

***COMPREHENSIVE ANNUAL FINANCIAL REPORT
OF THE
SAN ANTONIO WATER SYSTEM
A COMPONENT UNIT OF THE
CITY OF SAN ANTONIO, TEXAS
For the Year Ended December 31, 2004***

***Prepared by:
Financial Services Department***

***Stacey L. Isenberg
Interim Chief Financial Officer***

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INTRODUCTION

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COMPREHENSIVE ANNUAL FINANCIAL REPORT

SAN ANTONIO WATER SYSTEM

December 31, 2004

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Our Water. Our Future.

May 6, 2005

Mr. James M. Mayor, Chairman
Mr. R. Douglas Leonhard, Vice-Chairman
Mr. Salvadore M. Hernández, Secretary
Mr. Roberto Anguiano, Trustee
Mr. Michael W. Lackey, P.E., Trustee
Mr. Willie Mitchell, Trustee
Hon. Ed Garza, Mayor

Trustees:

In accordance with the requirements of City Ordinance No. 75686, we are pleased to submit herewith the Comprehensive Annual Financial Report of the San Antonio Water System (the System) for the year ended December 31, 2004. We believe that the financial and statistical information presented in the report is accurate in all material respects and that all disclosures necessary to enable the reader to gain an understanding of the System's financial status have been included. The information contained in this report is the responsibility of management.

DESCRIPTION OF THE COMPREHENSIVE ANNUAL FINANCIAL REPORT

The Comprehensive Annual Financial Report (CAFR) for the year ended December 31, 2004 conforms to governmental financial reporting principles prescribed by pronouncements of the Governmental Accounting Standards Board (GASB). The CAFR is presented in four major sections:

1. The Introduction section contains the title page, the table of contents, this letter of transmittal, a list of the members of the Board of Trustees, an organizational chart, and the Certificate of Achievement for Excellence in Financial Reporting.
2. The Financial section contains the auditor's report, management's discussion and analysis, the basic financial statements which provide an overview of the System's financial position and operating results, and other financial information that provide additional detailed information relative to the basic financial statements.
3. The Statistical section contains various financial and statistical data about the System generally presented on a multi-year basis.
4. The System was required to obtain a single audit in conformity with the provisions of the Single Audit Act Amendments of 1996 and the U.S. Office of Management and Budget Circular A-133, (*Audits of States, Local Governments, and Non-Profit Organizations*). Information related to the single audit, including the schedule of expenditures of federal awards, notes to the schedule of expenditures of federal awards, schedule of findings and questioned costs, summary schedule of prior audit findings, and auditors reports of internal control and compliance with applicable laws and regulations, are included in the federal awards section of this report.

DESCRIPTION OF ORGANIZATION AND REPORTING ENTITY

On February 13, 1992, the City Council determined that it was in the best interest of the citizens of San Antonio and the customers served by the water and wastewater systems to consolidate all water systems, agencies and activities into one institution. This action was taken due to the myriad of issues confronting the City related to the development and protection of its water resources. Such consolidation provided the City a singular voice of representation when promoting or defending the City's goals and objectives related to water resource planning and development with local, regional, state and federal water authorities and officials.

Final Council approval for such consolidation was given on April 30, 1992 with the approval of Ordinance No. 75686 which effectuated the consolidation of all city owned utilities related to water including the water, wastewater, and water reuse systems as the System and defeased all outstanding debt related to the consolidated entities through the issuance of Water System Revenue Refunding Bonds, Series 1992.

The System provides water and wastewater service to the majority of the population within the corporate limits of the City of San Antonio and Bexar County, which totals approximately 1.6 million residents. The System employs over 1,600 personnel and provides maintenance of over 9,488 miles of water and sewer mains.

The complete management and control of the System has been vested in a board of trustees known as the "San Antonio Water System Board of Trustees." The Board of Trustees consists of the Mayor and six Trustees who are residents of the City of San Antonio or reside within the area serviced by the System. With the exception of the Mayor, all other trustees are appointed by the City Council for four year staggered terms and are eligible for reappointment for one additional four-year term.

The general operations of the System are under the supervision of the President/Chief Executive Officer who is employed by the Board of Trustees. The Board of Trustees may appoint and employ all officers, employees, and professional consultants, which it may deem desirable.

The financial statements of the System are included with other enterprise funds in the CAFR of the City of San Antonio. The December 2004 CAFR for the System includes all activities and functions for which the Board of Trustees exercises management and control. As the City Council has placed absolute and complete authority and power in the Board of Trustees with respect to the control, management, and operation of the System, except for fixing rates and charges for service rendered by the System and approval of debt issuances, it is the practice of the System to prepare its CAFR on a comprehensive basis.

ECONOMIC CONDITIONS AND OUTLOOK

The San Antonio economy has experienced robust, sustained growth since the mid-1990's, at a rate considerably higher than national averages. This growth is expected to continue in the near term, but at more moderate levels due to the slowing national and statewide economies. San Antonio's economy has become more diverse over the last decade through decreased dependence on the military sector and the expansion into global markets. This gradual shift has increased San Antonio's exposure to the cyclical nature of the national economy.

The System provides water and wastewater services to the majority of the population within the corporate limits of the City of San Antonio. The System also provides water and wastewater services to other municipalities and certain users outside the corporate limits of the City. San Antonio's population, affected by the net in-migration trends experienced in many areas of Texas, continues to grow at rates that

exceed the national average. Currently, the System provides water and wastewater service to 315,000 and 339,727 customers respectively, including residential, commercial, industrial, and irrigation customers.

The growth rate in System water customers from fiscal year 2003 to 2004 of 2.8% generally tracks the San Antonio metropolitan area as outlined in Table 1.

Table 1	<u>Estimated Population at December 31.</u>		
	<u>2003</u>	<u>2004</u>	<u>% CHG</u>
City of San Antonio	1,266,700	1,282,800	1.3
Bexar County	1,536,600	1,560,500	1.6

Source: *San Antonio Region Economics Trends 1995-2005*; January 2005, The Greater San Antonio Chamber of Commerce.

In addition to population, other strong indicators for the local economy and System customer growth include employment, building permits and housing starts, indicated in Table 2 below.

Table 2	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>
Employment (thousands)	N/A**	781.6	767.2	761.7	754.5	746.5	731.4	715.9	699.2
Non Residential Building Permits	N/A**	N/A**	20,919	19,313	16,476	16,045	13,908	12,565	13,532
Subdivision Platting									
Plats	510*	455	407	480	529	458	439	469	483
Lots	14,060*	11,414	10,290	8,350	9,303	7,937	6,360	5,369	5,259
Single Family Building Permits	N/A**	5,958	6,347	6,132	5,494	5,771	5,630	4,240	4,306

Source: *San Antonio Region Economics Trends 1995-2005*; January 2005, The Greater San Antonio Chamber of Commerce.

*Estimated based on past trend analysis

**Not Available

During 2002, Toyota Motor Manufacturing, Texas, Inc. (TMMTX) announced plans to build a plant to build the Tundra truck on the Southside of San Antonio, Texas. This development will create an economic impact to the San Antonio area due to new jobs from both the Toyota plant and the suppliers that are expected to bring their operations in close proximity of the plant. At the end of 2004, Toyota had begun the employment process for a minimum of 1,800 jobs for its operations. The capital investment of \$800 million for the construction of the plant is underway with a completion date of 2006. A total of 18 Toyota suppliers have announced that they will have operations in San Antonio in December of 2005. The suppliers will create over 1,500 jobs and invest approximately \$150 million in facilities and equipment for their operations. Expected future economic impact to San Antonio due to the Toyota facility is reflected in the chart below.

	TMMTX (10 Years)	TMMTX Suppliers (10 Years)	Total for Toyota And Suppliers
Payroll	\$1.375 billion	\$692.4 million	\$2.067 billion
Payroll from Spin-off	\$1.5 billion	\$694.5 million	\$2.19 billion
Direct jobs	2,000	1,500	3,500
Spin-off jobs	5,300	2,000	7,300

Water Supply

The City currently obtains most of its water supply through wells drilled into a geologic formation known as the Edwards Limestone Formation. The portion of the formation supplying water in the San Antonio area has been designated the "Edwards Underground Water Aquifer" (the "Edwards Aquifer"). The Edwards Aquifer has been designated since 1978 as a sole-source aquifer under the Safe Drinking Water Act by the EPA and had historically been the System's sole source of water supply. The System began obtaining non-Edwards groundwater from the (Cow Creek Limestone Member of the Travis Peak Formation of the Middle Trinity Aquifer Unit) Trinity Group Aquifer during February 2002. (See "Water Resource Planning and Development at Local Level – Oliver Ranch/BSR Projects".)

The Edwards Aquifer is a complex system. It is unique geologically, hydrologically and biologically, as demonstrated by its prolific recharge ability. It is not the simple reservoir that one might envision, such as a surface water lake. Because of this complexity, it is difficult to predict future water levels in the Edwards Aquifer by utilizing historical long-term average water levels.

The Edwards Aquifer and its catchment area in the Edwards Plateau region is about 8,000 square miles and includes all or parts of 13 counties in south-central Texas. The recharge and artesian areas of the Edwards Aquifer underlie the six counties south and east of the Balcones escarpment. The Edwards Aquifer underlies about 3,600 square miles and, including its recharge zone, is about 175 miles long from Brackettville, Texas in Kinney County in the west to Kyle, Texas in Hays County in the east, and varies from about five to about 30 miles in width. The Edwards Aquifer receives most of its water from the drainage basins of streams that recharge the Edwards Aquifer.

Much of the Edwards Aquifer area is agricultural or ranch land with some areas of dense populations. At the present time, the Edwards Aquifer supplies all the water for the municipal, domestic, industrial and agricultural needs of the various users in the Edwards Aquifer area. The population of communities in the region during 2004 ranged from a few hundred residents in D'Hanis to over 1,200,000 residents in the San Antonio metropolitan area. Other cities in the area that have populations of more than 1,500 people include Brackettville, Uvalde, Hondo, Castroville, New Braunfels, Schertz, and San Marcos.

Recreational establishments located in Comal and Hays Counties northeast of the City depend on water from major springs such as San Marcos Springs and Comal Springs that flow from the Edwards Aquifer. In addition to recreational use, as the water moves downstream, it is used for municipal and agricultural supplies. Water from these springs also supports ecological systems in this area as rare and unique aquatic life live in the spring water and in the caverns from which the springs flow.

The water level of the Edwards Aquifer has never fallen below the uppermost part of the Edwards Aquifer even during record drought conditions from 1947 through 1956. The upper level of the Edwards Aquifer in the San Antonio area varies from land surface to 1,500 feet below the land surface. The maximum fluctuation of water levels at the index well in San Antonio has been about 91 feet, with the recorded low of 612 feet above sea level in August 1956, and a recorded high of 703 feet above sea level in June 1992. The historical (1934 to 2002) average water level at the index well in San Antonio is approximately 664 feet above

sea level. At the end of December 2004, the level was 697.3 feet above sea level. The System sets all pumps at 575 feet to insure continuous access to Edwards Aquifer supplies in any anticipated conditions.

The Edwards Aquifer is recharged naturally by seepage from streams and by precipitation infiltrating directly into the limestone outcropping in the northwestern and northern part of the reservoir. Opportunities for recharge are exceptionally good as the limestone is honey-combed and cavernous. Practically continuous recharge is furnished by spring-fed streams, and additional recharge occurs during rains by seepage from storm water runoff. The historical (1934 to 2001) annual recharge to the reservoir is approximately 679,000 acre-feet (one acre-foot equaling approximately 325,821 gallons). The average annual recharge over the last four decades, however, is approximately 791,300 acre-feet. The lowest recorded recharge was 43,000 acre-feet in 1956 and the highest was 2,485,000 acre-feet in 1992.

Natural recharge has been augmented by the construction of recharge dams over an area of the Edwards Aquifer exposed to the surface known as the "recharge zone." The recharge dams (or flood-retarding structures) slow the flood flows and allow much of the water that would have otherwise bypassed the recharge zone to infiltrate the Edwards Aquifer. The System is working with affected river authorities such as Guadalupe-Blanco River Authority, San Antonio River Authority and Nueces River Authority planning ways to increase recharge, and thereby enhancing water yield in the future.

As further described below, the System has entered into several contracts for non-Edwards Aquifer water supplies to diversify and meet future anticipated demand. The first non-Edwards Aquifer water source was introduced in February 2002, (see "Water Resource Planning and Development at Local Level").

Events and/or Conditions Leading Up to Edwards Aquifer Regulation

Until February 2002, the Edwards Aquifer served as the sole source of water for the City since the 1800's. The Edwards Aquifer is still the primary source of water for the agricultural economics in the two counties west of San Antonio and is the source of water for the Comal and San Marcos Springs in New Braunfels and San Marcos, respectively, which depend upon spring flow for their tourist-based economies. Edwards Aquifer water from these springs provides the habitat for species listed as endangered by the U.S. Fish & Wildlife Service under the Endangered Species Act. Water levels in the Edwards Aquifer are affected by rainfall or lack thereof, water usage region-wide and discharge from the springs. (See "Water Resource Planning and Development at Local Level – Oliver Ranch/BSR Projects".)

Ever increasing demands on the Edwards Aquifer, extremely dry conditions in the early 1980s and a near loss of Comal Springs in the summer of 1984 undertaken cooperatively by the City and the Edwards Underground Water District prompted the City and the Edwards Underground Water District to undertake cooperatively a plan for long-term aquifer management and supply. These two entities issued a report, which recommended legislation to authorize management of Edwards Aquifer usage and development of alternative additional water supplies. When these recommendations were not implemented, regional conflict over management of the Edwards Aquifer lead to state and federal court litigation to impose limits on groundwater usage from the Edwards Aquifer.

In *Sierra Club vs. Babbitt*, et.al., (MO 91-CA-069) filed in May, 1991, in the United States District Court, for the Western District of Texas, the Sierra Club brought suit against Bruce Babbitt, the Secretary of the Interior, alleging that the U.S. Fish and Wildlife Service had violated the Endangered Species Act by failing to inform aquifer users of spring flows required to insure that the protected species are not harmed. The City of San Antonio intervened in this case as a Defendant. Numerous aquifer users intervened, as did the State of Texas. After a bench trial, the trial court entered a judgment favorable to the Plaintiffs and ordered the U.S. Fish and Wildlife Service to define necessary spring flow levels and to amend the species recovery plan to insure required protection of the endangered species. The court also ordered the state to implement legislation to manage the Edwards Aquifer or risk further court orders seeking restrictions in water use. Delay in implementing legislation adopted by the state providing for aquifer management ultimately led to the appointment of a monitor and the preparation of an "Edwards Aquifer Emergency Action Plan". On

February 26, 1996, the U.S. Fifth Circuit Court of Appeals (the "Fifth Circuit") found that the case was moot in that the relief requested by the Plaintiff had been obtained. The Fifth Circuit further remanded the case to the trial court for dismissal, leading to the subsequent litigation described below.

In 1993, the 73rd Texas legislature adopted Senate Bill 1477 (Tex. S.B. 1477, Ch. 626, 73rd Leg., R.S. (1993)) which established a framework for regional management of the Edwards Aquifer. This Act created the Edwards Aquifer Authority, a nine member appointed Board, with the power to limit pumping from the aquifer and issue water rights permits. The Authority was also charged with developing a regional management plan incorporating conservation, enhanced recharge, reuse, lease or purchase of pumping rights, interbasin transfers, augmentation, and critical period strategies. In 1995, the 74th Texas Legislature amended Senate Bill 1477 to provide for an elected board and thus allow its implementation. The Edwards Aquifer Authority began its operations on July 1, 1996.

The Edwards Aquifer Authority has geographic jurisdiction over the vast majority of the area of the Edwards Aquifer and manages water usage of the Edwards Aquifer through a well permitting system limiting overall permitted withdrawal and requiring water users to implement water usage reduction measures during critical dry periods. The Edwards Aquifer Authority will be responsible for development of a habitat conservation plan to insure compliance with the Endangered Species Act and obtain administrative relief from the application of such Act's provisions through an incidental take permit.

Failure to adopt legislation providing for management of Edwards Aquifer to the Sierra Club's satisfaction led the Sierra Club and the Guadalupe Blanco River Authority to initiate litigation against the U.S. Fish and Wildlife Service alleging that the service had caused violations of the Endangered Species Act by failing to advise groundwater users in the Edwards of spring flows necessary to not violate the Endangered Species Act by causing a taking.

Water Resource Litigation

In *Sierra Club v. City of San Antonio, et al*, (M-96-CA-097) filed June 10, 1996, in the United States District Court, for the Western District of Texas, the Sierra Club brought suit against the City and the System, BexarMet and the Department of Defense, including the U.S. Air Force and the U.S. Army. The suit also names as defendants other individuals, corporations and municipal governments as representatives of defendant classes consisting of all municipal, commercial, domestic, industrial, irrigation and livestock pumpers of water in Bexar, Atascosa, Medina, Uvalde, Kinney, Hays and Comal Counties who rely on the Edwards Aquifer as their source of water. The suit alleges that the pumpers are "taking" threatened or endangered species by causing the spring flows at Comal and San Marcos Springs to fall below levels that the U.S. Fish and Wildlife Service has previously determined are necessary to prevent both "take" and "jeopardy" of threatened and endangered species at or immediately downstream of the springs. The plaintiffs in the *Sierra Club* suit petitioned the court to enter a temporary restraining order and preliminary injunction against aquifer users, including the City of San Antonio. After an evidentiary hearing on August 1, 1996, on August 23, 1996 the District Court entered a preliminary injunction requiring the City to reduce water usage to 1.2 times winter average, to be effective October 1, 1996. On August 26, 1996, the City filed an appeal from and moved to stay the preliminary injunction with the Fifth Circuit. The Fifth Circuit granted the stay request on September 10, 1996, and after oral argument and briefing, reversed the District Court decision and vacated the injunction.

The Fifth Circuit found that the State had indeed adopted legislation (*i.e.*, Senate Bill 1477) creating a regulatory management scheme for the water of the Edwards Aquifer to protect all interests dependent upon it, including the endangered species. The Fifth Circuit found that the Sierra Club would likely not prevail in its claims because the District Court should abstain to allow the state administrative regulatory agency to complete its management efforts free of federal court interference. The Fifth Circuit dissolved the preliminary injunction and remanded the case for further action by the district court. The Sierra Club's effort to have this decision reviewed by the U.S. Supreme Court was unsuccessful and the Fifth Circuit decision will control further action in this case.

The Fifth Circuit decision does not dispose of the entire claim of the Sierra Club. Since the City could appeal only from the issuance of the preliminary injunction, the Fifth Circuit's decision does not constitute a judgment on the merits in the City's favor. The decision, however, does control further action in the case by the Sierra Club and sets a standard, which must be overcome before the District Court, can overcome the requirements to abstain under the Burford Abstention Doctrine. The Sierra Club has taken no action in the lawsuit since the decision favorable to the City in its Interlocutory Appeal.

The System has been successful to date in defending any efforts to have Edwards Aquifer water usage regulated by the federal District Court to protect endangered species.

Water Resource Management Under Regulatory Process (Subsequent to July 1, 1996)

Management of the Edwards Aquifer could not be accomplished without specific state legislation in effect replacing the unregulated and unlimited rule of capture right with a regulated system. Efforts to manage withdrawals from the Edwards Aquifer resulted in passage of the Edwards Aquifer Authority Act in 1993 and its amendment in 1995 to allow its implementation. The Edwards Aquifer Authority began operations on July 1, 1996, and final implementation of the Edwards Aquifer Authority Act will ultimately result in elimination of uncertainties concerning access to and use of Edwards Aquifer water by the City and all other aquifer users.

The Edwards Aquifer Authority has jurisdiction over the vast majority of Edwards Aquifer pumping and manages water usage by limiting overall permitted withdrawal of and requiring water users to implement water usage reduction measures during critical dry periods. The Edwards Aquifer Authority is preparing a Habitat Conservation Plan to insure compliance under the Endangered Species Act by obtaining an "incidental take permit".

The Edwards Aquifer Authority has entered the final stages of completing the permitting process. Currently, the EAA has issued 868 permits, which composes 98% of the total permits issued. The permitting process should be completed by May 2005. The Edwards Aquifer Authority staff proposed permit(s) for 196,425 acre-feet for the Systems' permanent Edwards water right holdings. All final board action has been taken regarding these permits. In addition to the 196, 425 acre-feet SAWS holds an additional 28,500 acre-feet, of Edwards leases, five to ten year terms, bringing the System's total inventory to 224,925 acre-feet. The System pumped 159,051 acre-feet of Edwards water during 2004.

The System was instrumental in the creation and development of the Regional Water Resource Development Group ("RWRDG"), a joint purchasing group, to assist smaller community water systems in acquiring available Edwards Aquifer rights. Currently, 13 communities from throughout the five-county Edwards region participate in the RWRDG. This has been successful in helping these systems meet shortages between permit amounts and current demand.

Another major activity for the Edwards Aquifer Authority is the adoption of critical period management measures. The Edwards Aquifer Authority has adopted critical period rules on an emergency basis, most recently during the summer of 2000. Past critical period management rules have called for staged reductions in water usage by limiting discretionary use with successive measures based upon Edwards Aquifer levels. The City has had a critical period management ordinance since 1984, limiting discretionary water usage through primarily restrictions in outdoor water use and lawn watering. The Edwards Aquifer Authority has yet to propose final critical period rules; however, the City of San Antonio is required by law to adopt an ordinance that meets or exceeds whatever the Edwards Aquifer Authority establishes. The System does not expect these rules to materially adversely effect revenues or operations or the System's ability to supply water to its customers for primary needs.

Implementation of the legislation of creating and implementing the Edwards Aquifer Authority will benefit the City and the System. The legislation should provide a basis for resolving disputes concerning the

application of the Endangered Species Act to the Edwards Aquifer. The legislation creates permitted rights and hence, a market in the limited resource and an incentive to implement conservation measures region wide. The City believes that implementation of the legislation will also ultimately result in the elimination of litigation threats to existing water usage from the Edwards Aquifer. The System supports, and the region has benefited from, the management of the Edwards Aquifer by the Edwards Aquifer Authority.

The Edwards Aquifer Authority successfully defended its rules against a claim that state legislation requiring a takings impact assessment rendered void permit rules adopted by the Edwards Aquifer Authority. The Edwards Aquifer Authority has concluded that its actions fell within exceptions to the legislation's requirements and did not perform takings impact assessments. The Edwards Aquifer Authority appealed an adverse district court decision to the 4th Court of Appeals, which reviewed the trial court judgment and found the Edwards Aquifer Authority's rules valid. The landowner pursuing these claims appealed to the Texas Supreme Court, which affirmed the 4th Court of Appeals in a unanimous decision. The Supreme Court's decision validates the Edwards Aquifer Authority's conclusion that no takings impact assessment is required and removes any remaining uncertainty related to the Edwards Aquifer Authority's permit rules.

Additional Water Resource Legislation

In 1997, the 75th Texas Legislature established a new mechanism for statewide water planning with the passage of Senate Bill 1 ("SB-1"), an omnibus bill which assesses Texas water policy in seven general areas: water planning; water resources management, marketing, and transfers; emergency authorizations and enforcement; surface water and groundwater supplies; financial assistance for water needs and conservation; small communities assistance; and water data collection and dissemination.

The regional water planning groups established under SB-1 have finalized the development of the first regional water plans which were approved in July 2001 and incorporated into the approved State Water Plan in December 2001. The System is a significant water provider and the largest purveyor in the South Central Texas Regional Water Planning Group, which encompasses 20 ½ counties in south central Texas. In 1999, the 76th Texas Legislature passed several bills to enhance this planning process, both from an administrative and financial standpoint. The regional water planning process established under SB-1 is expected to play a significantly positive role in future water resource development for San Antonio and the entire State of Texas.

The most controversial aspect of SB-1 requires any water right transferred out of its basin of origin to become junior in priority to all other rights in the basin of origin. Adoption of this measure came only after numerous attempts to reach an alternative compromise. The language should have marginal impact on the System's current plans to develop water from the Lower Guadalupe River Basin. The 77th Legislature in 2001 left this limitation intact.

The System was successful in obtaining language in SB-1, which clarifies the System's right to use natural watercourses when possible to convey recycled water as part of its Water Recycling Program. Language was also included in SB-1, which will clarify the Texas Local Government Code with regard to the right of home-rule municipalities to monitor and protect the quality of groundwater that comprises the municipality's drinking water supply. House Bill 1016, a System-supported measure enacted in the 76th Legislature raised from \$2,000 to \$5,000 as the maximum fee which the Texas Commission on Environmental Quality (TCEQ) can impose for review for plans under its rules for protection of the Edwards Aquifer. The bill also amended the Texas Local Government Code to require fees collected under the TCEQ's Edwards program to be used specifically for the TCEQ's Edwards program. The System believes these statutory changes lay the groundwork for substantial improvement to TCEQ's administration of the TCEQ's Edwards program.

Groundwater management was extensively debated in 1999 and 2001 during the 76th and 77th Texas Legislative sessions, resulting in the creation of many new groundwater districts in the State. Of potential impact to the System, is the Lost Pines Groundwater District, which was established for management of the Simsboro Aquifer in Bastrop and Lee counties. The System has entered into contracts with City Public Service ("CPS") of San Antonio, as well as the Aluminum Company of America ("ALCOA") which secure

the right to develop up to 55,000 acre feet of water from the Simsboro Aquifer. This district is expected to play a positive role in the sustainable development and management of any potential water resources for San Antonio from the Simsboro Aquifer.

The legislation creating the Edwards Aquifer Authority was left intact, and the agency continues to move toward establishing firm regulation of the Edwards Aquifer, despite attempts to alter the authorization legislation. The City led an aggressive effort in 1999 to defeat several pieces of legislation in the 76th Legislature, which would have had a negative impact on the Edwards Aquifer Authority.

The System was also instrumental in 1997, 1999, and 2001 in advancing various pieces of legislation, which will enhance water resources management in the Edwards region and throughout the state. Among these were bills passed to enhance state support for brush control and weather modification programs, both of which are expected to be integral parts of management of the Edwards Aquifer. In summary, the System has greatly enhanced its interaction at the state legislative and regulatory levels to the benefit of the Edwards region.

Senate Bill 2 ("SB-2") adopted by the 77th Legislature contains substantial revisions to the Texas Water Code provisions outlining the powers and duties of the State's preferred method of managing groundwater usage in areas of the State where groundwater districts exist. Several of the System's projects involve production of groundwater from sources other than the Edwards Aquifer, which are or may be in the future subject to the jurisdiction of a groundwater district. SB-2 amendments to the Texas Water Code provide the framework for predictability and certainty in groundwater production and transfer while clarifying a district's authority to manage and protect the groundwater resources. While transfers can be regulated and limited surcharge may be imposed, transfers (and production for transfer) cannot be prohibited or restricted to any greater extent than other users in the district, except under extremely limited circumstances.

The 77th Legislature also adopted legislation amending the enabling legislation of the Lower Colorado River Authority ("LCRA") to permit LCRA to enter into an agreement with the System to supply up to 150,000 acre feet per year of Colorado River water to the System for up to 80 years. Signed into law by the Governor in May 2001, the authorization and the proposed project have been widely praised as the model for water resource development for Texas in the future. This project is more fully described below (see "Lower Colorado River Authority Project").

Water Resource Planning and Development at Local Level

The conservation and regulation of the water in the Edwards Aquifer was the subject of intense scrutiny through the 1980's into the 1990's and led to several regulatory actions taken by federal and state agencies as well as the litigation previously described herein. The City has taken several steps to address these matters including the creation of the System and the Board. Based upon population and water demand projections, coupled with regulatory and environmental issues, the System and its predecessor have long recognized that, in the long term, additional water resources and supplies must be developed to supplement the Edwards Aquifer and meet future increased demand.

In FY 1996, the City Council appointed a 34-member citizens committee to develop strategic policies and goals for water resources management. The Citizens Committee on Water Policy report "A Framework for Progress: Recommended Water Policy Strategy for the San Antonio Area" was unanimously accepted by City Council, becoming the foundation for the System's "Water Resources Plan." On November 5, 1998, the City Council accepted the Water Resources Plan "Securing Our Water Future Together" as the first comprehensive widely supported water resources plan for the City. The Plan establishes programs for immediate implementation as well as a process for developing long-term water resources. In October 2000, the City Council created a permanent funding mechanism (known as the Water Supply Fee) for water supply development and water quality protection through Ordinance No. 92753. The Ordinance approved a separate Water Supply Fee payable by customers. The Water Supply Fee provides a specific fund for water resource development and management and is projected to generate sufficient revenue to support

approximately \$519 million in capital expenditures as well as sufficient operational funds to conduct the planning, operation and maintenance of such water resource facilities through 2005. The multi-year financial plan will be updated every three years to ensure sufficient revenues to meet the water resource requirements. A progress report (Quarterly Report to City Council) provides information on water supply fee related projects can be found on the Systems website (www.saws.org).

The System has determined that these needs can be met through the implementation of an array of programs and projects including critical period management plan, conservation, agricultural irrigation efficiencies, reuse, surface water, non-Edwards groundwater, enhanced recharge capabilities and aquifer storage and recovery.

Critical Period Management Plan. The System and the City have adopted a critical period management plan to address water use in droughts.

Current critical period plans call for staged reductions in discretionary water usage and possible imposition of "surcharges" to reduce peak demand. The System has historically met and anticipates continuing to meet necessary water demands during all anticipated weather conditions in the future through the measures currently being implemented.

Development of additional non-Edwards Aquifer supplies as described below should result in predictable and certain water supply necessary to meet anticipated peak demands.

Conservation Program. Beginning in 1994, the System has progressively implemented aggressive water conservation programs, which have reduced total water production and use by 43.2%, going from 213 gallons per person per day (gpcd) in 1994 to approximately 121 gpcd in 2004. This represents one of the highest efficiencies for a major city not only in Texas, but nationally. The System's conservation plan aims to reduce water usage to 132 gallons per person per day, independent of weather variation, by 2030. Conservation will continue to aggressively pursue further reductions into the future. This will be accomplished through a variety of means including pricing, education, and rebates for water efficient technologies; System improvements to prevent water loss and other measures. Components include:

– **Incentives and Programs**

Residential Programs: Low-Flow Toilets, Community Challenge, WaterSaver Landscape Rebate, Welcome Home (New Home Conservation), Audits (Outdoor and Indoor), Rain Barrels, Rain Sensors, Wash Right (Water Efficient Washing Machines), Plumbers to People, Hot Water on Demand.

Commercial Programs: Large Scale Retrofits, Low-Flow Toilets, Site Conservation Plan, Industry Certification (Car Wash, Restaurants and Cooling Towers), Cooling Tower Audits, WaterSaver Awards, Workshops and Education Programs, Rainwater Harvest Models, Rain Sensors, Wash Right (Efficient Washing Machines), Hotel/Motel Linen Exchange Program, Golf Fore SA.

– **Education and Outreach:** Public outreach (Community Conservation Committee, Master Gardeners), K-12 curriculum and education (Watershed Festival, Scout Merit Badge programs, Student Water Environmental Council), media (TV, Radio, Print).

– **Increasing Block Rate:** The System's drinking water rate structure is a four block-inclining rate which means that the more water used on a monthly basis the higher the cost per 1,000 gallons. Additionally, there is a standard rate and a higher seasonal rate for the months of July through October when demand increases. Commercial irrigation is also assessed at a higher rate.

– **Watering Restrictions:** Year-round restrictions, no sprinklers from 10 am to 8 pm, no water wasting.

- **Enforcement:** The System has been given the responsibility by San Antonio City Council to enforce the provisions set forth by Chapter 34 Article IV of the City Ordinance.
 - Components of Enforcement:** Water Waster Hotline (704-SAWS), educational visits, water waster list.
 - Misdemeanor Ticket for Water Waste:** 1st violation, \$50 - \$100; 2nd violation, \$250 - \$500; 3rd or more violations, \$1000 - \$2000.
- **Leak Detection and Repair:** The System has full-time crews, which inspect the distribution system for leaks and damage.

The System has also developed partnerships with local river authorities, ground water districts and purveyors to ensure the conservation messages and programs are available throughout the region. The Water Advisory Group, consisting of cities throughout Bexar County and the Edwards Aquifer region meets regularly to coordinate conservation, drought management and other water resource policies.

[Agricultural Irrigation Efficiency](#) - The System has been successful in developing partners throughout the region as well as with federal agencies through cost-share programs. The amount of \$500,000 for fiscal year has been appropriated by the United States Department of Agriculture ("USDA") for the Edwards Aquifer region to assist landowners with agricultural irrigation efficiencies. The System has partnered with the USDA and farmers to acquire efficient irrigation systems in exchange for Edwards Aquifer water rights. The System is also currently working with the Army Corps of Engineers, the Natural Resource Conservation Service and other local sponsors on programs designed to enhance recharge of the Edwards Aquifer through impoundment structures and brush management.

[Water Reuse Program](#). The System owns the treated effluent from its wastewater treatment plants and has the authority to contract to acquire and to sell non-potable water inside and outside the System's water and wastewater service area. The System has developed a water reuse program utilizing the wastewater stream. The reuse water system phase I construction is complete. It is expected that construction of inter-connect pipeline segments between the two main lines will begin in the near future. Currently, approximately 23,000 acre feet are under contractual commitment and 12,600 acre feet are on-line. The system will deliver up to 35,000 acre feet per year of reuse water for non-potable water uses including golf courses and industrial uses that are currently being supplied from the Edwards Aquifer. This represents approximately 20% of the System's current usage. Reuse water will be delivered for industrial processes, cooling towers, and irrigation, which would otherwise rely on potable quality water. Combined with the 40,000 acre feet per year used by CPS, this is the largest reuse water project in the county. The System has a contract with CPS through 2030 for provision of such reused water. The revenues derived from the CPS contract have been excluded from the calculation of Gross Revenues, and are not included in any transfers to the City.

[Recharge Initiatives](#). Recharge Dams are structures that retain rainfall runoff water for short periods of time over the Edwards Aquifer Recharge Zone; recharge dams retain storm runoff and retain them long enough to allow for a larger volume of water to enter into the Edwards Aquifer. During storm events storm runoff flows at a faster rate than what can be taken by the recharge features located in the stream channels. The recharge dam allows for a longer retention for more water to filter into the Edwards Aquifer thus increasing recharge amounts. The Nueces, San Antonio, and Guadalupe River Basins are favorable for development of recharge projects. Of the three basins, the Nueces Basin is the most prolific in terms of recharge effectiveness. Studies are currently under way within the Cibolo Creek Watershed and the Nueces River Basin. The results of these studies will identify which sites will have the most potential for recharge enhancement. With the recharge structures tentatively identified, the System is planning on having a potential sustained yield of 13,400 acre-feet per year. This project is estimated to cost \$84.2 million in capital cost and \$940,000 in annual operation and maintenance

[Oliver Ranch/BSR Projects](#). The System also has contracted for delivery of approximately 5,000 acre feet per year of non-Edwards groundwater from the Trinity Aquifer Group from two properties located in northern Bexar County. The construction cost to produce and deliver this water supply is approximately \$5.8 million.

Initial delivery of water from the Oliver Ranch project began in February 25, 2002 with BSR production beginning in July 2003. The project was fully operational in June 2004 with the connection of BSR wells 3 and 4 to the System's distribution system.

[Simsboro Project.](#) On December 30, 1998, a contract for the delivery of up to 55,000 acre-feet per year of water from the Simsboro Aquifer was executed with ALCOA. At the same time the System acquired the permanent right to produce groundwater from approximately 11,500 acres of land in the Simsboro Aquifer owned by CPS. The ALCOA and CPS contracts collectively constitute the Simsboro Project. Groundwater availability studies conclude that 55,000 acre-feet per year can be sustainable from a combination of groundwater production from both contracts. This Project has been included in the approved State Water Plan. The Project is scheduled to begin delivering water in 2015 at an estimated Project cost to the System of approximately \$404.2 million.

[Western Canyon Project.](#) The Western Canyon project represents a partnership between the System, the San Antonio River Authority ("SARA"), Guadalupe-Blanco River Authority ("GBRA"), and Bexar Met and other water suppliers for the delivery of Canyon Lake water. The System will initially receive approximately 8,500 acre-feet per year for service to northern Bexar County. The long-term minimum yield will be 3,950 acre-feet per year. GBRA is required under the contract to divert, treat and deliver the water to a certain point into the System's delivery system. The permit was issued by the state's regulatory agency, the TCEQ. The project design work has been completed and notice to proceed on construction of various project components took place during the 4th quarter 2004 and 1st quarter of 2005.

[Bexar County Aquifer Storage and Recovery Project.](#) An Aquifer Storage and Recovery ("ASR") project involves injecting ground water into an aquifer, storing it and later retrieving it for use. Essentially this is storage that is additionally provided through surface water reservoirs. The System began study of an ASR project in 1996, acquired approximately 3,200 acres in southern Bexar County. Phase I was completed by the second quarter of 2004. The combined ASR project with system integration is approximately \$215 million. This project is primarily designed to optimize use of water from the Edwards Aquifer and reduce frequency and duration of critical periods. Additionally, the ASR project may produce "native" groundwater from the project area for use throughout the service areas. In December 2002, the Evergreen Underground Water Conservation District (EUWCD) and the System approved an Aquifer Protection and Management Agreement. This agreement ensures operation of the ASR site if the property is annexed in to the district, manages groundwater production, and commits the System to monitoring water levels and mitigation of potential negative impacts. Phase I of the project was dedicated on June 18, 2004. Construction of Phase II is anticipated for completion in late 2005.

[Gonzales County Project.](#) The System is refining plans for delivery and treatment of approximately 20,000 – 56,200 acre-feet of ground water from the Carrizo Aquifer in Gonzales County. The project will be developed in phases. The delivery of water from the first phase (22,500 AF) is anticipated in early 2008. Phase II and Phase III will be delivered in 2010 and 2012 respectively. Currently, the System's Board of Trustees has approved the design work for Phase I. The first phase of this project is estimated to cost approximately \$228 million. If all three phases of the project are completed, the combined capital costs are approximately \$409 million.

[Guadalupe-Blanco River Authority/San Antonio River Authority Project.](#) The System joined with the San Antonio River Authority (SARA) to jointly develop a project to deliver approximately 94,500-acre feet per year of water throughout the San Antonio Water System and the San Antonio River basin. In May 2001, the partners executed a contract with GBRA for delivery of 70,000 acre-feet of senior water rights from the lower Guadalupe River. The contract provides for delivery of water for 50 years as well as a 7-year period to define specific delivery plans for the project. The diversion for the project is located at the mouth of the Guadalupe River near the community of Tivoli. This contract provides a substantial volume of water that will be augmented from currently unappropriated surface water rights and groundwater from the Gulf Coast Aquifer. Permits authorizing delivery of the surface water to Bexar County have not yet been obtained.

Capital costs for the 94,500 acre-feet per year project are estimated at \$688 million with delivery scheduled for 2010-2012.

Lower Colorado River Authority Project. A Memorandum of Agreement with LCRA outlining the terms for a future binding contract for up to 150,000 acre feet of surface water per year from the Lower Colorado River Basin was signed in February 2001. As discussed above, legislation was passed in 2001 to authorize LCRA to sell water outside their statutory boundary to the System. The System and LCRA have now executed a definitive agreement outlining LCRA's and the System's obligations consistent with the Memorandum of Agreement. The contract provides for a seven-year study period to assess the environmental, engineering, and cost impacts. The estimated project cost is estimated at approximately \$1.168 billion. This contract will provide water for up to 80 years and provide significant transmission facilities to service Bexar County and the region. The System's Board of Trustees approved the second year of a seven-year study plan. The Board will decide on an annual basis whether to continue with the study period plan.

Edwards Aquifer Optimization. Edwards Aquifer Optimization ("AO") is a comprehensive program that identifies and evaluates technical options to increase available yield from the Edwards Aquifer and to attempt to use the aquifer's storage capacity more efficiently. The Edwards Aquifer Authority is the lead organization in this program, with the System assisting in the funding and technical guidance. The AO Program will evaluate a number of studies that have been proposed to maintain or increase available water in the aquifer. The goal of the program is to determine the feasibility of these alternatives, test them in a pilot project phase, and recommend the implementation of one or more that are found to be favorable. Another goal of the program is to determine through sound science whether the pumpage cap, currently 450,000 acre-ft. per year, should be lowered to 400,000 acre-ft per yr. in 2008, as is legislated by SB-1477. SB-1477 states that the reduction in the pumpage cap may be revised if some of these technical options determined through scientific research prove feasible. The AO studies are planned for completion in time to answer this question by 2007.

Water Quality Initiative. The TCEQ has adopted rules relating to activities of landowners in the recharge and drainage zones of the Edwards Aquifer to protect the high quality of water from the Edwards Aquifer. The City has adopted ordinances applicable within its city limits that limit or regulate activities which could be harmful to water quality and has, through its Unified Development Code, regulated certain development within the City's extraterritorial jurisdictional (five miles from city limits).

MAJOR ACTIVITIES

Effective October 1, 2001, the operations of the System were reorganized. As part of the reorganization, management staff was reduced by 24% and efforts were made to increase the span of control of supervisors and eliminate layers of management. During December 2003 and 2004 efforts continued to focus on the refinement of operations through the execution of the corporate mission and the setting of strategic plans for accomplishment of that mission.

Rate Advisory Committee. During FY 2003, the Board of Trustees formed a Rates Advisory Committee (RAC) in a desire to communicate to and involve a balanced and representative group of stakeholders whose charge was to study pricing objectives, alternative rate structures and other rate issues. The committee consisted of the System's Board of Trustees and fifteen members representing various industries, environmental groups, and customer classes. A well-known rates consultant company, Raftelis Financial Consulting, was also obtained to assist the committee and staff on its analysis of rates and cost of service study. The committee began a review of methodologies and policies for the setting of the rates on April 9, 2003 and finalized its work eleven meetings later on December 10, 2003. The committee made several recommendations including to maintain the current rate structure for the rate adjustments ultimately approved by the San Antonio City Council.

Other recommendations were:

- to adjust rates to maintain a \$110 million CIP program for Water Delivery and Wastewater,
- to further review the policies concerning the Irrigation exemptions for golf courses and others,

- to further investigate the Recycle water business from a business perspective to make it a more efficient use of the system's resources, and
- the establishment of a new affordability sliding scale program for qualifying customers.

The 2005 budget further increased the affordability program by increasing the sliding scale discount, with the goal to maintain water and wastewater bills at or below an acceptable percentage (4% for combined water and sewer customers) of their income. The affordability discount is based on the income of the customer with respect to the federal poverty guidelines and increases as the level of the customer's income is reduced with respect to the poverty guideline income level. As the affordability discount was restructured to provide a greater benefit to those with the most need, several members of the City Council of San Antonio commended this progressive approach to an affordability program.

On February 12, 2004 the City Council approved adjustments to the Residential, General, Wholesale and Irrigation water rates along with adjustments to the Residential, General, and Wholesale wastewater rates. The anticipated increase in 2004 water and wastewater revenue due to the rate adjustments was \$15.3 million or 9.5% of the projected water and wastewater revenues. The fourth increment of the Water Supply Fee was implemented for 2004 with the rate adjustment from \$0.0844 to \$0.1100 per 100 gallons. The additional increment is projected to increase Water Supply Fee revenues by \$13.2 million.

On November 18, 2004, rate adjustments for 2005 were approved by City Council to adjust the Residential, General, Wholesale and Irrigation water rates, in addition to rate adjustments to the Residential, General, and Wholesale wastewater rates. The anticipated increase in 2005 water and wastewater revenue due to the rate adjustments is \$17.5 million or 9.9% of the projected water and wastewater revenues. Additionally, for fiscal year 2005, the fifth increment of the Water Supply Fee was approved by the Board of Trustees. The Water Supply Fee was revised to \$0.1100 to \$0.1378 per 100 gallons and is projected to increase Water Supply Fee revenues by \$14.2 million.

FINANCIAL INFORMATION

Management of the System is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the System are protected from loss, theft, or misuse and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to provide reasonable, but not absolute, assurance that the objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived and (2) the valuation of costs and benefits requires estimates and judgments by management.

As a part of the System's audit, tests are made to determine the adequacy of the internal control structure, as well as to determine that the System has complied with applicable laws, regulations, and ordinances. The results of the audit of the System for the year ended December 31, 2004, provided no instances of material weaknesses in the internal control structure.

The System's Board of Trustees approved the Annual Budget for FY 2004 in October 2003.

The Annual Budget is prepared on a comprehensive basis and as such includes an Operating Budget that includes all water, wastewater, chilled water and steam, and reuse operations as well as a budget for routine construction. The Annual Budget is prepared in such a manner that expenses may be controlled on a line-item basis. Encumbrances are not formally recorded in the accounting system of the System, but are monitored and reported in the notes to financial statements if significant amounts are outstanding at year-end. Outstanding encumbrances lapse at year-end and must be reappropriated in the following year.

Long-term Financial Planning. Planning is critical for the System to accomplish its mission. In order to adequately plan for water sources and appropriate infrastructure, models have been developed to analyze the impacts of various growth and replacement scenarios on the company's financial position. Some of these models have a short-term focus, some are mid-range models, and some are long-term.

Short term planning is mainly focused in two areas, cash management and expense tracking. The Treasury function at the System balances the need for adequate cash resources and the need for maximum returns on assets. The Budgeting function at the System analyzes the monthly spending requirements in view of the other corporate obligations, such as ordinance requirements and obligations to bond holders and to the City of San Antonio.

Mid-range planning mainly focuses on the next year's activities. A comprehensive financial plan is developed using updated revenue forecasts, operating and maintenance estimates, capital requirements, and interest rate forecasts.

Long-range planning is the heart of the System's planning activities. Statistical models are used to estimate customer growth and water usage patterns. These are fed into a revenue model that incorporates the various rate class prices to produce detailed revenue forecasts. Simultaneously, the company produces capital and operating and maintenance budgets, from which twenty-year estimates are developed. Upon receiving these inputs, the financial planning model uses a debt optimization process to determine the correct balance and timing of funding sources.

Debt Administration. The System utilizes both long-term and short-term to finance the Capital Improvements Program (CIP). The System's long-term debt consists of fixed-rate debt and variable-rate debt swapped to a fixed rate to provide predictable debt service requirements. The System's short-term debt consists of a tax-exempt commercial paper program (TECP). TECP provides the System flexibility and efficiency in the timing and amount of debt issued. Additional information on the System's debt program can be found in Note G of the notes to the financial statements.

Cash Management Policies and Practices. Of the total investments of the System for the year ended December 31, 2004, approximately 63% are invested in U.S. Agency Securities. The remaining funds are invested in Money Market Funds and U.S. Treasury Securities. Approximately 57% of the portfolio has a maturity range of six months to one year, and the average days maturity of the portfolio is 358 days. The weighted average yield on investments for the portfolio was 2.04%. The investment portfolio is in compliance with the System's investment policy, and all transactions are in accordance with the System's investment strategy. Additional information on the System's investment activity can be found in Note C of the notes to the financial statements.

Risk Management. The System continues to manage its risk by self administering and self insuring claims under commercial general liability, automobile liability, public official's liability, environmental pollution remediation and legal liability and worker's compensation. Claims that exceed their respective coverage self-insured retention limit are covered through the System's comprehensive commercial insurance program. Commercial general liability, automobile liability, and worker's compensation each have a \$500,000 per occurrence, self-insured retention. Public official's liability has a \$500,000 per covered claim, self-insured retention and environmental pollution remediation and legal liability has a \$250,000 per covered claim, self-insured retention. The System did not experience any claims whose cost exceeded the respective self-insured retention level during 2004. Additional information on the System's Risk Management program can be found in Note F.

Pension and Other Post Employment Benefits. The System's pension plan is a single-employer defined benefit pension plan which serves as a supplement to the Texas Municipal Retirement System and Social Security benefits. The System has delegated authority to manage certain plan assets to Principal Mutual Life Insurance Company. The System provides certain health care and life insurance benefits for retired employees, which are financed on a pay-as-you-go basis. Additional information on the System's

pension and other post employment benefits can be found in Notes K and L of the notes to the financial statements.

OTHER INFORMATION

Independent Audit. The financial section of the December 2004 CAFR begins with the report of our independent auditors, Garza/Gonzalez and Associates. Their report expresses an unqualified opinion as to the fairness of the presentation of our financial statements. In addition to meeting the requirements set forth in City Ordinance No. 75686, the audit also was designed to meet the requirements of the Federal Single Audit Act Amendments of 1996 and related OMB Circular A-133.

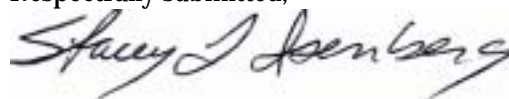
The Auditor's reports related specifically to the single audit are included in the federal awards section of this report.

Generally Accepted Accounting Principals (GAAP) requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). The letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The System's MD&A can be found immediately following the report of the independent auditors.

Certificate of Achievement for Excellence in Financial Reporting. The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the System for its Comprehensive Annual Financial Report for the year ended December 31, 2003. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement Program requirements, and we are submitting it to GFOA.

Acknowledgements. The timely preparation of the CAFR for the year ended December 31, 2004 could not have been accomplished without the cooperation and dedicated services of the Accounting Division under the direction of Mrs. Juanita Carabajal. We also wish to express sincere appreciation to each member of the Board of Trustees for the interest and support provided in conducting the financial affairs of the System in a sound and progressive manner.

Respectfully submitted,



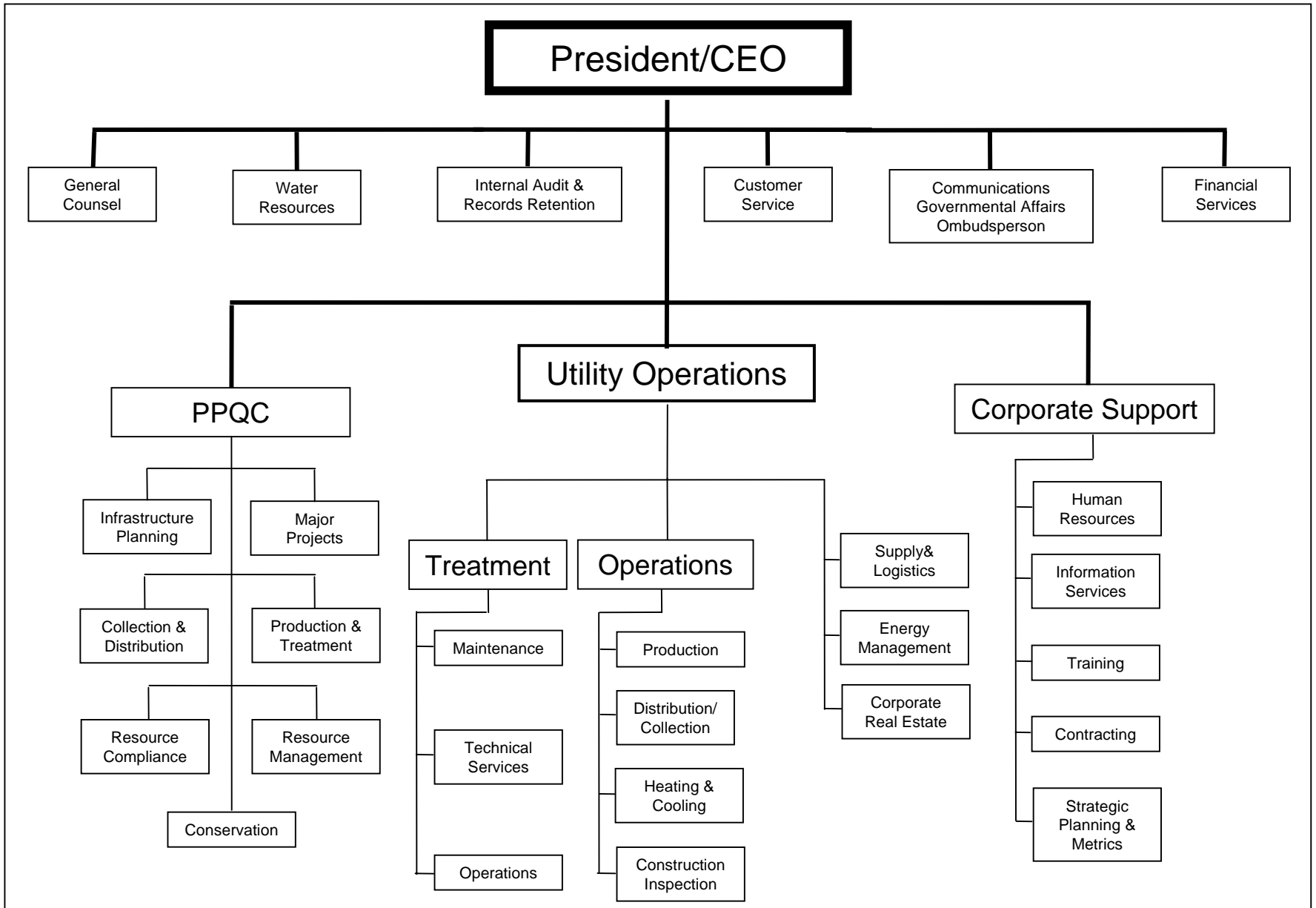
Stacey L. Isenberg
Interim Chief Financial Officer

**MEMBERS OF THE
SAN ANTONIO WATER SYSTEM BOARD OF TRUSTEES**

	<i>Term Expires</i> <u>May 31</u>
<i>James M. Mayor – Chairman</i>	2006
<i>R. Douglas Leonhard – Vice-Chairman</i>	2005
<i>Sal Hernández – Secretary</i>	2005
<i>Michael W. Lackey, P. E. – Trustee</i>	2005
<i>Roberto Anguiano – Trustee</i>	2008
<i>Willie A. Mitchell – Trustee</i>	2006
<i>Ed Garza – Mayor – Ex Officio</i>	



San Antonio Water System Organizational Chart



Certificate of Achievement for Excellence in Financial Reporting

Presented to

San Antonio Water System,
Texas

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
December 31, 2003

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Nancy L. Zielke

President

Jeffrey R. Emer

Executive Director