DRIPPING SPRINGS WATER SUPPLY CORPORATION

Financial Statements as of and for the Years Ended December 31, 2015 and 2014 and Independent Auditors' Report

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Dripping Springs Water Supply Corporation:

We have audited the accompanying financial statements of Dripping Springs Water Supply Corporation (the "Corporation") (a nonprofit organization), which comprise the statements of financial position as of December 31, 2015 and 2014, 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 audits. We conducted our audits 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 auditors' 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Corporation as of December 31, 2015 and 2014, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Maxwell Locke + Ritter LLP

Austin, Texas
April 15, 2016

DRIPPING SPRINGS WATER SUPPLY CORPORATION

STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2015 AND 2014

	2015	2014
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 2,643,707	$ 1,704,627
Restricted cash	11,190	42,826
Investments	162,286	200,078
Accounts receivable, net	544,694	242,088
Total current assets	3,361,877	2,189,619
PROPERTY AND EQUIPMENT, net	3,929,914	3,029,455
TOTAL ASSETS	$ 7,291,791	$ 5,219,074
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable	$ 88,081	$ 37,273
Accrued liabilities	12,076	65,002
Customer deposits	14,111	14,111
Deferred revenue	6,160	16,922
Current maturities of long-term debt	146,560	42,826
Total current liabilities	266,988	176,134
LONG-TERM DEBT	528,274	-
Total liabilities	795,262	176,134
NET ASSETS-		
Unrestricted net assets	6,496,529	5,042,940
TOTAL LIABILITIES AND NET ASSETS	$ 7,291,791	$ 5,219,074

See notes to financial statements.

DRIPPING SPRINGS WATER SUPPLY CORPORATION

STATEMENTS OF ACTIVITIES
YEARS ENDED DECEMBER 31, 2015 AND 2014

	2015	2014
REVENUES:		
Water sales	$ 1,798,961	$ 1,583,853
Developer and membership fees and capital contributions	1,302,333	161,700
Other fees and installations	160,666	204,413
Interest income	6,846	4,111
Other income	19,383	5,246
Total revenues	3,288,189	1,959,323
EXPENSES:		
Purchased water	682,013	558,342
Salaries and benefits	362,274	333,844
Materials, supplies, and maintenance	240,328	221,739
Depreciation	200,890	147,783
Professional services	187,592	132,222
Rent and utilities	55,073	66,402
Interest	5,988	6,199
Bad debt	562	1,586
Other	99,880	112,967
Total expenses	1,834,600	1,581,084
CHANGE IN NET ASSETS	1,453,589	378,239
NET ASSETS, beginning of year	5,042,940	4,664,701
NET ASSETS, end of year	$ 6,496,529	$ 5,042,940

See notes to financial statements.

DRIPPING SPRINGS WATER SUPPLY CORPORATION

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2015 AND 2014

	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	$ 1,453,589	$ 378,239
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Bad debt	562	1,586
Depreciation	200,890	147,783
Loss on disposal of property and equipment	8,553	-
Changes in assets and liabilities that provided (used) cash:		
Accounts receivable	(303,168)	67,154
Accounts payable	(48,767)	(10,623)
Accrued liabilities	(52,926)	11,517
Customer deposits	-	(874)
Deferred revenue	(10,762)	781
Net cash provided by operating activities	1,247,971	595,563
CASH FLOWS FROM INVESTING ACTIVITIES:		
Increase (decrease) in restricted cash	31,636	(583)
Net sales of investments	37,792	443,952
Purchases of property and equipment	(1,010,327)	(367,527)
Net cash (used in) provided by investing activities	(940,899)	75,842
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings on long term debt	681,893	-
Payments on long-term debt	(49,885)	(42,372)
Net cash provided by (used in) financing activities	632,008	(42,372)
CHANGE IN CASH AND CASH EQUIVALENTS	939,080	629,033
CASH AND CASH EQUIVALENTS, beginning of year	1,704,627	1,075,594
CASH AND CASH EQUIVALENTS, end of year	$ 2,643,707	$ 1,704,627
SUPPLEMENTAL CASH DISCLOSURE-		
Cash paid for interest	$ 5,988	$ 5,339
Noncash investing actvities-		
Additions to property and equipment funded through accounts payable	$ 99,575	$ -

See notes to financial statements.

1. ORGANIZATION

Dripping Springs Water Supply Corporation (the "Corporation") was organized under the laws of the State of Texas on February 4, 1964. The Corporation was formed for the purpose of furnishing water supply service for general farm use and domestic purposes to individuals and entities residing in the community of Dripping Springs, Texas and surrounding rural areas.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") as defined by the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). 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. Net assets, revenues and expenses are classified based on the existence or absence of donor-imposed restrictions.

Classification of Net Assets - The financial statements report information regarding the Corporation's financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the Corporation's net assets and changes therein are classified as follows:

Unrestricted net assets **-** net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets **-** net assets that are subject to donor-imposed stipulations that require passage of time or the occurrence of a specific event. Additionally, unconditional promises to give without explicit donor-imposed stipulations but due in future periods require the passage of time to release the donor's implicit time restriction. Contributions received with temporary restrictions that are met in the same reporting period are reported as unrestricted support and increase unrestricted net assets. There were no such amounts as of December 31, 2015 or 2014.

Permanently restricted net assets **-** net assets that are subject to donor-imposed stipulations that require resources be maintained in perpetuity to the exclusive benefit of the Corporation. There were no such amounts as of December 31, 2015 or 2014.

Use of Estimates - The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Fair Value Measurements - Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value accounting requires characterization of the inputs used to measure fair value into a three-level fair value hierarchy as follows:

Level 1 **-** Inputs based on quoted prices in active markets for identical assets or liabilities. An active market is a market in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 **-** Observable inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent from the entity.

Level 3 **-** Unobservable inputs that reflect the entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available.

There are three general valuation techniques that may be used to measure fair value: 1) market approach **-** uses prices generated by market transactions involving identical or comparable assets or liabilities, 2) cost approach **-** uses the amount that currently would be required to replace the service capacity of an asset (replacement cost), and 3) income approach **-** uses valuation techniques to convert future amounts to present amounts based on current market expectations.

Cash and Cash Equivalents and Restricted Cash - The Corporation considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Certain amounts of cash are restricted based on a provision in the notes payable to the United States Department of Agriculture ("USDA") that requires the Corporation to reserve cash in designated bank accounts totaling twelve months of note payments.

Investments - Investments, which consist of certificates of deposit with initial maturities ranging from six to twelve months, are recorded at fair value based on quoted market prices. Investments were measured at fair value using the market approach and Level 1 inputs. Realized and unrealized gains and losses are reported in the statement of activities as increases or decreases in unrestricted net assets.

Accounts Receivable - Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to bad debt expense and a credit to a valuation allowance based on its assessment of the current status of accounts. Balances still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. The Corporation continually monitors each customer's credit worthiness and recognizes allowances for estimated bad debts on specific customer accounts that are no longer estimated to be collectible. Late fees are charged on past due accounts. Interest is not charged on receivables, nor is collateral required. The Corporation had allowances for uncollectible accounts of approximately $14,592 as of December 31, 2015 and 2014.

Property and Equipment - Property and equipment with an estimated useful life greater than one year is capitalized at cost if purchased or fair value if contributed; costs that are specifically attributable to a project included in construction in progress are capitalized regardless of their cost. Expenditures for repairs and maintenance that do not significantly prolong the lives of the assets are charged to operations as incurred. Property and equipment, other than land and easements and construction in process, is depreciated using the straight-line method over the following useful lives:

Water distribution system	25 years
Buildings and improvements	15-40 years
Vehicles	5 years
Equipment	5 years

Impairment of Long-Lived Assets - Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the amount recorded may not be recoverable. An impairment loss is recognized by the amount in which carrying amount of the asset exceeds fair value, if the carrying amount of the asset is not recoverable. No impairment losses on long-lived assets have been recognized as of December 31, 2015 and 2014.

Customer Deposits - The Corporation proposed construction of a wastewater treatment facility and was issued a Texas Pollutant Discharge Elimination System ("TPDES") permit by the Texas Conservation Commission. The City of Dripping Springs, Texas also filed a TPDES permit application and requested that the Corporation relinquish its permit. Customer deposits collected for the construction of this facility were deposited in an interest bearing account and will be reimbursed to the customers.

Deferred Revenue - Deferred revenue includes water revenues received in advance of usage and will be recognized as revenue once the usage has been incurred by the customer.

Water Sales - The Corporation recognizes water sales revenue based on monthly usage at standard rates.

Developer and Membership Fees and Capital Contributions - The Corporation assesses its customers' one-time, non-refundable fees consisting of a membership fee of $100 and a capital contribution fee, which is based upon the meter size. Revenue is considered earned upon completion of meter installation and subsequent water service. The developer fees are reimbursements made to the Corporation for fees incurred by third party engineers on behalf of current or future members for feasibility assessments and other work. Revenue is considered earned when all work associated with reimbursements has been completed.

Income and Property Taxes - The Corporation is a nonprofit organization and is exempt from federal income taxes under section 501(c)(12) of the Internal Revenue Code, except with respect to any unrelated business income. The Corporation did not incur any tax liabilities due to unrelated business income during the years December 31, 2015 or 2014. The Corporation files Form 990 tax returns in the U.S. federal jurisdiction, and is subject to routine examinations of its returns; however, there are no examinations currently in progress. The 2012 and subsequent tax years remain subject to examination by the Internal Revenue Service.

Concentration of Credit Risk - Financial instruments which potentially subject the Corporation to credit risk consist of cash and cash equivalents, investments, and accounts receivable. The Corporation places its cash and cash equivalents with a limited number of high quality financial institutions and may exceed the amount of insurance provided on such deposits. Management believes no significant risk exists with respect to cash and cash equivalents.

Investments are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is at lease reasonably possible that changes in the near-term could materially affect the amounts reported in the statements of financial position. At December 31, 2015 and 2014, the Corporation's investments consisted only of certificates of deposit, which management believes substantially mitigates its concentration of credit risk in investments.

The Corporation's accounts receivable are comprised of amounts due from a large, diverse customer base, which management believes serves to mitigate the amount of credit risk incurred by the Corporation. The Corporation continually monitors each customer's account balance and writes off to bad debt expense those accounts that are no longer deemed collectible. At December 31, 2015, the Corporation had two customers that accounted for 43% of total accounts receivable and one customer that accounted for 17% of total accounts receivable at December 31, 2014.

Recently Issued Accounting Pronouncements - In May 2014 and August 2015, the FASB issued Accounting Standards Update ("ASU") No. 2014-09 and No. 2015-14, *Revenue from Contracts with Customers*, which supersede the revenue recognition requirements in ASC 605, *Revenue Recognition*, and most industry-specific guidance included in the ASC. The standard requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The standard is effective retrospectively for fiscal years beginning after December 15, 2018 and early adoption is permitted. The Corporation is currently evaluating the impact the new standard will have on its financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases* (Topic 842), which requires the recognition of lease assets and lease liabilities by lessees for all leases, including leases previously classified as operating leases, and modifies the classification criteria and accounting for sales-type and direct financing leases by lessors. Leases continue to be classified as finance or operating leases by lessees and both classifications require the recognition of a right-of-use asset and a lease liability, initially measured at the present value of the lease payments in the statement of financial position. Interest on the lease liability and amortization of the right-of-use asset are recognized separately in the statement of operations for finance leases and as a single lease cost recognized on the straight-line basis over the lease term for operating leases. The standard is effective using a modified retrospective approach for fiscal years beginning after December 15, 2019 and early adoption is permitted. The Corporation is currently evaluating the impact the standard will have on its financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements - Going Concern*, which provides guidance about management's responsibility to evaluate on an annual basis whether there is substantial doubt about an entity's ability to continue as a going concern within one year after the date that the financial statements are available to be issued and to provide certain related footnote disclosures. The standard is effective for fiscal years ending after December 15, 2016, and due to the change in requirements for reporting, presentation and disclosure of future evaluations of the entity's ability to continue as a going concern may be different than under current standards.

3. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following as of December 31:

	2015	2014
Land and easements	$ 246,509	$ 246,509
Water distribution system	5,001,298	4,754,045
Vehicles	176,281	104,249
Equipment	120,275	114,775
Buildings and improvements	57,678	57,678
Construction in progress	860,889	103,133
	6,462,930	5,380,389
Less accumulated depreciation	(2,533,016)	(2,350,934)
Property and equipment, net	$ 3,929,914	$ 3,029,455

4. LONG-TERM DEBT

Long-term debt consisted of the following as of December 31:

	2015	2014
$600,000 Note payable to a bank, uncollateralized, principal and interest paid in monthly installments totaling $11,113 at 4.15%, matures November 1, 2020.	$ 581,751	$ -
$31,444 Vehicle note payable to a financial service company, collateralized by vehicle, principal and interest paid in monthly installments totaling $928.19 at 3.89%, matures December 30, 2018.	$ 31,444	$ -
$31,191 Vehicle note payable to a financial service company, collateralized by vehicle, principal and interest paid in monthly installments totaling $920.73 at 3.89%, matures December 30, 2018.	$ 31,191	$ -
$19,258 Vehicle note payable to a financial service company, collateralized by vehicle, principal and interest paid in monthly installments totaling $928.19 at 3.89%, matures December 30, 2018.	$ 19,258	$ -
$500,000 Note payable to USDA, uncollateralized, principal and interest paid in monthly installments totaling $4,327 at 8.375%, matures January 31, 2026.	$ 11,190	$ 39,194
$70,000 Note payable to USDA, uncollateralized, principal and interest paid in annual installments totaling $4,152 at 5.0%, matures January 19, 2019.	-	3,632
Total	674,834	42,826
Less: current maturities of long-term debt	(146,560)	(42,826)
Total long-term debt	$ 528,274	$ -

The maturities of long-term debt at December 31, 2015 were as follows:

2016	$ 146,560
2017	143,261
2018	149,147
2019	128,414
2020	107,452
Totals	$ 674,834

Each of the USDA notes contain a cross default provision that would result in a default on the notes in the event that there was a default on any other borrowings.

Over the life of the promissory notes with the USDA, the Corporation has paid down the principal faster than required by increasing the monthly and annual payments on the notes and, in some cases, making additional principal payments on the notes. These accelerated payments have resulted in a reduction in the life of the notes, in some cases reducing the life by more than ten years. The USDA note outstanding as of December 31, 2015 will be paid off in 2016, prior to the scheduled maturity date of 2026.

5. COMMITMENTS AND CONTINGENCIES

The Corporation entered into a 40-year water service agreement with the Lower Colorado River Authority (the "LCRA") on August 23, 2000 to purchase up to, but not in excess of, 1,000,000 gallons per day. Under the LCRA contract, as amended, new meters are subject to a capital recovery fee per meter for each living unit equivalent ("LUE") serviced under the agreement. The capital recovery fee will be collected from the Corporation's new customers and is payable to LCRA within 45 days following collection. The LCRA now collects the capital recovery fees. In addition, the Corporation pays LCRA a monthly amount consisting of water impact fees, raw water diversion fees, plus actual meter volume charge of per 1,000 gallons. The contract may be terminated by the Corporation if all payments to LCRA are current and 30 days written notice is provided to LCRA. On July 2015, the Corporation completed the collection of capital recovery fees under the water services agreement. The water service agreement was assigned to the West Travis County Public Utility Agency (the "WTCPUA") as a successor and assignee of the LCRA commensurate with the LCRA's sale of certain assets to the WTCPUA.

6. FUNCTIONAL ALLOCATION OF EXPENSES

Expenses are categorized into functional classifications dependent upon the nature and ultimate purpose of the expenses. Accordingly, certain expenses are allocated between functional categories. The functional allocation of expenses for the years ended December 31, 2015 and 2014 were as follows:

	2015	2014
Program services	$ 1,524,746	$ 1,270,337
Management and general	350,155	310,747
Total expenses	$ 1,834,600	$ 1,581,084

7. RETIREMENT PLAN

Effective January 1, 2012, the Corporation established a savings incentive match plan (the "Simple IRA Plan") for eligible employees of the Corporation under Section 408(b) of the Internal Revenue Code. The Simple IRA Plan covers substantially all employees of the Corporation. Participants in the Simple IRA plan may contribute up to the maximum amount allowed by the IRC. The Corporation makes a quarterly contribution that matches 100% of the employee contributions, up to 3% of their annual compensation. These contributions vest immediately. Employer contributions totaled $6,000 and $6,137 for the years ended December 31, 2015 and 2014, respectively.

8. SUBSEQUENT EVENTS

The Corporation has evaluated subsequent events through April 15, 2016 (the date the financial statements were available to be issued). No events have occurred from the statement of financial position date through that date that would impact the financial statements.