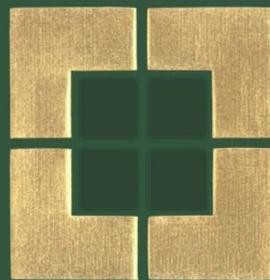


**Armstrong Water Supply
Corporation**

September 30, 2018 and 2017

Financial Statements



**BROCKWAY
GERSBACH
FRANKLIN &
NIEMEIER, P.C.**

CERTIFIED PUBLIC ACCOUNTANTS

ARMSTRONG WATER SUPPLY CORPORATION

FINANCIAL STATEMENTS AS OF

September 30, 2018 and 2017

TOGETHER WITH INDEPENDENT AUDITORS' REPORT THEREON

C O N T E N T S

Independent Auditors' Report	1 - 2
Financial Statements	
Statements of Financial Position	4 - 5
Statements of Activities	6
Statements of Cash Flows	7
Notes to Financial Statements	9 - 14



INDEPENDENT AUDITORS' REPORT

Board of Directors
Armstrong Supply Corporation
Holland, Texas

We have audited the accompanying financial statements of Armstrong Water Supply Corporation, which comprise the statements of financial position as of September 30, 2018 and 2017, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**INDEPENDENT AUDITORS' REPORT
(CONTINUED)**

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Armstrong Water Supply Corporation as of September 30, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink, reading "Brockway Busch, Matthew M. Mincer, P.C." The signature is written in a cursive style and is positioned above the printed text of the firm's name and location.

Temple, Texas
December 13, 2018

FINANCIAL STATEMENTS

LIABILITIES

	<u>2018</u>	<u>2017</u>
Current Liabilities		
Current portion of long term debt	\$ 66,339	\$ 70,292
Trade accounts payable	32,288	47,710
Regulatory assessment fee payable	3,711	3,162
Payroll taxes payable	-	7,309
Accrued interest	7,505	9,520
Member deposits	<u>20,000</u>	<u>20,000</u>
Total Current Liabilities	129,843	157,993
Long-Term Debt		
Long-term debt, net of current portion	<u>1,790,218</u>	<u>1,878,085</u>
Total Liabilities	1,920,061	2,036,078

NET ASSETS

Net Assets		
Unrestricted net assets	1,651,233	1,606,597
Temporarily restricted net assets	<u>156,559</u>	<u>133,206</u>
Total Net Assets	<u>1,807,792</u>	<u>1,739,803</u>
Total Liabilities and Net Assets	<u>\$ 3,727,853</u>	<u>\$ 3,775,881</u>

ARMSTRONG SUPPLY CORPORATION
STATEMENTS OF ACTIVITIES
For the Years Ended September 30, 2018 and 2017

	2018	2017
Operating Revenues		
Metered water sales	\$ 1,023,941	\$ 824,350
Tap and equity fees	64,900	66,100
Penalty and reconnect fees	15,845	15,275
Service charges	2,285	1,570
Miscellaneous income	-	4,793
Total Operating Revenues	1,106,971	912,088
Operating Expenses		
Water purchased	442,470	361,363
Salaries, wages and benefits	232,309	215,458
Depreciation and amortization	162,013	147,698
Interest expense	91,574	97,267
System repair and maintenance	54,050	56,143
Power for pumping and offices	34,631	29,919
Professional fees	28,229	56,275
Auto expense	17,911	24,057
Insurance expense	13,957	10,891
Office expense	10,278	10,472
Telephone	4,596	4,567
Miscellaneous expense	4,499	4,829
Dues and subscriptions	4,173	4,094
Other utilities	1,732	1,109
Bad debt	282	483
Total Operating Expenses	1,102,704	1,024,625
Excess (deficit) of operating revenues over operating expenses	4,267	(112,537)
Other Income (Expense)		
Investment and dividend income	28,812	24,476
Gain on disposition of assets	-	500
Unrealized loss on investments	(5,347)	(2,346)
Contributions in aid of construction	30,400	110,270
Total Other Income (Expense)	53,865	132,900
Changes in net assets from operations	58,132	20,363
Changes in Unrestricted Net Assets		
Member fees, net	9,857	11,333
Change in net assets	67,989	31,696
Net assets - beginning of year	1,739,803	1,708,107
Net assets - end of year	\$ 1,807,792	\$ 1,739,803

The accompanying notes are an integral part of the financial statements.

ARMSTRONG SUPPLY CORPORATION
STATEMENTS OF CASH FLOWS
For the Years Ended September 30, 2018 and 2017

	2018	2017
Cash Flows from Operating Activities		
Changes in net assets from operations	\$ 58,132	\$ 20,363
Adjustments to reconcile nets assets to net cash flows provided by operating activities:		
Depreciation and amortization	162,013	147,698
(Increase) decrease in:		
Accounts receivable	98,549	(117,525)
Prepays	(1,368)	(975)
Other assets	(2,116)	(5,360)
Increase (decrease) in:		
Accounts payable	(15,422)	(71,072)
Accrued liabilities	(8,775)	5,189
Member deposits	-	20,000
	232,881	(22,045)
Total Adjustments		
Net cash provided (used) by operating activities	291,013	(1,682)
Cash Flows from Investing Activities		
Cash payments for the purchase capital assets	(109,138)	(146,473)
Proceeds from the sale of investments	-	159,128
Purchase of investments	(26,154)	-
	(135,292)	12,655
Net cash provided (used) by investing activities		
Cash Flows from Financing Activities		
Proceeds from the issue of memberships, net	9,857	11,333
Proceeds from the issuance of long term debt	-	28,100
Principal payments on long term debt	(91,820)	(62,027)
	(81,963)	(22,594)
Net cash used by financing activities		
Net increase (decrease) in cash	73,758	(11,621)
Cash and cash equivalents - beginning of year	233,489	245,110
Cash and cash equivalents - end of year	\$ 307,247	\$ 233,489

Supplemental Cash Flow Information

Interest paid in the years ended September 30, 2018 and 2017, was \$ 91,574 and \$ 97,267, respectively.

The accompanying notes are an integral part of the financial statements.

This page is left blank intentionally.

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

1. Nature of Activities

Armstrong Water Supply Corporation (the Corporation) is a member-owned, non-profit organization incorporated pursuant to provisions of the Texas Revised Civil Statutes for the purpose of providing a potable water utility service, under the valid Certificate of Convenience and Necessity (CNN) number 10049, to members of the water utility. Member-consumers are located principally in rural areas between the towns of Belton, Holland and Little River – Academy. There are no large commercial consumers, although some farm operations use large amounts of water (in excess of 40,000 gallons) at various times during the year. Operating policies rates, tariffs and regulations are formulated by a Board of Directors, duly elected by the members of the organization.

2. Summary of Significant Accounting Policies

The following is a summary of certain significant accounting policies followed in the preparation of the financial statements of the Corporation.

Financial Statements Presentation

The Corporation is required to present its financial statements in accordance with ASC 958-205 Financial Statement Presentation for Not-for-Profit Entities. Under ASC 958-205 the Corporation is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted nets assets, and permanently restricted net assets. All of the Corporation’s net assets were unrestricted as of September 30, 2018 and 2017.

The schedule of unrestricted net assets is as follows:

	2018	2017
MEMBERSHIPS		
Balance, October 1,	\$ 167,133	\$ 155,800
Member investment - current year	9,857	11,333
Balance, September 30,	176,990	167,133
DESIGNATED AS RESERVE		
Balance, October 1,	133,206	132,840
Allocation from unappropriated net assets	23,353	366
Balance, September 30,	156,559	133,206
UNDESIGNATED		
Balance, October 1,	1,439,464	1,419,467
Allocations to Reserve	(23,353)	(366)
Change in net assets from operations	58,132	20,363
Balance, September 30	1,474,243	1,439,464
 Total Unrestricted Net Assets	 \$ 1,807,792	 \$ 1,739,803

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Under the accrual basis of accounting, revenue is recognized when earned regardless of when collected and expenses are recognized when the obligation is incurred regardless of when paid.

Cash and Cash Equivalents

The Corporation considers all liquid investments purchased with an initial maturity of three months or less and not designated as a component of the Reserve Fund, to be cash equivalents.

Trade Accounts Receivable

Accounts receivable are recorded at the value of the revenue earned and requires payment within thirty days. Account balances with charges over thirty days old are considered delinquent and collection efforts begin at this time. Accounts receivable are show net of an allowance for uncollectible amounts if applicable.

Property and Equipment

Property and equipment is carried on the basis of cost. Depreciation has been provided using the straight-line method in amounts sufficient to amortize the cost of depreciable assets over their estimated useful lives.

The following table summarizes the estimated lives in depreciating the fixed assets:

<u>Property</u>	<u>Life</u>
Distribution system	5 - 40 years
Equipment	5 - 12 years
Office equipment	3 - 10 years
Building and improvements	15 - 40 years

Invested Funds

Invested funds consist of reserve funds set aside as stipulated by the Corporation's debt agreements

Capitalized Interest

The Corporation capitalizes interest costs associated with the system improvement's debt during the active development and construction phases of the projects. Once the projects are substantially complete, the capitalized interest is considered part of the historical costs of the related assets and will be amortized over the assets' useful life.

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

Revenue Recognition

The Corporation generally sells water utility services under short-term, monthly billing cycles, using a tariff schedule approved by the Board of Directors. Revenues are recognized monthly, based on metered readings located at each member's place of residence or business.

Tax Exempt Status

The Corporation qualifies under state franchise tax regulations as an exempt organization. The Internal Revenue Service, under IRC Section 501(c)(12) has granted exempt status. A required information return (Form 990) is filed annually on or before the February 15 due date. The Corporation has not been examined by any major taxing jurisdictions for the fiscal years 2014-2016.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

3. Cash and Cash Equivalents

The Corporation maintains cash balances at several financial institutions located in Central Texas. Accounts at each institution are insured by the Federal Deposit Insurance Corporation up to \$ 250,000. As of September 30, 2018 and 2017, the Corporation maintained cash balances of \$ 56,302 and \$ -0-, respectively, in excess of FDIC insured limits.

4. Invested Funds

As of September 30, 2018 and 2017, the Company has invested funds, stated at market value, as follows:

<u>2018</u>	<u>Interest</u>	<u>Maturity</u>	<u>Amount</u>
Raymond James Mutual Fund	0.00%	Demand	\$ 51,487
			<u>\$ 51,487</u>
<u>2017</u>	<u>Interest</u>	<u>Maturity</u>	<u>Amount</u>
Raymond James Mutual Fund	0.00%	Demand	\$ 25,333
			<u>\$ 25,333</u>

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

5. Property, Plant and Equipment

Property, plant and equipment consisted of the following at September 30:

	<u>2018</u>	<u>2017</u>
Land	\$ 147,913	\$ 147,913
Distribution system	4,665,496	4,556,358
Equipment	167,018	167,018
Office equipment	18,402	18,402
Buildings and improvements	59,605	59,605
Total	<u>\$ 5,058,434</u>	<u>\$ 4,949,296</u>

Depreciation expense was \$ 162,013 and \$ 147,698 for the years ended September 30, 2018 and 2017, respectively.

6. Invested Funds – Reserve

The Corporation is required, as long as indebted to CoBank, to maintain a reserve account at CoBank or any other financial institution acceptable to CoBank. At September 30, 2018 and 2017, the reserve account consisted of the following:

	<u>2018</u>	<u>2017</u>
Invested funds - Reserve	\$ 156,559	\$ 133,206
Required fund balance	<u>157,500</u>	<u>157,500</u>
Funds in excess (insufficient) of loan agreement	<u>\$ (941)</u>	<u>\$ (24,294)</u>

7. Investment in Other Organizations

Central Texas Water Supply Corporation is a consortium of area rural water supply corporations formed to provide treated surface water to each individual entity's members. Membership requires a \$ 500 investment in order to use the system.

CoBank, a banking co-operative for rural infrastructure projects, requires as part lending policies, membership in the co-operative at an initial cost of \$ 1,000. Membership entitles members to participate in patronage dividends as declared by the CoBank board of directors. As of September 30, 2018 and 2017, the Corporation's investment in CoBank, including patronage dividends, was \$ 21,725 and \$ 16,886, respectively.

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

8. Changes in Long-Term Debt

Long-term debt activity for the year ended September 30, 2018 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Notes Payable:				
CoBank - 2871674	\$ 1,252,421	\$ -	\$ 32,125	\$ 1,220,296
CoBank - 2871656	667,856	-	31,595	636,261
Ally Financial	28,100	-	28,100	-
Total Notes Payable:	<u>\$ 1,948,377</u>	<u>\$ -</u>	<u>\$ 91,820</u>	<u>\$ 1,856,557</u>

9. Long-Term Debt

Long-term debt activity for the year ended September 30, 2018 was as follows:

	2018	2017
CoBank - 5.10% construction note, payable in monthly installments, including interest, with a maturity date of August 20, 2044	\$ 1,220,296	\$ 1,252,421
CoBank - 4.35% construction note, payable in monthly installments, including interest, with a maturity date of August 20, 2034	636,261	667,856
Ally - 3.54% vehicle note, payable in monthly installments of \$ 512.44, including interest, with a maturity date of October 22, 2022	-	28,100
	<u>1,856,557</u>	<u>1,948,377</u>
Less Current Portion	<u>(66,339)</u>	<u>(70,292)</u>
Long-Term Debt, net of current portion	<u>\$ 1,790,218</u>	<u>\$ 1,878,085</u>

All Assets of the Corporation are pledged as security for the above notes.

ARMSTRONG WATER SUPPLY CORPORATION
NOTES TO FINANCIAL STATEMENTS

Repayment of the long-term debt, at September 30, 2018 is scheduled as follows:

Years Ending September 30,	
2019	\$ 66,339
2020	67,707
2021	69,162
2022	70,708
2023	72,349
2024 and after	1,510,292
	<u>\$ 1,856,557</u>

10. Membership Investment

Membership in the Corporation is sold for \$ 400 per member and must be purchased to use the system. The membership cost is not refundable, however it is transferable. At September 30, 2018 and 2017, there were 959 and 932 memberships, respectively.

11. Commitments and Contingencies

The Corporation has entered into separate contracts to supply water currently and in future years. A minimum “take or pay” agreement stipulates a basic monthly payment of \$ 22,359 for 6,796,000 gallons, plus \$ 0.1009 per thousand gallons for actual usage. For usage in excess of the 6.796 million gallons, the monthly payment is \$ 22,359 plus \$ 3.29 per thousand gallons for the excess usage. The basic rate for the fiscal year ended September 30, 2018 was \$ 3.39. The charge for capital investment is \$.1009 per thousand gallons based on actual usage. A futures contract, paid annually, obligated the Corporation to \$ 4,363 and \$ 4,431 in 2018 and 2017 to reserve approximately 280 acre – feet of water, at \$ 15.60 per acre – foot, in Stillhouse Hollow Reservoir. The rate on this futures contract may fluctuate each year. The Corporation also pays \$ 74.00 per acre – foot for an additional 175 acre – feet in reserve in Stillhouse Hollow Reservoir. The cost for this water reserve was \$ 13,388 and \$ 12,950 for 2018 and 2017, respectively.

12. Reclassifications

Certain items from the September 30, 2017 financial statements have been reclassified for presentation at September 30, 2018. Net assets are unchanged due to these reclassifications.

13. Subsequent Events

Management has evaluated subsequent events through December 13, 2018, which is the date of the independent auditors’ report. No change to the financial statements for the fiscal year ending September 30, 2018 is deemed necessary as a result of this evaluation.