process for evaluating requests for fees.

The increase in the S&WB's financial independence should be accompanied by the removal of the four elected officials from the S&WB's board of directors. This would

de-politicize the board's process of proposing rate and tax increases. It would also remove the political relationships and campaign finance pressures that can skew the board's decision making. The remaining nine members should serve shorter terms, with evaluation of their performance as part of a reappointment process. They should be subject to term limits. The majority of its members should meet experience qualifications specified in law. Finally, the board should become more oriented toward policy. It should stop micromanaging S&WB contracts and start regularly evaluating the agency's top management.

## Recommendations

To better align the S&WB's responsibilities with funding authority and improve the City Council's decision making:

- The State Legislature should amend state law to authorize the S&WB to increase water and sewerage rates annually by an amount tied to a suitable index or other measure, without City Council approval. State law and the city charter should be amended to allow limited increases for drainage fees.
- The City Council should consider requests for larger increases using a formal review process, which at a minimum should provide for independent analysis of the requests, appropriate opportunities for public comment and clear timelines. The City Council should also adopt a formal process for considering S&WB requests to levy taxes and fees.
- The City Council should develop a comprehensive, ongoing process for regulating the S&WB, which includes reviewing the S&WB's strategic and financial plans and reports, and regularly monitoring the S&WB's performance.

To increase the effectiveness of the S&WB board of directors:

- The State Legislature should amend state law to remove the mayor and City Council members from the board, reducing it from 13 members

to nine. The City Council should initiate a corresponding charter amendment.

- The State Legislature should further amend state law to:
  - Reduce the terms of board members from nine years to four years and stagger the new terms.
  - Limit members to three consecutive terms.
  - Require that seven of the nine members of the board have extensive experience in one or more of the following areas: finance, accounting, business administration, engineering, law, information technology or public health.
- The S&WB's board should limit its role in the agency's contracting primarily to broad issues of policy and oversight. It should establish appropriate policies and goals to guide management's contracting processes, and set goals for the DBE program. It should monitor management's performance toward those goals and adherence to board policies. It should restrict its review of individual contracts to extraordinary ones, such as significant privatizations.
- The S&WB board should also establish an annual process for evaluating the performance of the executive management, including but not limited to measuring performance against objectives identified in strategic or financial plans adopted by the board.

To improve the upkeep of local drainage:

- The city should transfer responsibility for the maintenance and repair of its subsurface drainage from the Department of Public Works to the S&WB.
- The city and the S&WB should develop a new funding source for subsurface drainage.

## ENDNOTES

1 Behrman, Hon. Martin, Mayor of New Orleans, “New Orleans: A History of Three Great Public Utilities, Sewerage, Water and Drainage, and their influence upon the Health and Progress of a Big City,” paper read before convention of League of American Municipalities, Milwaukee, Wis., September 29, 1914.

2 The S&WB sold only 25.4% of the 54 billion gallons of river water it pumped, treated and distributed last year. Another 3.2% of the water was provided free of charge to public entities. The balance, 71.4%, represents “unaccounted for” water. Sewerage & Water Board, *Comprehensive Annual Financial Report for the Year Ended December 31, 2010*, p. IV-8. While this includes some unmetered use for putting out fires, cleaning streets and buildings, and flushing sewers, drains and gutters, most of it simply leaks into the ground. The norm for leakage in U.S. systems is 15% or less. Unfortunately, the S&WB must produce much more water than it sells in order to maintain sufficient water pressure in the leaky system.

3 Figure reflects the total sewerage capital program related to the consent decree for 2011 to 2015, as amended by the S&WB on June 15, 2011. The decree, originally signed in 1998, settled a federal lawsuit alleging violations of pollution control regulations in the east bank sewer system. Work to comply with the consent decree was interrupted by Hurricane Katrina. Following the storm, the S&WB’s schedule for completing the work was revised.

4 Krupa, Michelle, “No easy fixes for S&WB’s power plant,” *The Times-Picayune*, January 18, 2011.

5 Agreement between City of New Orleans, Department of Streets, and Sewerage and Water Board of New Orleans, July 1, 1992, p. 2. This agreement represents a revision of the original agreement reached in 1987.

6 Department of Public Works, *2011 Budget Offer: Roadway Maintenance*. As used in this report, the local drainage system excludes drainage built and maintained by state and federal entities.

7 BGR calculation based on mileage of drainage pipes and canals using data supplied by the S&WB and Public Works.

8 *State ex rel. Saunders v. Kohnke, et al.*, 109 La. 838, 33 So. 793 (La. 1/19/1903).

9 *Save Our Parkways, Inc., et al. v. City of New Orleans, et al.*, 357 So.2d 57 (La. App. 3/14/1978).

10 The Board of Liquidation recommends from among its six appointed or “syndicate” members, rather than its three other, ex officio members, who are the mayor and the two council members at large.

11 S&WB, *Comprehensive Annual Financial Report for the Year Ended December 31, 2010*, p. II-23.

12 State law provides that the S&WB “shall fix the rates” to be charged to water and sewerage system customers, but the rates “shall not become effective unless and until approved” by the Board of Liquidation and the City Council. La. R.S. 33:4096 (A) and 33:4121 (A).

13 The authority to raise rates without council approval is provided in La. R.S. 33:4096 (D) and (E) for water rates and 33:4121 (D) and (E) for the sewerage rates.

14 At the time, the S&WB imposed only “water” rates, which generated revenue for operating, maintaining and funding capital improvements to the water, sewerage and drainage systems.

15 U.S. Environmental Protection Agency, et al., *Effective Utility Management: A Primer for Water and Wastewater Utilities*, June 2008, p. 5; Chesnutt, Thomas W., and Janice A. Beecher, *A&N Technical Services Inc. White Paper: Revenue Effects of Conservation Programs: The Case of Lost Revenue*, October 2004, p. 7.

16 Raftelis, George, “Introduction to Water and Wastewater Finance and Pricing,” in Raftelis, George, *Water and Wastewater Finance and Pricing: A Comprehensive Guide*, 3<sup>rd</sup> ed. (Boca Raton, Fla.: Taylor & Francis Group, 2005), p. 2.

17 Official Statement, City of New Orleans, Louisiana, Sewerage Service Revenue Bonds, Series B, and Sewerage, Water and Drainage Serial Bonds, Series of 1976, October 27, 1976, p. 12.

18 Grady, Bill, and Joe Massa, “Reluctant OK Given Sewer Service Hike,” *The Times-Picayune*, May 11, 1979.

19 “Water Rate Boost Scored,” *The Times-Picayune*, December 8, 1971; BGR, *BGR Urges Water Rate Increase*, 1977.

20 At that time, state law required voter approval of any water revenue bond issue that would cause the annual debt service to exceed \$1,750,000 and result in an increase in water rates. This requirement no longer exists.

21 The five-step increase consisted of annual increases of 15% in the first four years and 10% in the fifth year. It was an alternative to a single increase of 53%. Black & Veatch Consulting Engineers, *Report on Revenue Requirements, Costs of Service, and Rates for Water Service*, prepared for the Sewerage & Water Board of New Orleans, Louisiana, November 21, 1979, Appendix A.

22 Warner, Coleman, “Water rates to increase,” *The Times-Picayune*, March 15, 1990.

23 DelGuzzi, Kristen, “City Council to put off sewer, drain rate increases,” *The Times-Picayune*, October 15, 1998.

24 DelGuzzi, Kristen, “S&WB increases face further delay,” *The Times-Picayune*, February 6, 1999.

25 Krupa, Michelle, “S&WB wants millage increase,” *The Times-Picayune*, November 4, 2010.



- 26 Lafferty, Angela K., and William C. Lauer, *Benchmarking Performance Indicators for Water and Wastewater Utilities: Survey Data and Analyses Report* (Denver: American Water Works Association, 2005), p. 27.
- 27 Mullin, Megan, *Governing the Tap: Special District Governance and the New Local Politics of Water* (Cambridge, Mass.: Massachusetts Institute of Technology, 2009), pp. 4 and 19.
- 28 Bakker, Karen, *Good Governance in Restructuring Water Supply: A Handbook*, prepared for the Federation of Canadian Municipalities and the Program on Water Issues at the University of Toronto's Munk Centre for International Studies, 2003, pp. 9-10.
- 29 BGR found that the local governing body has the final say on rates in 45 of the 55 largest U.S. cities served by a departmental water utility. In another case, the local governing body serves as the department's governing board. In the other nine cases, the utility needs the approval of an appointed governing board (4), a state public service commission (3), a department head, or a special fiscal policy board.
- 30 Rouse, Michael, *Institutional Governance and Regulation of Water Services: The Essential Elements* (London: IWA Publishing, 2007), p. 110; Pageler, Margaret, *Optimizing Municipal Water Utility Governance: The Seattle Case*, presentation to 3<sup>rd</sup> World Water Forum, Kyoto, Japan, 2003.
- 31 Rouse, Michael, p. 25; Baietti, Aldo, *Characteristics of Well-Performing Public Water Utilities*, Water Supply & Sanitation Working Notes, published by the Water Supply and Sanitation Sector Board of the Infrastructure Network of the World Bank Group, Note No. 9, February 2006, p. 25.
- 32 BGR examined who maintains and repairs subsurface drainage in 30 other jurisdictions. In all but one case, the responsibility is vested with the entity responsible for the larger drainage works in the jurisdiction. In 26 of the jurisdictions, the city or county government controls all drainage. In the other four cases, a separate agency controls the larger drainage works. Three of those agencies also maintain and repair subsurface drainage.
- 33 City of New Orleans, *2011 Adopted Operating Budget*, pp. 244-246, and information provided by Public Works, October 14, 2011. The personnel figures exclude Public Works' parking division, which handles parking tickets and meters, and the traffic control division.
- 34 The total reflects personnel figures in Public Works' adopted 2004 budget.
- 35 Official Statement, City of New Orleans, Louisiana, Sewerage Service Revenue Bonds and Sewerage Service Bond Anticipation Notes, Series 2004, December 2, 2004, p. 15.
- 36 The Public Strategies Group, *A Transformation Plan for City Government*, prepared for the City of New Orleans, March 1, 2011, p. 5.
- 37 City of New Orleans, *2011 Adopted Operating Budget*.
- 38 Estimate by Public Works. For a more detailed discussion on the department's capital needs, see BGR, *The Price of Civilization: Addressing Infrastructure Needs in New Orleans*, August 2010, p. 3.
- 39 According to state law, the S&WB's current drainage taxes are limited to the operation, maintenance, construction and extension of its drainage system, and cannot be spent on the city's subsurface drainage. This makes the S&WB unable to perform subsurface drainage maintenance and repair, as it agreed to do in a 1987 agreement with the city. At that time, the S&WB used revenue from an existing property tax. That tax expired at the end of 1991, leaving no recurring funding source available for the work. According to the S&WB, its subsurface drainage maintenance and repair work finally ground to a halt in 1997. The S&WB has estimated that resuming that level of maintenance and repair work today would cost approximately \$8.5 million a year. A more aggressive preventive maintenance program would cost between \$35 million and \$50 million a year.
- 40 BGR identified 27 of these utilities through its review of water providers in the 125 largest U.S. cities, and one smaller utility on the recommendation of an industry expert. Nine others responded to a BGR survey distributed to members of the Association of Metropolitan Water Agencies.
- 41 Davis, Frank, "Identification of Revenue Requirements," in Raftelis, George, *Water and Wastewater Finance and Pricing: A Comprehensive Guide*, 3<sup>rd</sup> ed. (Boca Raton, Fla.: Taylor & Francis Group, 2005), p. 194.
- 42 Charter of the City and County of Denver, Art. X, Secs. 10.1.9 and 10.1.10.
- 43 Wexelbaum, Gerald, "Capital and Financial Planning for Water and Wastewater Utilities," in Raftelis, George, *Water and Wastewater Finance and Pricing: A Comprehensive Guide*, 3<sup>rd</sup> ed. (Boca Raton, Fla.: Taylor & Francis Group, 2005), p. 10.
- 44 For instance, the American Water Works Association has developed a standard methodology for setting water rates, and the Water Environment Federation has developed one for sewerage rates.
- 45 Jefferson Parish Code of Ordinances, Sec. 27-47 and 27-196. The annual adjustment to these charges equals the 12-month percentage change in the U.S. City Average for All Items in the Consumer Price Index for All Urban Consumers (CPI-U) as compiled by the U.S. Bureau of Labor Statistics.
- 46 Official Statement, Miami-Dade County, Fla., Water and Sewer System Revenue Bonds, Series 2010, February 23, 2010, p. 34. From 1996 to 2008, charges for the average residential customer

rose by 4.21% annually for water and 4.39% annually for wastewater, both greater than the annual average increase in CPI during the period of 2.87%. American Water Works Association and Raftelis Financial Consultants, Inc., *2008 Water and Wastewater Rate Survey*, 2009, p. 5.

47 Fitch Ratings, *Fitch Rates Houston, Texas' Combined Utility System First Lien Revs "AA-"; Outlook Stable*, press release August 8, 2011. The Producer Price Index measures the average change over time in the selling prices received by domestic producers for their output. U.S. Bureau of Labor Statistics, [www.bls.gov/ppi](http://www.bls.gov/ppi).

48 The Florida Public Service Commission uses the U.S. Department of Commerce's average Gross Domestic Product Implicit Price Deflator Index for the preceding two years.

49 The price index and pass through adjustments are authorized by Fla. Stat. Sec. 367.081(4). Florida Public Service Commission, *Price Index and Pass Through Rate Adjustments for Water and Wastewater Utilities*, May 2009.

50 National Association of Water Companies, *Pass-Through Adjustments Survey*, 2010.

51 Miami-Dade County, Fla., Code of Ordinances, Sec. 32-64 (b).

52 Rubin, Scott, J., *What Does Water Really Cost? Rate Design Principles for an Era of Supply Shortages, Infrastructure Upgrades, and Enhanced Water Conservation*, prepared for the National Regulatory Research Institute, July 2010, p. 3.

53 Michigan State University Institute of Public Utilities, *Commission Jurisdiction Survey for 2011*.

54 La. Const. Art. IV, Sec. 21 provides that the LPSC "shall regulate all common carriers and public utilities," with the exception that it "shall have no power to regulate any common carrier or public utility owned, operated, or regulated on the effective date of this constitution by the governing authority of one or more political subdivisions, except by the approval of a majority of the electors voting in an election held for that purpose; ...." The city does not operate the S&WB, but it appears to be the owner under La. R.S. 33:4078, which states that title to all the public works constructed by the S&WB and all the property it acquires "shall be vested in the city of New Orleans."

55 BGR analysis of Michigan State University Institute of Public Utilities, *Commission Jurisdiction Survey for 2011 and Commissioner Demographics 2011*, March 1, 2011, Exhibit 5.

56 The current drainage taxes, as approved by voters, do not provide specific authorization for the S&WB to levy the taxes, nor for the City Council to transfer all or part of its taxing authority to the S&WB.

57 For a more detailed discussion of drainage fees, see: BGR, *The Nonprofit Margin: Addressing the Costs of the Nonprofit Exemp-*

*tion in New Orleans*, March 2011, pp. 13-15.

58 La. R.S. 38:90.17 (A)(1)(a).

59 Home Rule Charter of the City of New Orleans, Sec. 3-101(2).

60 D.C. Code Sec. 34-2202.04.

61 Bylaws of the El Paso Water Utilities Public Service Board of El Paso, Texas, Sec. 7; Official Statement, City of El Paso, Texas, Water and Sewer Revenue Refunding Bonds, Series 2011, July 13, 2011, p. 16.

62 La. R.S. 33:4071.

63 City of New Orleans, Code of Ordinances, Sec. 2-86.

64 In contrast, the Standard & Poor's ratings for the S&WB are barely investment grade at BB for the water system and BBB- for the sewerage and drainage systems.

65 Respectively, the utilities are: the Birmingham Water Works Board; Boston Water and Sewer Commission; Orange Water and Sewer Authority; Denver Water; Des Moines Water Works; El Paso Water Utilities; JEA; Louisville Water Company; San Antonio Water System; and DC Water.

66 The board typically adopts each committee report and corresponding resolutions in full at its monthly meeting with little or no discussion, based on BGR's review of board meeting minutes and observations of board meetings during the period from January 2007 to June 2011.

67 Gregory, Holly J., and Rebecca C. Grapsas, *Comparison of Corporate Governance Guidelines and Codes of Best Practice: United States*, September 2010, p. 19.

68 BGR analyzed attendance by elected and appointed members on the Finance and Operations Committee through April 2011 and the Infrastructure Committee through June 2011. It did not review attendance by members who have been on committees for less than five meetings. Because of this, it did not analyze attendance since April 2011, when the Finance and Operations Committee was split into separate committees.

69 The designee has the rights and powers of the mayor relative to the meetings, including the right to vote and be counted for purposes of a quorum. Act 101 of 2011.

70 The average is 8.3 members. National Association of Corporate Directors, "NACD Insight & Analysis: When Is the Board Too Big?" March 11, 2011.

71 Ibid.

72 BGR analysis of S&WB board meeting attendance from January 2007 to June 2011.

73 On a nine-member board, the equivalent quorum would be five members.

74 La. R.S. 33:4071 (A)(2).

75 City charter, Sec. 9-104 (2).

76 Donze, Frank, "Ex-N.O. water board member socked with 22 years in prison," *The Times-Picayune*, June 25, 2010.

77 Three of the boards with legal two-term limits have four-year terms; the other has six-year terms. Des Moines Water Works, which has an unofficial limit of two terms, has six-year terms. Louisville Water Company, which has an unofficial limit of three terms, has four-year terms.

78 HB 1301 of 2008 Regular Session and HB 278 of 2010 Regular Session.

79 Gregory and Grapsas, pp. 15-17; Brancato, Carolyn Kay, and Christian A. Plath, *Corporate Governance Best Practices: A Blueprint for the Post-Enron Era*, The Conference Board Special Report No. SR-03-05, 2003, p. 16.

80 Brancato and Plath, p. 11.

81 From January 2007 to March 2011, the S&WB's Finance and Operations Committee met 43 times. The board then separated it into the Finance Committee and the Operations Committee. From April 2011 to June 2011, the separate committees each met three times. The board's other standing committees met less frequently during the January 2007 to June 2011 period. The Infrastructure Committee met 22 times, and the Executive Committee met only twice (both meetings this spring).

82 The committee reviews and approves change orders for a contract once they reach 5% of the bid amount or \$100,000, whichever is less.

83 Specifically, the operations committee reviews and recommends, for both the advertisement and award of contracts, the specific goals for DBE participation. It also hears bid appeals relating to the interpretation and application of DBE program rules.

84 The threshold is set by the board itself or by state law. In Chapel Hill and San Antonio, the water boards must approve contracts above certain thresholds established in state law. N.C. Gen. Stat. Sec. 143-129 et seq. and information provided by the San Antonio Water System.

85 DC Water, Resolution of the Board of Directors No. 97-89, September 4, 1997.

86 Information provided by Louisville Water Company.

87 Under state law, the board appoints the executive director and the general superintendent. The board sets their salaries and de-

fines their duties, and can remove them at will. With the advice and consent of the board, the city attorney appoints the board's special counsel to conduct the legal business of the S&WB. The city attorney can remove the special counsel only with the advice and consent of the board and must remove him upon a two-thirds vote of the board. La. R.S. 33:4073, 33:4075 and 33:4077.



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