



FINANCIAL STATEMENTS

**December 31, 2017 and
December 31, 2016**

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**NORTH HARRIS COUNTY REGIONAL WATER AUTHORITY
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Independent Auditors' Report

Board of Directors
North Harris County Regional Water Authority
Harris County, Texas

We have audited the accompanying financial statements of the business type activities of North Harris County Regional Water Authority (the "Authority"), as of December 31, 2017 and December 31, 2016, which collectively comprise the Authority's basic financial statements and the related notes to the financial statements as listed in the table of contents.

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 opinions on these basic 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 basic financial statements are free of 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 principles used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

***Board of Directors
North Harris County Regional Water Authority
Harris County, Texas***

We believe that the audit evidence we have obtained is sufficient 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 North Harris County Regional Water Authority, as of December 31, 2017 and 2016, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other-Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Authority's financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied to the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

McGuire & Co, P.C.

Houston, Texas
May 7, 2018

Management's Discussion and Analysis

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***North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017***

Using this Annual Report

Within this section of the financial report of the North Harris County Regional Water Authority (the "Authority"), the Authority's Management provides narrative discussion and analysis of the financial activities of the Authority, for the fiscal years ended December 31, 2017 and 2016. This analysis should be read in conjunction with the basic financial statements that follow this section.

In addition to this discussion and analysis, this annual report consists of:

- The Authority's basic financial statements;
- Notes to the basic financial statements, which provide additional information essential to a full understanding of the data provided in the financial statements; and
- Additional supplementary information

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements, which are comprised of the following: 1) *Statement of Net Position*, 2) *Statement of Revenues, Expenses and Changes in Net Position*, and the 3) *Statement of Cash Flows*. This report also contains supplementary information in addition to the basic financial statements themselves.

The *Statement of Net Position* presents information on all of the Authority's assets, deferred outflows of resources, liabilities, deferred inflows of resources with the residual reported as net position. Over time, changes in net position may provide a useful indicator of whether the financial position of the Authority as a whole is improving or deteriorating.

Accounting standards establish three components of net position. The net investment in capital assets component represents the Authority's investments in capital assets, less any outstanding debt or other borrowings used to acquire those assets. Resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The restricted component of net position consists of financial resources that are restricted for a specific purpose by enabling legislation or external parties. The unrestricted component of net position represents resources not included in the other components.

The *Statement of Revenues, Expenses and Changes in Net Position* presents information showing how the Authority's net position has changed during the fiscal year. All revenues and expenses are included on this statement, regardless of whether cash has been received or paid.

The *Statement of Cash Flows* presents information on the Authority's cash inflows and outflows during the fiscal year. Cash flows are categorized as operating activities; capital and related financing activities and investing activities. This statement includes a reconciliation of cash provided by the Authority's operating activities to operating income as reported on the *Statement of Revenues, Expenses and Changes in Net Position*.

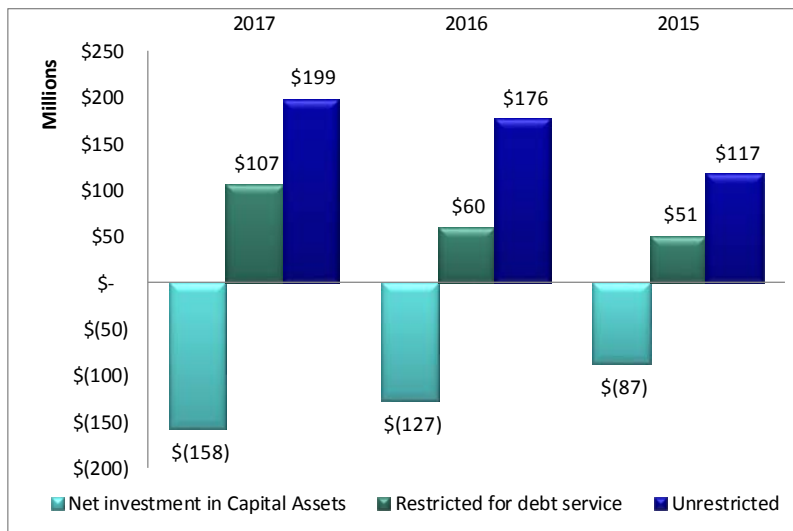
**North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017**

Financial Analysis of the Authority

The Authority's net position at December 31, 2017 and 2016, was \$147,336,243 and \$108,649,525 respectively. The Authority's overall financial position at December 31, 2017 as compared to the two prior years is summarized as follows:

	2017	2016	2015
Current and other assets	\$ 976,755,370	\$ 582,052,626	\$ 318,245,532
Capital assets	392,014,006	376,475,197	360,615,424
Total assets	<u>1,368,769,376</u>	<u>958,527,823</u>	<u>678,860,956</u>
Deferred difference on refunding	<u>23,756,317</u>	<u>24,926,994</u>	<u>1,861,054</u>
Current liabilities	27,673,899	20,450,537	17,812,528
Long term liabilities	<u>1,217,515,551</u>	<u>854,354,755</u>	<u>582,194,446</u>
Total liabilities	<u>1,245,189,450</u>	<u>874,805,292</u>	<u>600,006,974</u>
Net Position			
Net investment in capital assets	(157,857,999)	(127,235,277)	(87,345,670)
Restricted for debt service	106,597,702	59,773,844	50,574,270
Unrestricted	<u>198,596,540</u>	<u>176,110,958</u>	<u>117,486,436</u>
Total net position	<u><u>\$ 147,336,243</u></u>	<u><u>\$ 108,649,525</u></u>	<u><u>\$ 80,715,036</u></u>

The chart below illustrates the composition of the Authority's net position for the past three years:



**North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017**

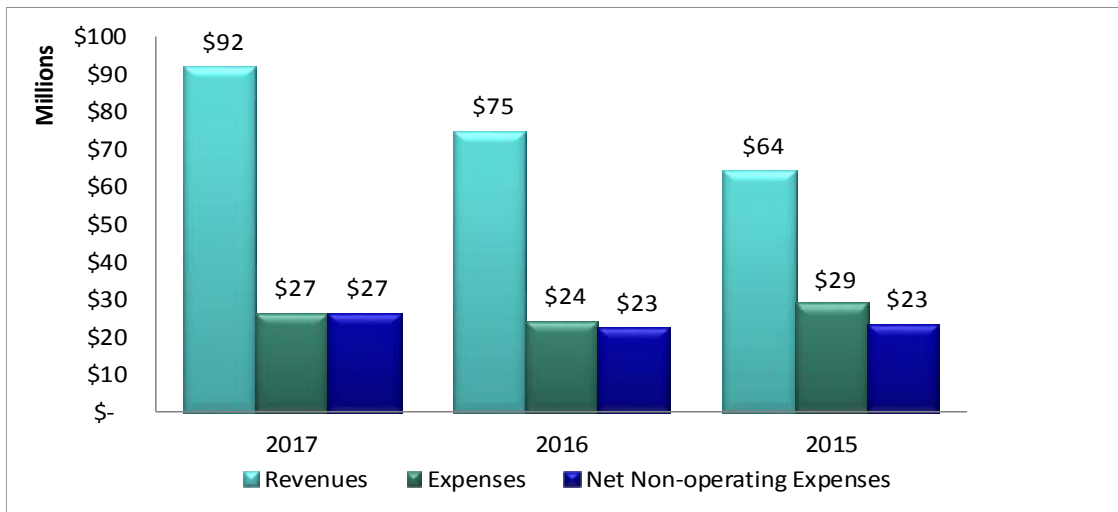
The total net position of the Authority increased during the current fiscal year by \$38,686,718. A comparative summary of the Authority's *Statement of Activities* for the past two years is as follows:

	2017	2016	2015
Operating revenues	\$ 91,869,846	\$ 74,823,583	\$ 64,140,149
Operating expenses	(26,581,233)	(24,322,240)	(28,707,523)
Net operating income	65,288,613	50,501,343	35,432,626
Net non-operating revenue (expense)	(26,601,895)	(22,566,854)	(23,473,728)
Change in net position	38,686,718	27,934,489	11,958,898
Net position, beginning of year	108,649,525	80,715,036	68,756,138
Net position, end of year	\$ 147,336,243	\$ 108,649,525	\$ 80,715,036

Non-operating revenues and non-operating expenses consist of interest income from the Authority's investments, interest expense from the Authority's debt and issuance costs for the Series 2017 Bonds.

The increase in net position for each year was the result of revenues exceeding normal expenses, which is consistent with the Authority's financial planning and budgeting and is used to satisfy bond covenants and debt service requirements.

The chart below illustrates the Authority's operating revenues, operating expenses and net non-operating expenses for the past three years:



***North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017***

Capital Assets

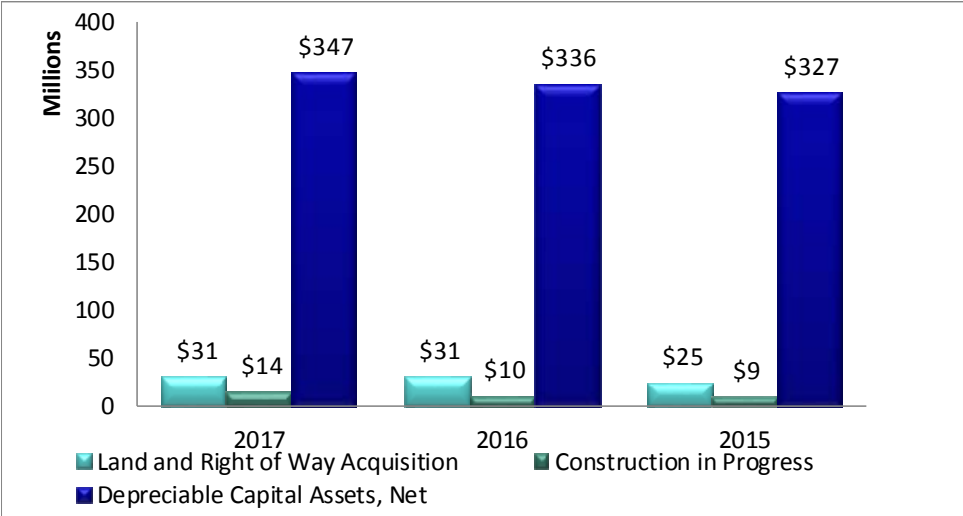
The Authority's capital assets primarily consist of land, construction in progress, infrastructure and the Authority's interest in treated water facilities and water transmission facilities. Capital assets at December 31, 2017, as compared to the two previous years are summarized as follows:

	2017	2016	2015
Capital assets not being depreciated			
Land and ROW acquisition	\$ 30,693,436	\$ 30,652,431	\$ 24,705,461
Construction in progress	14,447,317	10,262,968	9,307,447
Non-depreciable capital assets	<u>45,140,753</u>	<u>40,915,399</u>	<u>34,012,908</u>
Capital assets being depreciated or amortized			
Interest in treated water facilities	93,738,495	82,444,616	82,967,242
Interest in transmission facilities	48,787,920	40,362,827	29,902,714
Infrastructure	284,005,903	284,005,903	277,006,347
Furniture, computers & equipment	221,526	221,526	221,526
	<u>426,753,844</u>	<u>407,034,872</u>	<u>390,097,829</u>
Less accumulated depreciation and amortization			
Interest in treated water facilities	(22,127,497)	(20,949,464)	(20,044,938)
Interest in transmission facilities	(6,833,393)	(5,917,151)	(5,134,641)
Infrastructure	(50,698,172)	(44,386,930)	(38,094,205)
Furniture, computers & equipment	(221,529)	(221,529)	(221,529)
Total accumulated depreciation and amortization	<u>(79,880,591)</u>	<u>(71,475,074)</u>	<u>(63,495,313)</u>
Depreciable capital assets, net	<u>346,873,253</u>	<u>335,559,798</u>	<u>326,602,516</u>
Total capital assets, net	<u>\$ 392,014,006</u>	<u>\$ 376,475,197</u>	<u>\$ 360,615,424</u>

During the current year, the Authority had capital additions in the amount of \$19,718,972, which primarily consists of amounts paid to the City of Houston for their portion of Northeast Water Purification Plant Expansion project and the Northeast Transmission Line project. Projects that are not complete as of fiscal year end, along with related engineering fees, are recorded as construction in progress in the *Statement of Net Position*. Construction in progress is primarily for construction of a 54-inch waterline that is being constructed by Harris County for the Authority and State Highway 249 Regional Pump Station, including engineering fees.

*North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017*

The chart below illustrates the composition of capital assets as of December 31 for the past three years:



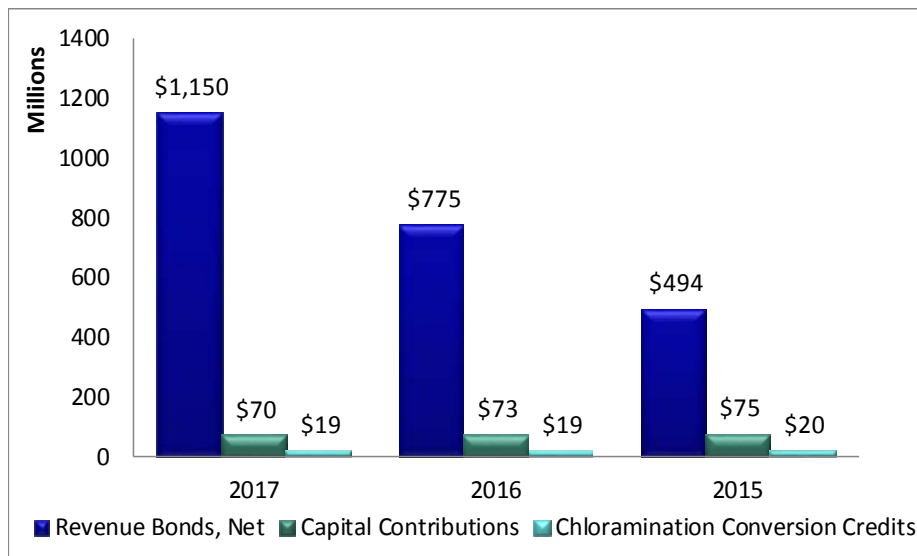
North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017

Long-Term Obligations

During the year, the Authority issued \$391,715,000 in senior lien revenue bonds. The Authority's total long-term obligations as of December 31, 2017, as compared to the previous two years are as follows:

	2017	2016	2015
Chloramination conversion credits payable	\$ 19,120,552	\$ 19,495,885	\$ 19,849,973
Capital contributions			
2003	25,622,055	26,648,135	27,624,852
2005	11,876,719	12,286,764	12,677,996
2008	32,802,111	33,637,587	34,430,443
	<u>70,300,885</u>	<u>72,572,486</u>	<u>74,733,291</u>
Revenue bonds			
Series 2008 Senior Lien	5,815,000	11,365,000	223,575,000
Series 2013 Senior Lien Refunding	91,420,000	95,380,000	99,155,000
Series 2014 Senior Lien Refunding	65,815,000	68,175,000	70,485,000
Series 2015 Senior Lien	78,405,000	80,435,000	80,435,000
Series 2016 Senior Lien and Refunding	258,125,000	258,125,000	
Series 2016A Senior Lien	195,050,000	195,050,000	
Series 2017 Senior Lien	391,715,000		
Unamortized bond premium	65,047,944	67,811,199	22,351,189
Unamortized bond discount	(1,641,023)	(1,704,923)	(1,902,406)
	<u>1,149,751,921</u>	<u>774,636,276</u>	<u>494,098,783</u>
Accrued compensated absences	154,952	144,423	123,423
	<u>\$ 1,239,328,310</u>	<u>\$ 866,849,070</u>	<u>\$ 588,805,470</u>

The chart below illustrates the composition of the Authority's long-term obligations as of December 31 for the last three years:



***North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017***

The Authority's bonds are secured by a pledge on the Authority's net revenues (total revenues less operating and maintenance costs). As further discussed in Note 6, the Authority's master resolution requires that the Authority maintain balances in the following funds: (1) interest and sinking fund, (2) reserve fund, (3) coverage fund, (4) operation and maintenance fund and (5) improvement fund. The Authority has continued to comply with all of its bonds covenants and has maintained these funds at required levels.

Economic Factors

The Harris-Galveston Subsidence District (H-GSD) groundwater regulatory plan (the Plan) requirements mandated the construction of infrastructure in order to meet the 2010 conversion target of a thirty percent reduction in groundwater use, along with additional requirements in order to meet higher conversion target thresholds (which will take effect through the year 2035). The Authority's Groundwater Reduction Plan (GRP) was approved in 2003 and it defines how it will comply with H-GSD's requirements. The H-GSD updated its regulatory plan, which includes the extension of the conversion deadlines, in January 2013. As a result of the Plan changes, existing GRP's must incorporate the changes required under the Plan. The Authority submitted the updated GRP to the H-GSD on June 26, 2014 for recertification. The 2018-2019 Capital Improvement Plan (CIP) defines several of the major components of the plan detailed in the Authority's updated GRP needed to facilitate continued compliance with the HGSD's conversion requirements.

Several disincentives were built into the H-GSD Regulatory Plan, including a \$7 per 1,000 gallons (groundwater pumped) "penalty" fee that would be triggered if: (1) the GRP was not submitted and certified according to the timeline; (2) construction had not begun on the surface water delivery infrastructure by 2005; and (3) the mandated groundwater pumpage reductions were not accomplished within the 2010, 2025 and 2035 timelines.

The Authority adopts a Capital Improvement Plan (CIP) each year to establish a guide to planning and defining the infrastructure needed to meet the H-GSD targets and determine how the infrastructure improvements will be financed.

The 2018-2019 CIP has been developed using the best, currently available information about the scope of each project along with cost information from a variety of sources, including cost experience from the Authority's projects completed to date. While the Authority's body of empirical cost data is expanding, especially in terms of water lines, the cost base is still evolving in several areas. Accordingly, the following points are offered to help keep the implementation of the 2018-2019 CIP in perspective:

- It is possible that conditions would evolve on a project that could materially impact the cost of the project
- Real estate and construction costs can be and are influenced by variables over which the Authority has no control
- It is common to experience unexpected costs in the implementation of a CIP. Provision of a contingency is the most practical way to attempt to address this issue

*North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017*

Significant activities addressed in the 2018-2019 CIP Plan are:

- Continue maintenance and enhancements of the Authority's existing Regional Pump Station and Water Plant
- Continue evaluation of the need for additional regional water wells and enhancements to the 2010 system to take necessary efforts to optimize use of the system
- Identify and purchase the sites for the third Regional Pump Station and second Regional Water Plant
- Initiate design of the initial phase of State Highway 249 Regional Pump Station
- Initiate design and construction of the 2025 transmission line
- Provide funding for the Authority's share of the cost of major expansion of the Northeast Water Purification Plant (the "NEWPP")
- Provide funding for the Authority's share of the cost of major rehabilitation, reconstruction and upgrading of the existing NEWPP
- Provide funding for the Authority's share of the cost for acquisition of real estate and the design of the proposed joint transmission line from the NEWPP site to the Authority's proposed 2025 transmission line
- Pay the Authority's portion of the initial loan costs for the Luce Bayou Interbasin Diversion Project
- Continue the planning and design and construction of the 2025 distribution system
- Provide funding for the Chloramination Credit
- Provide funding to help encourage and facilitate implementation of reuse systems
- Provide professional services to perform the wide variety of activities required to implement the 2018-2019 CIP

The proceeds from the Authority's Series 2003, 2005, 2008 and 2016 Senior Lien Revenue Bonds, capital contributions and interest earned (collectively called "Revenue Bonds") total approximately \$491 million.

North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017

As illustrated by the table that follows, approximately \$82 million of those Revenue Bonds will be used to implement the 2018-2019 CIP. Additionally, approximately \$727 million of Texas Water Development Board State Water Infrastructure Fund for Texas ("SWIFT") funds are committed to implement the 2018-2019 CIP.

Category	Authorizations ¹ (Thousands)		Fiscal Year Planned		Project Total
	1/1/03-9/30/17	10/1/17-12/31/17	Authorizations (Thousands)		
			2018	2019	
Acquisition	\$ 35,559	\$ -	\$ 8,405	\$ 7,552	\$ 51,516
Design	67,056		19,885	5,050	91,991
Construction	243,241		60,590	205,838	509,669
Equipment					
Other	145,270	386	376,570	135,871	658,097
Total Authorizations	\$ 491,126	\$ 386	\$ 465,450	\$ 354,311	\$ 1,311,273
Source of Funds					
Revenue Bonds	\$ 408,612	\$ 386	\$ 50,124	\$ 31,898	\$ 491,020
SWIFT Funds	82,964		415,326	311,308	809,598
To be determined				11,105	11,105
Total Funds	\$ 491,576	\$ 386	\$ 465,450	\$ 354,311	\$ 1,311,723

¹ Authorizations do not typically represent actual expenditures

Next Year's Budget

The Authority's 2018 budget as compared to actual results for 2017 is as follows:

	2017 Actual	2018 Budget
Operating revenues	\$ 91,869,846	\$ 83,855,465
Operating expenses	(26,581,233)	(26,757,647)
Net operating income	65,288,613	57,097,818
Non operating revenues (expenses)		
Interest expense	(30,790,594)	(29,682,333)
Interest and fees	4,974,049	500,000
Bond issuance costs	(785,350)	
Net non-operating expense	(26,601,895)	(29,182,333)
Change in net position	38,686,718	27,915,485
Beginning net position	108,649,525	147,336,243
Ending net position	\$ 147,336,243	\$ 175,251,728

Actual revenues for 2017 are higher than budgeted revenues for 2018 because the Authority takes a conservative approach to budgeting. The budget for 2018 assumes normal rainfall amounts. Expenses fluctuate proportionate with revenues.

*North Harris County Regional Water Authority
Management's Discussion and Analysis
December 31, 2017*

Request for Information

This financial report is designed to provide a general overview of the Authority's finances. Questions concerning any information provided in this report or requests for additional information should be addressed to the Financial Assistant, North Harris County Regional Water Authority, 3648 Cypress Creek Parkway, Suite 110, Houston, Texas 77068.

Basic Financial Statements

North Harris County Regional Water Authority
Statements of Net Position
December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Assets		
Current assets		
Cash and cash equivalents	\$ 96,910,952	\$ 77,106,673
Investments	83,102,477	82,589,991
Accounts receivable	7,936,551	6,673,815
Accrued interest receivable	325,363	255,285
Other receivables	10,049	10,049
Due from other governments	7,684,930	5,885,525
Total current assets	<u>195,970,322</u>	<u>172,521,338</u>
Noncurrent assets		
Restricted cash and cash equivalents	166,549,792	127,039,937
Restricted investments	64,825,159	74,970,293
Cash with escrow agent	548,684,224	206,795,185
Water conservation credits	725,873	725,873
Capital assets not being depreciated	45,140,753	40,915,399
Capital assets, net	346,873,253	335,559,798
Total noncurrent assets	<u>1,172,799,054</u>	<u>786,006,485</u>
Total assets	<u>1,368,769,376</u>	<u>958,527,823</u>
Deferred Outflows of Resources		
Deferred difference on refunding	<u>23,756,317</u>	<u>24,926,994</u>
Liabilities		
Current liabilities		
Accounts payable	2,579,073	2,410,201
Other payables	1,395	12,738
Interest payable on bonds	2,587,420	1,480,631
Current portion of long term liabilities		
Chloramine conversion credits payable	397,853	375,333
Capital contributions	2,388,158	2,271,634
Bonds payable	19,720,000	13,900,000
Total current liabilities	<u>27,673,899</u>	<u>20,450,537</u>
Noncurrent liabilities		
Accounts payable from restricted assets	693,252	4,052,635
Accrued compensated absences	154,952	144,423
Long term liabilities due in more than one year		
Chloramine conversion credits payable	18,722,699	19,120,552
Capital contributions	67,912,727	70,300,869
Bonds payable (net of unamortized bond premium and discount)	1,130,031,921	760,736,276
Total noncurrent liabilities	<u>1,217,515,551</u>	<u>854,354,755</u>
Total liabilities	<u>1,245,189,450</u>	<u>874,805,292</u>
Net Position		
Net investment in capital assets	(157,857,999)	(127,235,277)
Restricted for debt service	106,597,702	59,773,844
Unrestricted	198,596,540	176,110,958
Total net position	<u>\$ 147,336,243</u>	<u>\$ 108,649,525</u>

See Notes to Financial Statements.

North Harris County Regional Water Authority
Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended December 31, 2017 and 2016

	2017	2016
Operating revenues		
Charges for services		
Water fees	\$ 91,869,846	\$ 74,823,583
Total operating revenues	<u>91,869,846</u>	<u>74,823,583</u>
Operating expenses		
Personnel	1,701,960	1,436,653
Professional fees	618,799	1,095,068
Purchased water	11,313,413	9,519,465
Contracted services	2,405,270	2,184,816
Occupancy and office	1,029,274	1,147,716
Other	1,107,000	958,761
Depreciation and amortization	8,405,517	7,979,761
Total operating expenses	<u>26,581,233</u>	<u>24,322,240</u>
Net operating income	65,288,613	50,501,343
Non-operating revenues (expenses)		
Interest and fees	(30,790,594)	(23,424,409)
Investment income	4,974,049	2,310,900
Bond issuance costs	(785,350)	(1,453,345)
Net non-operating revenues (expenses)	<u>(26,601,895)</u>	<u>(22,566,854)</u>
Change in net position	38,686,718	27,934,489
Total net position - beginning	108,649,525	80,715,036
Total net position - ending	<u>\$ 147,336,243</u>	<u>\$ 108,649,525</u>

See Notes to Financial Statements.

*North Harris County Regional Water Authority
Statements of Cash Flows
For the Years Ended December 31, 2017 and 2016*

	2017	2016
Cash flows from operating activities		
Receipts from customers	\$ 83,043,663	\$ 66,346,570
Payments for personnel costs	(1,691,431)	(1,415,653)
Payments to contractors and vendors	(18,115,632)	(21,042,799)
Net cash provided by operating activities	<u>63,236,600</u>	<u>43,888,118</u>
Cash flows from capital and related financing activities		
Interest paid	(26,150,466)	(19,014,217)
Acquisition and construction of capital assets	(27,449,230)	(27,447,857)
Payment to escrow agent for refunded bonds		(229,629,813)
Proceeds from sale of bonds, net	391,715,000	500,015,044
Principal payments	(13,900,000)	(11,385,000)
Bond issuance costs	(785,350)	(1,453,345)
Net cash provided by capital and related financing activities	<u>323,429,954</u>	<u>211,084,812</u>
Cash flows from investing activities		
Interest received	4,903,971	2,303,256
Payments for investments	(121,626,031)	(94,185,986)
Receipts from investment sales and maturities	131,258,679	90,075,513
Net cash used by investing activities	<u>14,536,619</u>	<u>(1,807,217)</u>
Net increase in cash and cash equivalents	401,203,173	253,165,713
Balances - beginning of the year	<u>410,941,795</u>	<u>157,776,082</u>
Balances - end of the year	<u>\$ 812,144,968</u>	<u>\$ 410,941,795</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 65,288,613	\$ 50,051,343
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization expense	8,405,517	7,979,761
Non-cash revenue from capital contribution credit	(6,018,365)	(6,018,365)
Non-cash revenue from chloramine conversion credit	(1,545,082)	(1,545,083)
Change in assets and liabilities:		
(Increase) decrease in accounts receivable	(1,262,736)	(913,565)
(Increase) decrease in prepaid expenses		34,627
(Increase) decrease in due from other governments	(1,799,405)	(5,644,326)
Increase (decrease) in accounts payable	168,872	(527,445)
Increase (decrease) in other payable	(11,343)	171
Increase (decrease) in compensated absences	10,529	21,000
Total adjustments	<u>(2,052,013)</u>	<u>(6,613,225)</u>
Net cash provided by operating activities	<u>\$ 63,236,600</u>	<u>\$ 43,438,118</u>
Cash and cash equivalents per balance sheet:		
Cash and cash equivalents	\$ 96,910,952	\$ 77,106,673
Restricted cash and cash equivalents	166,549,792	127,039,937
Cash with escrow agent	548,684,224	206,795,185
	<u>\$ 812,144,968</u>	<u>\$ 410,941,795</u>

See Notes to Financial Statements.

*North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017*

Note 1 – Summary of Significant Accounting Policies

The North Harris County Regional Water Authority (the “Authority”) was created in 1999 under Article 16, Section 59 of the Texas Constitution by House Bill 2965, as passed by the 75th Texas Legislature and as amended (the “Act”). The Authority began operations in October 1999. The Act empowers the Authority to provide for the conservation, preservation, protection, recharge and prevention of waste of groundwater and for the reduction of groundwater withdrawals.

The Authority charges a fee, based on the amount of water pumped from the well, and/or the alternative water provided, to the owner of wells located in the Authority’s boundaries, unless exempted. The fees established by the Board of Directors must be sufficient to: (1) achieve water conservation, prevent waste of water, serve as a disincentive to pumping groundwater and make available alternative water supplies; and (2) enable the Authority to meet operation and maintenance expenses and pay the principal and interest on any debt issued by the Authority.

The accompanying financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America as promulgated by the Governmental Accounting Standards Board (GASB). The following is a summary of the most significant policies:

Reporting Entity

The Authority is a political subdivision of the State of Texas governed by an elected five member board. As required by generally accepted accounting principles, these financial statements have been prepared based on considerations regarding the potential for inclusion of other entities, organizations or functions as part of the Authority’s financial reporting entity. No other entities, organizations or functions have been included in the Authority’s financial reporting entity. Additionally, as the Authority is considered a primary government for financial reporting purposes, its activities are not considered a part of any other governmental or other type of reporting entity.

Considerations regarding the potential for inclusion of other entities, organizations or functions in the Authority’s financial reporting entity are based on criteria prescribed by generally accepted accounting principles. These same criteria are evaluated in considering whether the Authority is a part of any other governmental or other type of reporting entity. The overriding elements associated with prescribed criteria considered in determining that the Authority’s financial reporting entity status is that of a primary government are: that it has a separate governing body; it is legally separate; and it is fiscally independent of other state and local governments. Additional prescribed criteria under generally accepted accounting principles include; considerations pertaining to organizations for which the primary government is financially accountable; and considerations pertaining to other organizations 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.

Note 1 – Summary of Significant Accounting Policies (continued)

Basic Financial Statements

The basic financial statements include the *Statements of Net Position*, the *Statements of Revenues, Expenses and Changes in Net Position* and the *Statements of Cash Flows*. These statements focus on the sustainability of the Authority as an entity and the change in aggregate financial position resulting from these activities for the fiscal year.

Measurement Focus and Basis of Accounting

The Authority follows proprietary fund accounting and reporting requirements, which utilize the economic resources measurement focus and the accrual basis of accounting. Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges to customers for water fees. Operating expenses include the cost of services, administrative expenses and depreciation and amortization on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Net position is classified into the following three components:

- Net investment in capital assets – represents the Authority's investments in capital assets, less any outstanding debt or other borrowings used to acquire those assets. Resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.
- Restricted – financial resources are reported as restricted when constraints placed on the use of the financial resources are either externally imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or imposed through enabling legislation.
- Unrestricted – net resources not included in the determination of net investment in capital assets or restricted net position.

Cash and Cash Equivalents

For the purpose of the *Statement of Cash Flows*, the Authority defines cash and cash equivalents as cash on hand, demand deposits, certificates of deposit and investments in local government investment pools (i.e., TexPool, TexPool Prime and TexSTAR).

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by an allowance for amounts considered uncollectible. At December 31, 2017 an allowance for uncollectible accounts was not considered necessary.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 1 – Summary of Significant Accounting Policies (continued)

Restricted Assets

Proceeds of bonds or other resources set aside for specific purposes are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants or contractual agreements.

Capital Assets

The Authority defines capital assets as assets with an individual cost of \$5,000 or more and an estimated useful life in excess of one year. Capital assets, which include land, right of way acquisition costs, infrastructure and interest in infrastructure assets constructed by the City of Houston, are reported at historical cost. Donated assets are recorded at their estimated fair value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are not capitalized.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Computer and software	3
Furniture and equipment	5-7
Infrastructure	20-45

Interest costs on assets acquired with tax-exempt borrowings are capitalized, net of interest earned on related interest-bearing investments acquired with proceeds of the related borrowings, from the date of borrowing until the assets are ready for their intended use. During the current fiscal year, the Authority incurred interest costs of \$26,019,618 on construction related tax exempt borrowings and capitalized \$145,521 of net interest.

Long-term Obligations

Long-term debt and other long-term obligations are reported as liabilities on the Authority's *Statement of Net Position*. Bonds payable are reported net of any applicable discount or premium.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 1 – Summary of Significant Accounting Policies (continued)

Use of 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, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. These estimates include, among others, the collectability of receivables and the useful lives and impairment of capital assets. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the financial statements in the period they are determined to be necessary. Actual results could differ from the estimates.

Note 2 – Cash and Investments

Restricted Cash and Investments

Cash and investments were restricted for the following purposes at December 31, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Bond reserves	\$ 109,185,122	\$ 61,254,475
Capital improvements	122,189,829	140,755,755
Cash with escrow agent	548,684,224	206,795,185
	<u>\$ 780,059,175</u>	<u>\$ 408,805,415</u>

Deposit Custodial Credit Risk

Custodial credit risk as it applies to deposits (i.e. cash) is the risk that, in the event of the failure of the depository institution, a government will not be able to recover its deposits or will not be able to recover collateral securities. The *Public Funds Collateral Act* (Chapter 2257, Texas Government Code) requires that all of the Authority’s deposits with financial institutions be covered by federal depository insurance and, if necessary, pledged collateral held by a third party custodian. The act further specifies the types of securities that can be used as collateral. The Authority’s written investment policy establishes additional requirements for collateralization of deposits. As of December 31, 2017, and December 31, 2016, all of the Authority’s deposits are insured or fully collateralized.

Investment Risks

Investment credit risk is the risk that the investor may not recover the value of an investment from the issuer, while interest rate risk is the risk that the value of an investment will be adversely affected by changes in interest rates. Custodial credit risk is the risk that the investor will not be able to recover the value of its investments that are in the possession of an outside party if the counterparty fails. The Authority’s investment policies do not address these risks beyond the rating and maturity restrictions established by state statutes.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 2 - Cash and Investments (continued)

Investments

The Authority's is authorized by the *Public Funds Investment Act* (Chapter 2256, Texas Government Code) to invest in the following: (1) obligations, including letters of credit, of the United States or its agencies and instrumentalities, including Federal Home Loan Banks, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) certain collateralized mortgage obligations, (4) other obligations, which are unconditionally guaranteed or insured by the State of Texas or the United States or its agencies or instrumentalities, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States, (5) certain A rated or higher obligations of states and political subdivisions of any state, (6) bonds issued, assumed or guaranteed by the State of Israel, (7) certain insured or collateralized certificates of deposit and share certificates, (8) certain fully collateralized repurchase agreements, (9) bankers' acceptances with limitations, (10) commercial paper rated A-1 or P-1 or higher and a maturity of 270 days or less, (11) no-load money market mutual funds and no-load mutual funds, with limitations, (12) certain guaranteed investment contracts, (13) certain qualified governmental investment pools and (14) a qualified securities lending program.

The Authority has adopted a written investment policy to establish the principles by which the Authority's investment program should be managed. This policy further restricts the types of investments in which the Authority may invest.

As of December 31, 2017, the Authority's investments and maturities are as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Percentage of Total</u>	<u>Maturities in Years</u>	
			<u>Less Than 1</u>	<u>1-5</u>
Federal National Mortgage Association	\$ 9,321,688	2.3%	\$ 7,142,178	\$ 2,179,510
Federal Home Loan Mortgage Corporation	15,173,934	3.8%	12,083,139	3,090,795
Federal Home Loan Bank	15,821,833	3.9%	9,913,563	5,908,270
Federal Farm Credit Bank	4,517,752	1.1%	994,980	3,522,772
U.S. Treasury Notes/Bonds	95,590,326	23.8%	51,501,269	44,089,057
TexPool	53,859,128	13.4%	53,859,128	
TexPool Prime	134,673,010	33.6%	134,673,010	
TexSTAR	72,461,806	18.1%	72,461,806	
	<u>\$ 401,419,477</u>	<u>100.0%</u>	<u>\$ 342,629,073</u>	<u>\$ 58,790,404</u>

The Authority considers the investments in TexPool, TexPool Prime and TexSTAR to have a maturity of less than one year because the weighted average maturities of these pools are 33 days, 38 days and 36 days, respectively. The Authority's investments are rated Aaa by Moody's and AAA by Standard & Poor's. As previously noted, the investment pools are reported as cash equivalents on the *Statement of Net Position*.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 2 - Cash and Investments (continued)

Investments (continued)

As of December 31, 2016, the Authority's investments were as follows:

Investment Type	Fair Value	Percentage of Total	Maturities in Years	
			Less Than 1	1-5
Federal National Mortgage Association	\$ 51,903,365	14.5%	\$ 35,312,450	\$ 16,590,915
Federal Home Loan Mortgage Corporation	13,899,241	3.9%	7,072,916	6,826,325
Federal Home Loan Bank	11,805,481	3.3%	498,046	11,307,435
Federal Farm Credit Bank	13,764,019	3.8%	13,764,019	
U.S. Treasury Notes/Bonds	64,788,563	18.1%	47,153,245	17,635,318
TexPool	30,861,025	8.6%	30,861,025	
TexPool Prime	123,498,013	34.5%	123,498,013	
TexSTAR	47,927,700	13.4%	47,927,700	
	<u>\$ 358,447,407</u>	<u>100.0%</u>	<u>\$ 306,087,414</u>	<u>\$ 52,359,993</u>

The Authority considers the investments in TexPool, TexPool Prime and TexSTAR to have a maturity of less than one year because the weighted average maturities of these pools at December 31, 2016 was 43 days, 47 days and 42 days, respectively. The Authority's investment securities are rated Aaa by Moody's and AA+ by Standard & Poor's.

Investment Valuation

The Authority's investments in U.S. treasuries, U.S. agencies and instrumentality securities and TexSTAR are reported at fair value in the *Statement of Net Position*. Governmental accounting standards establish the following hierarchy of inputs used to measure fair value: Level 1 inputs are based on quoted prices in active markets, Level 2 inputs are based on significant other observable inputs, and Level 3 inputs are based on significant unobservable inputs.

Fair value measurements of the Authority's investments as of December 31, 2017 are as follows:

- U.S. Treasury Notes and Bonds: valued at \$95,590,326 based on quoted market prices (level 1 inputs).
- U.S. Government Agency and Instrumentality Securities: valued at \$44,835,207 based on matrix pricing for similar securities (level 2 inputs).
- TexSTAR: valued at \$72,461,806 based on published fair value per share (level 1 inputs).

*North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017*

Note 2 - Cash and Investments (continued)

Investments (continued)

Fair value measurements of the Authority's investments as of December 31, 2016 are as follows:

- U.S. Treasury Notes and Bonds: valued at \$64,788,563 based on quoted market prices (level 1 inputs).
- U.S. Government Agency and Instrumentality Securities: valued at \$91,372,106 based on matrix pricing for similar securities (level 2 inputs).
- TexSTAR: valued at \$47,927,700 based on published fair value per share (level 1 inputs).

TexPool and TexPool Prime

The Authority participates in two investment pools offered by the Texas Local Government Investment Pool, TexPool and TexPool Prime. The State Comptroller of Public Accounts exercises oversight responsibility of the Texas Local Government Investment Pool which includes (1) the ability to significantly influence operations, (2) designation of management and (3) accountability for fiscal matters. Additionally, the State Comptroller has established an advisory board composed of participants in TexPool/Texpool Prime and other persons who do not have a business relationship with Texas Local Government Investment Pool. The Advisory Board members review the investment policy and management fee structure.

As permitted by GAAP, TexPool and TexPool Prime use amortized cost (which excludes unrealized gains and losses) rather than market value to compute share price and seek to maintain a constant dollar value per share. Accordingly, the fair value of the Authority's position in each pool is the same as the value of TexPool/TexPool Prime shares.

Investments in TexPool may be withdrawn on a same day basis, as long as the transaction is initiated by 3:30 p.m. Investments in TexPool Prime may be withdrawn via wire transfer on a same day basis, as long as the transaction is initiated by 2 p.m. ACH withdrawals made by 2 p.m. will settle on the business day following the date the transaction was initiated.

TexSTAR

The Authority participates in Texas Short Term Asset Reserve fund (TexSTAR) which is managed by Hilltop Securities, Inc., and J.P. Morgan Investment Management, Inc. Hilltop Securities provides participant and marketing services while J.P. Morgan provides investment management services. Custodial and depository services are provided by J.P. Morgan Chase Bank N.A. or its subsidiary.

Investments in TexSTAR may be withdrawn via wire transfer on a same day basis, as long as the transaction is executed by 4 p.m. ACH withdrawals made by 4 p.m. will settle on the next business day.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 3 – Capital Assets

A summary of changes in capital assets during the year ended December 31, 2017, follows:

	Beginning Balance	Additions	Ending Balance
Capital assets not being depreciated			
Land and ROW acquisition	\$ 30,652,431	\$ 41,005	\$ 30,693,436
Construction in progress	10,262,968	4,184,349	14,447,317
Non-depreciable capital assets	<u>40,915,399</u>	<u>4,225,354</u>	<u>45,140,753</u>
Capital assets being depreciated/amortized			
Interest in water facilities	82,444,616	11,293,879	93,738,495
Interest in transmission facilities	40,362,827	8,425,093	48,787,920
Infrastructure	284,005,903		284,005,903
Furniture, computers & equipment	221,526		221,526
Subtotal	<u>407,034,872</u>	<u>19,718,972</u>	<u>426,753,844</u>
Less accumulated depreciation/amortization			
Interest in water facilities	(20,949,464)	(1,178,033)	(22,127,497)
Interest in transmission facilities	(5,917,151)	(916,242)	(6,833,393)
Infrastructure	(44,386,930)	(6,311,242)	(50,698,172)
Furniture, computers & equipment	(221,529)		(221,529)
Subtotal	<u>(71,475,074)</u>	<u>(8,405,517)</u>	<u>(79,880,591)</u>
Depreciable capital assets, net	<u>335,559,798</u>	<u>11,313,455</u>	<u>346,873,253</u>
Total capital assets, net	<u>\$ 376,475,197</u>	<u>\$ 15,538,809</u>	<u>\$ 392,014,006</u>

Depreciation and amortization expense for the current year was \$8,405,517.

Note 4 – Leases

In 2000, the Authority entered into a lease agreement for office space. The lease was amended November 1, 2005, February 14, 2011 and July 17, 2014. The fourth amendment of the lease was executed in October 2016, and will terminate March 31, 2022. The Authority may terminate the lease any time after thirty-six months, by giving six months written notice and by paying a lease termination penalty of \$15,000 if the lease is terminated during the lease term months of 41-52 or a penalty of \$10,000 if the lease is terminated during the lease term months of 53-65. The Authority has also entered into various leases for office equipment.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 4 – Leases (continued)

The Authority paid \$139,101 under these leases during the current period. Future annual commitments for leases are as follows:

<u>Year Ending</u>	<u>Amount</u>
2018	\$ 117,890
2019	117,308
2020	121,187
2021	131,658
2022	32,915
	<u>\$ 520,958</u>

Note 5 – Compensated Absences

The change in the Authority’s liability for compensated absences for years ending 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Balance at beginning of year	\$ 144,423	\$ 123,423
Increase in liability	10,529	21,000
Balance at end of year	<u>\$ 154,952</u>	<u>\$ 144,423</u>

Note 6 – Senior Lien Revenue Bonds

The Authority issues Senior Lien Revenue Bonds (Senior Bonds) primarily to finance the design, acquisition and construction of regional water production, transmission, pumping, storage and distribution systems. The principal and interest on the Authority’s bonds will be repaid from net revenues.

Bonds payable, as reported on the financial statements for years ending 2017 and 2016 consists of the following:

	<u>2017</u>	<u>2016</u>
Bonds payable	\$ 1,086,345,000	\$ 708,530,000
Unamortized premiums	65,047,944	67,811,199
Unamortized discounts	(1,641,023)	(1,704,923)
Total	<u>\$ 1,149,751,921</u>	<u>\$ 774,636,276</u>
Due within one year	<u>\$ 19,720,000</u>	<u>\$ 13,900,000</u>

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 6 – Senior Lien Revenue Bonds (continued)

The Authority’s outstanding bonds payable at December 31, 2017 are comprised of the following individual issues:

Series	Amounts Outstanding	Original Issue Amount	Interest Rates	Maturity Date, Serially, Beginning /Ending	Interest Payment Dates	Callable Date
2008	\$ 5,815,000	\$ 238,115,000	4.00% - 5.50%	December 15, 2013/2038	June 15 / December 15	December 15, 2018
2013 Refunding	91,420,000	106,320,000	2.00% - 5.00%	December 15, 2014/2033	June 15 / December 15	December 15, 2022
2014 Refunding	65,815,000	72,510,000	2.00% - 5.00%	December 15, 2015/2035	June 15 / December 15	December 15, 2024
2015	78,405,000	80,435,000	0.45% - 3.21%	December 15, 2017/2045	June 15 / December 15	December 15, 2025
2016 and Refunding	258,125,000	258,125,000	5.00%	December 15, 2019/2046	June 15 / December 15	December 15, 2026
2016A	195,050,000	195,050,000	0.65% - 3.07%	December 15, 2018/2046	June 15 / December 15	December 15, 2026
2017	391,715,000	391,715,000	0.76% - 3.02%	December 15, 2019/2047	June 15 / December 15	December 15, 2027
	<u>\$ 1,086,345,000</u>	<u>\$ 1,342,270,000</u>				

The 2016 Senior Lien Revenue and Refunding Bonds were issued to advance refund portions of the Authority’s Series 2008 Senior Lien Revenue Bonds. Since the Series 2008 bonds were not yet subject to redemption, the Authority defeased them by placing proceeds of the bonds in an escrow account with an escrow agent and irrevocably pledging the escrow account to the payment of future debt service payments. Accordingly, the defeased bonds are not included in the Authority’s financial statements. As of December 31, 2017, the outstanding principal of defeased bonds was \$206,910,000.

As of December 31, 2017, the Texas Water Development Board has approved a total of \$1,179,080,000 in multi-year commitments in SWIRFT bonds to the Authority. The Authority intends to issue SWIRFT bonds for each fiscal year from 2015 through 2021 to fund the Authority’s costs for the Northeast Water Purification Plant Expansion, the Northeast Transmission Line Phase I and II and the 2025 Distribution System. On November 15, 2017 the Authority issued its third series of SWIRFT bonds, the \$391,715,000 Series 2017 Senior Lien Revenue Bonds. As of December 31, 2017, the Authority has issued \$667,200,000 in SWIRFT bonds.

***North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017***

Note 6 – Senior Lien Revenue Bonds (continued)

The change in the Authority’s long-term debt for the last two years is as follows:

	<u>2017</u>	<u>2016</u>
Bonds payable, beginning of year	\$ 708,530,000	\$ 473,650,000
Bonds issued	391,715,000	453,175,000
Bonds refunded		(206,910,000)
Bonds retired	(13,900,000)	(11,385,000)
Payable, end of year	<u>\$ 1,086,345,000</u>	<u>\$ 708,530,000</u>

The Senior Bonds are secured by a lien on and pledge out the net revenues of the Authority. As additional security, the bond resolutions required the establishment of an Interest and Sinking Fund, a Reserve Fund and a Coverage Fund. A description of each fund follows:

- Interest and Sinking Fund – Used to accumulate the funds required to make the scheduled payments of debt service on the Senior Bonds. Money in the Interest and Sinking Fund shall be used solely for the purpose of paying principal, interest and any bank charges and other costs associated with payments of debt service on the Senior Bonds. As of December 31, 2017, the Interest and Sinking Fund requirements were \$22,503,928. Investments restricted for this fund were \$33,403,935, of which \$10,900,007 has been classified as unrestricted for reporting purposes.
- The Reserve Fund – Used (to the extent that amounts on deposit in the Interest and Sinking Fund and the Coverage Fund are insufficient) to secure and provide for the payment of principal and interest on the Senior Bonds as they become payable. As of December 31, 2017, the Reserve Fund requirements were \$66,329,846. The Authority has investments and cash equivalents restricted for this fund in the amount of \$67,489,114, of which \$1,159,268 has been classified as unrestricted for reporting purposes.
- The Coverage Fund – Used to accumulate funds equal to 25% of the maximum annual debt service requirements for outstanding debt in any fiscal year. The Coverage Fund requirement as of December 31, 2017, was \$16,582,462. The Authority has investments and cash equivalents restricted for this fund of \$28,854,613, of which \$12,272,151 has been classified as unrestricted for reporting purposes.
- Operation and Maintenance Reserve Fund – Funds from gross revenues of the Authority will be deposited on or before the last business day of the month into this account. The Operation and Maintenance requirement, as of December 31, 2017 was \$3,754,150. The Authority has investments and cash equivalents restricted for this fund of \$3,846,000 of which \$91,850 has been classified as unrestricted for reporting purposes.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 6 – Senior Lien Revenue Bonds (continued)

Historical Debt Service Coverage

The Authority maintains certain financial ratios as required by its bond resolutions. The following table summarizes the key ratios:

	2017	2016	2015
Net operating income per financial statements	\$ 65,288,613	\$ 50,501,343	\$ 35,432,626
Add back depreciation and amortization	8,405,517	7,979,761	7,637,169
Net revenues for debt service	73,694,130	58,481,104	43,069,795
Add:			
Coverage fund	28,854,613	8,777,688	8,701,137
Improvement fund	132,483,844	127,074,550	116,247,150
Adjusted net revenues	<u>\$ 235,032,587</u>	<u>\$ 194,333,342</u>	<u>\$ 168,018,082</u>
Debt Service Requirements	<u>\$ 55,451,921</u>	<u>\$ 40,341,506</u>	<u>\$ 32,873,812</u>
Debt service coverage	1.33	1.45	1.31
Adjusted debt service coverage	4.24	4.82	5.11

Reserve Fund

The purpose of the Reserve Fund is to provide for ready access to funds on short notice in the event that the Authority is ever unable to make debt service payments in a timely manner. Accordingly, the Reserve Fund must contain cash and investments in a required minimum amount (the “Reserve Fund Requirement”) which is equal to the maximum annual debt service payments on the related bonds. In the alternative, the Reserve Fund Requirement may be satisfied with either: (i) a surety bond or insurance policy, if the insurer strength rating of the issuer of the surety bond or insurance policy is rated “AAA” or the equivalent; or (ii) an unconditional irrevocable letter of credit issued by a bank rated “AA” or the equivalent.

The Master Resolution provides that, in the event the insurer strength rating of the provider of a surety bond satisfying the Reserve Fund Requirements falls below “AAA” (but not below “A”), the Authority must take one of the following steps:

- i. deposit into the Reserve Fund cash sufficient to cause money in the Reserve Fund to accumulate to the Reserve Fund Requirement, such amount to be paid over the ensuing five years in equal installments at least semi-annually, or
- ii. replace the surety bond with another surety bond, insurance policy or letter of credit issued by an adequately rated provider within six months of such downgrade.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 6 – Senior Lien Revenue Bonds (continued)

The Master Resolution further provides that in the event the insurer strength rating of the provider of a surety bond satisfying the Reserve Fund Requirement falls below “A”, the Authority must take one of the following steps:

- i. deposit into the Reserve Fund cash sufficient to cause the money in the Reserve Fund to accumulate to the Reserve Fund Requirement, such amount to be paid over the ensuing year in equal installments on at least a monthly basis, or
- ii. replace such instrument with a surety bond, insurance policy or letter of credit issued by an adequately rated provider within six months of such occurrence.

As of December 31, 2017, the Reserve Fund Requirement is \$66,329,846, which consists of \$6,090,056 for the Series 2008 Senior Bonds, \$8,051,006 for the 2013 Senior Lien Revenue Refunding Bonds, \$5,559,850 for the 2014 Senior Lien Revenue Refunding Bonds, \$4,180,005 for the 2015 Senior Lien Revenue Bonds, \$19,266,000 for the 2016 Senior Lien Revenue and Refunding, \$9,650,800 for the Series 2016A Senior Lien Revenue bonds, and \$20,444,320 for the Series 2017 Senior Lien Revenue Bonds. All of the Reserve Fund Requirements have been met. Additionally, there was a surplus of \$1,159,268 in the aggregate Reserve Fund Requirements.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 6 – Senior Lien Revenue Bonds (continued)

Debt Service Requirements

Principal and interest payments on the Senior Bonds will be provided through the payment of water fees by utility districts and non-exempt well owners. As of December 31, 2017, the debt service requirements on the Senior Bonds outstanding are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Totals</u>
2018	\$ 19,720,000	\$ 35,731,921	\$ 55,451,921
2019	29,955,000	34,366,187	64,321,187
2020	30,705,000	33,629,783	64,334,783
2021	31,455,000	32,903,541	64,358,541
2022	33,745,000	32,054,063	65,799,063
2023	34,715,000	31,107,939	65,822,939
2024	35,770,000	30,101,383	65,871,383
2025	36,805,000	29,120,585	65,925,585
2026	38,045,000	27,938,857	65,983,857
2027	39,325,000	26,685,625	66,010,625
2028	40,590,000	25,472,531	66,062,531
2029	41,955,000	24,172,560	66,127,560
2030	43,450,000	22,735,618	66,185,618
2031	45,115,000	21,122,623	66,237,623
2032	46,835,000	19,445,349	66,280,349
2033	48,660,000	17,669,846	66,329,846
2034	42,490,000	15,838,567	58,328,567
2035	44,130,000	14,250,129	58,380,129
2036	40,140,000	12,744,428	52,884,428
2037	41,345,000	11,606,900	52,951,900
2038	42,760,000	10,250,412	53,010,412
2039	29,280,000	8,838,938	38,118,938
2040	30,210,000	7,955,510	38,165,510
2041	31,185,000	7,042,130	38,227,130
2042	32,195,000	6,096,120	38,291,120
2043	33,285,000	5,056,270	38,341,270
2044	34,415,000	3,965,813	38,380,813
2045	35,590,000	2,837,197	38,427,197
2046	32,630,000	1,670,784	34,300,784
2047	19,845,000	599,320	20,444,320
	<u>\$ 1,086,345,000</u>	<u>\$ 553,010,929</u>	<u>\$ 1,639,355,929</u>

North Harris County Regional Water Authority
Notes to Basic Financial Statements
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Note 7 – Capital Contributions

In 2003, the Authority entered into contracts with twenty-four Municipal Utility Districts (MUDs) to provide funds to pay capital expenses of the Authority’s system. Each MUD has paid a Capital Contribution based on a percentage of its pro-rata share of the total groundwater production for all water utilities during the calendar year 2002. Capital contributions of \$32,573,177 were made to the Authority in the 2003 fiscal year. The participating MUDs began receiving contribution credits against their individual water fees distributed over the life of the Series 2003 Senior Bonds beginning with the 2003 third quarter pumpage fees. Any amounts remaining plus accrued interest at the end of the capital contribution expiration date will be credited against any amounts owed to the Authority by the MUDs or paid to the MUDs by the Authority.

Future contribution credits including interest, principal and remaining balance, at the effective interest rate of the Senior Bonds for the 2003 capital contributions as of December 31, 2017 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Remaining Balance</u>
2018	\$ 1,078,008	\$ 1,295,834	\$ 2,373,842	\$ 24,544,047
2019	1,132,527	1,241,315	2,373,842	23,411,520
2020	1,189,804	1,184,038	2,373,842	22,221,716
2021	1,249,979	1,123,863	2,373,842	20,971,737
2022	1,313,196	1,060,646	2,373,842	19,658,541
2023	1,379,611	994,231	2,373,842	18,278,930
2024	1,449,385	924,457	2,373,842	16,829,545
2025	1,522,688	851,154	2,373,842	15,306,857
2026	1,599,698	774,144	2,373,842	13,707,159
2027	1,680,602	693,240	2,373,842	12,026,557
2028	1,765,599	608,243	2,373,842	10,260,958
2029	1,854,894	518,948	2,373,842	8,406,064
2030	1,948,705	425,137	2,373,842	6,457,359
2031	2,047,261	326,581	2,373,842	4,410,098
2032	2,150,801	223,041	2,373,842	2,259,297
2033	2,259,297	114,264	2,373,561	
	<u>\$ 25,622,055</u>	<u>\$ 12,359,136</u>	<u>\$ 37,981,191</u>	

In 2005, the Authority entered into agreements with nineteen MUDs. Capital contributions of \$14,675,978 were made to the Authority in the 2005 fiscal year. The participating MUDs began receiving contribution credits against their individual water fees distributed over the life of the Series 2005 Senior Bonds beginning with the 2005 third quarter pumpage fees. As with the 2003 contribution credits, any amounts remaining plus accrued interest at the end of the capital contribution date will be credited against any amounts owed to the Authority by the MUDs or paid to the MUDs by the Authority.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 7 – Capital Contributions (continued)

Future contribution credits including interest, principal and remaining balance, at the effective interest rate of the Senior Bonds for the 2005 capital contributions as of December 31, 2017 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Remaining Balance</u>
2018	\$ 429,763	\$ 571,116	\$ 1,000,879	\$ 11,446,956
2019	450,429	550,450	1,000,879	10,996,527
2020	472,089	528,790	1,000,879	10,524,438
2021	494,790	506,089	1,000,879	10,029,648
2022	518,583	482,296	1,000,879	9,511,065
2023	543,520	457,359	1,000,879	8,967,545
2024	569,657	431,222	1,000,879	8,397,888
2025	597,050	403,829	1,000,879	7,800,838
2026	625,760	375,119	1,000,879	7,175,078
2027	655,851	345,028	1,000,879	6,519,227
2028	687,389	313,490	1,000,879	5,831,838
2029	720,443	280,436	1,000,879	5,111,395
2030	755,087	245,792	1,000,879	4,356,308
2031	791,397	209,482	1,000,879	3,564,911
2032	829,453	171,426	1,000,879	2,735,458
2033	869,339	131,540	1,000,879	1,866,119
2034	911,143	89,736	1,000,879	954,976
2035	954,976	45,922	1,000,898	
	<u>\$ 11,876,719</u>	<u>\$ 6,139,122</u>	<u>\$ 18,015,841</u>	

In 2008, the Authority entered into contracts with twenty MUDs to provide funds to pay capital expenses of the Authority's system. Each MUD has paid a Capital Contribution based on a percentage of its pro-rata share of the total groundwater production for all water utilities during the calendar year 2009. Capital contributions of \$30,936,787 and \$4,960,093 were made to the Authority in the 2008 and 2009 fiscal years, respectively, for total 2008 contributions of \$35,896,880. The participating MUDs began receiving contribution credits against their individual water fees distributed over the life of the Series 2008 Senior Bonds beginning with the 2009 first quarter pumpage fees. Any amounts remaining plus accrued interest at the end of the capital contribution expiration date will be credited against any amounts owed to the Authority by the MUDs or paid to the MUDs by the Authority.

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 7 – Capital Contributions (continued)

Future contribution credits including interest, principal and remaining balance, at the effective interest rate of the Senior Bonds for the 2008 capital contributions as of December 31, 2017 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Remaining Balance</u>
2018	\$ 880,387	\$ 1,763,277	\$ 2,643,664	\$ 31,921,724
2019	927,712	1,715,952	2,643,664	30,994,012
2020	977,581	1,666,083	2,643,664	30,016,431
2021	1,030,131	1,613,533	2,643,664	28,986,300
2022	1,085,505	1,558,159	2,643,664	27,900,795
2023	1,143,857	1,499,807	2,643,664	26,756,938
2024	1,205,345	1,438,319	2,643,664	25,551,593
2025	1,270,138	1,373,526	2,643,664	24,281,455
2026	1,338,414	1,305,250	2,643,664	22,943,041
2027	1,410,361	1,233,303	2,643,664	21,532,680
2028	1,486,175	1,157,489	2,643,664	20,046,505
2029	1,566,064	1,077,600	2,643,664	18,480,441
2030	1,650,248	993,416	2,643,664	16,830,193
2031	1,738,957	904,707	2,643,664	15,091,236
2032	1,832,435	811,229	2,643,664	13,258,801
2033	1,930,937	712,727	2,643,664	11,327,864
2034	2,034,735	608,929	2,643,664	9,293,129
2035	2,144,112	499,552	2,643,664	7,149,017
2036	2,259,369	384,295	2,643,664	4,889,648
2037	2,380,821	262,843	2,643,664	2,508,827
2038	2,508,827	134,862	2,643,689	
	<u>\$ 32,802,111</u>	<u>\$ 22,714,858</u>	<u>\$ 55,516,969</u>	

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 7 – Capital Contributions (continued)

Future contribution credits including interest, principal and remaining balance, at the effective interest rate of the Senior Bonds for all capital contributions as of December 31, 2017 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Remaining Balance</u>
2018	\$ 2,388,158	\$ 3,630,227	\$ 6,018,385	\$ 67,912,727
2019	2,510,668	3,507,717	6,018,385	65,402,059
2020	2,639,474	3,378,911	6,018,385	62,762,585
2021	2,774,900	3,243,485	6,018,385	59,987,685
2022	2,917,284	3,101,101	6,018,385	57,070,401
2023	3,066,988	2,951,397	6,018,385	54,003,413
2024	3,224,387	2,793,998	6,018,385	50,779,026
2025	3,389,876	2,628,509	6,018,385	47,389,150
2026	3,563,872	2,454,513	6,018,385	43,825,278
2027	3,746,814	2,271,571	6,018,385	40,078,464
2028	3,939,163	2,079,222	6,018,385	36,139,301
2029	4,141,401	1,876,984	6,018,385	31,997,900
2030	4,354,040	1,664,345	6,018,385	27,643,860
2031	4,577,615	1,440,770	6,018,385	23,066,245
2032	4,812,689	1,205,696	6,018,385	18,253,556
2033	5,059,573	958,531	6,018,104	13,193,983
2034	2,945,878	698,665	3,644,543	10,248,105
2035	3,099,088	545,474	3,644,562	7,149,017
2036	2,259,369	384,295	2,643,664	4,889,648
2037	2,380,821	262,843	2,643,664	2,508,827
2038	2,508,827	134,862	2,643,689	
	<u>\$ 70,300,885</u>	<u>\$ 41,213,116</u>	<u>\$ 111,514,001</u>	

Changes in capital contributions for the current and prior year are as follows:

	<u>2017</u>	<u>2016</u>
Capital contributions, beginning balance	\$ 72,572,486	\$ 74,733,291
Principal repayments	(2,271,601)	(2,160,805)
Capital contributions, ending balance	<u>\$ 70,300,885</u>	<u>\$ 72,572,486</u>

North Harris County Regional Water Authority
Notes to Basic Financial Statements
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Note 8 – Chloramination Conversion Credits

Entities designated to receive surface water from the Authority were required to install chloramine disinfection systems at their facilities. The Authority has established a program to reimburse entities for the cost of constructing these systems. The reimbursement is in the form of a credit against pumpage and/or surface water fees. The credit is calculated by amortizing the cost of the chloramines system at six percent interest over a thirty year period, which will begin the year that the facilities are placed in service. The annual credit will be divided by twelve and the resulting amount will be credited monthly toward the fees payable to the Authority for water used. As of December 31, 2017, approximately fifty entities have provided the required documentation to the Authority and are receiving the monthly chloramination credit.

During the current fiscal year, the Authority reimbursed \$375,333 in principal and \$1,169,749 in interest to districts for chloramination conversion facilities.

Changes to the Authority’s liability for chloramination credits for the current and prior year are as follows:

	2017	2016
Chloramine credits payable, beginning of year	\$ 19,495,885	\$ 19,849,973
Principal repayments	(375,333)	(354,088)
Chloramine credits payable, end of year	<u>\$ 19,120,552</u>	<u>\$ 19,495,885</u>

North Harris County Regional Water Authority
Notes to Basic Financial Statements
December 31, 2017

Note 8 – Chloramination Conversion Credits (continued)

As of December 31, 2017, the annual chloramination credits, including principal, interest and remaining balance are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Remaining Balance</u>
2018	\$ 397,853	\$ 1,147,229	\$ 1,545,082	\$ 18,722,699
2019	421,724	1,123,358	1,545,082	18,300,975
2020	447,028	1,098,055	1,545,083	17,853,947
2021	473,850	1,071,233	1,545,083	17,380,097
2022	502,281	1,042,802	1,545,083	16,877,816
2023	532,417	1,012,665	1,545,082	16,345,399
2024	564,362	980,720	1,545,082	15,781,037
2025	598,224	946,858	1,545,082	15,182,813
2026	634,118	910,965	1,545,083	14,548,695
2027	672,165	872,918	1,545,083	13,876,530
2028	712,495	832,588	1,545,083	13,164,035
2029	755,244	789,838	1,545,082	12,408,791
2030	800,559	744,524	1,545,083	11,608,232
2031	848,592	696,490	1,545,082	10,759,640
2032	899,508	645,575	1,545,083	9,860,132
2033	953,478	591,604	1,545,082	8,906,654
2034	1,010,687	534,395	1,545,082	7,895,967
2035	1,071,328	473,754	1,545,082	6,824,639
2036	1,135,608	409,475	1,545,083	5,689,031
2037	1,203,744	341,338	1,545,082	4,485,287
2038	1,275,969	269,113	1,545,082	3,209,318
2039	1,352,527	192,555	1,545,082	1,856,791
2040	1,363,300	111,404	1,474,704	493,491
2041	456,167	21,112	477,279	37,324
2042	37,324	1,131	38,455	
	<u>\$ 19,120,552</u>	<u>\$ 16,861,699</u>	<u>\$ 35,982,251</u>	

Note 9 – Unrestricted Net Position

Included in the Authority's unrestricted net position (i.e., the residual of assets plus deferred outflows less liabilities) of \$198,596,540, is \$132,467,344 in cash and investments, which the Authority has designated as additional bond reserves and has deposited in the Improvement Fund.

*North Harris County Regional Water Authority
Notes to Basic Financial Statements
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Note 10 – Risk Management

The Authority is exposed to various risks related to torts: theft of, damage to and destruction of assets; errors and omissions; and natural disasters. The Authority's risk management program encompasses various means of protecting the Authority against loss by obtaining property, casualty and liability coverage through commercial insurance carriers. There have been no significant reductions in insurance coverage. Settlement amounts have not exceeded insurance coverage for the current year or the three prior years.

Note 11 – Deferred Compensation Plans

The Authority offers its employees a deferred compensation plan created in accordance with Internal Revenue Code, Section 457. The plan is available and permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency. The plan is administered by the International City Management Association - Retirement Corporation (ICMA-RC).

Note 12 – Pension Plan

The Authority has established the North Harris County Regional Water Authority Qualified Pension Plan 401(a) (the "Plan"). The Plan covers all employees. Under the terms of the Plan, active participants become 100% vested on the fifth anniversary of employment. Participants are eligible for payment of benefits upon reaching age 70½, becoming disabled or separating from service for any other reason. Benefits are distributed in accordance with the instructions of the participants. The Board of Directors appointed ICMA-RC to serve as Plan administrator and trustee. The Plan provides for a minimum Authority contribution of 7% of total current covered payroll. At December 31, 2017, all of the Authority's employees were members of the Plan. Non-vested contributions are immaterial to total contributions at December 31, 2017. Vested contributions are solely the possession of participating employees. Total covered payroll was \$1,324,767 for the year ended December 31, 2017. Employer contributions to the Plan were \$117,303.

In 2003, the Authority established an additional 401(a) plan for management employees only. It is identical to the above Plan with the following exceptions: 1) management employees are fully vested on the second anniversary of employment and 2) the Plan provides for a minimum Authority contribution of 25% for the current year annual covered payroll of the General Manager. The total payroll and employer contributions for this plan are included in the totals above.

Note 13 – Water Supply Contracts

In December 2002, the Authority entered into a forty year contract with the City of Houston (Houston) for the purchase of capacity in certain untreated water facilities and treated water facilities, including transmission facilities, of Houston. Under the terms of the contract, Houston will provide surface water to the Authority at a point of delivery to be located near Highway 59 and Beltway 8.

Note 13 – Water Supply Contracts (continued)

The contract stipulates that the Authority will purchase capacity, in phases, in Houston’s surface water system. Houston will be responsible for the design, construction, ownership, maintenance and operation of both treated and untreated water facilities prior to a mutually agreeable delivery point(s). The Authority will be responsible for the design, construction, ownership, maintenance and operation of all facilities located beyond the point of delivery.

During 2003, the Authority made its first payment of \$51,492,844 to Houston for the purchase of capacity in Houston’s treated water facilities and transmission facilities constructed prior to the effective date of the contract. In 2009, the Authority made additional payments for the total amount of \$21,799,523 for the Existing Untreated Water Facilities Initial Untreated Water Demand Allocation of 31 million gallons per day (“MGD”).

The Authority will pay Houston, on a monthly basis, its pro-rata share of operating and maintenance costs of the treated and untreated water facilities and transmission lines based on an annual operating budget. Such monthly payments will include an amount adequate to establish an operating reserve. The contract also provides the Authority with the option to purchase additional capacity in the future. The Authority paid Houston for purchased surface water during the current year. Pursuant to the contract, Houston engages an independent auditor to calculate the true-up of operating costs on an annual basis. As of December 31, 2017, the net amount owed to the Authority by the City of Houston for the true-up for Houston’s fiscal year ended June 30, 2017 is \$7,684,930, which has been recorded as Due from other governments in the *Statement of Net Position*.

Luce Bayou Interbasin Transfer Project

In January 2009, the Authority and Houston executed the First Supplement (the “Supplement”) to the Water Supply Contract to increase the supply of untreated surface water available to the Authority, Houston and the other entities through the construction of the Luce Bayou Interbasin Transfer Project (“Luce Bayou”). When completed, Luce Bayou will convey approximately 400 MGD of untreated surface water from the Trinity River to Lake Houston. The Supplement addresses the allocation of capacity in Luce Bayou and how the costs of the project will be shared by the Authority, the other entities and Houston. The Supplement and Water Supply Contract remain in effect until 2080.

The Coastal Water Authority (CWA) has been designated as the project manager and, working with Houston, is responsible for all decisions and actions relating to the design, development, procurement and construction of all aspects of Luce Bayou. Houston will issue (or cause CWA to issue) bonds, notes or other obligations to pay for all of the costs of the project, except for the right-of-way costs and CWA interest amount (\$360,836 as calculated in the Supplement). In addition to the other terms of the Supplement, neither party shall have any obligation to pay any funds for the project unless and until Houston or CWA have obtained \$28,000,000 in funding from the Texas Water Development Board’s Water Infrastructure Fund that provides for: (i) the accrual of zero interest on such funds for up to 10 years or until the project is completed, whichever occurs first; and (ii) no interest or principal payments on such funds during the 10 year period.

*North Harris County Regional Water Authority
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Note 13 – Water Supply Contracts (continued)

Houston agrees to cause the construction of the project so that it is substantially complete by June 30, 2019. The project will be completed in two stages as follows: (1) Phase I will be the permitting, engineering, surveying, right-of-way and site acquisition, which is currently estimated at a cost of \$43,000,000 and (2) Phase II of the project will be the construction and related costs, which is currently estimated at a cost of \$214,000,000.

Under the terms of the contract, the Authority will make the following payments to Houston:

- Lump Sum Payments for Project Right of Way Costs and Payment of CWA Interest Costs;
- Payments for Existing Untreated Water Supply Facilities; and
- Payments for Phases 1 and 2 Annual New Untreated Water Facilities.

Lump Sum Payments. As of December 31, 2017, the Authority has paid Houston \$2,999,038 for its pro-rata share of estimated right of way costs, net of refunds.

Payments for Existing Untreated Water Facilities. The Authority seeks to increase its Untreated Water Facilities Demand from 31 MGD to 159 MGD, which is currently estimated to be the Authority's surface water demand in the year 2040. Under the terms of the Supplement, the Authority is required to make four payments to Houston for Existing Untreated Water Facilities. Each payment is based on a formula defined in the Supplement based on the Authority's water demand needs in 2025, 2030, 2035 and 2040.

The first payment is due within 60 days of receiving notification from Houston of the completion of Luce Bayou; the second payment is due the earlier of 60 days after sending notice to Houston of the Authority's water demand needs for 2030 or June 30, 2025; the third payment is due the earlier of 60 days after sending notice to Houston of the Authority's water demand needs for 2035 or June 30, 2030; and the fourth payment is due the earlier of 60 days after sending notice to Houston of the Authority's water demand needs for 2040 or June 30, 2035.

Payment for Phases 1 and 2 Annual New Untreated Water Facilities. Payments made to Houston for Phase 1 and 2 Annual New Untreated Water Facilities are to be used only for the purpose of making debt service payments on obligations issued by either Houston or CWA for the construction of Phase 1 and Phase 2 of Luce Bayou. The formulas used to calculate payments are defined in the contract and take into consideration the Authority's 159 MGD untreated water reservation, the total amount of untreated water sold by Houston to all customers and Houston's annual debt service requirement. In the 2013 fiscal year, the CWA received financial assistance in the amount of \$28,754,000 from the State of Texas under the State Participation Program. The Authority's pro-rata share of debt service payments on this obligation will be repaid over 33 years. During the current fiscal year, the Authority paid Houston \$105,960 for its portion of the annual debt service requirement.

Note 13 – Water Supply Contracts (continued)

Northeast Water Purification Plant Expansion Project

On February 25, 2015, the Authority and Houston executed the Second Supplement to the Water Supply Contract to increase the supply of treated water to the Authority from 31 MGD to 144 MGD. In order to provide this additional capacity, Houston will expand the Northeast Water Purification Plant in 2 phases. Phase 1 will provide the Authority with an additional 51.05 MGD capacity no later than August 31, 2021 and Phase 2 will provide an additional 61.95 MGD of capacity no later than June 30, 2024.

The Authority's estimated share of total costs is approximately \$469 million; however, these cost assumptions are currently under review by the parties participating in the project and it is anticipated that, upon completion the review, the cost estimate will increase, the phasing may be adjusted and the delivery dates may be delayed. These revisions could substantially increase the cost of the project and delay completion of the project.

Houston will issue cash calls as needed to fund the expansion. These funds will be held in escrow by Houston in the Authority's name until such time that Houston requests withdrawals from the escrow account to pay for ongoing project costs. As of December 31, 2017, the Authority has paid Houston \$16,485,656 in cash call withdrawals from the escrow account and has \$42,655,797 remaining in escrow.

Northeast Transmission Line

On November 10, 2015, the Authority and Houston executed the Third Supplement to the Water Supply Contract to clarify and agree to the terms for the cost sharing, permitting, engineering, surveying, construction, operation and maintenance necessary for the Segment 1 of the Northeast Transmission Line. The Authority's estimated share of the total costs is approximately \$3,604,970. Houston will invoice the Authority prior to engaging a design engineer and prior to awarding the construction contract. In the prior year, the Authority incurred costs of \$48,450 for its pro-rata share of project costs incurred through the effective date of the Third Supplement.

Also on November 10, 2015, the Authority and Houston executed the Fourth Supplement to the Water Supply Contract to clarify and agree to the terms for the cost sharing, permitting, engineering, surveying, construction, operation and maintenance necessary for the Segment 2 of the Northeast Transmission Line. The Authority's estimated share of the total costs is approximately \$238,040,085. Houston will invoice the Authority prior to engaging a design engineer and prior to awarding the construction contract. In prior years, the Authority incurred costs of \$6,817,194 for its pro-rata share of project costs incurred through the effective date of the Fourth Supplement. During the current fiscal year, the Authority paid Houston \$8,425,093 for their share of design costs for Segment 2.

*North Harris County Regional Water Authority
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Note 14 – Joint Facilities

In 2004, the Authority entered into an Agreement for Joint Financing, Design, Construction, Operation and Maintenance of Surface Water Transmission Facilities (“Joint Financing Agreement”) with Harris County Municipal Utility District No. 33 (No. 33) on behalf of the Central Harris County Water Users Consortium, now Central Harris County Regional Water Authority (the “Central Authority”), a consortium of conservation and reclamation Districts established and operating pursuant to the Central Harris County Water Users Consortium Agreement, dated December 13, 2002. The purpose of the Joint Financing Agreement was to memorialize the terms under which the Authority and the Central Authority would share the cost of constructing certain joint facilities necessary to receive treated surface water from Houston.

In October 2007, the Authority and Central Authority entered into an Interlocal Agreement to establish the terms under which the Authority and the Central Authority agreed to share the costs of acquiring properties, rights-of-way, easements and other property interests necessary to construct the joint facilities.

In February 2008, the Authority entered into a Letter of Understanding (the “LOU”) with the Central Authority, which served as an amendment to the Joint Financing Agreement. The LOU expressed the mutual understanding that it was in the best interest of both parties for the Authority to construct a portion of the proposed Central Authority facilities in conjunction with the Authority’s facilities.

On November 6, 2013 the Authority and Central Authority amended and restated the Joint Financing Agreement (the “Amended Agreement”) to consolidate the respective rights and obligations of both parties under the previous agreements and to establish the terms and conditions under which the parties would share the costs of construction, operation and maintenance of the joint facilities constructed by the Authority.

The terms of the Amended Agreement establish that capital costs for each existing joint facility will be allocated between the Authority and the Central Authority on a pro rata basis. Accordingly, the Central Authority paid the Authority \$7,679,119 for its pro rata share of existing joint facilities in December 2013. In the event that the parties decide to jointly finance and construct additional facilities, a separate written agreement will have to be executed. The Authority holds legal title to the joint facilities; however, each party has the use and benefit of its pro rata share of capacity.

The Authority is responsible for the operation and maintenance of the joint facilities. Upon execution of the Amended Agreement, the Central Authority owed the Authority \$170,503 for operation and maintenance costs through December 31, 2012. This amount was paid in December 2013.

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Supplementary Information

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North Harris County Regional Water Authority
Schedule of Expenses
Last Five Fiscal Years

	2017	2016	2015	2014	2013
Personnel					
Employee salaries	\$ 1,346,367	\$ 1,143,146	\$ 955,192	\$ 925,728	\$ 846,823
Employee retirement	117,303	104,607	88,977	85,641	79,095
Group insurance	152,197	113,838	104,225	98,521	80,894
Medicare/ Social security	84,594	73,522	59,232	58,178	53,119
Unemployment compensation	1,499	1,540	62	1,656	63
	<u>1,701,960</u>	<u>1,436,653</u>	<u>1,207,688</u>	<u>1,169,724</u>	<u>1,059,994</u>
Professional fees					
Legal	213,773	269,269	150,616	298,558	157,581
Engineering	143,259	554,388	1,702,550	2,361,412	1,989,815
Financial services	2,970	3,510	4,860	5,805	4,330
Legislative consultant	130,000	130,000	130,000	130,000	130,000
Investment management services	98,297	102,891	142,930	148,317	147,560
Redistricting/mapping		6,960		2,300	
Audit	30,500	28,050	27,500	27,750	26,450
	<u>618,799</u>	<u>1,095,068</u>	<u>2,158,456</u>	<u>2,974,142</u>	<u>2,455,736</u>
Purchased Services					
Bulk water purchases	11,313,413	9,519,465	13,725,609	15,395,630	14,199,064
	<u>11,313,413</u>	<u>9,519,465</u>	<u>13,725,609</u>	<u>15,395,630</u>	<u>14,199,064</u>
Contracted services					
Operations and maintenance	2,392,895	2,172,966	1,983,564	1,765,057	2,233,857
Temporary services	12,375	11,850	4,960	16,564	14,170
	<u>2,405,270</u>	<u>2,184,816</u>	<u>1,988,524</u>	<u>1,781,621</u>	<u>2,248,027</u>
Occupancy and office					
Office lease	124,305	120,913	110,017	107,319	102,804
Safe deposit box	75				75
Bank charges	16,229	6,227	4,202	3,325	11,153
Printing and office	57,734	184,943	102,404	42,798	141,087
Postage and delivery	3,513	73,384	38,807	4,563	3,896
Telephone	50,863	50,494	47,906	47,017	84,383
Utilities	644,197	578,632	715,751	784,545	779,591
Equipment leases	14,797	15,673	14,810	14,709	16,115
Internet service	42,561	45,450	38,376	41,935	34,517
Communication services	75,000	72,000	72,000	79,129	72,000
	<u>1,029,274</u>	<u>1,147,716</u>	<u>1,144,273</u>	<u>1,125,340</u>	<u>1,245,621</u>

See accompanying auditors' report.

North Harris County Regional Water Authority
Schedule of Expenses
Last Five Fiscal Years

	2017	2016	2015	2014	2013
Other					
Director fees	\$ 21,600	\$ 23,700	\$ 25,650	\$ 24,450	\$ 23,100
Election expense			31,956	48,785	
Technology transfer projects	56,082	41,888	34,788	34,863	34,863
Insurance	80,504	78,404	80,917	83,871	82,763
Travel	56,479	43,301	37,065	32,224	29,309
Legal notices				25,841	
Membership/Subscription fees	19,632	15,238	13,035	11,887	11,083
Computer services	38,466	7,172	11,295	14,264	16,083
Computer software and equipment	18,737	12,844	9,200	1,845	7,806
Maintenance and repairs	25,474	15,191	5,864	16,502	16,397
Office furniture	2,794	3,240	1,300		2,760
Public education				7,981	
Water conservation	48,859	43,739	48,845	42,499	48,450
Mileage reimbursement	8,269	6,196	6,788	5,506	4,664
Permit fees	573,095	508,025	506,700	507,110	534,784
Seminars/training	13,112	13,660	9,950	8,443	8,760
Security	5,909	936	830	1,088	744
Miscellaneous	137,988	145,227	21,621		
Administrative					55,534
	<u>1,107,000</u>	<u>958,761</u>	<u>845,804</u>	<u>867,159</u>	<u>877,100</u>
Expenses Before Depreciation and Amortization	<u>18,175,716</u>	<u>16,342,479</u>	<u>21,070,354</u>	<u>23,313,616</u>	<u>22,085,542</u>
Depreciation and Amortization	<u>8,405,517</u>	<u>7,979,761</u>	<u>7,637,169</u>	<u>8,509,077</u>	<u>7,947,351</u>
Total Expenses	<u>\$ 26,581,233</u>	<u>\$ 24,322,240</u>	<u>\$ 28,707,523</u>	<u>\$ 31,822,693</u>	<u>\$ 30,032,893</u>

See accompanying auditors' report.

*North Harris County Regional Water Authority
Schedule of Principal Water Users
December 31, 2017*

<u>Name</u>	<u>Total Gallons</u>	<u>Fees Paid</u>	<u>Share (%)</u>
Harris Co. M.U.D. 358	\$ 1,042,202,862	\$ 3,022,388	3.3205%
NW Harris Co. M.U.D. 5	1,026,732,309	3,019,715	3.2712%
Harris Co. M.U.D. 387	914,676,035	2,652,561	2.9142%
Harris Co. F.W.S.D. 61	792,463,793	2,298,145	2.5248%
Tomball, City of	787,401,517	2,283,464	2.5087%
Bridgestone M.U.D.	761,755,867	2,241,843	2.4270%
Harris Co. M.U.D. 367 & 383	715,280,433	2,304,354	2.2789%
Harris Co. M.U.D. 24	516,489,784	1,601,321	1.6455%
Harris Co. M.U.D. 280/281/282	487,820,173	1,414,679	1.5542%
Timber Lane U.D.	484,852,241	1,406,072	1.5448%
Subtotal	7,529,675,014	22,244,542	23.9897%
All other retail utilities	22,993,560,372	62,903,981	73.2580%
All private well owners	863,851,561	2,335,739	2.7523%
Total	<u>31,387,086,947</u>	<u>\$ 87,484,262</u>	<u>100.0000%</u>

See accompanying auditors' report.

*North Harris County Regional Water Authority
Historical Rates and Charges
December 31, 2017*

<u>Effective Date</u>		<u>Fee Schedule (Rate Per 1,000 Gallons of Water)</u>
January 1, 2000		\$ 0.12
April 1, 2000		0.25
October 1, 2003		0.34
April 1, 2005		0.59
October 1, 2006		0.84
October 1, 2007		0.99
October 1, 2008		0.99
January 1, 2009		1.50
January 1, 2010	Groundwater	1.75
	Surface Water	2.20
January 1, 2011	Groundwater	1.75
	Surface Water	2.20
January 1, 2012	Groundwater	1.75
	Surface Water	2.20
April 1, 2014	Groundwater	2.00
	Surface Water	2.45
April 1, 2016	Groundwater	2.40
	Surface Water	2.85
April 1, 2017	Groundwater	2.90
	Surface Water	3.35
April 1, 2018	Groundwater	3.40
	Surface Water	3.85

See accompanying auditors' report.

***North Harris County Regional Water Authority
Billing and Collection Experience
December 31, 2017***

<u>Calendar Year Ending</u>	<u>Volume Reported to Subsidence District (gallons)</u>	<u>Volume Reported to Authority (gallons)</u>	<u>Percentage</u>
2002	23,385,003,226	23,304,243,101	99.65%
2003	23,922,957,131	23,919,899,118	99.99%
2004	23,055,346,850	23,002,955,882	99.77%
2005	28,356,373,609	28,351,195,157	99.98%
2006	26,834,935,391	26,822,777,163	99.95%
2007	24,218,161,044	24,199,057,244	99.92%
2008	28,302,980,773	28,274,930,225	99.90%
2009	31,526,248,907	31,449,510,733	99.76%
2010	29,420,861,157	29,371,543,844	99.83%
2011	37,728,453,603	37,713,940,912	99.96%
2012	30,901,831,428	30,871,013,986	99.90%
2013	32,260,208,375	32,204,714,683	99.83%
2014	30,122,900,716	30,080,759,406	99.86%
2015	30,100,833,135	30,054,229,914	99.85%
2016	30,697,514,276	30,632,783,562	99.79%
2017	31,429,861,292	31,387,086,947	99.86%

See accompanying auditors' report.