

# San Antonio Water System

Report to the Audit Committee and Board of Trustees  
May 31, 2017





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To the Audit Committee and Board of Trustees  
San Antonio Water System  
San Antonio, Texas

**RSM US LLP**

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Attention: Members of the Audit Committee and Board of Trustees

We are pleased to present this report related to our audit of the basic financial statements of San Antonio Water System (SAWS) as of and for the year ended December 31, 2016. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for SAWS' financial reporting process.

This report is intended solely for the information and use of the Board of Trustees, Audit Committee and management, and is not intended to be, and should not be, used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have about this report. We appreciate the opportunity to continue to be of service to SAWS.

*RSM US LLP*

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## Required Communications

Generally accepted auditing standards (AU-C 260, *The Auditor's Communication With Those Charged With Governance*) require the auditor to promote effective two-way communication between the auditor and those charged with governance. Consistent with this requirement, the following summarizes our responsibilities regarding the basic financial statement audit, as well as observations arising from our audit that are significant and relevant to your responsibility to oversee the financial reporting process.

<b>Area</b>	<b>Comments</b>
<b>Our Responsibilities With Regard to the Financial Statement Audit</b>	<p>Our responsibilities under auditing standards generally accepted in the United States of America and <i>Government Auditing Standards</i> issued by the Comptroller General of the United States have been described to you in our arrangement letter, dated December 5, 2016. Our audit of the financial statements does not relieve management or those charged with governance of their responsibilities, which are also described in that letter.</p>
<b>Overview of the Planned Scope and Timing of the Financial Statement Audit</b>	<p>We have issued a separate communication regarding the planned scope and timing of our audit and have discussed with you our identification of, and planned audit response to, significant risks of material misstatement.</p>
<b>Accounting Policies and Practices</b>	<p><b>Preferability of Accounting Policies and Practices</b> Under accounting principles generally accepted in the United States of America, in certain circumstances, management may select among alternative accounting practices. In our view, in such circumstances, management has selected the preferable accounting practice.</p> <p><b>Adoption of, or Change in, Accounting Policies</b> Management has the ultimate responsibility for the appropriateness of the accounting policies used by SAWS. Following is a description of significant accounting policies or their application that were either initially selected or changed during the year:</p> <p>During the year ended December 31, 2016, SAWS adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 72, <i>Fair Value Measurement and Application</i>; GASB Statement No. 76, <i>The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments</i> and GASB Statement No. 79, <i>Certain External Investment Pools and Pool Participants</i>. There was no material impact to the financial statements as a result of these new pronouncements other than additional disclosures about SAWS' investments measured at fair value.</p> <p><b>Significant or Unusual Transactions</b> We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.</p>

Area	Comments
<b>Accounting Policies and Practices (Continued)</b>	<b>Management's Judgments and Accounting Estimates</b> Summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates is in the attached Summary of Significant Accounting Estimates.
<b>Audit Adjustments</b>	Audit adjustments proposed by us and recorded by SAWS are listed in the attached Summary of Recorded Audit Adjustments.
<b>Uncorrected Misstatements</b>	Uncorrected misstatements are summarized in the attached Summary of Uncorrected Misstatements.
<b>Disagreements With Management</b>	We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the basic financial statements.
<b>Consultations With Other Accountants</b>	We are not aware of any consultations management had with other accountants about accounting or auditing matters.
<b>Significant Issues Discussed With Management</b>	No significant issues arising from the audit were discussed with or were the subject of correspondence with management, other than the discussions held with management regarding the accounting and financial reporting for the capitalization of self-constructed assets.
<b>Significant Difficulties Encountered in Performing the Audit</b>	We did not encounter any significant difficulties in dealing with management during the audit.
<b>Letter Communicating Significant Deficiency in Internal Control Over Financial Reporting</b>	We have separately communicated the significant deficiency in internal control over financial reporting identified during our audit of the basic financial statements, as required by <i>Government Auditing Standards</i> . This communication is included in the compliance and internal control communication.
<b>Significant Written Communication Between Management and Our Firm</b>	A copy of a material written communication between our firm and management of SAWS, the representation letter provided to us by management, is attached as Exhibit A.

## Summary of Significant Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses its knowledge and experience about past and current events, and certain assumptions about future events. Management may wish to monitor throughout the year the process used to determine and record these accounting estimates. The following describes the significant accounting estimates reflected in the SAWS' December 31, 2016, basic financial statements.

<b>Estimate</b>	<b>Accounting Policy</b>	<b>Management's Estimation Process</b>	<b>Basis for Our Conclusions on Reasonableness of Estimate</b>
<b>Depreciable Useful Lives of Capital Assets</b>	The depreciable useful lives of capital assets are set at the estimated useful life of the related asset.	The determination is made at the time the asset is placed into service and involves assumptions on the estimated useful life based on past experience and management's general knowledge.	We scanned the estimated useful lives assigned to asset categories with in-service assets. We believe the estimates are reasonable.
<b>Fair Value of Investments</b>	SAWS records its investments at fair value.	The fair value of investment securities is provided by investment advisors, who value the securities using a computerized pricing service utilizing a yield-based matrix system to arrive at an estimated market value.	We tested the proprietary of information underlying management's estimates, including obtaining an independent price verification with a specialist. We conclude that management's estimates are reasonable.
<b>Allowance for Uncollectible Accounts</b>	All receivables are reported at net realizable value.	The allowance is estimated based on applying noncollectible percentages to an aging of the accounts. Management evaluates and adjusts based on current economic conditions.	We have audited the underlying data supporting the estimate and conclude the resulting estimate to be reasonable.

<u>Estimate</u>	<u>Accounting Policy</u>	<u>Management's Estimation Process</u>	<u>Basis for Our Conclusions on Reasonableness of Estimate</u>
<b>Accounting for Pension Plans and Related Net Pension Liabilities</b>	Net pension liabilities and related pension amounts are actuarially determined in accordance with the parameters established by GASB.	Management and the actuary develop the actuarial assumptions based on relevant criteria for investments returns, mortality, inflation, discount rates and others. The actuary prepares the actuarial reports and GASB Statement No. 68 schedules. Management reviews and approves the resulting pension related estimates.	We tested the underlying participant data, obtained the actuarial reports and had an internal specialist review the significant assumptions and conclusions. We conclude that the estimates are reasonable.
<b>Accounting for Other Post Employment Benefits (OPEB)</b>	The OPEB cost is recognized based on the annual required contribution of the employer, and the amount is actuarially determined in accordance with parameters of GASB Statement No. 45.	Management, with input from its OPEB actuary, developed the actuarial assumptions based on relevant criteria. Management reviewed and approved the financial statement estimates derived from the OPEB actuarial report.	We tested the underlying data, obtained the actuarial reports and had an internal specialist review the significant assumptions and conclusions. We conclude that the estimates are reasonable.
<b>Derivative Instrument Liability</b>	SAWS records its derivative instrument at estimated fair value.	The derivative instrument liability is calculated by an external specialist and reviewed by management for reasonableness.	We tested the proprietary of information underlying management's estimates. Based on our procedures, which included obtaining independent pricing information, we conclude that management's estimates are reasonable.

# Summary of Recorded Audit Adjustments

Number	Date	Name	Debit	Credit
AJE 1	12/31/2016	Costs Capitalized to Construction in Progress (Expense)	\$ 4,810,283	
AJE 1	12/31/2016	Construction in Progress		\$ 4,810,283
			\$ 4,810,283	\$ 4,810,283

## Summary of Uncorrected Misstatements

During the course of our audit, we accumulated an uncorrected misstatement that was determined by management to be immaterial, both individually and in the aggregate, to the financial position, results of operations, cash flows and related basic financial statement disclosures. Following is a summary of the difference.

Description	Debit (Credit) to Correct the Misstatements				
	Assets	Liabilities	Net Position	Revenue	Expense
Actual misstatement:					
To decrease capitalized self-constructed assets and increase expenses	\$ (5,283,189)	\$ -	\$ 5,283,189	\$ -	\$ 5,283,189

**Exhibit A—Significant Written Communication Between Management and Our Firm**



May 31, 2017

RSM US LLP  
19026 Ridgewood Parkway, Suite 400  
San Antonio, Texas 78259

This representation letter is provided in connection with your audit of the basic financial statements of the San Antonio Water System, a component unit of the City of San Antonio, Texas ("SAWS, entity or auditee"), as of and for the year ended December 31, 2016 for the purpose of expressing an opinion on whether the financial statements are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

We confirm, to the best of our knowledge and belief, that as of May 31, 2017:

#### **Financial Statements**

1. We have fulfilled our responsibilities, as set out in the terms of the audit arrangement letter dated December 5, 2016 for the preparation and fair presentation of the financial statements referred to above in accordance with U.S. GAAP.
2. We acknowledge our responsibility for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.
3. We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.
4. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable and reflect our judgment based on our knowledge and experience about past and current events, and our assumptions about conditions we expect to exist and courses of action we expect to take.
5. We agree with the findings of specialists in evaluating our self-insurance program, the estimated liability for other post-employment benefit obligations and the pension plans net pension liability and related pension amounts, and have adequately considered the qualifications of the specialists in determining the amounts and disclosures used in the financial statements and underlying accounting records. We did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an impact on the independence or objectivity of the specialists.
6. Related-party transactions, including those with the primary government having accountability for SAWS, and interfund transactions, including interfund accounts and advances receivable and payable, sale and purchase transactions, interfund transfers, long-term loans, leasing arrangements and guarantees, have been recorded in accordance with the economic substance of the transaction and appropriately accounted for and disclosed in accordance with the requirements of U.S. GAAP.
7. We are a component unit of the City of San Antonio, Texas as this term is defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards.

8. All events subsequent to the date of the financial statements, and for which U.S. GAAP requires adjustment or disclosure, have been adjusted or disclosed.
9. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with U.S. GAAP.
10. We have no direct or indirect legal or moral obligation for any debt of any organization, public or private, that is not disclosed in the financial statements.
11. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
12. We represent that the accounting and financial reporting related to the presentation and disclosure of the change in net position reporting for accumulated but unspent capital recovery fees as well as the capitalization or expensing of self-constructed assets is appropriate. Management believes the reporting of these items in the previously issued financial statements would not have misled the users of SAWS' financial statements.
13. We represent there are no consultations management had with other accountants about accounting or auditing matters.
14. Management has reviewed the accounting and reporting requirements under GASB 69 *Government Combinations and Disposals of Government Operations* ("GASB 69") related to the SAWS DSP dissolution and transfer of assets, liabilities and operations to SAWS which was treated as a government merger in accordance with GASB 69 and thus agrees with the restatement of the December 31, 2015 financial statements. In that regard, we do not believe it is necessary to recall those financial statements and all users of those financial statements will receive a copy of the current year's financial statements and independent auditor's report.
15. We believe that the effects of the adjustment proposed as part of your "Summary of Unrecorded Misstatements" in your Report to the Audit Committee and Board of Trustees dated May 31, 2017 related to internal costs capitalized to self-constructed assets in the amount of \$5,283,189 is immaterial, both individually and in the aggregate, to the basic financial statements as of and for the year ended December 31, 2016. For purposes of this representation, we consider items to be material, regardless of their size, if they involve the misstatement or omission of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement. The proposed adjustment has not been reflected in the financial statements as of and for the year ended December 31, 2016. If the adjustment had been reflected in those financial statement, reported Assets and Net Position would decrease \$5,283,189 and Expenses would increase \$5,283,189.

### Information Provided

16. We have provided you with:
  - a. Access to all information of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation and other matters;
  - b. Additional information that you have requested from us for the purpose of the audit;
  - c. Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence; and
  - d. Minutes of the meetings of the governing board and committees, or summaries of actions of recent meetings for which minutes have not yet been prepared.
17. All transactions have been recorded in the accounting records and are reflected in the financial statements.
18. We have disclosed to you the results of our assessment of risk that the financial statements may be materially misstated as a result of fraud.
19. We have no knowledge of allegations of fraud or suspected fraud affecting the entity's financial statements involving:
  - a. Management.
  - b. Employees who have significant roles in internal control.
  - c. Others where the fraud could have a material effect on the financial statements.
20. We have no knowledge of any allegations of fraud or suspected fraud affecting the entity's financial statements received in communications from employees, former employees, analysts, regulators or others.
21. We have no knowledge of noncompliance or suspected noncompliance with laws and regulations whose effects were considered when preparing financial statements.
22. We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.
23. We have disclosed to you the identity of the entity's related parties and all the related-party relationships and transactions of which we are aware.
24. We informed you of all significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect SAWS' ability to record, process, summarize and report financial data.
25. We are aware of no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
26. We represent that during the year ending December 31, 2016 management determined that overhead costs related to self-constructed assets, even though allowed and part of the grant budget would no longer be charged as expenditures to the Texas Water Development Board

("TWDB") Capitalization Grant for Clean Water State Revolving Funds. As part of this change, management contacted TWDB to coordinate a reimbursement of the costs charged and funds received during 2016 but instead, at the advice of TWDB, it was agreed that such reimbursement would be handled via a reduction of subsequent requests for reimbursement.

27. During the course of your audit, you may have accumulated records containing data that should be reflected in our books and records. All such data have been so reflected. Accordingly, copies of such records in your possession are no longer needed by us.
28. We have provided all water supply agreements, have analyzed such agreements and concluded that reporting as commitments under U.S. GAAP is appropriate.

### **Supplementary Information**

29. With respect to supplementary information presented in relation to the financial statements as a whole:
  - a. We acknowledge our responsibility for the presentation of such information.
  - b. We believe such information, including its form and content, is fairly presented in accordance with U.S. GAAP.
  - c. The methods of measurement or presentation have not changed from those used in the prior period.
  - d. When supplementary information is not presented with the audited financial statements, we will make the audited financial statements readily available to the intended users of the supplementary information no later than the date of issuance of the supplementary information and the auditor's report thereon.
30. With respect to:
  - 1) the Management's Discussion and Analysis,
  - 2) Texas Municipal Retirement System – San Antonio Water System Schedule of Changes in Net Pension Liability and Related Ratios,
  - 3) Texas Municipal Retirement System – San Antonio Water System Schedule of Contributions,
  - 4) San Antonio Water System Retirement Plan – Defined Benefit Component Schedule of Changes in Net Pension Liability and Related Ratios,
  - 5) San Antonio Water System Retirement Plan – Defined Benefit Component Schedule of Contributions,
  - 6) San Antonio Water System Retirement Plan – Defined Benefit Component Schedule of Investment Returns,
  - 7) District Special Project Retirement Income Plan – Schedule of Changes in Net Pension Liability and Related Ratios,
  - 8) District Special Project Retirement Income Plan – Schedule of Contributions,
  - 9) District Special Project Retirement Income Plan – Schedule of Investment Returns,
  - 10) Other Post Employment Benefit Plan – Schedule of Funding Progress, and
  - 11) Other Post Employment Benefit Plan – Schedule of Employer Contributionspresented as required by the Governmental Accounting Board to supplement the basic financial statements:

- a. We acknowledge our responsibility for the presentation of such required supplementary information.
- b. We believe such required supplementary information is measured and presented in accordance with guidelines prescribed by U.S. GAAP.
- c. The methods of measurement or presentation have not changed from those used in the prior period.
- d. The underlying significant assumptions or interpretations regarding the measurement or presentation of such information include the actuary assumptions to the pension and OPEB plans.

### **Compliance Considerations**

In connection with your audit conducted in accordance with *Government Auditing Standards*, we confirm that management:

31. Is responsible for the preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework.
32. Is responsible for compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to the auditee.
33. Has informed the auditor that there are no instances that have occurred, or are likely to have occurred, of fraud and noncompliance with provisions of laws and regulations that have a material effect on the financial statements or other financial data significant to the audit objectives, and any other instances that warrant the attention of those charged with governance.
34. Has informed the auditor that there are no instances that have occurred, or are likely to have occurred, of noncompliance with provisions of contracts and grant agreements that have a material effect on the determination of financial statement amounts.
35. Has informed the auditor that there are no instances that have occurred, or are likely to have occurred, of abuse that could be quantitatively or qualitatively material to the financial statements.
36. Is responsible for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.
37. Acknowledges its responsibility for the design, implementation and maintenance of internal controls to prevent and detect fraud.
38. Has taken timely and appropriate steps to remedy fraud; noncompliance with provisions of laws, regulations, contracts and grant agreements; or abuse that the auditor reports.
39. Has a process to track the status of audit findings and recommendations.
40. Has identified for the auditor previous audits, attestation engagements and other studies related to the audit objectives and whether related recommendations have been implemented.
41. Has provided views on the auditor's reported findings, conclusions and recommendations, as well as management's planned corrective actions, for the report.

In connection with your audit of federal awards conducted in accordance with Subpart F of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), we confirm:

42. Management is responsible for complying, and has complied, with the requirements of Uniform Guidance.
43. Management is responsible for understanding and complying with the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of its federal programs.
44. Management is responsible for establishing and maintaining, and has established and maintained, effective internal control over compliance for federal programs that provides reasonable assurance that the auditee is managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on its federal programs.
45. Management has prepared the schedule of expenditures of federal awards in accordance with Uniform Guidance and has included expenditures made during the period being audited for all awards provided by federal agencies in the form of grants, federal cost reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations and other assistance.
46. Management has identified and disclosed all of its government programs and related activities subject to the Uniform Guidance compliance audit.
47. Management has identified and disclosed to the auditor the requirements of federal statutes, regulations, and the terms and conditions of federal awards that are considered to have a direct and material effect on each major program.
48. Management has made available all federal awards (including amendments, if any) and any other correspondence relevant to federal programs and related activities that have taken place with federal agencies or pass-through entities.
49. Management has identified and disclosed to the auditor all amounts questioned and all known noncompliance with the direct and material compliance requirements of federal awards or stated that there was not such noncompliance.
50. Management believes that SAWS has complied with the direct and material compliance requirements (except for any noncompliance it may have been disclosed to the auditor).
51. Management has made available all documentation related to compliance with the direct and material compliance requirements, including information related to federal program financial reports and claims for advances and reimbursements.
52. Management has provided to the auditor its interpretations of any compliance requirements that are subject to varying interpretations.
53. Management has disclosed to the auditor any communications from federal awarding agencies and pass-through entities concerning possible noncompliance with the direct and material compliance requirements, including communications received from the end of the period covered by the compliance audit to the date of the auditor's report.

54. If any, management has disclosed to the auditor the findings received and related corrective actions taken for previous audits, attestation engagements, and internal or external monitoring that directly relate to the objectives of the compliance audit, including findings received and corrective actions taken from the end of the period covered by the compliance audit to the date of the auditor's report.
55. If any, management is responsible for taking corrective action on audit findings of the compliance audit and developing a corrective action plan that meets the requirements of the Uniform Guidance
56. If any, management has provided the auditor with all information on the status of the follow-up on prior audit findings by federal awarding agencies and pass-through entities, including all management decisions.
57. Management has disclosed the nature of any subsequent events that provide additional evidence with respect to conditions that existed at the end of the reporting period that affect noncompliance during the reporting period.
58. Management has disclosed all known noncompliance with direct and material compliance requirements occurring subsequent to the period covered by the auditor's report or stated that there were no such known instances.
59. Management has disclosed whether any changes in internal control over compliance or other factors that might significantly affect internal control, including any corrective action taken by management with regard to significant deficiencies and material weaknesses in internal control over compliance, have occurred subsequent to the period covered by the auditor's report.
60. Federal program financial reports and claims for advances and reimbursements are supported by the books and records from which the basic financial statements have been prepared.
61. The copies of federal program financial reports provided to the auditor are true copies of the reports submitted, or electronically transmitted, to the federal agency or pass-through entity, as applicable.
62. Management has charged costs to federal awards in accordance with applicable cost principles.
63. Management is responsible for, and has accurately prepared, the summary schedule of prior audit findings to include all findings required to be included by Uniform Guidance.
64. The reporting package does not contain protected personally identifiable information.
65. Management has accurately completed the appropriate sections of the data collection form.

San Antonio Water System



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Robert R. Puente  
President/ Chief Executive Officer



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Douglas P. Evanson  
Sr. Vice President/ Chief Financial Officer



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Mary Bailey  
Vice President – Business Planning/ Controller



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Gregg Henderson  
Assistant Controller

