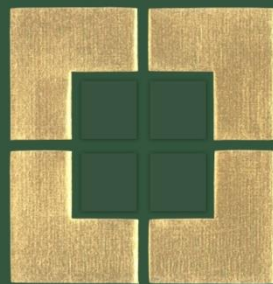


**Armstrong  
Water Supply Corporation**  
**September 30, 2016 and 2015**  
***Financial Statements***



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

**CERTIFIED PUBLIC ACCOUNTANTS**



**ARMSTRONG WATER SUPPLY CORPORATION**

**FINANCIAL STATEMENTS AS OF**

**September 30, 2016 and 2015**

**TOGETHER WITH INDEPENDENT AUDITORS' REPORT THEREON**



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## **INDEPENDENT AUDITORS' REPORT**

Board of Directors  
Armstrong Supply Corporation  
Holland, Texas

We have audited the accompanying financial statements of Armstrong Water Supply Corporation, (a nonprofit organization), which comprise the statements of financial position as of September 30, 2016, and the related statements of activities and cash flows for the year 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, 2016, 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.

**Prior Period Financial Statements**

The financial statements of Armstrong Water Supply Corporation as of September 30, 2015 were audited by other auditors whose report dated January 19, 2016 expressed an unmodified opinion.

*Brockway, Strubel, Franklin & Nimsin, P.C.*

Temple, Texas  
December 30, 2016



**FINANCIAL STATEMENTS**

**ARMSTRONG WATER SUPPLY CORPORATION**  
**STATEMENTS OF FINANCIAL POSITION**  
**September 30, 2016 and 2015**

<b>ASSETS</b>	<u>2016</u>	<u>2015</u>
<b>Current Assets</b>		
Cash and cash equivalents	\$ 245,110	\$ 335,949
Invested funds	184,463	277,516
Trade accounts receivable	70,632	80,847
Prepaid expenses	<u>3,430</u>	<u>5,632</u>
 Total Current Assets	 503,635	 699,944
<b>Property, Plant and Equipment</b>		
Property, plant and equipment	4,759,869	4,435,171
Less: accumulated depreciation	<u>(1,624,151)</u>	<u>(1,505,413)</u>
 Property, Plant and Equipment, net	 3,135,718	 2,929,758
<b>Other Assets</b>		
Invested funds - reserve	129,297	125,480
Member investment	500	500
Investment in CoBank	11,892	6,750
Construction period interest	<u>42,954</u>	<u>44,115</u>
 Total Other Assets	 <u>184,643</u>	 <u>176,845</u>
 Total Assets	 <u><u>\$ 3,823,996</u></u>	 <u><u>\$ 3,806,547</u></u>

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

**LIABILITIES**

	<u>2016</u>	<u>2015</u>
<b>Current Liabilities</b>		
Current portion of long term debt	\$ 63,847	\$ 60,661
Trade accounts payable	118,782	35,345
Regulatory assessment fee payable	2,961	2,915
Payroll taxes payable	3,607	3,443
Accrued interest	<u>8,235</u>	<u>8,234</u>
 Total Current Liabilities	 197,432	 110,598
 <b>Long-Term Debt</b>		
Long-term debt, net of current portion	<u>1,918,457</u>	<u>1,981,874</u>
 Total Liabilities	 2,115,889	 2,092,472

**NET ASSETS**

<b>Net Assets</b>		
Unrestricted	<u>1,708,107</u>	<u>1,714,075</u>
 Total Liabilities and Net Assets	 <u>\$ 3,823,996</u>	 <u>\$ 3,806,547</u>

**ARMSTRONG SUPPLY CORPORATION**  
**STATEMENTS OF ACTIVITIES**  
**For the Years Ended September 30, 2016 and 2015**

	2016	2015
<b>Operating Revenues</b>		
Metered water sales	\$ 795,236	\$ 761,823
Tap and equity fees	49,100	15,183
Penalty and reconnect fees	15,640	17,140
Service charges	1,400	420
Miscellaneous income	-	381
Total Operating Revenues	861,376	794,947
<b>Operating Expenses</b>		
Water purchased	297,733	319,234
Salaries, wages and benefits	216,598	191,823
Depreciation and amortization	118,738	122,712
Interest expense	100,389	86,651
System repair and maintenance	53,847	43,479
Professional fees	35,263	7,837
Power for pumping and offices	28,265	31,321
Insurance expense	16,250	12,401
Auto expense	15,853	19,524
Office expense	9,764	11,741
Telephone	5,392	4,348
Miscellaneous expense	4,190	5,914
Dues and subscriptions	3,643	3,508
Other utilities	1,083	1,846
Bad debt	-	60
Total Operating Expenses	907,008	862,399
Excess of operating revenues over operating expenses	(45,632)	(67,452)
<b>Other Income (Expense)</b>		
Investment and dividend income	26,421	27,864
Gain on disposition of assets	-	31,500
Unrealized gain (loss) on investments	5,943	(2,674)
Total Other Income (Expense)	32,364	56,690
Changes in net assets from operations	(13,268)	(10,762)
<b>Changes in Unrestricted Net Assets</b>		
Member fees, net	7,300	2,000
	7,300	2,000
Change in net assets	(5,968)	(8,762)
Net assets - beginning of year	1,714,075	1,722,837
Net assets - end of year	\$ 1,708,107	\$ 1,714,075

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

**ARMSTRONG SUPPLY CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended September 30, 2016 and 2015**

	2016	2015
<b>Cash Flows from Operating Activities</b>		
Changes in net assets from operations	\$ (13,268)	\$ (10,762)
Adjustments to reconcile net assets to net cash flows provided by operating activities:		
Depreciation and amortization	118,738	122,712
(Increase) decrease in:		
Accounts receivable	10,215	3,898
Prepays	2,202	(3,449)
Other assets	(7,798)	(1,114)
Increase (decrease) in:		
Accounts payable	(31,563)	(4,253)
Accrued liabilities	211	3,827
	92,005	121,621
Net cash provided by operating activities	78,737	110,859
<b>Cash Flows from Investing Activities</b>		
Cash payments for the purchase capital assets	(209,698)	(50,609)
Proceeds from the redemption of invested funds	93,053	1,775
	(116,645)	(48,834)
Net cash used by investing activities	(116,645)	(48,834)
<b>Cash Flows from Financing Activities</b>		
Proceeds from the issue of memberships, net	7,300	2,000
Principal payments on long term debt	(60,231)	(58,777)
	(52,931)	(56,777)
Net cash used by financing activities	(52,931)	(56,777)
Net increase (decrease) in cash	(90,839)	5,248
<b>Cash and cash equivalents - beginning of year</b>	335,949	330,701
<b>Cash and cash equivalents - end of year</b>	\$ 245,110	\$ 335,949

**Supplemental Cash Flow Information**

Interest paid in the years ended September 30, 2016 and 2015, was \$ 99,228 and \$ 81,916, respectively.

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

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**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, 2016 and 2015.

The schedule of unrestricted net assets is as follows:

	2016	2015
<b>MEMBERSHIPS</b>		
Balance, October 1,	\$ 148,500	\$ 146,500
Member investment - current year	7,300	2,000
Balance, September 30,	155,800	148,500
<b>DESIGNATED AS RESERVE</b>		
Balance, October 1,	120,482	122,257
Allocation (to) from unappropriated net assets	4,998	(1,775)
Balance, September 30,	125,480	120,482
<b>UNDESIGNATED</b>		
Balance, October 1,	1,445,093	1,454,080
Allocations (to) from Reserve	(4,998)	1,775
Change in net assets from operations	(13,268)	(10,762)
Balance, September 30	1,426,827	1,445,093
 Total Unrestricted Net Assets	 \$ 1,708,107	 \$ 1,714,075

**ARMSTRONG WATER SUPPLY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**

**2. Summary of Significant Accounting Policies (Continued)**

***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 (CONTINUED)**

**2. Summary of Significant Accounting Policies (Continued)**

***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 2013-2015.

***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, 2016 and 2015, the Corporation maintained cash balances within FDIC insured limits.

**4. Invested Funds**

As of September 30, 2016 and 2015, the Company has invested funds, stated at market value, as follows:

<u>2016</u>	<u>Interest</u>	<u>Maturity</u>	<u>Amount</u>
Invesco Short-Term Bond Fund			
Raymond James	0.00%	Demand	\$ 184,463
			<u>\$ 184,463</u>
<u>2015</u>	<u>Interest</u>	<u>Maturity</u>	<u>Amount</u>
Invesco Short-Term Bond Fund			
Edward Jones	0.00%	Demand	\$ 277,516
			<u>\$ 277,516</u>

**ARMSTRONG WATER SUPPLY CORPORATION  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)**

**5. Property, Plant and Equipment**

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

	<u>2016</u>	<u>2015</u>
Land	\$ 147,913	\$ 147,913
Distribution system	4,401,827	4,078,765
Equipment	132,122	130,917
Office equipment	18,402	18,402
Buildings and improvements	59,605	59,174
Total	<u>\$ 4,759,869</u>	<u>\$ 4,435,171</u>

Depreciation expense was \$ 118,738 and \$ 122,712 for the years ended September 30, 2016 and 2015, 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, 2016 and 2015, the reserve account consisted of the following:

	<u>2016</u>	<u>2015</u>
Invested funds - Reserve	\$ 129,297	\$ 125,480
Required fund balance	<u>115,000</u>	<u>115,000</u>
Funds in excess of loan agreement	<u>\$ 14,297</u>	<u>\$ 10,480</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, 2016 and 2015, the Corporation's investment in CoBank, including patronage dividends, was \$ 11,892 and \$ 6,750, respectively.

**ARMSTRONG WATER SUPPLY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**

**8. Construction Period Interest**

The following table summarizes the Corporation's interest cost incurred, capitalized and expensed as interest expense during the years ended September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Capitalized interest - beginning of year	\$ 44,115	\$ 45,276
Interest incurred	-	-
Interest expensed:		
Amortized directly to interest expense	(1,161)	(1,161)
Capitalized interest - end of year	<u>\$ 42,954</u>	<u>\$ 44,115</u>

**9. Changes in Long-Term Debt**

Long-term debt activity for the year ended September 30, 2016 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Notes Payable:				
CoBank - 2871674	\$ 1,314,039	\$ -	\$ 30,346	\$ 1,283,693
CoBank - 2871656	728,496	-	29,885	698,611
Total Notes Payable:	<u>\$ 2,042,535</u>	<u>\$ -</u>	<u>\$ 60,231</u>	<u>\$ 1,982,304</u>

**10. Long-Term Debt**

Long-term debt activity for the year ended September 30, 2016 was as follows:

	<u>2016</u>	<u>2015</u>
CoBank - 5.10% construction note, payable in monthly installments of \$ 8,166, including interest, with a maturity date of August 20, 2044	\$ 1,283,693	\$ 1,314,039
CoBank - 4.35% construction note, payable in monthly installments of \$ 5,118, including interest, with a maturity date of August 20, 2034	698,611	728,496
	1,982,304	2,042,535
Less Current Portion	<u>(63,847)</u>	<u>(60,661)</u>
Long-Term Debt, net of current portion	<u>\$ 1,918,457</u>	<u>\$ 1,981,874</u>

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

**ARMSTRONG WATER SUPPLY CORPORATION  
NOTES TO FINANCIAL STATEMENTS (CONTINUED)**

**10. Long-Term Debt (Continued)**

Repayment of the long-term debt, at September 30, 2016 is scheduled as follows:

Years Ending September 30,	
2017	\$ 63,847
2018	65,053
2019	66,339
2020	67,707
2021	69,163
2022 and after	<u>1,650,195</u>
	<u>\$ 1,982,304</u>

**11. 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, 2016 and 2015, there were 927 and 910 memberships, respectively.

**12. 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 \$ 20,184 for 6,796,000 gallons, plus \$ 0.0953 per thousand gallons for actual usage. For usage in excess of the 6.796 million gallons, the monthly payment is \$ 20,184 plus \$ 3.0598 per thousand gallons for the excess usage. The basic rate for the fiscal year ended September 30, 2016 was \$ 3.05. The charge for capital investment is \$ .0953 per thousand gallons based on actual usage. A futures contract, paid annually, obligated the Corporation to \$ 4,402 and \$ 4,399 in 2016 and 2015 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 \$ 72.00 per acre – foot for an additional 175 acre – feet in reserve in Stillhouse Hollow Reservoir. The cost for this water reserve was \$ 12,600 and \$ 12,338 for 2016 and 2015, respectively.

**13. Subsequent Events**

Management has evaluated subsequent events through December 30, 2016, which is the date of the independent auditors’ report. No change to the financial statements for the fiscal year ending September 30, 2016 is deemed necessary as a result of this evaluation.