



REPORT OF INDEPENDENT AUDITORS
AND FINANCIAL STATEMENTS

**LAS CAMPANAS WATER AND SEWER
COOPERATIVE**

December 31, 2017 and 2016

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Report of Independent Auditors

To the Members of
Las Campanas Water and Sewer Cooperative
Santa Fe, New Mexico

Report on Financial Statements

We have audited the accompanying financial statements of Las Campanas Water and Sewer Cooperative (the "Co-op"), which comprise the balance sheets as of December 31, 2017 and December 31, 2016, and the related statements of activities, members' capital, 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.

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 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 Las Campanas Water and Sewer Cooperative as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years ended December 31, 2017 and 2016 in accordance with accounting principles generally accepted in the United States of America.

Mess Adams LLP

Albuquerque, New Mexico
April 26, 2018

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Las Campanas Water and Sewer Cooperative

Balance Sheets

ASSETS

| | December 31, | |
|---|-----------------------------|-----------------------------|
| | <u>2017</u> | <u>2016</u> |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 1,709,933 | \$ 1,293,471 |
| Investment securities | 4,753,483 | 4,633,320 |
| Accounts receivable from members, net of allowance of \$11,570 and \$18,000, respectively | 240,437 | 203,073 |
| Prepaid assets | <u>16,046</u> | <u>31,370</u> |
| Total current assets | 6,719,899 | 6,161,234 |
| Property and equipment, net of accumulated depreciation | <u>14,799,500</u> | <u>15,083,149</u> |
| Total assets | <u><u>\$ 21,519,399</u></u> | <u><u>\$ 21,244,383</u></u> |

LIABILITIES AND MEMBERS' CAPITAL

| | | |
|--|-----------------------------|-----------------------------|
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 71,510 | \$ 79,896 |
| Accrued liabilities | <u>28,828</u> | <u>46,342</u> |
| Total liabilities | <u>100,338</u> | <u>126,238</u> |
| MEMBERS' CAPITAL | | |
| Accumulated deficit | (897,521) | (1,131,577) |
| Contributed capital | <u>22,316,582</u> | <u>22,249,722</u> |
| Total members' capital | <u>21,419,061</u> | <u>21,118,145</u> |
| Total liabilities and members' capital | <u><u>\$ 21,519,399</u></u> | <u><u>\$ 21,244,383</u></u> |

Las Campanas Water and Sewer Cooperative Statements of Activities

| | December 31, | |
|---|-------------------|-------------------|
| | 2017 | 2016 |
| REVENUES | | |
| Fees | \$ 1,945,085 | \$ 1,956,483 |
| Surcharges, net of abatements | 162,902 | 175,290 |
| Total operating revenues | <u>2,107,987</u> | <u>2,131,773</u> |
| EXPENSES | | |
| Purchased water | 471,781 | 477,247 |
| Outside services | 492,416 | 455,232 |
| Administrative | 374,525 | 341,038 |
| Repairs and maintenance | 130,024 | 127,249 |
| Electricity | 106,634 | 103,011 |
| Buckman Direct Diversion project costs | 9,477 | 47,841 |
| Insurance | 26,943 | 26,581 |
| Meters expense | 3,160 | 10,303 |
| Licenses and other taxes | 2,982 | 1,671 |
| | <u>1,617,942</u> | <u>1,590,173</u> |
| INCOME FROM OPERATIONS BEFORE DEPRECIATION | 490,045 | 541,600 |
| Depreciation | <u>377,079</u> | <u>386,583</u> |
| INCOME FROM OPERATIONS | <u>112,966</u> | <u>155,017</u> |
| NON-OPERATING ACTIVITY | | |
| Net realized and unrealized gain | 18,845 | 35,353 |
| Refund of gross receipts tax | - | 65,410 |
| Interest Income | 235 | 305 |
| Dividend income | 107,400 | 103,498 |
| Total non-operating income, net | <u>126,480</u> | <u>204,566</u> |
| Bad debt recovery | 6,430 | 24,259 |
| Bad debt expense | <u>(11,820)</u> | <u>-</u> |
| NET INCOME | <u>\$ 234,056</u> | <u>\$ 383,842</u> |

Las Campanas Water and Sewer Cooperative

Statements of Members' Capital

| | Accumulated Balance (Deficit) | Contributed Capital | Total |
|--------------------------------------|----------------------------------|------------------------|---------------|
| BALANCE, December 31, 2015 (deficit) | \$ (1,515,419) | \$ 22,202,562 | \$ 20,687,143 |
| Membership fees | - | 47,160 | 47,160 |
| Net Income | 383,842 | - | 383,842 |
| BALANCE, December 31, 2016 (deficit) | (1,131,577) | 22,249,722 | 21,118,145 |
| Membership fees | - | 66,860 | 66,860 |
| Net Income | 234,056 | - | 234,056 |
| BALANCE, December 31, 2017 (deficit) | \$ (897,521) | \$ 22,316,582 | \$ 21,419,061 |

Las Campanas Water and Sewer Cooperative Statements of Cash Flows

| | Years Ended December 31, | |
|--|--------------------------|---------------------|
| | 2017 | 2016 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net Income | \$ 234,056 | \$ 383,842 |
| Adjustments to reconcile operating income to net cash provided by operating activities | | |
| Depreciation | 377,079 | 386,583 |
| Net realized and unrealized (gain) | (18,845) | (35,353) |
| Changes in allowance for doubtful accounts | (6,430) | (28,710) |
| Changes in operating assets and liabilities | | |
| Accounts receivable from members | (30,934) | 4,320 |
| Prepaid assets | 15,324 | 43 |
| Accounts payable | (8,386) | (18,103) |
| Accrued liabilities | (17,514) | 21,436 |
| Net cash provided by operating activities | <u>544,350</u> | <u>714,058</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of securities | (101,318) | (103,498) |
| Purchase of property and equipment | (93,430) | (48,085) |
| Net cash used by investing activities | <u>(194,748)</u> | <u>(151,583)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Membership fees received | 66,860 | 47,160 |
| Net cash provided by financing activities | <u>66,860</u> | <u>47,160</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 416,462 | 609,635 |
| CASH AND CASH EQUIVALENTS, beginning of period | 1,293,471 | 683,836 |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 1,709,933</u> | <u>\$ 1,293,471</u> |

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies

Organization and Background

Las Campanas Homeowners Water Cooperative was formed on January 22, 1993, under the laws of the state of New Mexico, for the purpose of providing water service to its members located in the residential community known as Las Campanas in Santa Fe, New Mexico. The members of the Las Campanas Homeowners Water Cooperative consist of residential lot purchasers in the Las Campanas development. The operations of the Las Campanas Homeowners Water Cooperative began July 1, 1994.

Las Campanas Sewer Cooperative was formed on June 26, 1995 under the laws of the state of New Mexico, for the purpose of providing sewer service to its members located in the residential community known as Las Campanas in Santa Fe, New Mexico. The members of the Las Campanas Sewer Cooperative consist of residential lot purchasers in the Las Campanas development. The operations of the Las Campanas Sewer Cooperative began July 1, 1995.

The assets and operations of the Las Campanas Homeowners Water Cooperative and Las Campanas Sewer Cooperative were combined effective June 1, 2012. The combined entity, Las Campanas Water and Sewer Cooperative (the Co-op), is controlled by a Board of Directors consisting of cooperative members. The Board of Directors is responsible for oversight of the Co-op's management and is responsible for establishing policies. The Directors are not compensated for their services.

Buckman Direct Diversion Project

The Buckman Direct Diversion Project is a shared facility with the City of Santa Fe, Santa Fe County, the Co-op, and The Club at Las Campanas. This relationship is described, from design through operations, in the Facility Operations Agreement between the proponents. This project, which diverts water from the Rio Grande, is the fulfillment of the 1994 Replacement Water Agreement with the Santa Fe County for a 100-year water supply as required by the Master Plan. The Co-op signed the First Amendment to the Facility Operations and Procedures Agreement ("the Agreement") for the Buckman Diversion Project with an effective date of July 1, 2016.

Bulk Water Service Agreement

On October 16, 2009, the Co-op and Santa Fe County approved at the Board of County Commissioners a Bulk Water Service Agreement (BWSA) with full build-out anticipated to be 2030. This agreement provides potable water to the Co-op as a bulk wholesale customer of the County on a perpetual basis. Deliveries pursuant to this agreement commenced on May 1, 2011. Prior to May 1, 2011, all water was purchased from the City of Santa Fe.

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.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents

The Co-op considers highly liquid investments with original maturities of three months or less when purchased to be cash equivalents.

Cash is held in depository accounts at various financial institutions. The combined account balance at any given institution may exceed the Federal Deposit Insurance Corporation (FDIC) insurance coverage and, as a result, there is a concentration of credit risk related to amounts on deposits in excess of FDIC insurance coverage. Management believes, based on the quality of the financial institutions, that the risk is not significant.

Investments

Investment securities are carried by the Co-op at fair value in accordance with accounting principles generally accepted in the United States. The fair value of investment securities is determined based on quoted market prices and estimates of value for non-traded securities. Investment securities are comprised of mutual funds in 2017 and in 2016.

Accounts Receivable

Accounts receivable are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a quarterly basis. Management determines the allowance for uncollectible accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Accounts receivable are written off when deemed uncollectible. Recoveries of accounts receivable previously written off are recorded when received. An account receivable is considered to be past due if any portion of the receivable balance is outstanding for more than 30 days.

Property and Equipment

A “Capital Asset” is defined by the co-op as a unit of property that: (1) has an economic useful life that extends beyond 12 months and was acquired or produced for a cost of \$5,000 or more. Fixed assets include items of property and equipment such as buildings, office furniture, fixtures, computers and other related technology equipment.

In line with Industry standards, the Co-op utilizes the composite rate depreciation method. The composite method includes all utility plant assets segregated into a single category in which a depreciation rate of 2.5% is applied to the entire group of assets based on the estimated useful lives of those utility plant assets.

Income Taxes

The Co-op qualifies as a tax-exempt organization under Section 501(c)(12) of the Internal Revenue Code and, accordingly, if certain conditions are met, is not subject to federal income tax, except to the extent that it has unrelated business income.

The Co-op applies the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740, Income Taxes. FASB ASC 740 provides detailed guidance for the financial statement recognition, measurement, and disclosure of uncertain tax positions in an enterprise’s financial statements. Uncertain income tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon the adoption of FASB ASC 740 and in subsequent periods.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

The provisions of FASB ASC 740 have been applied to all Co-op income tax positions commencing from that date. The Co-op's policy is to classify income tax penalties and interest according to their natural classification in its financial statements. During the years ended December 31, 2017 and 2016, the Co-op incurred no interest and penalties. As of December 31, 2017, management does not believe the Co-op has any uncertain tax positions that would require financial statement recognition, measurement, or disclosure under FASB ASC 740.

Fees and Deposits

Fees consist of sewer and water usage charges for residential and commercial customers, and system maintenance charges in accordance with a published rate schedule approved by the Co-op's Board of Directors.

To admit new residential members, the Co-op collects a deposit (currently \$2,490 for water and \$2,250 for sewer) and warrants that service will be provided to the member when needed. The deposits are non-refundable and are recognized as contributed capital upon receipt. Sale or transfer of a member's lot effectively terminates the membership of the seller and the initial deposit collected as contributed capital transfers to the new owner. Annual revenues in excess of annual expenses are invested at the discretion of the Board of Directors.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. The Co-op recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. The Co-op's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are available to be issued.

The Co-op has evaluated subsequent events through April 26, 2018, which is the date the financial statements were available for issuance.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 2 – Reserve Fund

The Board of Directors established a Replacement Reserve Fund (the Fund) for future replacement costs of physical plant or equipment. The Co-op agreed to dedicate cash to the Fund on an annual basis at least one half the annual revenues in excess of annual expenses, until such time as the Fund's assets reach an amount consistent with prudent management of a sewer and water cooperative. As of December 31, 2017 and 2016, this amount has been met.

Note 3 – Fair Value Measurements

Financial Accounting Standards Board (FASB) *Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures*, provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820 are described as follows:

Basis of Fair Value Measurement –

Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Co-op has the ability to access.

Level 2 – Quoted prices in markets that are not considered to be active or financial instruments without quoted market prices, but for which all significant inputs are observable, either directly or indirectly.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2017 and 2016.

Mutual Funds

Valued at market value of shares held by the Co-op at year end using prices quoted by the relevant pricing agent.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 3 – Fair Value Measurements (continued)

The valuation methods used by the Co-op may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Co-op believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The mutual funds had a fair value of \$4,753,483 and \$4,633,320 as of December 31, 2017 and 2016, respectively. All mutual funds were valued using level 1 measurements.

Realized and unrealized gains included in changes in net assets for the years ended December 31, 2017 and 2016 were \$18,845 and \$35,353, respectively, and are reported on the statements of activities.

Note 4 – Accounts Receivable

Accounts receivable consists of outstanding bills to members for water and sewer usage.

Receivables consisted of the following at December 31:

| | December 31, | |
|--|-------------------|-------------------|
| | <u>2017</u> | <u>2016</u> |
| Accounts receivable, members (net of allowances of \$11,570 and \$18,000 in 2017 and 2016, respectively) | <u>\$ 240,437</u> | <u>\$ 203,073</u> |

Changes in the Cooperative's allowance for doubtful accounts are as follows at December 31:

| | <u>2017</u> | <u>2016</u> |
|----------------------|------------------|------------------|
| Beginning balance | \$ 18,000 | \$ 46,710 |
| Bad debt expense | (11,820) | - |
| Accounts written off | 5,390 | (4,451) |
| Recoveries | <u>-</u> | <u>(24,259)</u> |
| Ending balance | <u>\$ 11,570</u> | <u>\$ 18,000</u> |

Las Campanas Water and Sewer Cooperative Notes to Financial Statements

Note 5 – Property and Equipment

The following is a summary of Property and Equipment as of December 31, 2017 and 2016, respectively:

| | For the Year Ended December 31, 2017 | | | | Ending Balance |
|---------------------------------|--------------------------------------|--------------|-------------|-------------|-------------------|
| | Beginning Balance | Additions | Retirements | Adjustments | |
| Furniture and equipment | \$ 677,496 | \$ 80,207 | \$ - | \$ - | \$ 757,703 |
| Collection and treatment system | 12,185,676 | - | - | (33,990) | 12,151,686 |
| Water distribution system | 5,178,501 | 13,223 | - | 33,990 | 5,225,714 |
| | 18,041,673 | 93,430 | - | - | 18,135,103 |
| Accumulated depreciation | (2,958,524) | (377,079) | - | - | (3,335,603) |
| Total capital assets, net | \$ 15,083,149 | \$ (283,649) | \$ - | \$ - | \$ 14,799,500 |

| | For the Year Ended December 31, 2016 | | | | Ending Balance |
|---------------------------------|--------------------------------------|--------------|-------------|-------------|-------------------|
| | Beginning Balance | Additions | Retirements | Adjustments | |
| Furniture and equipment | \$ 671,075 | \$ 6,421 | \$ - | \$ - | \$ 677,496 |
| Collection and treatment system | 12,185,676 | - | - | - | 12,185,676 |
| Water distribution system | 5,178,501 | - | - | - | 5,178,501 |
| | 18,035,252 | 6,421 | - | - | 18,041,673 |
| Accumulated depreciation | (2,571,941) | (386,583) | - | - | (2,958,524) |
| Total capital assets, net | \$ 15,463,311 | \$ (380,162) | - | - | \$ 15,083,149 |

Note 6 – Operations, Maintenance and Management Services Agreement

The Co-op entered into an operation, maintenance, and management service agreement effective December 1, 2010, with Operations Management International, Inc. to manage, operate and maintain the wastewater collection, pumping and treatment facilities, water treatment facilities, distribution and metering system for the Co-op. The agreement was amended and restated October 28, 2015 for five years and will automatically renew for an additional five years unless cancelled by either party 120 days prior to expiration on November 30, 2020. Under the agreement, the Co-op is required to pay one-twelfth of the agreed upon annual base fee each month. Changes in the base fee amount are negotiated annually, limited to a maximum five percent annual increase unless otherwise agreed upon.

As of December 31, 2017 and 2016, the Co-op incurred costs of \$492,259 and \$453,485, respectively, under the agreement for their services.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 7 – Related Party Transactions

The Club at Las Campanas, Inc.

The Club at Las Campanas, Inc. is a customer of the Co-op. The Co-op invoiced \$205,943 and \$189,314, respectively, for sewer and water services, including effluent water, leased water rights, and fees as of December 31, 2017 and 2016.

Las Campanas Owners Association

The Las Campanas Master Association is a customer of the Co-op. The Co-op invoiced \$90,833 and \$101,111, respectively, for sewer and water services, and fees as of December 31, 2017 and 2016.

The Las Campanas Master Association and Co-op have entered into an arrangement dated October 11, 2016 whereby certain changes were made to the May 2013 Agreement for Financial, Operational and Customer Support Services. These changes affected the basis of allocation of staff time from a “percentage of time” to a “functional allocation basis” and extended the allocations to six core functions: Customer Care Services, Financial Services, Human Resources/Operations Services, Gatehouse Services, Rent and Administrative Expense Services. As of December 31, 2017 and 2016, the Co-op paid \$90,784 and \$110,699, respectively, to the Las Campanas Master Association for the contractual costs, not including rent.

In January 2010, the Co-op began renting office space on a month to month basis from the Las Campanas Master Association and paid rent expense of \$23,400 respectively, as of December 31, 2017 and 2016.

Note 8 – Commitments and Contingencies

Sewer System Interconnection Agreement

The Las Campanas Sewer Cooperative entered into an agreement on February 26, 2008 with Suerte Del Sur Homeowner’s Association (“Suerte”), a New Mexico nonprofit association, to connect to their system. Under the agreement, the Co-op will be required to collect, pump, treat and dispose of the sewage for the development and will receive usage fees for this. The Co-op will receive up to \$1.5 million in revenues one year following Suerte’s filing of their plat with Santa Fe County, which has not yet occurred. Since the entire subdivision will not be platted at one time, the revenue will be received in phases. As of December 31, 2017 and 2016, the Co-op incurred and received no amounts under the agreement since no activity has yet occurred. This agreement expires in 2023.

Other

The Co-op’s commitments and contingencies include the usual obligations incurred by providers of water and sewer services to members located in a residential community in the normal course of business. In the opinion of management, any matters arising from providing water and sewer services will not have a material effect on the Co-op’s financial position or results of operations.

Las Campanas Water and Sewer Cooperative

Notes to Financial Statements

Note 8 – Commitments and Contingencies (continued)

Buckman Direct Diversion

Dating back to 2015, management was advised that the allocations of certain costs associated with the operation of the Buckman Direct Diversion Project (“BDD”) were being debated among officials at the City of Santa Fe and Santa Fe County. The Co-op, as a result, has experienced delayed and inconsistent billings for the past three years. The Co-op and other partners involved in the BDD signed the First Amendment to the Facility Operations and Procedures Agreement (“the Agreement”) with an effective date of July 1, 2016. Management has continued to track and accrue all monthly BDD estimated invoice amounts even if the invoice was not received. Additionally, as a result of the signed Agreement and continued negotiations with the BDD partners, a recalculated allocation of Santa Fe County water rights was agreed to and the Co-op has recorded an estimated accounts receivable related to their proportional BDD water rights.

Note 9 – Line of Credit

In August 2012, the Co-op obtained a \$1,000,000 revolving line of credit from a bank. Interest is payable monthly on outstanding balances at an interest rate of 1.0% over the “Wall Street Journal” Prime Rate (which was 3.25% at the time of the agreement) but not less than 4.750%. On September 6, 2017 the line of credit with New Mexico Bank and Trust was renewed. At December 31, 2017 and 2016, the line’s effective rate of interest was 4.75%, and no borrowings occurred.