

ANNUAL FINANCIAL REPORT

of the

Lone Star Groundwater Conservation District

**For the Year Ended
December 31, 2015**

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Lone Star Groundwater Conservation District

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Independent Auditor's Report

To the Board of Directors of the
Lone Star Groundwater Conservation District
655 Conroe Park North Drive
Conroe, Texas 77303

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Lone Star Groundwater Conservation District (the "District"), as of and for the year ended December 31, 2015, and the related notes to the financial statements, which collectively comprise Lone Star Groundwater Conservation District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Lone Star Groundwater Conservation District's 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.

Auditor's 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Lone Star Groundwater Conservation District, as of December 31, 2015, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

Correction of an Error

As disclosed in Note 8, in the year ending December 31, 2015, the District restated its net position as of December 31, 2014 to correct an error. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information on pages 7 - 11 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise Lone Star Groundwater Conservation District's basic financial statements. The accompanying budgetary comparison schedule and Texas Supplementary Information on

pages 36 - 37 and 40 – 45, respectively, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

These schedules have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Brooks Cardiel, PLLC

BrooksCardiel, PLLC
The Woodlands, Texas
April 19, 2016

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the Year Ended December 31, 2015

As management of the Lone Star Groundwater Conservation District (the "District"), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended December 31, 2015.

FINANCIAL HIGHLIGHTS

- The assets of the District exceeded its liabilities (net position) at December 31, 2015 by \$2,972,724.
- The District's total net position decreased by \$54,731. The majority of the District's net position is unrestricted.
- At the end of the fiscal year unrestricted portion of net position was \$1,509,014 or 70% of total annual expenses.

OVERVIEW OF THE FINANCIAL STATEMENTS

Financial Statements

The District is designated as a special-purpose government engaged only in business-type activities consistent with GASB 34. Governments engaged only in business-type activities should present only the financial statements required for enterprise funds. As a result, the financial statements presented within this report consist of the enterprise fund financial statements (i.e., the Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position, and Statement of Cash Flows). The District has one enterprise fund.

Enterprise Fund Types

Enterprise funds are used to account for activities that are similar to those often found in the private sector. For the District this covers all activities. The measurement focus is on determination of net income, financial position, and cash flows. Enterprise funds distinguish operating revenues and expenses from non-operating items. Operating revenues include charges for services. Operating expenses include costs of materials, contracts, personnel, and depreciation. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Enterprise fund types follow Generally Accepted Accounting Principles "GAAP" as prescribed by the Governmental Accounting Standards Board "GASB".

Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

For the Year Ended December 31, 2015

Notes to Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes can be found after the financial statements within this report.

Other Information

In addition to basic financial statements and accompanying notes, this report also presents certain other supplementary information. A budgetary comparison schedule for the general fund has been included as a part of the other supplementary information. Additionally, Texas Supplementary Information (TSI) has been included to comply with state reporting requirements.

DISTRICT FINANCIAL ANALYSIS

As noted earlier, net position over time, may serve as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$2,972,724 at the close of the most recent fiscal year.

An important portion of the District's net position, assets, \$1,463,710, reflects its investments in capital assets (e.g., land, building, machinery, equipment, infrastructure, etc.), less any debt used to acquire those assets that is still outstanding. The District uses its capital assets, and a significant portion of its expenses, to develop, promote, and implement water conservation, augmentation, and management strategies to protect water resources for the benefit of the citizens of Montgomery County; consequently, these capital assets are not available for future spending.

Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

For the Year Ended December 31, 2015

Statement of Net Position:

The following table reflects the condensed Statement of Net Position as of December 31:

	Business-Type Activities	
	2015	(Restated) 2014
Current and other assets	\$ 1,970,651	\$ 2,636,547
Capital assets, net	1,723,897	1,759,736
Total Assets	3,694,548	4,396,283
Accounts payable & accrued expenses	106,090	189,666
Unearned revenue	615,734	1,179,162
Total Liabilities	721,824	1,368,828
Net position:		
Net investment in capital assets	1,723,897	1,759,736
Unrestricted	1,248,827	1,267,719
Total Net Position	\$ 2,972,724	\$ 3,027,455

The District's net position decreased to \$2,972,724 from \$3,027,455. The District had a decrease in current and other assets due to cash used in operations during the year. The District had a decrease in unearned revenue due to implementation of the District Regulatory Plan Phase II (B), effective 1/1/16, which mandates that all large volume groundwater user's annual production be limited to 70% of their total qualifying demand, as determined through public hearings conducted by the District.

Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

For the Year Ended December 31, 2015

Statement of Revenues, Expenses, and Changes in Net Position:

The following table provides a summary of the District's changes in net position for the years ended December 31:

	Governmental Activities	
	2015	(Restated) 2014
Revenues		
Water use fees	\$ 2,071,781	\$ 1,998,386
Interest and other	34,424	39,683
Total Revenues	2,106,205	2,038,069
Expenses		
Programs	335,246	286,524
Personnel	630,589	587,763
Legal	474,438	344,281
Education and public awareness	154,782	182,522
Other	478,690	419,657
Depreciation	87,191	82,240
Total Expenses	2,160,936	1,902,987
Change in Net Position	(54,731)	135,082
Beginning Net Position	3,027,455	2,892,373
Ending Net Position	\$ 2,972,724	\$ 3,027,455

Water use fees increased by \$73,395 due to increased consumption. Program expenses increased by \$48,722 due to increases in funds spent on studies during the current year. Personnel costs increased due to increases in salaries and healthcare costs. Legal expenses increased due to current litigation and related matters; see Note 5.

BUDGETARY HIGHLIGHTS

Actual revenues were less than final budgeted revenues by \$39,584 during the year. Water use fees were under budgeted amounts by \$48,032. Actual expenses were under the final budget by \$201,317. The most significant expense groupings under budget were personnel, engineering, and programs for \$124,404, \$34,530, and \$38,129, respectively. The net variance was a positive variance of \$161,733.

Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

For the Year Ended December 31, 2015

CAPITAL ASSETS

As of the end of the year, the District had invested \$1,723,897 in a variety of capital assets and infrastructure, net of accumulated depreciation.

Major capital asset events during the current year include the following:

- Purchase of vehicle for \$24,807
- Construction remodeling for \$14,286

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The District's appointed officials considered many factors when setting the 2016 annual budget. In its continuing conversion effort, which formally began in 2006, the District adopted Phase I, of the District Regulatory Plan (DRP), providing a 10-year advance notice to water users of the need for a 30% reduction and groundwater pumping. Based on this premise, each large volume ground water user is required to meet its initial conservation obligation, which is no more than 70% of its total qualifying demand, based on its 2009 permitted allocation.

This significantly affects the 2016 revenues of the District, since water use fees are collected based on permitted allocations. Permitted allocations in 2015 were approximately 33 billion gallons, as compared to 23 billion gallons in 2016. Revenue was budgeted at \$1,516,568, which is a decrease of \$629,221 compared to the budget for the 2015 year.

Operating expenses are budgeted at \$2,201,284, which is a reduction of \$125,130 from the budget for the 2015 year. Approximately 20%, or \$419,075 is budgeted for programs focused on groundwater monitoring, historical trends, water-level networks, and providing information and technical explanation to stakeholders and the public. Another 10%, or \$209,857 is budgeted for education and public awareness which focuses on community outreach programs and educating school age children, and the general public, in the importance of water conservation.

The reduction in revenue and on-going operational expenses, and increased legal expenses, resulted in a projected deficit of \$684,716. The District officials are proactively working to meet the management goals set forth in the DRP, and sustain the economic viability of the District.

The fiscal year 2016 budget was presented and adopted by the Board of Directors on January 12, 2016, with the agreement that the Budget Committee would continue to review the budget

Lone Star Groundwater Conservation District

MANAGEMENT'S DISCUSSION AND ANALYSIS *(Continued)*

For the Year Ended December 31, 2015

for additional cuts and if warranted, bring back to the Board for their consideration and amendment.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, customers, and creditors with a general overview of the District's finances to show the District's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the General Manager at 655 Conroe Park, North Drive, Conroe, TX 77303.

FINANCIAL STATEMENTS

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Lone Star Groundwater Conservation District

STATEMENT OF NET POSITION

December 31, 2015

<u>Assets</u>	<u>Business-Type Activities</u>
Current Assets	
Cash	\$ 1,882,594
Receivables	81,677
Prepaid expenses	6,380
Total Current Assets	<u>\$ 1,970,651</u>
Noncurrent Assets	
Capital assets, non-depreciable	260,187
Capital assets (net of accumulated depreciation)	1,463,710
Total Assets	<u>\$ 3,694,548</u>
Liabilities	
Current Liabilities	
Accounts payable and accrued expenses	\$ 106,090
Unearned revenue	615,734
Total Current Liabilities	<u>721,824</u>
Net Position	
Net investment in capital assets	1,723,897
Unrestricted	1,248,827
Net Position	<u>\$ 2,972,724</u>

See Notes to Financial Statements.

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Lone Star Groundwater Conservation District

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

For the Year Ended December 31, 2015

	<u>Business-Type Activities</u>
Revenues	
Water use fee	\$ 2,010,907
Administrative use fee	9,312
Application fee	34,850
Overpumpage fee	16,712
Penalty & interest on fees	16,630
Other income	16,029
Export fee	1,765
Total Revenues	<u>2,106,205</u>
Expenses	
Programs	335,246
Personnel	630,589
Legal	474,438
Audit	8,000
Engineering	146,970
Education & Public awareness	154,782
Board expenses	74,092
Rebate on water use fees	77,526
Manager expenses	21,912
Computer support	30,604
Office expenses	13,824
Supplies & other	11,479
Advertising & public notices	7,525
Travel and training staff	7,760
Membership dues	4,264
Building maintenance & utilities	52,259
Vehicle costs	9,061
Insurance	9,122
Miscellaneous	4,292
Depreciation	87,191
Total Expenses	<u>2,160,936</u>
Excess (Deficiency) of Revenues Over (Under) Expenses	(54,731)
Beginning Net Position	<u>3,027,455</u>
Ending Net Position	<u>\$ 2,972,724</u>

See Notes to Financial Statements.

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Lone Star Groundwater Conservation District

STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2015

	Business-Type Activities
<u>Cash Flows from Operating Activities</u>	
Receipts from customers	\$ 1,597,960
Payments to employees	(736,198)
Payments to suppliers	(1,345,055)
Net Cash Provided by / (Used) in Operating Activities	(483,293)
 <u>Cash Flows from Capital and Related Financing Activities</u>	
Capital purchases	(51,352)
Net Cash Provided by / (Used) in Capital and Related Financing Activities	(51,352)
Net Increase / (Decrease) in Cash and Cash Equivalents	(534,645)
Beginning cash and cash equivalents	2,417,239
Ending Cash and Cash Equivalents	\$ 1,882,594
 <u>Reconciliation of Operating Income / (Loss)</u>	
<u>to Net Cash Provided by / (Used) in Operating Activities</u>	
Operating loss	\$ (54,731)
Adjustments to reconcile operating loss to net cash provided:	
Depreciation	87,191
Changes in Operating Assets and Liabilities:	
(Increase) Decrease in:	
Accounts receivable	132,709
Other receivable	4,922
Prepaid expenses	(6,380)
Increase (Decrease) in:	
Accounts payable and accrued liabilities	(83,576)
Unearned revenue	(563,428)
Net Cash Provided by / (Used) in Operating Activities	\$ (483,293)

See Notes to Financial Statements.

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Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS

For the Year Ended December 31, 2015

NOTE 1 – CREATION OF DISTRICT

The Lone Star Groundwater Conservation District (District) was created by the 77th Legislature under the authority of Section 59, Article XVI, of the Texas Constitution and in accordance with Chapter 36 of the Texas Water Code to conserve, protect, and enhance the groundwater resources of Montgomery County, Texas.

The District was formed in 2001 and is governed by a board of directors who are appointed by various local government agencies and serve staggered four-year terms.

The mission of the District is to manage and protect the groundwater resources of Montgomery County, Texas and to work with others to ensure a sustainable, adequate, high quality and cost effective water supply for current and future needs.

The District is not a taxing authority. Operations of the District are funded by charges to water well users in the jurisdictions serviced by the District.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements and accounting policies of the District are prepared in conformity with generally accepted accounting principles for local governmental units as prescribed by the Governmental Accounting Standards Board, which is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District's significant accounting policies are described below.

A. Reporting Entity

The District has adopted Governmental Accounting Standards Board Statement No. 14, *The Financial Reporting Entity*. In accordance with this statement, a financial reporting entity consists of the primary government, organizations for which the primary government is financially accountable, and other organizations for which the primary government is not accountable, but for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The District is governed by a Board of Directors consisting of nine individuals who are appointed by local governing bodies. As required by generally accepted accounting principles, these financial statements present the activities of the District, which is considered to be the primary government as well as the reporting entity. There are no other organizations which meet the criteria for inclusion herein as part of the financial reporting entity.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

B. Basis of presentation – financial statements

Since the District is not a taxing authority and earns all revenue through fees, no governmental funds exist for the District. The District is designated as a special-purpose government engaged only in business-type activities consistent with GASB 34. Governments engaged only in business-type activities should present only the financial statements required for enterprise funds. As a result, the financial statements presented within this report consist of the enterprise fund financial statements (i.e., the Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position, and Statement of Cash Flows). The District has one enterprise fund.

C. Basis of presentation – fund financial statements

Enterprise Fund Types

Enterprise funds are used to account for activities that are similar to those often found in the private sector. For the District this covers all activities. The measurement focus is on determination of net income, financial position, and cash flows. Enterprise funds distinguish operating revenues and expenses from non-operating items. Operating revenues include charges for fees. Operating expenses include costs of materials, contracts, personnel, and depreciation. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Enterprise fund types follow GAAP prescribed by the Governmental Accounting Standards Board (GASB).

D. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

The accrual basis of accounting is used for the enterprise fund types. This basis of accounting recognizes revenues in the accounting period in which they are earned and become measurable, and expenses in the accounting period in which they are incurred and become measurable.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

E. Assets, liabilities, and net position

1. *Cash and cash equivalents*

The District's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

2. *Investments*

Temporary investments consist of money market funds and external investment pools and are presented at market value.

Applicable state laws and regulations allow the District to invest its funds in direct or indirect obligations of the United States, the State, or any county, city, school district, or other political subdivision of the State. Funds may also be placed in certificates of deposit of state or national banks or savings and loan associations (depository institutions) domiciled within the State. Related state statutes and provisions included in the District's bond resolutions require that all funds invested in depository institutions be guaranteed by federal depository insurance and/or be secured in the manner provided by law for the security of public funds.

In accordance with GASB Statement No. 31, *Accounting and Reporting for Certain Investments and External Investment Pools*, the District reports all investments at fair value, except for "money market investments" and "2a7-like pools." Money market investments, which are short-term highly liquid debt instruments that may include U.S. Treasury and agency obligations, are reported at amortized costs. Investment positions in external investment pools that are operated in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940, such as TexPool, are reported using the pools' share price.

Credit Risk – Investments. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. At year end, the District's investment in money market mutual funds was rated AAA by Standard & Poor's and Moody's.

Interest Rate Risk – Investments. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The District considers the investment in the money market mutual fund to have a maturity of less than one year due to the fact the share positions can usually be redeemed each day at the discretion of the District, unless there has been a significant change in value.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

3. *Receivables*

All trade receivables are shown net of any allowance for uncollectible amounts. The District estimates the allowance for doubtful accounts based on collections after the balance sheet date. As of December 31, 2015 the allowance for doubtful accounts was \$20,085.

4. *Capital Assets*

Capital assets, which include property, plant, equipment, are defined by the government as assets with an initial individual cost of more than \$1,500 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Property, plant, and equipment of the primary government are depreciated using the straight-line method over the following estimated useful years:

<u>Asset Description</u>	<u>Estimated Useful Life</u>
Buildings	30 years
Furniture, vehicles, and equipment	5 to 7 years

5. *Prepaid expenses*

Certain payments to vendors reflect costs applicable to future accounting periods (prepaid expenses) are recognized as expenses when utilized.

6. *Deferred outflows/inflows of resources*

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/ expenditure) until then.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. This amount is deferred and recognized as an inflow of resources in the period that the amounts become available.

7. *Net position flow assumption*

Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted net position in the financial statements, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

8. *Compensated absences*

The liability for compensated absences reported in the proprietary fund statements consist of unpaid, accumulated vacation and compensatory time balances. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. Vested or accumulated vacation leave and compensated leave of proprietary funds are recognized as an expense and liability of those funds as the benefits accrue to employees.

The District's personnel policy grants its eligible employees vacation pay benefits in varying amounts to specified maximums depending on tenure with the District. District employees may carry forward into the subsequent year, with management approval, earned but unused vacation pay benefits up to specified maximums. Upon separation with the District, employees will be paid for their accrued and unused vacation pay benefits. At December 31, 2015, the accrued vacation pay benefit balance was \$7,548.

The District's personnel policy permits its eligible employees to accrue up to 160 hours of sick leave per year. Unused, accumulated sick leave may be carried forward into the subsequent year with management approval. Upon separation with the District, employees will not be paid for unused, accumulated sick leave.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

9. Estimates

The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts 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 expenditures/expenses during the reporting period. Actual results could differ from those estimates.

10. Unearned revenue

Unearned revenue represents revenues billed but not earned as of December 31, 2015. This is comprised of revenue for well permits billed in the current year that relate to the annual or quarterly periods following December 31, 2015. The revenue is deferred and recognized in the permit year. As of December 31, 2015, unearned revenue was \$615,734.

NOTE 3 – STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

The original budget is adopted by the Board of Directors prior to the beginning of the year. Management may not amend the budget without the approval of the Board.

The District has adopted a non-appropriated budget in accordance with Title 30 of the Texas Administrative Code, Section 293.97. The budget is prepared using the modified accrual method of accounting. The budgetary comparison schedule is presented as other supplementary information to the basic financial statements.

NOTE 4 - DETAILED NOTES

A. Deposits and Investments

As of December 31, 2015, the District had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturity (years)</u>
Money market funds	\$ 1,582,722	-
External investment pools	264,711	0.11
	<u>\$ 1,847,433</u>	
Portfolio weighted average maturity		0.01

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

Interest rate risk. In accordance with its investment policy, the District manages its exposure to declines in fair values by limiting the weighted average of maturity not to exceed two years; structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations; monitoring credit ratings of portfolio position to assure compliance with rating requirements imposed by the Public Funds Investment Act; and invest operating funds primarily in short-term securities or similar government investment pools.

Credit risk. The District's investment policy limits investments in money market mutual funds rated as to investment quality not less than AAA by Standard & Poor's. As of December 31, 2015, the District's investment in TexPool was rated AAAM by Standard & Poor's.

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. State statutes require that all deposits in financial institutions be insured or fully collateralized by U.S. government obligations or its agencies and instrumentalities or direct obligations of Texas or its agencies and instrumentalities that have a market value of not less than the principal amount of the deposits. As of December 31, 2015 the District's insurance plus pledged collateral covered all deposits.

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District's investment policy requires that it will seek to safekeeping securities at financial institutions, avoiding physical possession. Further, all trades, where applicable, are executed by delivery versus payment to ensure that securities are deposited in the District's safekeeping account prior to the release of funds.

TexPool

TexPool was established as a trust company with the Treasurer of the State of Texas as trustee, segregated from all other trustees, investments, and activities of the trust company. The State Comptroller of Public Accounts exercises oversight responsibility over TexPool. Oversight includes the ability to significantly influence operations, designation of management, and accountability for fiscal matters. Additionally, the State Comptroller has established an advisory board composed of both participants in TexPool and other persons who do not have a business relationship with TexPool. The advisory board members review the investment policy and management fee structure. Finally, Standard & Poor's rate TexPool AAAM. As a requirement to maintain the rating, weekly portfolio information must

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

be submitted to Standard & Poor's, as well as to the office of the Comptroller of Public Accounts for review.

B. Receivables

The following comprise the receivable balances at year end:

<u>Type</u>	<u>Total</u>
Permit receivables	\$ 101,762
Allowance for doubtful accounts	(20,085)
Total	\$ 81,677

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

C. Capital Assets

A summary of changes in capital assets for the year ended is as follows:

	<u>Beginning Balances</u>	<u>Increases</u>	<u>Decreases/ Reclassifications</u>	<u>Ending Balances</u>
Capital assets, not being depreciated:				
Land	\$ 260,187	\$ -	\$ -	\$ 260,187
Total capital assets not being depreciated	<u>260,187</u>	<u>-</u>	<u>-</u>	<u>260,187</u>
Capital assets, being depreciated:				
Building	1,579,267	14,286	-	1,593,553
Furniture, vehicles & equipment	204,009	37,066	-	241,075
Total capital assets being depreciated	<u>1,783,276</u>	<u>51,352</u>	<u>-</u>	<u>1,834,628</u>
Less accumulated depreciation				
Building	(158,723)	(30,657)	-	(189,380)
Furniture, vehicles & equipment	(125,004)	(56,534)	-	(181,538)
Total accumulated depreciation	<u>(283,727)</u>	<u>(87,191)</u>	<u>-</u>	<u>(370,918)</u>
Net capital assets being depreciated	<u>1,499,549</u>	<u>(35,839)</u>	<u>-</u>	<u>1,463,710</u>
Total capital assets	<u>\$ 1,759,736</u>	<u>\$ (35,839)</u>	<u>\$ -</u>	<u>\$ 1,723,897</u>

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

NOTE 5 – OTHER INFORMATION

A. The 401(a) - Money Purchase Plan (401a Plan)

The 401a Plan is an employer-sponsored deferred contribution plan established by the District to provide benefits at retirement for its employees. Participation in the 401a Plan is mandatory. 401a Plan participants are required to contribute 3% of their gross wages per year, not to exceed federal maximums. The District will match the employee's 3% contributions at a 2:1 ratio to a maximum of 6%. Any employee contribution greater than 3% will not be matched. Employer matching contributions vest according to the 401a Plan policy.

Unvested employer contributions will be used to pay administrative expenses of the 401a Plan, with any remainder being applied to reduce employer contributions. 401a Plan provisions and contribution requirements are established and may be amended by the District.

The assets of the 401a Plan are administered by ICMA Retirement Corporation. The District does not exercise any control over these assets.

District contributions to the 401a Plan for the year ended December 31, 2015 were \$10,369. Additional contributions from plan forfeitures were \$18,345.

A. The 457 – Defined Contribution Plan (457 Plan)

The District also offers a defined contribution pension 457 Plan to its employees. Plans of deferred compensation described in Internal Revenue Code (IRC) section 457 are available to employees of certain state and local governments and non-governmental entities that are tax-exempt under IRC 501. As the District is a local government entity and is tax-exempt, the 457 Plan is a governmental eligible 457(b) plan. Plans eligible under 457(b) allow employees of sponsoring organizations to defer income taxation on retirement savings into future years. Employee participation in the District 457 Plan is optional. Employees contribute based on federal limits and guidelines. There is no District match. The Plan's assets are administered by ICMA Retirement Corporation. The District does not exercise any control over the plan assets.

In addition to its retirement plans, the District also makes contributions into the Social Security system. Effective January 1, 2000, the Internal Revenue Service determined that members of Boards of Directors are considered to be "employees" for federal payroll tax purposes only.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

B. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the District carries insurance coverage. There have been no significant reductions in coverage from the prior year.

The District is presently defending the following pending litigation; Cause No. 15-08-08942; City of Conroe et al v. Lone Star Groundwater Conservation District et al; in the 284th Judicial District Court of Montgomery County, Texas. In the suit, in addition to seeking recovery of attorneys' fees and costs, the Plaintiffs allege that the Defendants' actions with regard to adoption of its District Regulatory Plan exceed their statutory authority and constitute takings of their property without just compensation, but neither identify the specific property nor the dollar amount of their claims. The District, directors, and general manager have vigorously contested and defended themselves against the lawsuit and are awaiting the judge's ruling on their Pleas to the Jurisdiction seeking dismissal of all of the claims in the Original Petition. If unsuccessful in doing so, at this early stage in the lawsuit, the District is unable to estimate the likelihood of an unfavorable outcome or estimated range of loss if an unfavorable outcome for the District were to occur.

NOTE 6 – COMMITMENTS

Regarding conservation education, the District first entered into agreement in 2011 with National Cinemedia for in-theater advertising at four area movie theaters in Montgomery County using various water conservation clips to promote conservation and reduction in outdoor irrigation practices. The following October of 2012, the District extended the agreement for an additional year adding one other area theater to the overall media project for a total of five theaters in Montgomery County. Also added that year, was the showing of the same theater ad on lobby screens in the four theaters which had this feature. Upon contract renewal in 2013/14 year, the annual amount totaled \$38,064. The first eight months of the contract was identical to the previous year, with WJPA sharing in the partnership, so the cost-sharing was recalculated to reflect each partner equally sharing the total cost. This meant that each organization began to pay 33.3%. The 2015/16 contract year continued this new partnership, with each group paying an annual share of \$20,886 to make up the total contract amount of \$62,660.

Near the end of 2014, the District's board of directors embarked on an updated Strategic Water Resources Plan (the "Strategic Plan") to serve as a guide in the conservation and management of groundwater resources in Montgomery County. This Strategic Plan is designed to evaluate potential opportunities for the additional development of groundwater resources while ensuring the long-term viability of aquifers located in Montgomery County.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

The first part of the board approved study is a groundwater production and water-level data assessment, the second task is a review of the Total Estimated Recoverable Storage (TERS) and the third portion is determination of future groundwater availability. The study is expected to take 2-3 years to complete, and the District will share findings as they become available.

In December 2014, the District authorized a \$308,000 joint funding agreement for data collection with the U.S. Geological Survey (USGS) for fiscal year 2015 for (1) Ground Water Program to inventory new large capacity wells and properly record and archive discontinued sites; to prepare water-level, water quality, and hydrograph data for publication in the USGS Water Resources Data of Texas, operation and maintenance of continuous water-level gages in Montgomery County; measure nested Jasper and Catahoula wells in the county monthly and provide public information; and install one new continuous water-level gage (2) Groundwater Monitoring and Historical Trend Analysis as a component of the USGS Groundwater Collection and Subsidence Program in efforts to determine the magnitude and extent of land-surface subsidence due to withdrawals of groundwater and to create an annual series of water level reports to determine possible relationships; (3) Water-level Monitoring Network – measure static groundwater levels in active Gulf Coast aquifer wells during the winter; prepare a report of water-level altitudes and altitude changes in the Gulf Coast aquifer System for the current year; and measure pumping ground-water levels in active Gulf Coast aquifer wells during the summer; and (4) \$20,000 for Technical Assistance & Special Projects as may be required or necessary throughout the cooperative year. The District will contribute \$251,375 to the joint-funding agreement, and the USGS will contribute \$56,625, for a total of \$308,000. In December of 2015 this agreement was renewed under the same terms.

NOTE 7 – RELATED PARTY

District board members, Mr. Wood and Mr. Baker, are both also board members with First Financial Bank, which holds the majority of the District's deposits. These directors abstain from voting on matters related to First Financial Bank.

Lone Star Groundwater Conservation District

NOTES TO FINANCIAL STATEMENTS (Continued)

For the Year Ended December 31, 2015

NOTE 8 - RESTATEMENT

The District has restated its beginning net position due to a difference in depreciation expense applicable to the prior year. The restatement of beginning net position is as follows:

	Business Type
	Activities
Prior year ending net position	\$ 3,037,802
Correction of accumulated depreciation	(10,347)
Restated net position	<u>\$ 3,027,455</u>

NOTE 9 - SUBSEQUENT EVENTS

There were no material subsequent events through the date the financial statements were issued.

NOTE 10 - NEW ACCOUNTING PRONOUNCEMENTS

The Governmental Accounting Standards Board (GASB) has issued several new pronouncements. The District has reviewed these new pronouncements and has determined that, at this time, they do not appear to be applicable to the District.

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OTHER SUPPLEMENTARY INFORMATION

Lone Star Groundwater Conservation District

BUDGETARY COMPARISON - PROPRIETARY FUND (Page 1 of 2)

For the Year ended December 31, 2015

	Original Budget Amounts	Final Budget Amounts	Actual	Variance Positive (Negative)
Revenues				
Water use fee	\$ 2,058,939	\$ 2,058,939	\$ 2,010,907	\$ (48,032)
Administrative use fee	7,350	7,350	9,312	1,962
Application fee	42,000	42,000	34,850	(7,150)
Overpumpage fee	12,000	12,000	16,712	4,712
Penalty & interest on fees	15,000	15,000	16,630	1,630
Other income	5,500	5,500	16,029	10,529
Export fee	5,000	5,000	1,765	(3,235)
Total Revenues	<u>2,145,789</u>	<u>2,145,789</u>	<u>2,106,205</u>	<u>(39,584)</u>
Expenses				
Programs	373,375	373,375	335,246	38,129
Personnel	754,993	754,993	630,589	124,404
Legal	204,000	404,000	474,438	(70,438)
Audit	8,000	8,000	8,000	-
Engineering	181,500	181,500	146,970	34,530
Education & Public awareness	193,033	193,033	154,782	38,251
Board expenses	69,200	69,200	74,092	(4,892)
Rebate on water use fees	30,000	30,000	77,526	(47,526)
Manager expenses	12,000	12,000	21,912	(9,912)
Computer support	34,100	34,100	30,604	3,496
Office expenses	37,700	37,700	13,824	23,876
Supplies & other	25,518	25,518	11,479	14,039
Advertising & public notices	8,000	8,000	7,525	475

Lone Star Groundwater Conservation District

BUDGETARY COMPARISON - PROPRIETARY FUND (Page 2 of 2)

For the Year ended December 31, 2015

	Original Budget Amounts	Final Budget Amounts	Actual	Variance Positive (Negative)
Expenses (continued)				
Travel and training staff	26,000	26,000	7,760	18,240
Membership dues	5,500	5,500	4,264	1,236
Building maintenance & utilities	42,000	42,000	52,259	(10,259)
Vehicle costs	13,500	13,500	9,061	4,439
Insurance	14,995	14,995	9,122	5,873
Miscellaneous	3,000	3,000	4,292	(1,292)
Capital outlay - vehicles	40,000	40,000	24,807 ¹	15,193
Capital outlay - other	50,000	50,000	26,545 ¹	23,455
Total Expenses	<u>\$ 2,126,414</u>	<u>\$ 2,326,414</u>	<u>\$ 2,125,097</u>	<u>\$ 201,317</u>
Revenues over (under) expenses	<u>\$ 19,375</u>	<u>\$ (180,625)</u>	<u>\$ (18,892)</u>	<u>\$ 161,733</u>
Beginning Net Position			<u>3,027,455</u>	
Ending Net Position - modified			<u>\$ 3,008,563 ¹</u>	
Capital outlay			51,352	
Depreciation expense			(87,191)	
Ending Net Position			<u>\$ 2,972,724</u>	

¹ Budget presented on modified accrual basis.

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TEXAS SUPPLEMENTARY INFORMATION

Lone Star Groundwater Conservation District

COMPARATIVE SCHEDULE OF REVENUES AND EXPENDITURES

Last Five Years

	Amounts				
	2015	2014	2013	2012	2011
Revenues					
Application fees	\$ 34,850	\$ 44,460	\$ 42,939	\$ 35,197	\$ 71,565
Export fees	1,765	2,942	18,842	10,193	2,393
Water use fees	2,020,219	1,964,785	1,895,988	1,841,087	2,016,048
Interest income	4,657	5,096	6,744	8,683	10,243
Overpumpage fee	16,712	7,296	27,534	76,680	36,669
Miscellaneous	11,372	11,560	2,401	2,248	2,912
Penalty & interest	16,630	1,930	14,351	35,954	31,024
Total Revenues	<u>2,106,205</u>	<u>2,038,069</u>	<u>2,008,799</u>	<u>2,010,042</u>	<u>2,170,854</u>
Total Expenses	<u>2,160,936</u>	<u>1,902,987</u>	<u>1,668,815</u>	<u>1,810,071</u>	<u>2,484,925</u>
Revenues Over (Under)					
Expenditures	<u>\$ (54,731)</u>	<u>\$ 135,082</u>	<u>\$ 339,984</u>	<u>\$ 199,971</u>	<u>\$ (314,071)</u>

Percent of Total Fund Revenues

<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
1.7 %	2.2 %	2.1 %	1.8 %	3.3 %
0.1 %	0.1 %	0.9 %	0.5 %	0.1 %
95.9 %	96.4 %	94.4 %	91.6 %	92.9 %
0.2 %	0.3 %	0.3 %	0.4 %	0.5 %
0.8 %	0.4 %	1.4 %	3.8 %	1.7 %
0.5 %	0.6 %	0.1 %	0.1 %	0.1 %
0.8 %	0.1 %	0.7 %	1.8 %	1.4 %
<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>	<u>100.0 %</u>
<u>102.6 %</u>	<u>93.4 %</u>	<u>83.1 %</u>	<u>90.1 %</u>	<u>114.5 %</u>
<u>(2.6) %</u>	<u>6.6 %</u>	<u>16.9 %</u>	<u>9.9 %</u>	<u>(14.5) %</u>

Lone Star Groundwater Conservation District

PROPRIETARY FUND EXPENDITURES

For the Years Ended December 31, 2015 and 2014

	2015	2014
<u>Current</u>		
Personnel Services (including benefits)	\$ 630,589	\$ 587,763
Professional Fees:		
Auditing	8,000	8,000
Legal	474,438	344,281
Consulting	146,970	148,438
	629,408	500,719
 Administrative programs		
Directors' fees	63,094	49,750
Office supplies & Postage	11,479	23,013
Insurance	9,122	9,237
	83,695	82,000
 Community programs		
Well spacing	1,688	19,141
Hydrogeological modeling	2,655	-
Comprehensive production & water level	-	23,000
Strategic planning & other	142,373	5,508
USGS - joint funding agreement	188,530	238,875
	335,246	286,524
 Other Expenditures		
Building expense, including depreciation	108,793	79,626
Depreciation on equipment	30,657	40,939
Education & public awareness	154,782	182,522
Travel/training for staff & board	40,670	51,125
Computer support	30,604	16,191
Advertising	7,525	8,028
Membership dues & subscriptions	4,264	5,659
User fees rebates	77,526	41,419
Miscellaneous & other expenses	18,116	6,431
Interest & loan origination fees	-	4,887
Field & technical	9,061	9,154
	481,998	445,981
Total Expenditures	\$ 2,160,936	\$ 1,902,987

Lone Star Groundwater Conservation District

CASH AND TEMPORARY INVESTMENTS

December 31, 2015

<u>Funds</u>	<u>Identification or Certificate Number</u>	<u>Interest Rate (%)</u>	<u>Maturity Date</u>	<u>Balance</u>
Checking - operating	1049725	0.00%	N/A	\$ 35,161
Checking - money market	1026172	0.15%	N/A	1,582,722
TexPool	788420	0.25%	N/A	<u>264,711</u>
	Total			<u><u>\$ 1,882,594</u></u>

Lone Star Groundwater Conservation District

BOARD MEMBERS, KEY PERSONNEL AND CONSULTANTS

For the Year Ending December 31, 2015

District's Mailing Address: 655 Conroe Park North Drive
Conroe, Texas 77303

District's Business Telephone Number: (936) 494-3436

<u>Board Members</u>	<u>Term Expires</u>	<u>Fees</u>	<u>Expenses</u>	<u>Title</u>
Richard J. Tramm	1/31/2017	\$ 9,000	\$ 1,106	President
1 Sam Baker	N/A	\$ 5,500	\$ - *	Vice President
Scott Weisinger, PG	1/31/2017	\$ 3,750	\$ -	Secretary
James M. Stinson, PE	1/31/2019	\$ 8,000	\$ -	Treasurer
John Bleyl, PE	1/31/2017	\$ 9,000	\$ -	Director
Jace Houston	1/31/2017	\$ 6,250	\$ -	Director
Rick Moffatt	1/31/2019	\$ 8,500	\$ 508	Director
Roy McCoy, Jr.	1/31/2019	\$ 1,000	\$ -	Director
W.B. Wood	1/31/2019	\$ 8,500	\$ 1,149 *	Director

* Mr. Wood and Mr. Baker are board members with First Financial Bank, which holds some of the District's deposits. These directors abstain from voting on matters related to First Financial Bank.

1 Mr. Baker resigned during 2015. Mr. Gregg Hope has assumed his position with the board.

<u>Name and Address</u>		<u>Amount</u>	<u>Title</u>
<u>Key Administrative Personnel</u>			
Kathy Turner Jones	Salary	\$ 127,000	General Manager
	Expenses	\$ 13,863	
Paul R. Nelson (Part time)	Salary	\$ 53,668	Asst. G.M.
	Expenses	\$ 4,238	
<u>Consultants</u>			
Sledge Law & Public Strategies		\$ 379,926	Legal
Martin Earl & Stilwell, LLP		\$ 33,554	Legal
Smith, Robertson, Elliott & Douglas, LLP		\$ 22,524	Legal
Department of Interior - USGS		\$ 248,250	Research & development
Mark Lowry, PE		\$ 59,354	Engineering
Halff Associates		\$ 54,764	Engineering
LBG-Guyton Associates		\$ 130,689	Engineering
Mullican and Associates		\$ 50,841	Consultant
VanWassehnova & Associates		\$ 8,000	Auditor

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