

**Flexible Rate Revolving Note Private Placement Program
Second Group of Questions and Answers - May 3, 2012**

1. The 2011 Bexar Met Auditor's Report discloses that they also issued an opinion on Bexar Met's internal controls and compliance (A-133), yet this report is not attached to the 2011 Audit that was posted on EMMA. Can we get a copy of that report? If there are any issues, material items, etc. can you describe them and let us know the status of each and what SAWS is doing in response to them?

Response – Attached is the Bexar Met Summary Report to the Audit Committee for Year Ended April 30, 2011. We are currently evaluating the responses to the report. Padgett & Stratemann is currently performing an audit of Bexar Met's financial results as of 1/31/2012. Any findings from the 1/31/2012 audit will be reviewed and appropriate action will be taken.

2. Note 17 of the Bexar Met audit discloses that pending litigation could have a material impact. Please describe all pending litigation, its pending impact and current status.

Response – The DSP is a defendant in various lawsuits and is aware of pending litigation arising in the ordinary course of its operations, certain of which seek various amounts of damages. The DSP intends to defend vigorously against the litigation; however, no prediction can be made as of the date hereof with respect to the liability of the DSP for such claims or the outcome of such lawsuits. Following is a list of known pending litigation that we believe could have a material impact:

2011-CI-08007; 166th Judicial District Court of Bexar County, Texas; Victor Mercado v. Bexar Metropolitan Water District Public Facility Corporation. This is an employment claim alleging breach of contract. Plaintiff Victor Mercado, former General Manager for Bexar Metropolitan Water District was terminated on or about December 16, 2010. Mr. Mercado has alleged damages in the amount of \$190,000, plus attorneys fees, costs and interest. Discovery is currently ongoing. A trial date has not yet been set.

2005-CI-19527; 288th Judicial District Court of Bexar County, Texas; Sylvia Gamez v. Bexar Metropolitan Water District, et. al. This is an employment suit alleging defamation of character, invasion of privacy, civil conspiracy, tortious interference with contract, violations of the Public Information Act, and violations of the Texas Open Meetings Act. Plaintiff, a former BexarMet employee, was terminated in 2005 based on information contained in an investigative report regarding improper conduct between Plaintiff and BexarMet General Manager, Tom Moreno. Plaintiff alleges damages in the amount within the jurisdictional limits of the Court, exemplary damages, costs and interest. The suit was filed on December 14, 2005, and the last trial setting of November 2010 was dropped. There is not a current trial date set for this matter.

Please refer to the *Bexar Met/Water Exploration Company Water Supply Agreements* disclosure under the LITIGATION AND REGULATORY MATTERS: San Antonio Water System Litigation and Claims section of the official statement for the \$31,890,000 City of San Antonio Water System Junior Lien Revenue Refunding Bonds, Series 2012 (NO RESERVE FUND) for a description of potential litigation.

3. What provision in Bexar Met's Additional Bonds Test allows for Bexar Met (DSP) to still be in compliance with that test when the DSP is taking on what will essentially be a \$70 million - \$100 million bullet payment at the end of 5 years (the requested Note Purchase Program)?

Response – Chapter 1371 of the Texas Government Code allows for an assumed amortization period of 40 years. Amortizing the notes over the allowable period of 40 years, the DSP is in compliance with the Additional Bonds Test. This position will be confirmed with the Texas Attorney General during the approval process.

4. Please clarify the lien of the Note Program? In the RFP, Section I C. "Security for the Notes", the RFP indicates the Notes are secured by a subordinate lien on and pledge of the DSP Net Revenues. However, on Page 5 of the sample Note Purchase Agreement - Section 1.1(a) – last sentence - indicates "Notes are payable from and secured by a subordinate and inferior lien on and pledge of Net Revenues" - which matches the *DSP Inferior Lien Obligations* definition located in Section DDD. on page 14 of the Ordinance.

Response – The Notes will be issued at the subordinate lien level. The Notes Agreement will be revised.

5. In Section 4a (vi) - the Ordinance states that the City will fix and maintain rates and collect charges and provide revenues sufficient at all times:(vi) to produce DSP Net Revenues equal to at least 1.10X maximum annual requirement for the payment of principal of an interest on the DSP Subordinate Lien Obligations. Since the Notes have annual maturities, will rates and charges be sufficient to meet this test? If not, does Section 4 (vii) apply which refers to DSP Inferior Lien Obligations and includes the proceeds of other DSP Debt Obligations in addition to DSP Net Revenues?

Response – Chapter 1371 of the Texas Government Code allows for an assumed amortization period of 40 years. Amortizing the notes over the allowable period of 40 years, the DSP is in compliance with the coverage requirements. This position will be confirmed with the Texas Attorney General during the approval process.

6. Please provide proforma coverage calculations for both the Senior Lien and Subordinate Lien Obligations of SAWS, after the initial draw on the Note Program and refunding of the Senior Lien Obligations. Also, please provide SAWS estimates of Average Annual Debt Service Requirements for the Notes, and the assumptions regarding the Note interest rate.

Response – The projected coverage ratios are outlined on page 11 and 12 of the presentation reviewed at the bank meetings. The projections on page 12 assumes refunding of the Series 1998, Series 2002 Bonds and Loan Notes with approximately \$71 million of the Note Program, with no principal amortization of the Note Program during the term of the Note Purchase Agreement.

7. Will the Note Ordinance include pre-approved authorization to issue up to \$100MM of Notes at anytime over the next 3 years, or will subsequent approvals be required by to meet the issuance of Additional Subordinate Lien Obligations?

Response – The Note Ordinance will approve a financing program authorizing the issuance of up to \$100MM notes at anytime outstanding. This authorization will remain

in effect until System Integration (as provided for under the DSP Ordinance). No additional City Council approval is required. This programmatic authorization could extend beyond the termination of the initial note purchase agreement (including the optional extension periods).

8. In the Note Purchase Agreement, Section 1.1 (f), please clarify whether each Note has a maturity date of 1 year, or the Termination Date (3 years in the future)?

Response – All Notes will have a maturity of one year or less with maturing notes being replaced with new notes during the term of the Note Purchase Agreement.

9. On the Termination Date, will all amounts under the Note Program be due and payable?

Response – Upon the termination of the Note Purchase Agreement, all notes will be due and payable.

10. Are Note Maturity Dates limited to May 1 of each year per the various references to Additional Subordinate Lien Obligations in the Ordinance?

Response – As required by the subordinate lien ordinance, the notes will mature on May 1. The initial notes may have a maturity of less than one year, with maturing notes being replaced with new notes during the term of the Note Purchase Agreement.

11. What does SAWS value the assets of the DSP at (if different from what we will see in the financial statement of the DSP)?

Response – Padgett & Stratemann is currently performing an audit of Bexar Met's financial results as of 1/31/2012. We are currently evaluating certain potential adjustments that may affect those results.