

SAN ANTONIO WATER SYSTEM
Memorandum

TO: Audit Committee of San Antonio Water System Board of Trustees

FROM: Doug Evanson, Sr. Vice President/Chief Financial Officer
Mary Bailey, Controller

SUBJECT: 2013 Management Letter Comments

DATE: March 31, 2014

The following summarizes the status of various points raised by the external auditors in connection with their fiscal year 2013 audit. The following reiterates the findings and recommendations by the auditors as well as the responses of management relative to each finding. If you desire further information, relative to any of these matters, please do not hesitate to contact me.

Section B – Management Letter

CONTROL DEFICIENCIES

Actuarial Review of Workers' Compensation, General Liability, and Automobile Claims

SAWS currently has a system for estimating the liability for workers' compensation, general liability, and automobile claims, which includes an estimate for incurred, but not reported ("IBNR") claims and reserves for workers' compensation claims. The estimate used for IBNR claims is based on a percentage of claims outstanding at the end of each year. The percentage used in this calculation has not been compared to claims history or other information to determine if the IBNR reserve is sufficient. SAWS has not historically engaged an outside actuarial firm to review the IBNR claim estimate for these liabilities. Since these are significant estimates, a periodic actuarial review could provide for a more accurate estimate of the liabilities as of the end of the year.

We recommend SAWS consider having the estimated liability actuarially determined on a periodic basis and review its internal risk management claims system for information that can be used to assess the accuracy of the reserves established.

Management's Response:

SAWS will engage an outside actuarial firm in 2014 to determine the appropriate liability for incurred claims. Thereafter, we will engage a consultant for a review at a minimum frequency of every three years to ensure that the recorded liability for claims is accurate.

Wire Transfers

During our review of control procedures over wire transfers, we had the following observations:

- Wire transfer limits for concentration accounts have a limit of \$99.9 million.
- There is one primary administrator for wire transfers who, based on current settings, can add and delete users, change passwords, as well as assign a token or electronic key fob (method of authentication).

We recommend SAWS consider strengthening the segregation of duties over wire transfers to mitigate the chances of any unauthorized transactions by implementing the following:

- Reduce the wire transfer limit to a smaller dollar amount. Twice a year SAWS is required to make large wire transfers for debt service; during that period, the wire transfer limit could be raised and then lowered to a more reasonable amount after the debt service payments are made.
- Assign a second wire transfer administrator whereby one administrator would be responsible for adding users and the second administrator would be responsible for assigning roles to any new user.

Management's Response:

The current wire transfer process requires two staff members to complete a wire transfer, one to enter the wire amount and instructions, and another to approve the wire transfer. There is a limited number of SAWS staff, a total of five, who are authorized in the Frost Bank system to make wire transfers.

SAWS will reduce the limit of allowable wire transfers to \$5 million for each of the five staff members who are authorized to make wire transfers, and temporarily increase the limit when debt service payments are due .

SAWS agrees that there should be a segregation of duties among system users. SAWS will implement an internal policy whereby one system administrator will add users and another will assign roles. SAWS will meet with Frost Bank personnel to determine if we can utilize system functionality to limit these duties. To the extent that the system will not allow limited administrative access, SAWS will pursue other controls to review system user activity and compliance with this policy.

Pension Plan Disbursements (SAWS DSP Only)

SAWS DSP currently administers a frozen defined benefit pension plan. The plan administrator or sponsor, as fiduciary of the plan, has the primary responsibility for administering plan assets. SAWS DSP currently uses a third-party administrator (“TPA”) to perform administrative functions for the plan; however, SAWS DSP still has ultimate fiduciary responsibility for plan assets. During our testing of disbursements (lump-sum distributions, partial lump-sum distributions, and retirement benefit payments) from the plan, we noted that, out of a sample of 16 distributions, 6 were lump-sum distributions and 4 were partial lump-sum distributions. However, due to turnover in personnel, we could not determine, due to lack of documentation, if the inputs used to determine the amounts of each distribution were reviewed and authorized by SAWS DSP. The TPA did provide a Retirement Benefit Final Calculation letter to each separating plan member and SAWS DSP during the year.

We recommend SAWS DSP review new distributions or withdrawals and verify information, such as years of service, salary history, etc., to ensure the TPA is using the proper information when calculating the distributions. Additionally, SAWS DSP should review change reports to determine if any regular distributions have changed and if those changes are proper. This review should be performed monthly and documented.

Management’s Response:

In March 2014, SAWS outlined a series of procedures that will be followed with regard to verifying the data used in retiree distribution calculations and monitoring changes in retiree distributions. SAWS will work with the TPA of the SAWS DSP frozen retirement plan to ensure that these procedures are followed for all distributions.