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***GENERAL PURPOSE FINANCIAL STATEMENTS***



**San Antonio Water System  
BALANCE SHEET**

**ASSETS**

		<b>December 31, 2001</b>
<b>CURRENT ASSETS</b>		
Investments - Note C	\$	22,901,490
Accrued interest receivable		537,435
Accounts receivable, net of allowances for uncollectable accounts of \$ 272,697		22,851,119
Inventory - materials and supplies		4,028,953
Prepaid expenses		1,072,086
Total current assets		51,391,083
 <b>UNAMORTIZED REFUNDING BOND EXPENSES</b>		 5,531,782
 <b>RESTRICTED ASSETS</b>		
Debt Service Fund:		
Cash and cash equivalents - Note C		493,270
Investments - Note C		22,367,038
Construction Funds:		
Cash and cash equivalents - Note C		30,954,603
Investments - Note C		81,416,857
Conservation:		
Investments - Note C		7,400,223
Customers' deposits:		
Investments - Note C		5,007,576
Total restricted assets		147,639,567
 <b>UTILITY PLANT</b>		
Utility plant in service - Note D		1,908,240,918
Less allowance for depreciation/amortization		643,936,011
		1,264,304,907
Land and land rights - Note D		45,223,776
Construction in progress		339,399,414
Total utility plant		1,648,928,097
 <b>TOTAL ASSETS</b>	 \$	 <u><u>1,853,490,529</u></u>

The accompanying notes to financial statements form an integral part of this statement.

**San Antonio Water System  
BALANCE SHEET**

**LIABILITIES AND EQUITY**

		<u>December 31, 2001</u>
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$	3,636,943
Sewer service collections payable		190,482
Capital leases and notes payable - Note E		516,368
Accrued vacation payable		3,900,802
Accrued payroll and benefits		4,320,059
Accrued claims payable - Note F		1,728,796
Accrued stormwater services		1,078,861
Sundry payables and accruals		<u>6,095,803</u>
Total current liabilities		21,468,114
<b>CURRENT LIABILITIES PAYABLE FROM RESTRICTED FUNDS</b>		
Debt Service Fund:		
Accrued interest payable		5,594,868
Construction Funds:		
Contract retainage payable		3,364,173
Advances for construction		2,718,434
Customers' deposits		5,007,576
Revenue bonds payable within one year - Note G		<u>25,045,000</u>
Total liabilities of restricted funds		41,730,051
<b>NONCURRENT LIABILITIES</b>		
Capital leases and notes payable - Note E		2,929,809
Commercial paper notes - Note H		185,000,000
Revenue bonds payable after one year - Note G		703,410,000
Unamortized premium		1,638,523
Less unamortized loss		(8,571,819)
Less unamortized discount		<u>(15,542,613)</u>
Total noncurrent liabilities		868,863,900
Total liabilities		932,062,065
<b>EQUITY</b>		
Retained earnings reserved for:		
Debt Service Fund		17,265,440
Construction		106,288,853
Conservation		<u>7,400,223</u>
		130,954,516
Unreserved		<u>167,889,386</u>
		298,843,902
Contributions in aid of construction - Note D		<u>622,584,562</u>
Total equity		921,428,464
<b>CONTINGENCIES AND COMMITMENTS - Note I</b>		
		-
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$</b>	<u><u>1,853,490,529</u></u>

The accompanying notes to financial statements form an integral part of this statement.

**San Antonio Water System**  
**STATEMENT OF REVENUES, EXPENSES**  
**AND CHANGES IN RETAINED EARNINGS**  
**For the Seven Months Ended December 31, 2001**

**OPERATING REVENUES**

Water delivery system	\$ 52,803,937
Water supply system	23,537,496
Wastewater system	51,541,185
Chilled water and steam system	6,822,031
Total operating revenues	<u>134,704,649</u>

**OPERATING EXPENSES**

Operating expenses before depreciation	78,448,318
Depreciation/ amortization expense	29,454,496
Total operating expenses	<u>107,902,814</u>

Operating income 26,801,835

**NONOPERATING REVENUES**

Interest earned and miscellaneous	5,299,740
	<u>5,299,740</u>

**NONOPERATING EXPENSES**

Amortization of refunding bond expense	304,736
Interest expense:	
Revenue bonds and commercial paper	21,358,315
Amortized discount/ premium expense	733,901
Capital leases	145,932
Loss on sale of fixed assets	159,026
Payments to the City of San Antonio	3,621,427
Total nonoperating expenses before contributions	<u>26,323,337</u>
Contributions	6,949,745

**NET INCOME** 12,727,983

Retained earnings, beginning of year - as Restated 286,115,919

**RETAINED EARNINGS, END OF YEAR** \$ 298,843,902

The accompanying notes to financial statements form an integral part of this statement.

**San Antonio Water System  
STATEMENT OF CASH FLOWS**

**For the Seven Months Ended December 31, 2001**

**CASH FLOWS FROM OPERATING ACTIVITIES**

Cash received from customers	\$	135,194,233
Cash paid to vendors for operations		(53,222,227)
Cash paid to employees for services		(34,343,213)
Net cash provided by operating activities		47,628,793

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES**

Payments to the City of San Antonio		(1,932,317)
Net cash used for noncapital financing activities		(1,932,317)

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES**

Proceeds from sale of fixed assets		827
Proceeds from developers for plant construction		6,933,403
Payment to employees for construction of plant		(4,097,620)
Payment to vendors for construction of plant		(5,562,726)
Payments for acquisition of equipment and furniture		(3,836,660)
Payments for acquisition of property and plant		(39,754,168)
Proceeds from commercial paper		20,000,000
Payment of interest on tax exempt commercial paper		(2,541,849)
Payment of interest on revenue bonds		(20,345,257)
Payment of bond sale expenses		(27,095)
Payment on capital leases		(167,085)
Payment on CPS note		(280,000)
Net cash provided by/(used for) capital and related financing		(49,678,230)

**CASH FLOWS FROM INVESTING ACTIVITIES**

Purchase of investments		(152,407,569)
Maturity of investments		147,357,225
Interest income		5,246,467
Net cash used for investing activities		196,123

**NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** (3,785,631)

<b>CASH AND CASH EQUIVALENTS, AT BEGINNING OF YEAR</b>		35,233,504
<b>CASH AND CASH EQUIVALENTS, AT END OF PERIOD</b>	\$	31,447,873

**San Antonio Water System**  
**STATEMENT OF CASH FLOWS**  
**For the Seven Months Ended December 31, 2001**

**RECONCILIATION OF CASH AND CASH EQUIVALENTS PER STATEMENT OF CASH FLOWS  
TO THE BALANCE SHEET**

Cash and Cash Equivalents		
Restricted		
Debt Service Fund	\$	493,270
Construction Fund		<u>30,954,603</u>
	\$	<u><u>31,447,873</u></u>

**RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES**

Operating Income	\$	26,801,835
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense		29,454,496
Change in assets and liabilities:		
Decrease in accounts receivable		546,722
Decrease in inventory		297,049
Decrease in prepaid expenses		679,143
Increase in working capital fund utility plant		1,060,033
Increase in working capital fund allowance		(1,055,071)
Decrease in accounts payable		(8,012,667)
Increase in amount due for sewer collections		4,638
Increase in accrued payroll and benefits		634,611
Decrease in accrued vacation payable		(221,080)
Decrease in sundry payables and accruals		(1,723,663)
Decrease in accrued stormwater services		(330,159)
Decrease in claims payables		(445,318)
Decrease in customers' deposits		<u>(61,776)</u>
Total Adjustments		<u><u>20,826,958</u></u>
Net cash provided by operating activities	\$	<u><u>47,628,793</u></u>

**NONCASH CAPITAL AND FINANCING ACTIVITIES**

The System recorded noncash payments of \$1,689,112 for the water, reuse, supply and sewer billings to the City of San Antonio.

The System recorded noncash payments of \$480,000 on a note for water rights to City Public Service.

## ***NOTES TO FINANCIAL STATEMENTS***

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**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**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 provides 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. It was further determined by the Council that the interests of the citizens and customers could best be served by placing authority for management and control of the system, as consolidated, in a board of trustees appointed by the City Council. Additionally, it was determined that the best mechanism for effecting the consolidation of all water systems, agencies and activities into a single institution was through a refunding of all then outstanding water and sewer bonds.

Final Council approval for such consolidation and refunding 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 San Antonio Water System (the "System") through the issuance of Water System Revenue Refunding Bonds, Series 1992. The proceeds of the Series 1992 Bonds were used to defease all outstanding revenue bonds and related long-term debt of the water and wastewater systems.

The pension and retirement plans described in Note L are administered by third parties and are not a part of the reporting entity.

This Comprehensive Annual Financial Report of the System includes no component units. However, the operations of the System as reported herewith are included as a component unit of the City of San Antonio.

**Management of the System:** 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 must reside within the City of San Antonio or the service area of the System. With the exception of the Mayor all other trustees are appointed by the City Council for four-year staggered terms, however, no person who has served two terms is eligible for reappointment. The Mayor, with the concurrence of the City Council, annually appoints one of the other members of the Board as the Chairman of the Board. In addition to appointment of members of the Board of Trustees, the City Council also has retained authority for approval of requests for rate adjustments, and any sale of additional revenue bonds. 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 may appoint and employ all officers, employees, and professional consultants, which it may deem desirable

## ***NOTES TO FINANCIAL STATEMENTS***

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**Annual Budget:** The System prepares and presents, sixty days prior to the beginning of each fiscal year, an annual budget prepared on an accrual basis to serve as a tool in controlling and administering the management and operation of the System. The annual budget reflects an estimate of Gross Revenues and an estimate of the disposition of these revenues in accordance with the flow of funds required by Ordinance No. 75686. (See Note B) The annual budget is submitted to City Council for review and consultation. Encumbrances are not formally recorded in the accounting system but are monitored and disclosed if significant amounts are outstanding at year-end. Outstanding encumbrances lapse at year-end and must be reappropriated in the following year.

**Accounting Standards:** The System applies all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as any FASB statements and interpretations, APB opinions and ARB's issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements.

**Fund Accounting:** Within the System's enterprise fund accounts, separate self-balancing funds are maintained to account for resources for various purposes, thereby distinguishing balances restricted by management or outside sources from unrestricted resources. These restrictions are more fully explained in Note B. Interfund receivable and payable accounts have been eliminated in the financial statements.

Funds being designated for conservation are presented by reclassifying assets from unrestricted to restricted. The funds designated for conservation total \$7,400,223 as of December 31, 2001.

**Business Segments:** System Fund operations are segregated into four core businesses. The System's cost reporting structure on the four utilities follows:

- Water Supply – the functions related to the development and provision of additional water resources
- Water Delivery – the function of distributing water to the customer
- Wastewater – the functions of collecting and treating wastewater from the user customer
- Chilled Water and Steam – the function related to providing chilled water and steam to specific customers of the System

The Water Supply core business also includes revenues and expenses of the recycled water system, conservation and stormwater activities (reimbursement for the stormwater activities program from the City of San Antonio).

**Basis of Accounting:** The financial statements are prepared using the accrual basis of accounting and on the flow of economic resources measurement focus. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

## ***NOTES TO FINANCIAL STATEMENTS***

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**Change in Fiscal Year:** On April 3, 2001, the Board of Trustees approved the changing of the fiscal year for the System from a year-end of May 31 to December 31. Management has taken all necessary actions to effect the change, including the preparation of this comprehensive annual financial report for the seven month period ending December 31, 2001, and notification to bondholders, nationally recognized municipal security information repositories, and others, of the change in the fiscal year.

The change in fiscal year to a calendar year was approved to increase the effectiveness and efficiency for the implementation of capital improvement programs, rate studies and other financial planning.

**Investments:** The System reports investments in accordance with GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools". Under the provisions of GASB Statement No. 31, "Governmental Entities should report investments at fair value in the balance sheet." Investment income should include unrealized gains and losses (representing the change in market value) and be reported as revenue in the operating statement.

**Nonparticipating Interest-Earning Investment Contracts:** Under the provisions of GASB Statement No. 31, certificates of deposits are considered nonparticipating contracts since they cannot be negotiated or transferred and their redemption terms do not consider market rates. Therefore, the cost-based measure is used to report the value of the System's certificates of deposit and does not include any unrealized gains and losses.

**Money Market Investments:** Under the provisions of GASB Statement No. 31, money market investments with a remaining maturity at time of purchase of one year or less may be reported at amortized cost, which approximates fair value. As of December 31, 2001 the difference between the reported amount (amortized cost) and fair value of the money market investments with an original maturity of greater than one year was \$133,690 and deemed immaterial, therefore an unrealized loss was not reported.

**Inventory:** Inventories are valued at the lower of average cost or market.

**Unamortized Refunding Bond Expense:** Expenses relating to the sale of revenue refunding bonds are amortized on a straight-line basis over the life of the issue.

**Compensated Absences:** It is the policy of the System to accrue employee vacation pay as earned. In accordance with GASB Statement No. 16 "Accounting for Compensated Absences," the System accrues an additional amount for its portion of Social Security taxes. Sick leave is not accrued, as a terminating employee is not paid for accumulated sick leave.

**NOTES TO FINANCIAL STATEMENTS**

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**Self-Insurance:** The System is self-insured for a portion of workers' compensation, employee's health, employer's liability, public officials' liability, property damage, and certain elements of general liability. A liability has been recorded for the estimated amount of eventual loss, which will be incurred on claims arising prior to the end of the period.

**Cash Flows Statement:** For purposes of the statement of cash flows, the System considers all investments and time deposits with an original maturity of 90 days or less to be cash equivalents.

**Utility Plant:** Utility plant in service is recorded on the cost basis. Assets acquired through capital leases are recorded on the cost basis and included in utility plant in service. Assets acquired through contributions, such as those from land developers, are capitalized and recorded in the plant accounts at estimated fair market value at date of donation. It is the policy of the System to capitalize certain interest costs on revenue bonds and commercial paper associated with newly constructed utility plant additions. Maintenance, repairs, and minor renewals are charged to operating expense; major plant replacements are capitalized.

Utility plant is depreciated and property under capital lease is amortized on the straight-line method. This method is applied to all individual assets except distribution mains. Groups of mains are depreciated on the straight-line method using rates estimated to fully depreciate the costs of the asset group over their estimated average useful lives. The table below shows an estimated average of useful lives used in providing for depreciation of utility plant:

Structures and improvements	50 years
Pumping and purification equipment	10 - 50 years
Distribution and transmission system	25 - 50 years
Collection system	50 years
Treatment facilities	25 years
Equipment and machinery	5 - 20 years
Furniture and fixtures	20 - 50 years
Computer equipment	5 years
Software	3 years

## ***NOTES TO FINANCIAL STATEMENTS***

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**Capital Contributions:** The State of Texas allows the assessment of system development on capital recovery fees that may be used only for additional infrastructure capacity. The System assesses impact fees and has recorded these in the amount of \$6,949,745 as nonoperating revenues in accordance with GASB Statement No. 33.

**Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

### **NOTE B - CITY ORDINANCE NO. 75686**

**Purpose:** On April 30, 1992, City Ordinance No. 75686 was adopted. This ordinance authorized the issuance of \$635,925,000 Water System Revenue Refunding Bonds, Series 1992, dated April 15, 1992. These bonds were issued to refund in advance of maturity \$253,064,519 Water Revenue Bonds authorized and outstanding under terms of City Ordinance No. 52091, \$330,125,000 Sewer Revenue Bonds authorized and outstanding under terms of City Ordinance No. 51975, \$14,500,000 of other bonded debt of annexed water districts, and \$49,200,000 Sewer System Commercial Paper. The purpose of this advance refunding was to release and discharge the covenants contained in City Ordinance No. 52091 and No. 51975 in order to permit the City to consolidate the operations of the water related utilities as stated in Note A.

**The System:** The System has been defined in City Ordinance No. 75686 as all properties, facilities, and plants currently owned, operated and maintained by the City and/or the Board of Trustees, for the supply, treatment, transmission and distribution of treated potable water, chilled water and steam, for the collection and treatment of wastewater and for water reuse, together with all future extensions, improvements, purchases, repairs, replacements and additions thereto, and any other projects and programs of the System; provided however, that the City retains the right to incorporate a stormwater system as provided by the Texas Local Government Code.

**Funds Flow:** City Ordinance No. 75686 requires that Gross Revenues of the System be applied in sequence to: (1) System Fund for payment of current maintenance and operating expenses including a two-month reserve amount based upon the budgeted amount of maintenance and operating expenses for the current fiscal year; (2) Debt Service Fund requirements of Senior Lien Obligations; (3) Reserve Fund requirements of Senior Lien Obligations; (4) Interest and Sinking Fund and Reserve Fund requirements of Junior Lien Obligations; (5) Interest and Sinking Fund and Reserve Fund requirements of Subordinate

## ***NOTES TO FINANCIAL STATEMENTS***

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Lien Obligations; (6) Payment of amounts required on Inferior Lien Obligations, and (7) Transfers to the City's General Fund and to the Renewal and Replacement Fund.

**Reuse Contract:** The System has a contract with City Public Service; the city owned electricity and gas utility, for the provision of reuse water. The revenues derived from the contract have been restricted in use to only reuse activities and are excluded from the calculation of Gross Revenues, and are not included in any transfers to the City's General Fund. Revenue derived from this contract was \$1,166,669 during the seven months ending December 31, 2001.

The System is developing a recycled water system, which will provide no potable water to various customers now using Edwards Aquifer water. During the seven months ended December 31, 2001, the System generated an additional \$252,085 in revenue from sales of recycled water. Revenue from recycled water sales is recorded as revenue of the System and has the same restrictions of the reuse contract.

**No Free Service:** City Ordinance No. 75686 also provides for no free services except for municipal fire-fighting purposes.

### **NOTE C - DEPOSITS AND INVESTMENTS**

City Ordinance No. 75686 permits the System to invest in time deposits or certificates of deposit secured in the manner required by law for public funds, or to invest in direct obligations of, including obligations guaranteed as to both principal and interest by, the United States of America, in obligations of any agencies or instrumentalities of the United States of America or as otherwise permitted by the System's investment policy, which is governed by state statutes.

The System's general depository agreement does not require the System to maintain an average monthly balance.

**Deposits:** All deposits are in two financial institutions and are carried at cost or amortized cost. Deposits at year-end are categorized below to give an indication of the level of risk assumed. Category 1 includes deposits insured by federal depository insurance or collateralized with securities held by the System or by its agent in the System's name. Category 2 includes deposits collateralized with securities held by the pledging financial institution's trust department or agents in the System's name. Category 3 includes deposits, which are considered uncollateralized.

**NOTES TO FINANCIAL STATEMENTS**

Deposits:	Category			Total Bank Balance	Book Balance
	1	2	3		
Cash on Hand	\$ -	\$ -	\$ -	\$ -	\$ 26,070
Demand and Savings Accounts	7,328,552	-	-	7,328,552	4,027,302
Certificates of Deposit	59,500,000	-	-	59,500,000	59,500,000
	<u>\$ 66,828,552</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 66,828,552</u>	<u>\$ 63,553,372</u>

**Investments:** The System has included as investments, certificates of deposit with an original maturity of over 90 days. All certificates of deposits classified as investments on December 31, 2001 were held at Bank of America, Dallas, Texas. All other investments as of December 31, 2001 were in securities of the U.S. Treasury or instrumentalities of the United States and were held in safekeeping by the System's general depository bank registered for the account of the System.

The System's investments are categorized below to give an indication of the level of risk assumed as of December 31, 2001. Category 1 includes investments that are insured, registered, or for which the securities are held by the System or its agent in the System's name. Category 2 includes, uninsured and unregistered investments for which the counter party's holds the securities by the counter party's trust department or agent in the System's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counter party's trust department or agent but not in the System's name.

Investments:	Category			Total Reported Amount	Fair Value
	1	2	3		
Money Market Investments: First Union Bank Held in Escrow	\$ -	\$ 24,746,588	\$ -	\$ 24,746,588	\$ 24,903,595
Money Market Investments: U.S. Treasury & Government Agency Securities	82,241,097	-	-	82,241,097	82,569,590
	<u>\$ 82,241,097</u>	<u>\$ 24,746,588</u>	<u>\$ -</u>	<u>\$ 106,987,685</u>	<u>\$ 107,473,185</u>

*NOTES TO FINANCIAL STATEMENTS*

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The following is a reconciliation of deposits and investments from the note to the balance sheet:

Reported Amounts from Note as presented above	
Deposits	\$ 63,553,372
Investments	<u>106,987,685</u>
	\$ <u>170,541,057</u>
Totals from Balance Sheet	
Restricted - Cash and Cash Equivalents	
Debt Service Fund	\$ 493,270
Construction Funds	<u>30,954,603</u>
Cash and Cash Equivalents	31,447,873
Investments	
Unrestricted	22,901,490
Restricted	
Debt Service Fund	22,367,038
Construction Funds	81,416,857
Customer's Deposits	5,007,576
Conservation	<u>7,400,223</u>
Investments	<u>116,191,694</u>
Total Cash, Cash Equivalents and Investments	\$ <u>170,541,057</u>

*NOTES TO FINANCIAL STATEMENTS*

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**NOTE D – UTILITY PLANT IN SERVICE**

Components of utility plant as of December 31, 2001 are summarized in the table below.

	<u>December 31, 2001</u>
Structures and improvements	\$199,352,035
Pumping and purification equipment	34,498,771
Distribution and transmission system	699,605,560
Collection system	453,754,532
Treatment facilities	406,920,184
Equipment and machinery	78,262,338
Furniture and fixtures	5,373,484
Computer equipment	11,412,296
Software	5,492,554
Water and water rights	<u>13,569,164</u>
Subtotal	1,908,240,918
Land and land rights	<u>45,223,776</u>
Total	<u>\$ 1,953,464,694</u>

Contributions in aid of construction were as follows:

Contributed capital May 31, 2000	\$ 598,076,317
Contributions FY 2000-01	<u>24,508,245</u>
Contributed capital May 31, 2001	<u>622,584,562</u>
Contributions FY 2002	-
Contributed capital December 31, 2001	<u>\$ 622,584,562</u>

The System implemented GASB 33 for the December 31, 2001 Comprehensive Annual Financial Report which requires that capital contributions in the amount of \$6,949,745 be recognized as revenues, not contributed capital.

**NOTE E – Leases / Note Payable**

**Leases:** The System entered into various lease agreements for financing the acquisition of computer equipment, software and heavy equipment. These lease agreements meet the requirements of a capital lease for accounting purposes and, therefore, are recorded at the present value of the future minimum lease payments as of the inception date. The terms of the leases are for three to five years with payments of \$23,869 monthly and \$286,435 annually. The annual percentage rate of the leases ranges from 3.18% to 5.8%. At the end of the respective lease terms, the ownership of the equipment transfers to the System. The following is a summary of changes in lease obligations for the seven months ended December 31, 2001:

Balance June 1, 2001	\$ 910,415
Less: Principal Payments	<u>142,316</u>
Balance December 31, 2001	<u>\$768,099</u>

The future minimum lease obligations and the present value of these minimum lease payments as of December 31, 2001, are as follows:

<u>Years Ending December 31,</u>	
2002	\$340,850
2003	340,850
2004	131,752
2005	<u>76,855</u>
Total Minimum Lease Payments	890,307
Less: Amount Representing Interest	<u>122,208</u>
Present value of minimum lease payments	<u>\$768,099</u>

**CPS Note Payable:** During fiscal year 2000, a contract was entered into between the System and City Public Service Board of San Antonio (CPS) whereby the System acquired water rights from certain CPS owned properties. A note was signed for 116 payments of \$40,000 at an interest rate of 7.5%. Total payments on this note are \$4,640,000 including interest. The liability as of December 31, 2001 is reflected on the balance sheet for both the current portion of \$268,127 and long-term amount of \$2,409,951. Payments in future years are as follows:

**NOTES TO FINANCIAL STATEMENTS**

<b>CPS NOTE PAYABLE</b>			
<u>Years Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Requirements</u>
2002	\$ 288,942	\$ 191,058	\$ 480,000
2003	311,374	168,266	480,000
2004	335,547	144,453	480,000
2005	361,596	118,405	480,000
2006	389,668	90,332	480,000
Thereafter	<u>990,952</u>	<u>89,048</u>	<u>1,080,000</u>
Total	<u>\$ 2,678,078</u>	<u>\$ 801,922</u>	<u>\$ 3,480,000</u>

**NOTE F - RISK MANAGEMENT**

The System is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

The System is self administered and self-insured for the first \$500,000 of each worker's compensation and \$250,000 for general liability, automobile liability and public official's liability and \$100,000 for pollution legal liability claim. Claims that exceed the self-insured retention limit are covered through the System's comprehensive commercial insurance program. For the seven months ended December 31, 2001, there were no reductions in insurance coverage from the previous year and there were no claims, which exceeded the self-insured retention limit. Settled claims have not exceeded the insurance coverage in any of the past three fiscal years. The System has recorded an accrued claims liability in the amount of \$1,728,796 as of December 31, 2001, which is reported as a current liability of the System.

The claims liability, including incurred but not reported claims, is based on the estimated ultimate cost of settling the claims. The claims liability includes medical and rehabilitation costs, which are considered incremental claim adjustment expenses. Changes in the liability amount for the last two fiscal years were:

	<u>Balance at Beginning-of- Fiscal-Year Liability</u>	<u>Current-Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>Balance at Fiscal Year-End Liability</u>
Year Ended May 31, 2001	\$ 2,863,236	\$ 912,726	\$ <1,601,848>	\$ 2,174,114
7 Months Ended December 31, 2001	2,174,114	823,838	<1,269,156>	1,728,796

**NOTES TO FINANCIAL STATEMENTS**

**NOTE G - REVENUE BONDS**

Senior Lien Water System Revenue Bonds, comprised of Series 1992, Series 1996, Series 1997, Series 1999 and Series 2001, outstanding in the amounts of \$594,200,000 are collateralized by a senior lien and pledge of the Gross Revenues of the System after deducting and paying the current expenses of operation and maintenance of the System and maintaining an operating reserve for operating and maintenance expenses. At December 31, 2001 these bonds are due in varying amounts, from a low of \$13,540,000 in 2019 to a high of \$38,690,000 in 2012.

Junior Lien Water System Revenue Bonds, comprised of Series 1999, Series 1999-A, Series 2001, and Series 2001-A outstanding in the amount of \$134,255,000 at December 31, 2001, are collateralized by a junior lien and pledge of the Gross Revenues of the System after deducting and paying the current expenses of operation and maintenance of the System maintaining an operating reserve for operating and maintenance expenses, and debt service on senior lien debt. At December 31, 2001 the Junior Lien bonds are due in varying amounts, from a low of \$1,920,000 in 2020 to a high of \$10,900,000 in 2019.

Annual debt service requirements are shown on the following page:

Annual Debt Service Requirements Revenue Bonds			
<u>Year Ended December 31,</u>	<u>Junior Lien Revenue and Refunding Bonds</u>	<u>Senior Lien Revenue and Refunding Bonds</u>	<u>Total</u>
2002	\$ 9,372,173	\$ 54,438,386	\$ 63,810,559
2003	9,366,401	54,694,590	64,060,991
2004	9,365,936	54,680,695	64,046,631
2005	9,355,712	54,705,534	64,061,246
2006	9,350,909	54,673,679	64,024,588
Thereafter	<u>142,175,958</u>	<u>708,947,831</u>	<u>851,123,789</u>
	<u>\$188,987,089</u>	<u>\$982,140,715</u>	<u>\$1,171,127,803</u>
Principal	\$134,255,000	\$594,200,000	\$ 728,455,000
Interest	<u>54,732,088</u>	<u>387,940,751</u>	<u>442,672,803</u>
	<u>\$188,987,088</u>	<u>\$982,140,715</u>	<u>\$1,171,127,803</u>

**Debt Covenants:** The System is required to comply with various provisions included in the ordinances, which authorized the bond issuance. The System is in compliance with all significant provisions of the ordinances.

**Prior Year of Defeasance of Debt:** In prior years, the System defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and liability for the defeased bonds are not included in the System's financial statements. At December 31, 2001, \$9,085,000 of bonds outstanding are considered defeased.

#### **NOTE H - COMMERCIAL PAPER PROGRAM**

The System maintains a Commercial Paper Program that is used to provide funds for the interim financing of a portion of capital improvements to the System.

On January 11, 2001, the City Council of the City of San Antonio approved the expansion of the Tax Exempt Commercial Paper Program (the "Commercial Paper Program) from \$175 million to \$350 million. The increase in the program provides interim financing for the increased level of future expenditures on water resource projects. Notes payable under the program cannot exceed maturities of 270 days and scheduled maturities of the short-term borrowing under the Commercial Paper Program may not extend past May 14, 2032.

The City has covenanted in the Ordinance authorizing the Commercial Paper Program (the "Note Ordinance") to maintain at all times credit facilities with banks or other financial institutions which would provide available borrowing sufficient to pay the principal of the Commercial Paper Program. The credit facility is maintained under the terms of a revolving credit agreement.

To further support the issuance of the Commercial Paper Program, on June 2, 2001 the City entered into the agreements with the following:

- Dealer Agreements with Goldman, Sachs & Co., J.P. Morgan Securities Inc., and Ramirez & Co., Inc.
- Revolving Credit Agreement with Westdeutsche Landesbank Girozentrale and Landesbank Baden-Wurttemberg.
- Issuing and Paying Agency Agreement with Bank One, National Association Chicago, Illinois.

**NOTES TO FINANCIAL STATEMENTS**

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The borrowings under the Commercial Paper Program are equally and ratably secured by and are payable from (i) the proceeds from the sale of bonds or additional borrowing under the Commercial Paper Program and (ii) borrowing under and pursuant to the revolving credit agreement

Commercial paper notes of \$185,000,000 are outstanding as of December 31, 2001. The proceeds of the notes have been used solely for financing of capital improvements of the System. The tax exempt commercial paper notes have been classified as long-term in accordance with the refinancing terms of the Credit Agreement and since management intends to continue the remarking of the tax exempt commercial paper notes to maintain a portion of its debt in variable rates. Interest rates on the notes outstanding at year- end range from 1.45% to 2.50% and from 34 to 153 days in maturity. The outstanding notes at December 31, 2001 had an average rate of 1.82% and averaged 85 days to maturity. The following summarizes transactions of the commercial paper program for the seven months ending December 31, 2001.

		December 31, 2001
Balances at beginning of fiscal year	\$	165,000,000
Issues of new notes		<u>20,000,000</u>
Balances at end of fiscal year	\$	185,000,000

**NOTE I- CONTINGENCIES AND COMMITMENTS**

The System is the subject of various claims and litigation, which have risen in the ordinary course of its operations. Management, in consultation with legal counsel, is of the opinion that the System's liabilities in these cases, if decided adversely to the System, will not be material.

The System is committed under various contracts for completion of construction or acquisition of utility plant totaling approximately \$93.8 million as of December 31, 2001. Funding of this amount will come from available revenues of the System, contributions from developers, and restricted assets.

**NOTE J - CAPITALIZED INTEREST COSTS**

Interest costs incurred on revenue bonds and commercial paper totaled \$25,527,512 during the seven months ended December 31, 2001 of which \$4,169,197 was capitalized as part of the cost of the System's utility plant additions.

**NOTE K - STORMWATER PROGRAM**

The Stormwater Program is a federally mandated program, under the Environmental Protection Agency for the monitoring of the quality and quantity of pollution found in rain runoff.

The City of San Antonio and the System have administrative responsibility for the Stormwater Program and have entered into an interlocal agreement, which establishes the entities' respective responsibilities. The System's responsibility is in various aspects of data collection and analysis related to the water quality of stormwater and responsibility for customer billings and collection. Costs incurred by the System related to the Stormwater Program are reflected as expenses and are reimbursed by the City. The following information provides a summary of the operations of the Stormwater Program.

	December <u>31, 2001</u>
Operating Revenues	\$2,145,880
Operating Expenses	<u>2,145,880</u>
Revenues over Expenses	\$ _____ =

As defined in City Ordinance No. 75686, the Stormwater Program is not considered a part of the "System" and as such, revenues generated by the Stormwater Program are used to pay expenses of the Stormwater Program but are not available for debt service of the System or for transfer to the City of San Antonio.

**NOTE L - PENSION AND RETIREMENT PLANS**

The System's retirement program includes benefits provided by Texas Municipal Retirement System, a contract with Principal Mutual Life Insurance Company, and Social Security.

Covered employees are eligible to retire upon attaining the normal retirement age of 65. An employee may elect early retirement, with reduced benefits, upon attainment of,

1. 20 Years of credited service regardless of age, or
2. 25 Years of credited service and at least age 50, or

## ***NOTES TO FINANCIAL STATEMENTS***

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3. 10 years of credited service and at least age 60.

The normal retirement benefit is based upon two factors, average compensation and years of credited service.

Average Compensation is defined as the monthly average of total compensation received for the three consecutive years ending December 31, out of the latest ten compensation years prior to normal retirement date which gives the highest average. The normal retirement benefit under the Principal Mutual contract is equal to:

1. 1.2% of the Average Compensation, times years of credited service not in excess of 25 years, plus
2. 0.75% of the Average Compensation, times years of credited service in excess of 25 years but not in excess of 35 years, plus
3. 0.375% of the Average Compensation, times years of credited service in excess of 35 years.

Upon retirement, an employee must select from one of seven alternative payment plans. Each payment plan provides for monthly payments as long as the retired employee lives. The options available address how plan benefits are to be distributed to the designated beneficiary of the retired employee. The program also provides death and disability benefits.

The following information related to the Texas Municipal Retirement System and Principal Mutual Life Insurance has been prepared as of January 1, 2001.

### **Texas Municipal Retirement System**

The Texas Municipal Retirement System (TMRS) was established in 1948 as a retirement and disability pension system for municipal employees in the State of Texas. It is administered in accordance with the Texas Municipal Retirement System Act (the Act), Subtitle G of Title 110B, Revised Civil Statutes of Texas, 1925 as amended, and is governed by a Board of Directors appointed by the Governor of Texas in accordance with the Act. TMRS issues a publicly available financial report that includes financial information related to participating municipalities. The report may be obtained by writing to: TMRS, P.O. Box 149153, Austin, Texas 78714-9153 or calling (512) 476-7577.

**Plan Description:** The System provides pension benefits for all of its full-time employees through a nontraditional, joint contributory, defined contribution plan in the state-wide Texas Municipal Retirement System (TMRS), one of 758 administered by TMRS, an agent multiple-employer public employee retirement system. It is the opinion of the TMRS Management that the plans in TMRS are

## *NOTES TO FINANCIAL STATEMENTS*

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substantially defined contribution plans, but they have elected to provide additional voluntary disclosure to help foster a better understanding of some nontraditional characteristics of the plan.

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the System- financed monetary credits, with interest. At the date the plan began, the System granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percent (100%, 150%, 200%) of the employee's accumulated contributions. In addition, the System can grant as often as annually another type of monetary credit referred to as an updated service credit which is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and System matching percent had always been in existence and if the employee's salary had always been the average of his salary in the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the employer-financed monetary credits with interest were used to purchase an annuity.

Members can retire at ages 60 and above with 5 or more years of service or with 20 years of service regardless of age. A member is vested after 5 years. The plan provisions are adopted by the System within the options available in the state statutes governing TMRS and within the actuarial constraints also in the statutes.

**Contributions:** The contribution rate for the employees is 3% of salary, and the System matching percent ratio is currently 1 to 1, both as adopted by the System. Under the state law governing TMRS, the actuary annually determines the System contribution rate. This rate consists of the normal cost contribution rate and the prior service cost contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the currently accruing monetary credits due to the System matching percent, which are the obligation of the System as of an employee's retirement date not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the System to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period.

**NOTES TO FINANCIAL STATEMENTS**

The unit credit actuarial cost method is used for determining the System contribution rate. Both the employees and the System make contributions monthly. Since the System needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that is the basis of the rate and the calendar year when the rate goes into effect. (i.e. December 31, 2001 valuation is effective for rates beginning January 2003)

Texas Municipal Retirement System				
Calculation of Net Pension Obligation (NPO)				
Year	Annual Required Contribution (ARC)	Annual Pension Cost (APC)	Percentage of APC Contributed	NPO Balance
2000(1)	\$1,592,935	\$1,592,935	100%	\$0
2001(1)	\$1,619,608	\$1,619,608	100%	0
2001(2)	\$1,044,414	\$1,044,414	100%	0

- (1) Covers year ended May 31, 2000, and 2001, respectively
- (2) Covers seven months ended December 31, 2001.

**Required Three- Year Trend Information:**

The Schedules of Funding Progress for the last three fiscal years as required under GASB Statement No. 27 are located in the “Required Supplementary Information” section of this report. The Schedules are designed to provide information about the System’s progress in accumulating sufficient assets to pay benefits due.

Texas Municipal Retirement System			
Schedule of Contributions			
	<u>2001 (2)</u>	<u>2001 (1)</u>	<u>2000 (1)</u>
Employer Contribution	\$1,044,414	\$1,619,608	\$1,592,935
Employee Contribution	1,007,637	1,508,732	1,494,947
Employer Contribution Rate	3.11%	3.11%	3.05%

- 1) Covers year ended May 31, 2000, and 2001 respectively
- 2) Covers seven months ended December 31, 2001.

<b>Texas Municipal Retirement System Actuarial Assumptions</b>	
Actuarial Cost Method -	Unit Credit
Amortization Method -	Level Percent of Payroll
Remaining Amortization Period -	25 Years – Open Period
Asset Valuation Method -	Amortized Cost
Investment Rate of Return -	8%
Projected Salary Increases -	None
Includes Inflation At -	None
Cost – Of – Living Adjustments -	None

**Principal Mutual Life Insurance**

**Plan Description:** The San Antonio Water System Pension Plan is a single-employer defined benefit pension plan controlled by the provisions of Ordinance No. 75686, which serves as a supplement to the TMRS and Social Security benefits. The plan is governed by the System which may amend plan provisions and which is responsible for the management of plan assets. The System has delegated the authority to manage certain plan assets to Principal Mutual Life Insurance Company. The System's covered payroll for employees at January 1, 2001 under this contract was \$51,050,189.

The System provides supplemental pension benefits for all persons customarily employed at least 20 hours per week and five months per year through this defined benefit pension plan. Employees are eligible to participate in the plan on January 1 of the calendar year following date of hire. An employee covered by the plan may vest a portion of the plan benefits if termination occurs after sufficient years of service have been credited. The plan allows an employee to accrue vesting benefits as follows:

<b>Principal Mutual Life Insurance</b>	
<u>Years of Service</u>	<u>Vested Percentage</u>
Less than 5	0%
5	50%
6	60%
7	70%
8	80%
9	90%
10 or more	100%

**NOTES TO FINANCIAL STATEMENTS**

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An employee is automatically 100% vested upon attainment of age 65 or upon becoming totally and permanently disabled.

Benefits for retired employees are fully guaranteed at retirement. The pension plans unallocated insurance contracts are valued at contract value. Contract value represents contributions made under the contract, plus interest at the contract rate, less funds used to purchase annuities or pay administrative expense charged by Principal Life Insurance Company.

**Actuarially Determined Contribution Requirements and Contributions Made:** The plan's funding policy provides for actuarially determined periodic contributions so that sufficient assets will be available to pay benefits when due. The actuarial cost method is known as the Entry Age Normal-Frozen Initial Liability Method. This method spreads the total cost of the projected pension benefits for each employee evenly from the date the employee is first eligible for the plan to the employee's assumed retirement age. As plan benefits are related to compensation, the cost is spread as a level percentage of compensation. The total of annual amounts for all employees combined is called the Normal Cost. The employee's Entry Age is determined as if the plan had always been in existence. As of the plan effective date, there are some accumulated Normal Costs for past years that have not been paid. The value of these costs is called the Frozen Initial Liability.

In subsequent years the Frozen Initial Liability is reduced by employer deposits to the plan in excess of employer Normal Cost and interest requirements. This reduced amount is known as the Unfunded Frozen Initial Liability. Contribution requirements are established and maybe amended by the System. Active members are not required to contribute to the plan. Any obligation with respect to the pension plan shall be paid by the System. The actuarial valuation which was performed for the plan year ended December 31, 2001 reflects an unfunded frozen initial liability of \$8,884,276.

<u>Plan Year</u>	<u>Annual Required Contribution (ARC)</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>NPO Balance</u>
1999	\$ 4,753,030	\$ 4,753,030	100%	\$ -
2000	2,770,064	2,770,064	100%	-
2001	2,968,831	2,968,831	100%	-

If the Normal Cost or Unfunded Frozen Liability becomes negative through the normal operation of the plan, the unfunded Frozen Liability will be reestablished using the Entry Age Normal method. If the

**NOTES TO FINANCIAL STATEMENTS**

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reestablishment would result in a negative Normal Cost or Unfunded Frozen Liability, the method will be changed to the Aggregate method. If the actuarial value of assets exceeds the total present value of benefits, the Aggregate Normal Cost will be zero. Then the Frozen Initial Liability will be reestablished when a positive Entry Age Normal unfunded liability results from a change in assumptions or a plan amendment.

<b>Principal Mutual Life Insurance Actuarial Assumptions</b>	
Actuarial Cost Method -	Entry Age Normal – Frozen Initial Liability Period
Amortization Method -	Level Dollar
Remaining Amortization Period -	39 Years – Closed Period
Asset Valuation Method -	Amortized Cost
Investment Rate of Return -	8.5%
Salary Scale -	Table S-5 from the Actuary’s Pension Handbook plus 3.4%
Cost -of -Living Adjustments-	None

**Required Three-Year Trend Information:** The schedule of funding progress for the last three fiscal years are required under GASB Statement No. 27 and are located in the “Required Supplementary Information” section of this report. The schedules are designed to provide information about the system’s progress in accumulating sufficient assets to pay benefits due.

The Pension Fund issues a publicly available financial report that includes financial statements and required supplemental information. That report may be obtained by writing to: Principal Life Insurance Company, Pension Diversified Retirement Services, Des Moines, Iowa 50392-0001 or by calling (515) 247-5111.

**NOTE M - OTHER POST EMPLOYMENT BENEFITS**

In addition to providing pension benefits described in Note L, the System provides certain health care and life insurance benefits for retired employees. Substantially all full-time employees who retire from the System may become eligible for those benefits. On December 31, 2001, there were 368 retirees with life insurance and 316 retirees with medical coverage.

The System provides medical and life insurance for retirees and recognizes the cost of providing these benefits on a pay-as-you-go basis by expensing the annual insurance. Premiums for medical insurance

**NOTES TO FINANCIAL STATEMENTS**

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amounted to \$1,572,783 for June 1, 2001 through December 31, 2001. Premiums for life insurance amounted to \$29,231 for June 1, 2001 through December 31, 2001. Those and similar benefits for active employees are provided through insurance companies.

**NOTE N – RESTATED RETAINED EARNINGS**

Prior Year retained earnings have been restated due to an asset that was capitalized that had previously been expensed in the amount of \$175,000.

Balance, May 31, 2001	\$285,940,919
Asset reclassification	\$ 175,000
Balance, December 31, 2001	\$286,115,919

**NOTE O – SUBSEQUENT EVENTS**

On March 21, 2002, the System issued \$300,510,000 in City of San Antonio Water System Revenue Refunding Bonds, Series 2002. The proceeds from the sale of the Bonds were used to (1) refund \$282,000,000 Series 1992 water system revenue bonds of the System, and (2) to pay the cost of issuance. The Net interest rate of the refunding issue is 5.22% and represents substantial savings on the debt previously outstanding from 1992. The present value of debt service payments over the life of the bonds is estimated at \$7.7 million or a 2.756% savings.

On March 21, 2002, the System issued \$137,820,000 in City of San Antonio Water System Revenue Bonds, Series 2002-A. The proceeds from the sales of the Bonds will be used to (1) acquire, purchase, construct, improve, renovate, enlarge or equip the System, and (2) pay the cost of issuance.

On March 28, 2002, the System issued \$15,560,000 in City of San Antonio Water System Junior Lien Revenue Bonds, series 2002, and \$12,090,000 in City of San Antonio Water System Junior Lien Revenue Bonds, Series 2002-A with the Texas Water Development Board. The proceeds from the sale of the Bonds will be used to (1) finance capital improvement projects involving water recycling which qualify under the Texas Water Development Board program, (2) finance capital improved projects involving waste water which qualify under the Texas Water Development Board Program, and (3) pay the cost of issuance.