
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-K

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2017

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number: 001-37756

Global Water Resources, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

21410 N. 19th Avenue #220, Phoenix, AZ

(Address of principal executive offices)

90-0632193

(I.R.S. Employer
Identification No.)

85027

(Zip Code)

Registrant's telephone number, including area code: (480) 360-7775

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Common Stock, par value \$0.01 per share

Name of Each Exchange on Which Registered

The NASDAQ Stock Market, LLC
(NASDAQ Global Select Market)

Securities registered pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined by Rule 405 of the Securities Act. ☐ Yes ☒ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ☐ Yes ☒ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company)

Accelerated filer ☒

Smaller reporting company ☐

Emerging growth company ☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ☐ Yes ☒ No

The aggregate market value of the common stock held by non-affiliates of the registrant as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2017) was \$194.1 million based upon the closing sale price of the registrant's common stock as reported on the NASDAQ Global Select Market. As of March 9, 2018, the registrant had 19,631,266 shares of common stock, \$0.01 par value per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III of this Form 10-K, to the extent not set forth herein, is incorporated herein by reference to the registrant's definitive proxy statement relating to the 2018 annual meeting of stockholders to be filed with the Securities and Exchange Commission not later than 120 days after the end of the registrant's fiscal year ended December 31, 2017.

EXPLANATORY NOTE

On April 28, 2016, Global Water Resources, Inc. effected a 100.68 to 1.00 stock split. Certain prior period information has been adjusted to conform to the current year presentation to reflect the stock split. All share and per share amounts presented within the financial statements and management's discussion and analysis of financial condition and results of operations have been retrospectively adjusted to reflect the impact of the stock split.

TABLE OF CONTENTS

PART I.

Item 1.	Business	3
Item 1A.	Risk Factors	17
Item 1B.	Unresolved Staff Comments	32
Item 2.	Properties	32
Item 3.	Legal Proceedings	32
Item 4.	Mine Safety Disclosures	32

PART II.

Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities	33
Item 6.	Selected Financial Data	35
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	37
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	56
Item 8.	Financial Statements and Supplementary Data	#Section
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	#Section
Item 9A.	Controls and Procedures	#Section
Item 9B.	Other Information	#Section
		Page#

PART III.

Item 10.	Directors, Executive Officers of the Registrant and Corporate Governance	#Section
Item 11.	Executive Compensation	#Section
	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	#Section
Item 12.		Page#
Item 13.	Certain Relationships and Related Transactions and Director Independence	#Section
Item 14.	Principal Accountant Fees and Services	#Section
		Page#

PART IV.

Item 15.	Exhibits and Financial Statement Schedules	#Section
Item 16.	Form 10-K Summary	#Section
	Signatures	#Section
	Exhibit Index	#Section
		Page#

FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Report on Form 10-K (this “Form 10-K”) of Global Water Resources, Inc. (the “Company”, “GWRI”, “we”, or “us”) and documents incorporated herein by reference are forward-looking in nature and may constitute “forward-looking information” within the meaning of applicable securities laws. Often, but not always, forward-looking statements can be identified by the words “believes”, “anticipates”, “plans”, “expects”, “intends”, “projects”, “estimates”, “objective”, “goal”, “focus”, “aim”, “should”, “could”, “may”, and similar expressions. These forward-looking statements include, but are not limited to, statements about our strategies; expectations about future business plans, prospective performance, and opportunities, including potential acquisitions; future financial performance; population and growth projections; technologies; revenues; metrics; operating expenses; market trends, including those in the markets in which we operate; liquidity; cash flows and uses of cash; dividends; amount and timing of capital expenditures; depreciation and amortization; tax payments; hedging arrangements; our ability to repay indebtedness and invest in initiatives; impact and resolutions of legal matters; the impact of tax reform; and the impact of accounting changes and other pronouncements. Forward-looking statements should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not, or the times at or by which, such performance or results will be achieved. Investors are cautioned not to place undue reliance on forward-looking information. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under “Risk Factors” in Item 1A of this Form 10-K and future reports that we file from time to time with the Securities and Exchange Commission (“SEC”). Although the forward-looking statements are based upon what management believes to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. Except as required by law, we undertake no obligation to publicly release the results of any revision to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PART I

ITEM 1. BUSINESS

Overview

We are a water resource management company that owns, operates, and manages water, wastewater, and recycled water utilities in strategically located communities, principally in metropolitan Phoenix, Arizona. We seek to deploy our integrated approach, which we refer to as “Total Water Management,” a term we use to mean managing the entire water cycle by owning and operating the water, wastewater, and recycled water utilities within the same geographic areas in order to both conserve water and maximize its total economic and social value. We use Total Water Management to promote sustainable communities in areas where we expect growth to outpace the existing potable water supply. Our model focuses on the broad issues of water supply and scarcity and applies principles of water conservation through water reclamation and reuse. Our basic premise is that the world’s water supply is limited and yet can be stretched significantly through effective planning, the use of recycled water, and by providing individuals and communities resources that promote wise water usage practices.

We currently own nine water and wastewater utilities in strategically targeted communities in metropolitan Phoenix. We currently serve more than 51,000 people in approximately 20,000 homes within our 336 square miles of certificated service areas, which are serviced by five wholly-owned regulated operating subsidiaries as of December 31, 2017. Approximately 98.8% of our active service connections are customers of our Santa Cruz Water Company, LLC (“Santa Cruz”) and Palo Verde Utilities Company, LLC (“Palo Verde”) utilities, which are located within a single service area. We have grown significantly since our formation in 2003, with total revenues increasing from \$4.9 million in 2004 to \$31.2 million in 2017, and total service connections increasing from 8,113 as of December 31, 2004 to 39,618 as of December 31, 2017, with regionally planned areas large enough to serve approximately two million service connections.

Our Corporate History

Global Water Resources, LLC (“GWR”) was organized in 2003 to acquire, own, and manage a portfolio of water and wastewater utilities in the southwestern region of the United States (“U.S.”). Global Water Management, LLC (“GWM”) was formed as an affiliated company to provide business development, management, construction project management, operations, and administrative services to GWR and all of its regulated subsidiaries.

In early 2010, the members of GWR made the decision to raise money through the capital markets, and GWR and GWM were reorganized to form Global Water Resources, Inc., a Delaware corporation. The members established a new entity, GWR Global Water Resources Corp. (“GWRC”), which was incorporated under the Business Corporations Act (British Columbia) on March 23, 2010 to acquire shares of our common stock and to actively participate in our management, business, and operations

through its representation on our board of directors and its shared management. On December 30, 2010, GWRC completed its initial public offering in Canada and its common shares were listed on the Toronto Stock Exchange.

On May 3, 2016, GWRC merged with and into the Company (the "Reorganization Transaction"). At the effective time of the merger, holders of GWRC's common shares received one share of the Company's common stock for each outstanding common share of GWRC. As a result of the merger, GWRC ceased to exist as a British Columbia corporation and the Company, governed by the corporate laws of the State of Delaware, was the surviving entity. The Reorganization Transaction was conditional upon the concurrent completion of an initial public offering of shares of common stock of the Company in the U.S. (the "U.S. IPO"), which was completed on May 3, 2016.

"Emerging Growth Company" Reporting Requirements

The Company qualifies as an "emerging growth company" as defined in the Jumpstart Our Business Startups Act (the "JOBS Act"). For as long as the Company is deemed to be an emerging growth company, the Company may take advantage of certain exemptions from various regulatory reporting requirements that are applicable to other public companies. Among other things, the Company is not required to (i) provide an auditor's attestation report on the effectiveness of our system of internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act"); (ii) comply with any new rules that may be adopted by the Public Company Accounting Oversight Board ("PCAOB") requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer; (iii) comply with any new audit rules adopted by the PCAOB after April 5, 2012 unless the SEC determines otherwise; (iv) comply with any new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies under Section 102(b)(1) of the JOBS Act; (v) provide certain disclosure regarding executive compensation required of larger public companies; or (vi) hold a nonbinding advisory vote on executive compensation and obtain stockholder approval of any golden parachute payments not previously approved.

As an emerging growth company, the Company has elected to take advantage of the extended transition period for complying with new or revised accounting standards until such standards are also applicable to private companies. As a result of this election, our financial statements may not be comparable with any other public company that is not an emerging growth company (or an emerging growth company that has opted out of using the extended transition provision).

The Company will remain an emerging growth company until the earliest of (i) the last day of the first fiscal year in which our total annual gross revenues exceed \$1.07 billion; (ii) the date on which the Company is deemed to be a "large accelerated filer," as defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), or any successor statute, which would occur if the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the last business day of our most recently completed second fiscal quarter; (iii) the date on which the Company issues more than \$1 billion in non-convertible debt during the preceding three-year period; or (iv) the end of the 2021 fiscal year.

U.S. Water Industry Overview

U.S. Water Industry Areas of Business

The U.S. water industry has two main areas of business:

- *Utility Services to Customers.* This business includes municipal water and wastewater utilities, which are owned and operated by local governments or governmental subdivisions, and investor-owned water and wastewater utilities. Investor-owned water and wastewater utilities are generally economically regulated, including with respect to rate regulation, by public utility commissions in the states in which they operate. The utility segment is characterized by high barriers to entry, including high capital spending requirements.
- *General Water Products and Services.* This business includes manufacturing, engineering and consulting companies, and numerous other fee-for-service businesses. The activities of these businesses include the building, financing, and operating of water and wastewater utilities, utility repair services, contract operations, laboratory services, manufacturing and distribution of infrastructure and technology components, and other specialized services. At present, and upon the prior sale of the FATHOM™ business and the Loop 303 Contracts (as defined in "Management's Discussion and Analysis of Financial Condition and Results of Operations – Recent Events" in Part II, Item 7 of this Form 10-K), the Company no longer performs any of these unregulated services.

Key Characteristics of the U.S. Water Industry

In the U.S., the water industry is characterized by:

- *Significant Constraints on the Availability of Fresh Water.* In Arizona, the Arizona Department of Water Resources estimates that annual water usage is 7 million acre-feet per year. Arizona has the right to use 2.8 million acre-feet from the Colorado River and approximately half of that can be delivered through the Central Arizona Project, a 336 mile diversion canal from the Colorado River to central Arizona. The Colorado River is presently over-allocated, which means that more surface water right allocations have been issued than the actual average annual flow, with allocations being determined based on data from a period during which flows were significantly higher than in recent years. The Central Arizona Project is the only means of transporting Colorado River water into central Arizona. Approximately 41% of the water used in Arizona comes from groundwater. Water in the western U.S. is being pumped from groundwater sources faster than it is replenished naturally, a condition known as overdraft. In areas of water scarcity, such as the arid western U.S., water recycling represents a relatively simple, inexpensive, and energy-efficient means of augmenting water supply as compared to transporting surface water, groundwater, or desalinated water from other locations. Approximately 70% of the water provided by municipalities is currently used for non-potable applications where recycled water could potentially be utilized.
- *Lack of Technology Utilization to Increase Operating Efficiencies and Decrease Operating Costs.* The U.S. water industry has traditionally not taken advantage of advances in technology available to enhance revenue, increase operating efficiencies, and decrease operating costs (including labor and energy costs). Areas of opportunity include automated meter reading, systems management, and administrative functions, such as customer billing and remittance systems. Key drivers for the lack of investment in technology in water and wastewater utilities have been the historical lack of incentives offered or standards imposed by regulators to achieve efficiencies and lower costs and the ownership of the U.S. water utility sector, which largely consists of small, undercapitalized, municipally-owned utilities that lack the financial and technical resources to pursue technology opportunities.
- *Highly Fragmented Ownership.* The utility segment of the U.S. water industry is highly fragmented, with approximately 50,000 water utilities and approximately 16,000 community wastewater utilities, according to the U.S. Environmental Protection Agency ("EPA"). The majority of the approximately 50,000 water utilities are small, serving a population of 500 or less, and 86% of the water utilities serve only 10% of the population.
- *Large Public Sector Ownership.* Municipally-owned utilities provide water and wastewater services for the vast majority of the U.S. population. For homes connected to a community water system, approximately 80% are provided service by municipally-owned utilities. For homes connected to a community wastewater system, about 75% are provided service by municipally-owned utilities.
- *Aging Infrastructure in Need of Significant Capital Expenditures.* Water infrastructure in the U.S. is aging and requires significant investment and stringent focus on cost control to upgrade or replace aging facilities and to provide service to growing populations. Throughout the U.S., utilities are required to make expenditures on the rehabilitation of existing utilities and on the installation of new infrastructure to accommodate growth and make improvements to water quality and wastewater discharges mandated by stricter water quality standards. Water quality standards, first introduced with the Clean Water Act in 1972 and the Safe Drinking Water Act in 1974, are becoming increasingly stringent and numerous. For water, the American Water Works Association estimates capital investments to restore aging infrastructure and to build additional infrastructure for the growing population may be as much as \$1 trillion over the next 25 years. The American Society of Civil Engineers estimates capital investment needs to update and grow the nation's wastewater systems may be as much as \$271 billion over the next twenty years.

Private Sector Opportunities

Municipal water utilities typically fund their capital expenditure needs through user-based water and wastewater rates, municipal taxes, or the issuance of bonds. However, raising large amounts of funds required for capital investment is often challenging for municipal water utilities, which affects their ability to fund capital spending. Many smaller utilities also do not have the in-house technical and engineering resources to manage significant infrastructure or technology-related investments. In order to meet their capital spending challenges and take advantage of technology-related operating efficiencies, many municipalities are examining a combination of outsourcing and partnerships with the private sector or outright privatizations.

- Outsourcing involves municipally-owned utilities contracting with private sector service providers to provide services, such as meter reading, billing, maintenance, or asset management services.
- Public-private partnerships among government, operating companies, and private investors include arrangements, such as design, build, operate contracts; build, own, operate, and transfer contracts; and own, leaseback, and operate contracts.

- Privatization involves a transfer of responsibility for, and ownership of, the utility from the municipality to private investors.

We believe investor-owned utilities that have greater access to capital are generally more capable of making mandated and other necessary infrastructure upgrades to both water and wastewater utilities, addressing increasingly stringent environmental and human health standards, and navigating a wide variety of regulatory processes. In addition, investor-owned utilities that achieve larger scales are able to spread overhead expenses over a larger customer base, thereby reducing the costs to serve each customer. Since many administrative and support activities can be efficiently centralized to gain economies of scale and sharing of best practices, companies that participate in industry consolidation have the potential to improve operating efficiencies, lower costs, and improve service at the same time.

Our Strategy

We are a water resource management company that provides water, wastewater, and recycled water utility services. We believe we are a leader in Total Water Management practices, such as water scarcity management and advanced water recycling applications. Our long-term goal is to become one of the largest investor-owned operators of integrated water and wastewater utilities in areas of the arid western U.S. where water scarcity management is necessary for long-term economic sustainability and growth.

Our growth strategy involves the elements listed below:

- acquiring or forming utilities in the path of prospective population growth;
- expanding our service areas geographically and organically growing our customer base within those areas; and
- deploying our Total Water Management approach into these utilities and service areas.

We believe this plan can be executed in our current service areas and in other geographic areas where water scarcity management is necessary to support long-term growth and in which regulatory authorities recognize the need for water conservation through water recycling.

Total Water Management is a demand-side-management framework (in that it is a solution intended to drive down demand for renewable supplies versus develop new renewable water supplies) that alleviates the pressures of water scarcity in communities where growth is reasonably expected to outpace potable water supply. Built on an all-encompassing view of the water cycle, Total Water Management promotes sustainable community development through reduced potable water consumption while monetizing the value of water through each stage of delivery, collection, and reuse.

Our business model applies Total Water Management in high growth communities. Components of our Total Water Management approach include:

- Regional planning to reduce overall design and implementation costs, leveraging the benefits of replicable designs, gaining the benefits of economies of scale, and enhancing the Company's position as a primary water and wastewater service provider in the region.
 - For example, the Company has secured three separate area-wide Clean Water Act Section 208 Regional Water Quality Management Plans in its major planning areas, covering more than 500 square miles of land. To obtain these plans, a provider must develop, amongst other things, a regional wastewater solution, including plans for engineering, infrastructure location and size, and goals for the management of treated reclaimed water, which the Company successfully demonstrated in obtaining its plans.
- Stretching a limited resource by maximizing the use of recycled water, using renewable surface water where available and recharging aquifers with any available excess water.
 - For example, the Company's water recycling model has been fully implemented in the City of Maricopa. The Company is the water, wastewater, and recycled water provider for the City of Maricopa, which currently has a population of approximately 50,000. A community of this size produces approximately an annual average of 2.6 million gallons of wastewater per day. Because the Company requires developers to take back and utilize recycled water within their communities and invest in "purple pipe" recycled water infrastructure during the initial development of subdivisions, the Company is now able to distribute almost all of the 2.6 million gallons back to the community for beneficial purposes. Approximately 90% of the recycled water goes towards common area non-potable irrigation and for use at a local farm, which allows for the recycled water to naturally recharge into the aquifer. This reduces the total amount of limited ground

or surface water that would otherwise be required within the community by over 40%. To date, the Company has reused 6.9 billion gallons of recycled water in the City of Maricopa.

- Integrating and standardizing water, wastewater, and recycled water infrastructure delivery systems using a separate distribution system of purple pipes to conserve water resources, reduce energy, treatment, and consumable costs (e.g., chemicals, filter media, other general materials, and supplies), provide operational efficiencies, and align the otherwise disparate objectives of water sales and conservation.
 - In addition to the previous example, which related to the requirements for recycled water usage, the separate distribution system of purple pipes, and water conservation achievements, the Company believes that its model results in additional benefits from an economic perspective due to lower use of power and consumables. For every gallon of recycled water that is directly reused while already on land surface, the need to pump additional scarce groundwater and surface water is eliminated. Such additional groundwater and surface water would otherwise need to be treated and distributed in accordance with the Safe Drinking Water Act, which is costly and requires a lot of energy.
- Gaining market and regulatory acceptance of broad utilization of recycled water through agreements with developers, strategic relationships with governments, academic research, and publication as industry experts, coupled with public education and community outreach campaigns.
 - For example, the Company has public-private partnerships formally adopted through memorandums of understanding with the City of Maricopa, the City of Casa Grande, and the City of Eloy. Each memorandum of understanding reflects the Company's intent to deploy Total Water Management. The Company also has 154 infrastructure coordination and financing agreements with landowners or developer entities that include requirements for usage of recycled water and other attributes that support the Company's Total Water Management model. As discussed above, the Company's integrated provider model, which is focused on the maximum use of recycled water, underpins its Clean Water Act Section 208 Regional Water Quality Management Plans and Designations of Assured Water Supply. In addition, the Company has won numerous awards for education, outreach, and conservation in the water industry. Further, the Company's experts have published academic papers regarding Total Water Management, as well as provided insight to industry publications.
- Incorporating automated processes, such as supervisory control and data acquisition, automated meter reading, and back-office technologies and "green" billing, which reduce operating costs and manpower requirements, improve system availability and reliability, and improve customer interface.
 - *Supervisory Control and Data Acquisition.* The Company employs supervisory control and data acquisition in all of its utility systems, which provides continuous monitoring, instantaneous alarming, and historical trending on all key operating assets, including instrumentation and dynamic components (e.g., pumps, motor controlled valves, treatment systems, etc.). This data is reported back to the appropriate operations personnel through a standard industry software known as Wonderware. The benefits of this system include the significantly enhanced ability to: achieve compliance and safety mandates; reduce service outages; troubleshoot systems; provide for remote operations; and allow for proactive maintenance and lower costs related to efficient real-time operations
 - *Automated Meter Reading.* The Company implements automated meter reading by utilizing the FATHOM™ platform's Automated Reading Infrastructure technology, with over 99% of all meters being read by such technology. This technology reads each meter numerous times per day (often hourly) and continuously transmits the meter readings back to a centralized data base through a communications tower and cellular transmission units. The data is then presented to the utility, and may be available to customers, through a simple user interface. Reading meters at this frequency provides many benefits to both the utility and the customer. With this data, utilities can better model demand usage, identify system water loss, identify leaks on the customer side of the meter, monitor for abnormal usage, and present interval, hourly, daily, weekly, or monthly usage back to the customers.
 - *Back-Office Technologies and Paperless Billing.* The Company employs a series of technologies that allow for the complete automation of the billing and remittance process. The Company also provides its customers with over seven ways to pay, with the majority of options being integrated with the Company's back-office technologies. In combination with automated meter reading, this suite of technology has minimized the use

of human labor and reduced the potential for human error for the entire billing and remittance process, while providing better customer service.

We believe our Total Water Management-based business model provides us with a significant competitive advantage in high growth, water scarce regions. Based on our experience and discussions with developers, we believe developers prefer our approach because it provides a bundled solution to infrastructure provision and improves housing density in areas of scarce water resources. Developers are also focusing on increased consumer and regulatory demands for environmentally friendly or “green” housing alternatives. Communities prefer the approach because it provides a partnering platform which promotes economic development, reduces their traditional dependence on bond financing and ensures long term water sustainability.

Our competitive advantage facilitates the execution of our growth strategy. Our proven conservation methods lead to successful permitting for more connections in expanded and new service areas.

Our Regulated Utilities

We own and operate regulated water, wastewater and recycled water utilities in communities principally located in metropolitan Phoenix. Our utilities are regulated by the Arizona Corporation Commission (the “ACC”), as described further under “—Regulation —Arizona Regulatory Agencies” below. As of December 31, 2017, our utilities collectively had 38,997 active service connections offering predictable rate-regulated cash flows. Revenues from our regulated utilities accounted for approximately 99.8% of total revenues in 2017. Our utilities currently possess the high-level regional permits that allow us to implement our business model; thus, we believe we are well-positioned for organic growth in our current service areas that are generally located in Arizona’s population growth corridors: Maricopa/Casa Grande, West Valley, and Eloy Regions.

A key component of our water utility business is the use of recycled water. Recycled water is highly treated and purified wastewater that is distributed through a separate distribution system of purple pipes for a variety of beneficial, non-potable uses. Recycled water can be delivered for all common area irrigation needs, as well as delivered direct to homes where it can be used for outdoor residential irrigation. Total Water Management model, an integrated approach to the use of potable and non-potable water to manage the entire water cycle, both conserves water and maximizes its total economic value. The application of the Total Water Management model has proven to be effective as a means of water scarcity management that promotes sustainable communities and helps achieve greater dwelling unit density in areas where the availability of sustainable water can be a key constraint on development. Our implementation of the Total Water Management philosophy in Arizona has led to the development of relationships with key regulatory bodies.

A summary description of our water utilities at December 31, 2017 is set forth in the following table and described in more detail below:

Company	Date of Acquisition (A) or Formation (F)	Service Provided	Square Miles of Service Area (1)	Active Service Connections	Average Monthly Rate Per Service Connection
MARICOPA / CASA GRANDE REGION					
Global Water-Santa Cruz Water Company	2004 (A)	Water	73	19,375	\$ 57
Global Water-Palo Verde Utilities Company	2004 (A)	Wastewater and Recycled Water	102	19,146	\$ 71
WEST VALLEY REGION					
Water Utility of Greater Tonopah	2006 (A)	Water	105	340	\$ 97
Water Utility of Northern Scottsdale	2006 (A)	Water	1	82	\$ 180
Eagletail Water Company	2017 (A)	Water	8	54	\$ 62
Balterra Sewer Corp	2008 (A)	Wastewater and Recycled Water	2	—	—
Hassayampa Utility Company	2005 (F)	Wastewater and Recycled Water	41	—	—
ELOY REGION					
Global Water - Picacho Cove Water Company	2006 (F)	Water	2	—	—
Global Water - Picacho Cove Utilities Company	2006 (F)	Wastewater and Recycled Water	2	—	—
Total			336	38,997	

(1) Certified areas may overlap in whole or in part for separate utilities.

Maricopa/Casa Grande Region

The City of Maricopa is located approximately 12 miles south of Phoenix. The relative proximity to a significant urban center, coupled with relatively abundant and inexpensive land, were the key drivers of the real estate boom experienced by this community. In 2005, the City of Maricopa was one of the fastest growing cities in the nation. While growth has slowed nationally since 2007, the City of Maricopa continues to grow, as demonstrated by our addition of 7,904 active service connections (representing approximately 4,000 homes) from December 2009 to December 2017. Development in the area is considered to be affordable and represents one of the few areas within the U.S. where a new home can be purchased from the mid \$100,000s.

We operate in this region through Santa Cruz and Palo Verde.

We acquired Santa Cruz and Palo Verde in 2004. Santa Cruz serves 19,375 active service connections as of December 31, 2017 and revenues from Santa Cruz represented approximately 42.7% and 43.9% of our total revenue for the years ended December 31, 2017 and 2016, respectively. Palo Verde serves 19,146 active service connections as of December 31, 2017 and revenues from Palo Verde represented approximately 52.6% and 53.0% of our total revenue for the years ended December 31, 2017 and 2016, respectively.

The Santa Cruz and Palo Verde service areas include approximately 175 square miles, which we believe provide further opportunities for growth once development returns to these areas and water and wastewater utility services are required. Most of the Santa Cruz and Palo Verde infrastructure is less than fifteen years old. Santa Cruz and Palo Verde provide water and wastewater services, respectively, under an innovative public- private partnership memorandum of understanding with the City of Maricopa in Pinal County for approximately 278 square miles of its planning area. We signed a similar memorandum of understanding with the City of Casa Grande to partner in providing water, wastewater, and recycled water services to an approximate 100 square miles of its western region for anticipated growth.

Rate proceedings were completed in 2010 for both Santa Cruz and Palo Verde. In July 2012, these two utilities filed applications with the ACC for increased rates using 2011 as the test year on which the ACC will use to evaluate the utilities' rates. The rate proceedings were completed in February 2014. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Recent Rate Case Activity", included in Part II, Item 7 of this Form 10-K, for additional information.

We acquired CP Water Company ("CP Water") in 2006. CP Water provided water service within parts of Pinal County. CP Water received a Certificate of Convenience and Necessity ("CC&N") for approximately two square miles of service area in 1984 and currently has 12 active service connections. We acquired this small utility as part of our consolidation strategy to enable the deployment of new integrated infrastructure as development occurs in the corridor between the cities of Maricopa and Casa Grande. CP Water's service area, customers, and assets have been transferred to Santa Cruz.

West Valley Region

We operate in this region through Water Utility of Greater Tonopah ("Greater Tonopah"), Water Utility of Northern Scottsdale, Inc. ("Northern Scottsdale"), Balterra Sewer Corp ("Balterra"), and Hassayampa Utility Company Inc. ("Hassayampa"), and formerly through Valencia Water Company, Inc. ("Valencia"), Water Utility of Greater Buckeye ("Greater Buckeye") and Willow Water Valley Co., Inc. ("Willow Valley").

We acquired Greater Tonopah in 2006. Greater Tonopah serves 340 active service connections as of December 31, 2017. Greater Tonopah has a CC&N for 105 square miles of service area and provides water services to Maricopa County west of the Hassayampa River. The acquisition of Greater Tonopah allowed us to enter into agreements with developers to serve a total of roughly 100,000 home sites plus commercial, schools, parks, and industrial developments.

In November 2017, the Bill and Melinda Gates Investment Group, through an investment vehicle, acquired 20,000 acres in the Belmont development, located in the West Valley Region. Belmont is a mixed use, master planned community and is included within the service area of Greater Tonopah and Hassayampa.

We acquired Northern Scottsdale in 2006. Northern Scottsdale serves 82 active service connections as of December 31, 2017. Northern Scottsdale has a CC&N for one square mile and provides water services to two small subdivisions in Northern Scottsdale.

Rate proceedings were completed in 2010 for Greater Tonopah. Northern Scottsdale completed a rate proceeding in 2008. In July 2012, these five utilities filed applications with the ACC for increased rates using 2011 as the test year on which the ACC evaluates the utilities' rates. The rate proceedings were completed in February 2014. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Recent Rate Case Activity", included in Part II, Item 7 of this Form 10-K, for additional information.

We acquired Balterra in 2006. Balterra is a wastewater utility and has a CC&N for two square miles in an area in western Maricopa County known as Tonopah. Balterra currently has no active service connections; however, its service area lies directly in the expected path of future growth in the far west valley of metropolitan Phoenix, which we believe should provide opportunities for growth once development commences in this area.

We formed Hassayampa in 2005. Hassayampa is a wastewater utility and has a CC&N for 41 square miles in an area that is contiguous to Balterra. Hassayampa currently has no active service connections; however, like Balterra, its service area lies directly in the path of future growth in the far west valley of metropolitan Phoenix, which we believe should provide opportunities for growth once development commences in this area.

In October 2012, we and our subsidiary, 303 Utilities Company, and the City of Glendale entered into an agreement for future wastewater and recycled water services, advancing our public-private-partnership originally approved by the city council in March 2010. The agreement named 303 Utilities Company as the future wastewater and recycled water provider for a 7,000-acre territory within a portion of Glendale's western planning area known as the Loop 303 Corridor. The 303 Utilities Company also signed certain wastewater facilities main extension agreements with numerous developers/landowners in the service area to fund the initial design and construction of a wastewater and recycled water utility. In addition, we signed separate offsite water management agreements with these same developers/landowners to provide the coordination, permitting, and engineering work for the related water utility service element of the project. In September 2013, we entered into an agreement to sell the Loop 303 Contracts to a third-party. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Recent Events—Sale of Loop 303 Contracts", included in Part II, Item 7 of this Form 10-K, for additional information.

We formerly operated additional utilities in the West Valley Region through Valencia, Greater Buckeye and Willow Valley. Valencia was consolidated with Greater Buckeye in 2008, and on July 14, 2015, we closed the stipulated condemnation to transfer the operations and assets of Valencia to the City of Buckeye. See "Management's Discussion and Analysis of Financial Condition

and Results of Operations—Recent Events—Stipulated Condemnation of the Operations and Assets of Valencia”, included in Part II, Item 7 of this Form 10-K, for additional information.

In addition, on May 9, 2016, we closed the sale of Willow Valley to EPCOR Water Arizona Inc. (“EPCOR”). See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Recent Events—Sale of Willow Valley”, included in Part II, Item 7 of this Form 10-K, for additional information.

On May 15, 2017, we acquired Eagletail Water Company (“Eagletail”) via merger. Eagletail serves 54 active connections as of December 31, 2017. Eagletail has a CC&N for eight square miles located west of metropolitan Phoenix.

Eloy Region

The City of Eloy, Arizona is located in Arizona’s “sun corridor” and is approximately equidistant between Phoenix and Tucson. The City of Eloy represents an area of 100 square miles and has a population of approximately 19,000.

We operate in this region through Global Water-Picacho Cove Water Company and Global Water-Picacho Cove Utilities Company (collectively, “Picacho Cove”). We formed Picacho Cove in 2006 to provide water and wastewater services in the City of Eloy and currently have a CC&N for two congruent square miles. The utilities currently have no active service connections and no facilities.

Operations

We treat water to potable standards and also treat, clean, and recycle wastewater for a variety of non-potable uses. A description of these operations follows.

Sources of Water Supply

Our water supplies are primarily derived from groundwater; however, we currently augment these supplies with recycled water and intend to augment them with surface water and increased use of recycled water in the future.

- **Potable Water.** Our utilities presently employ groundwater systems for potable water production. Water is brought to the surface from underground aquifers (water levels vary from approximately 60 to 500 feet below land surface depending on the area), disinfected and stored in tanks for distribution to customers. In some instances, individual raw water supplies do not meet the legislative requirements for certain constituents. In those cases, we use well-head, centralized, point-of-use, or blending treatment systems to ensure water quality meets potable standards.
- **Recycled Water.** Recycled water is created by taking wastewater and applying advanced tertiary treatment (i.e., screening, biological reduction, and filtration and disinfection processes) to create a high quality, non-potable water source. Each step is monitored and controlled in order that the stringent requirements for recycled water are continuously met. Recycled water generated by us meets Arizona’s Aquifer Water Quality Standards before it leaves the treatment facility and is recognized as Class A+, the highest quality of recycled water regulated by the Arizona Department of Environmental Quality. Recycled water can be used for irrigation, facilities cooling, and industrial applications and in a residential setting for toilet flushing and lawn watering.

Technology

We use sophisticated technology as a principal means of improving our margins. We focus on technological innovations that allow us to deliver high-quality water and customer service with minimal potential for human error, delays, and inefficiencies. Our comprehensive technology platform includes supervisory control and data acquisition, automated meter reading, and geographical information system technologies, which we use to map and monitor our physical assets and water resources on an automated, real-time basis with fewer people than the standard water utility model requires. Our systems allow us to detect and resolve potential problems promptly, accurately, and efficiently before they become more serious, which both improves customer service and optimizes and extends the efficient performance and life of our assets. Our automated meter reading technology, which allows us to read water meters remotely rather than physically, improves water resources accounting, allows for identification of high water usage and water theft from disconnected meters. We also use automated voice, internet billing, payment processing, and customer service applications that contribute to additional reduced headcount and a reduction in associated personnel costs.

Decentralized Treatment Facilities

We design and build standard, decentralized facilities that are scaled to the service areas they serve in order to achieve optimum efficiency in providing both water and wastewater services. The replication of our standard facility also improves design, construction, and operating efficiency because we are able to employ similar, proven processes and equipment and technologies at each of our facilities. As a result, our operating efficiency is improved significantly by reducing equipment costs and employee training costs, and our exposure to operational performance risks often associated with larger, custom-built plants is reduced.

Although there has not traditionally been a significant economic incentive or other reward for automation and resource efficiency in our industry, we believe our use of automation in lieu of labor, together with our emphasis on streamlined operations and conservation, will position us well for continued profitable growth and allow us to take advantage of future incentives or rewards that may be available to water utilities that are able to successfully enhance the use of renewable resources.

Regulation

Our water and wastewater utility operations are subject to extensive regulation by U.S. federal, state, and local regulatory agencies that enforce environmental, health and safety requirements, which affect all of our regulated subsidiaries. These requirements include the Safe Drinking Water Act, the Clean Water Act, and the regulations issued under these laws by the EPA. We are also subject to state environmental laws and regulations, such as Arizona's Aquifer Protection Program and other environmental laws and regulations enforced by the Arizona Department of Environmental Quality, and extensive regulation by the ACC, which regulates public utilities. The ACC also has broad administrative power and authority to set rates and charges, determine service areas and conditions of service, and authorize the issuance of securities as well as authority to establish uniform systems of accounts and approve the terms of contracts with both affiliates and customers.

We are also subject to various federal, state, and local laws and regulations governing the storage of hazardous materials, the management and disposal of hazardous and solid wastes, discharges to air and water, the cleanup of contaminated sites, dam safety, fire protection services in the areas we serve, and other matters relating to the protection of the environment, health, and safety.

We maintain a comprehensive environmental program which addresses, among other things, responsible business practices and compliance with environmental laws and regulations, including the use and conservation of natural resources. Water samples across our water system are analyzed on a regular basis in material compliance with regulatory requirements. We conducted more than 9,700 water quality tests in 2017 at subcontracted laboratory facilities in addition to providing continuous online instrumentations for monitoring parameters such as turbidity and disinfectant residuals and allowing for adjustments to chemical treatment based on changes in incoming water quality. For 2017, we achieved a compliance rate of 99.9% for meeting state and federal drinking water standards and 99.1% for compliance with wastewater requirements, for an overall compliance rating of 99.1%. Compliance with governmental regulations is of utmost importance to us, and considerable time and resources are spent ensuring compliance with all applicable federal, state, and local laws and regulations.

In addition to regulation by governmental entities, our operations may also be affected by civic or consumer advocacy groups. These organizations provide a voice for customers at local and national levels to communicate their service priorities and concerns. Although these organizations may lack regulatory or enforcement authority, they may be influential in achieving service quality and rate improvements for customers.

Safe Drinking Water Act

The federal Safe Drinking Water Act and regulations promulgated thereunder establish minimum national quality standards for drinking water. The EPA has issued rules governing the levels of numerous naturally occurring and man-made chemical and microbial contaminants and radionuclides allowable in drinking water and continues to propose new rules. These rules also prescribe testing requirements for detecting contaminants, the treatment systems that may be used for removing contaminants, and other requirements. Federal and state water quality requirements have become increasingly more stringent, including increased water testing requirements, to reflect public health concerns. In Arizona, the requirements of the Safe Drinking Water Act are incorporated by reference into the Arizona Administrative Code.

In order to remove or inactivate microbial organisms, the EPA has promulgated various rules to improve the disinfection and filtration of drinking water and to reduce consumers' exposure to disinfectants and by-products of the disinfection process.

Significant attention has recently been focused on contaminants of emerging concern (chemicals and other substances that have no regulatory standard, have been recently "discovered" in natural streams (often because of improved analytical chemistry detection levels), and potentially cause deleterious effects in aquatic life at environmentally relevant concentrations), including endocrine disrupting compounds and pharmaceuticals and personal care products, in drinking water supplies, municipal wastewater

effluents, and recycled water. Endocrine disrupting compounds are substances that are not produced in the body but act by mimicking or antagonizing natural hormones, and there is research associating exposure with endocrine disrupting compounds to various reproductive problems in both women and men as well as for increases in the frequency of certain types of cancer. Pharmaceuticals and personal care products, such as fragrances, cosmetics, prescription and over-the-counter therapeutic drugs, veterinary drugs, and sunscreen products, enter the environment through excretion, bathing, and disposal of unwanted medications to sewers and trash. We believe contaminants of emerging concern may form the basis for additional regulatory initiatives and requirements in the future.

Although it is difficult to project the ultimate costs of complying with the above or other pending or future requirements, we do not expect current requirements under the Safe Drinking Water Act to have a material impact on our operations or financial condition, although it is possible new methods of treating drinking water may be required if additional regulations become effective in the future. In addition, capital expenditures and operating costs to comply with environmental mandates traditionally have been recognized by state public utility commissions as appropriate for inclusion in establishing rates, although rate recovery may be delayed by “regulatory lag”, that is, the delay between the utility’s test year and the issuance of a rate order approving new rates.

Clean Water Act

The federal Clean Water Act regulates discharges of liquid effluents from drinking water and wastewater treatment facilities into waters of the U.S., including lakes, rivers, streams and subsurface, or sanitary sewers. In Arizona, with the exception of Clean Water Act Section 208 Regional Water Quality Management Plans, capacity management and operations and maintenance requirements, and source control requirements, wastewater operations are primarily regulated under the Aquifer Protection Permit program and the Arizona Pollutant Discharge Elimination System program (see below).

The EPA certifies Clean Water Act Section 208 Regional Water Quality Management Plans and Amendments which govern the location of water reclamation facilities and wastewater treatment plants. The EPA’s 40 C.F.R. Pt. 503 bio-solids requirements are reported to the EPA through the Arizona Department of Environmental Quality. While we are not presently regulated to meet source control requirements, we maintain source control through various Codes of Practice that have been accepted by the ACC as enforceable limits on consumer discharges to sanitary sewer systems. We believe we maintain the necessary permits and approvals for the discharges from our water and wastewater facilities.

Arizona Regulatory Agencies

In Arizona, the ACC is the regulatory authority with jurisdiction over water and wastewater utilities. The ACC has exclusive authority to approve rates, mandate accounting treatments, authorize long-term financing programs, evaluate significant capital expenditures and plant additions, examine and regulate transactions between a regulated subsidiary and its affiliated entities, and approve or disapprove reorganizations, mergers, and acquisitions prior to their completion. Additionally, the ACC has statutory authority to oversee service quality and consumer complaints, and approve or disapprove expansion of service areas. The ACC is comprised of five elected members, each serving four year terms. Companies that wish to provide water or wastewater service are granted a CC&N, which allows them to serve customers within a geographic area specified by a legal description of the property. In considering an application for a CC&N, the ACC will determine if the applicant is fit and proper to provide service within a specified area, whether the applicant has sufficient technical, managerial, and financial capabilities to provide the service, and if that service is necessary and in the public interest. Once a CC&N is granted, the utility falls under the ACC’s jurisdiction and must abide by the rules and laws by which a public service corporation operates.

In February 2014, the ACC issued Rate Decision No. 74364 for our rate cases filed in July 2012 for the following utilities: Santa Cruz, Palo Verde, Valencia, Greater Buckeye, Greater Tonopah, Northern Scottsdale, and Willow Valley. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Recent Rate Case Activity,” included in Part II, Item 7 of this Form 10-K, for additional information.

Arizona water and wastewater utilities must also comply with state environmental regulation regarding drinking water and wastewater, including environmental regulations set by Councils of Government (such as the Central Arizona Association of Governments and the Maricopa Association of Governments), the Arizona Department of Environmental Quality, and the Arizona Department of Water Resources. The Central Arizona Association of Governments is the designated management authority for Section 208 of the Clean Water Act for Pinal and Gila Counties and administers the requirements of the Regional Water Quality Management Plans and Amendments at the local level. The Maricopa Association of Governments is the designated management authority for Section 208 of the Clean Water Act for Maricopa County and administers the requirements of the Regional Water Quality Management Plans and Amendments at the local level. The Maricopa County Environmental Services Department has delegated authority for overseeing Arizona Department of Environmental Quality requirements in Maricopa County. The Arizona Department of Environmental Quality regulates water quality and permits water reclamation facilities, discharges of recycled water, re-use of recycled water, and recharge of recycled water. The Arizona Department of Environmental Quality also regulates

the clean closure requirements of facilities. In Arizona, the Arizona Department of Environmental Quality has received delegated authority from the EPA for the administration of the Clean Water Act's National Pollution Discharge Elimination System program. Permits issued by the Arizona Department of Environmental Quality for discharges to waters of the U.S. in Arizona are termed "Arizona Pollutant Discharge Elimination System," or "AzPDES," permits. The Arizona Department of Environmental Quality also administers the drinking water quality requirements set by the federal Safe Drinking Water Act within Arizona. Finally, the Arizona Department of Water Resources regulates surface water extraction, groundwater withdrawal, designations and certificates of assured water supply, extinguishment of irrigation grandfathered water rights, groundwater savings facilities, recharge facilities, recharge permits, recovery well permits, storage accounts, and well construction, abandonment, or replacement. We must file periodic reports with the ACC, Arizona Department of Environmental Quality, and Arizona Department of Water Resources.

Within each regulatory organization, we have invested in developing cooperative relationships at all levels, from staff to executives to elected and appointed officials. These relationships, coupled with our proactive attitude toward regulatory compliance, have resulted in a number of significantly positive regulatory determinations.

Assured and Adequate Water Supply Regulations

We intend to seek access to renewable water supplies as we grow our water resource portfolio. However, we currently rely almost exclusively (and are likely to continue to rely) on the pumping of groundwater and the generation and delivery of recycled water for non-potable uses to meet future demands in our service areas. Aside from some rights to water through the Central Arizona Project, groundwater (and recycled water derived from groundwater) is the only water supply available to us.

Although we intend to rely on recycled water to help meet water demands in areas, the infrastructure, permits, and customer base necessary to generate and deliver recycled water are not necessarily in place in most of our service areas. In addition, although recycling can extend a limited supply, it does not actually generate a new supply of water. As such, although our proposed generation and delivery of recycled water is likely to help reduce the amount of groundwater that will be required to serve future customers, our ability to serve new customers will remain dependent on its ability to access groundwater. Groundwater is a limited resource in Arizona, and access to new uses of groundwater is closely regulated in the areas served by us. See "Risk Factors—Inadequate water and wastewater supplies could have a material adverse effect upon our ability to achieve the customer growth necessary to increase our revenues," included in Part I, Item 1A of this Form 10-K, for additional information.

Nearly all of our service areas are located in "Active Management Areas," areas within which the use of groundwater is regulated by the Arizona Department of Water Resources in order to manage ongoing problems with groundwater overdraft. The Phoenix, Prescott, and Tucson Active Management Areas are legally mandated to achieve "safe yield" by 2025 or sooner. However, we do not expect any of these Active Management Areas to achieve their safe yield goals. Safe yield requires groundwater pumping to not draw down the groundwater aquifers, or "over-draft," as all pumping is offset or replaced within the Active Management Area from a renewable supply. The Pinal Active Management Area, which encompasses our major service areas near Maricopa, is managed to allow development of non-irrigation uses and to preserve existing agricultural economies in the Active Management Area for as long as feasible, consistent with the necessity to preserve future water supplies for non-irrigation uses.

Under Arizona's assured water supply laws and regulations, a new subdivision inside an Active Management Area must demonstrate that it has an "assured water supply" to the satisfaction of the Arizona Department of Water Resources before the developer is permitted to sell lots. Demonstration of an assured water supply requires, among other things, that an applicant demonstrate that water supplies will be physically, continuously, and legally available to satisfy the water needs of the proposed use for at least 100 years. A developer may make an independent showing of an assured water supply (resulting in a Certificate of Assured Water Supply for a subdivision) or may obtain a written commitment for service from a designated water supplier, such as a privately owned water company or a municipal water supplier. Under the latter approach, the water supplier must demonstrate satisfaction of assured water supply requirements for the developments within its service areas (resulting in a Designation of Assured Water Supply for the provider). At present, we have obtained a Designation of Assured Water Supply in the Maricopa/Casa Grande service territory (Santa Cruz) for approximately 22,900 acre-feet of groundwater use. A Designation of Assured Water Supply is subject to periodic review and renewal by the Arizona Department of Water Resources, and can be increased as demand grows within the service territory, subject to the physical availability of water. A recent physical availability determination for Santa Cruz suggests that, over time, its Designation of Assured Water Supply could potentially be increased to approximately 45,000 acre-feet once sufficient increased demand is established in the area, assuming that water is still physically available by that time (i.e., the groundwater has not been committed to users in surrounding areas). Under our high efficiency Total Water Management model, which is intended to achieve much lower per-unit potable water use rates than would be expected for average developments, 45,000 acre-feet could be sufficient water supply for approximately 180,000 homes per year.

In our West Valley service territory (Greater Tonopah), we expect to receive a Designation of Assured Water Supply in the near future for 10,428 acre-feet with the ability to access the reserved physical availability of an additional 38,100 acre-feet as population grows. Assuming implementation of our high-efficiency Total Water Management model throughout the service area, this could

be a sufficient water supply for approximately 250,000 homes. There is no assurance that the Arizona Department of Water Resources would add any additional acre-feet to either Designation of Assured Water Supply in the future.

In our other service areas, we rely upon a Certificate of Assured Water Supply obtained by developers to demonstrate an assured water supply, or will apply for a Designation of Assured Water Supply in the future when required.

Outside of Arizona's Active Management Areas, the "adequate water supply" program requires a determination of whether there is an adequate water supply—similar to an assured water supply—but it does not necessarily foreclose development when the showing cannot be made. Unless the county government has voted to make the requirement mandatory, a development (outside of Active Management Areas) that cannot demonstrate access to an adequate water supply is generally required only to disclose this fact, although as a practical matter few developments have proceeded on this basis. In addition, whether a water provider to such a development has access to an adequate water supply is nevertheless relevant to its business.

Other Environmental, Health and Safety (including Water Quality) Matters

Our operations also involve the use, storage and disposal of hazardous substances and wastes. For example, our water and wastewater treatment facilities store and use chlorine and other chemicals and generate wastes that require proper handling and disposal under applicable environmental regulations. We could also incur remedial costs in connection with any environmental contamination relating to our operations or facilities, releases or our off-site disposal of wastes. Although we are not aware of any material cleanup or decontamination obligations, the discovery of contamination or the imposition of such obligations arising under relevant federal, state and local laws and regulations in the future could result in additional costs. Our facilities and operations also are subject to requirements under the U.S. Occupational Safety and Health Act and similar laws in Arizona.

Our compliance with all of the environmental, health and safety (including water quality) requirements described above may be subject to inspections and enforcement measures by federal, state and local agencies.

Security

Due to security, vandalism, terrorism and other risks, we take precautions to protect our employees and the water delivered to our customers. In 2002, federal legislation was enacted that resulted in new regulations concerning security of water facilities, including submitting vulnerability assessment studies to the federal government. We have complied with EPA regulations concerning vulnerability assessments and have made filings to the EPA as required. Vulnerability assessments are conducted regularly to evaluate the effectiveness of existing security controls and serve as the basis for further capital investment in security for the facility. Information security controls are deployed or integrated to prevent unauthorized access to company information systems, assure the continuity of business processes dependent upon automation, ensure the integrity of our data and support regulatory and legislative compliance requirements. In addition, communication plans have been developed as a component of our procedures. While we do not make public comments on the details of our security programs, we have been in contact with federal, state, and local law enforcement agencies to coordinate and improve the security of our water delivery systems and to safeguard our water supply.

Competition

As an owner and operator of regulated utilities, we do not face competition within our existing service areas because Arizona law provides the holder of a CC&N for water and wastewater service with an exclusive right to provide that service within the certificated area, as against other public service corporations. In addition, the high cost of constructing water and wastewater systems in an existing market creates a barrier to entry. We do, however, face competition from other water and wastewater utilities for new service areas and with respect to the acquisition of smaller utilities. We believe our principal competitors for new service areas and acquisitions in Arizona are EPCOR Water Arizona Inc., Arizona Water Company, and Liberty Utilities. We believe competition for new service areas and acquisitions is based on relationships with municipalities and developers, experience in making acquisitions, the ability to finance and obtain regulatory approval, quality and breadth of products and services, the ability to integrate both water and wastewater services, and emplace conservation practices throughout the service areas, price, speed, and ease of implementation.

If we seek to extend our services outside Arizona, we will face competition from other regional or national water utilities for these opportunities.

Although we believe we compete effectively in our regulated businesses, our competitors may have more resources and experience than we have and may therefore have a competitive advantage.

Segment Reporting

We currently operate in one geographic region within the State of Arizona, wherein each operating utility operates within the same regulatory environment, and is operated as one reportable segment. For additional information, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Segment Reporting” in Part II, Item 7 of this Form 10-K.

Seasonality

Customer demand for our water during the warmer months is generally greater than other times of the year due primarily to additional consumption of water in connection with irrigation systems, swimming pools, cooling systems, and other outside water use. Throughout the year, and particularly during typically warmer months, demand may vary with temperature, as well as the timing and overall levels of rainfall. In the event that temperatures during the typically warmer months are cooler than normal, or if there is more rainfall than normal, the customer demand for our water may decrease and therefore, adversely affect our revenues. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Factors Affecting our Results of Operations—Weather and Seasonality,” included in Part II, Item 7 of this Form 10-K, for additional information.

Employees

As of December 31, 2017, we employed 47 full-time individuals and no part-time employees. Currently, none of our employees participate in collective bargaining agreements, and we consider our employee relations to be good.

Available Information

We maintain an Internet website at www.gwresources.com. Our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are accessible through our website, free of charge, as soon as reasonably practicable after these reports are filed electronically with the SEC. To access these reports, go to our website at www.gwresources.com. The foregoing information regarding our website is provided for convenience and the content of our website is not deemed to be incorporated by reference in this report filed with the SEC.

The public may read and copy any materials filed by the Company with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

ITEM 1A. RISK FACTORS

Regulatory and Legislative Factors

We have significant obligations under Infrastructure Coordination and Financing Agreements (“ICFAs”), yet funds from our ICFAs are dependent on development activities by developers which we do not control and are also subject to certain regulatory requirements.

In the past, we extended water and wastewater infrastructure financing to developers and builders through ICFAs. These agreements are contracts with developers or builders in which we coordinate and fund the construction of water, wastewater, and recycled water facilities that will be owned and operated by our regulated subsidiaries in advance of completion of developments in the area. Our investment can be considerable, as we phase-in the construction of facilities in accordance with a regional master plan, as opposed to a single development. Developers and builders pay us agreed-upon fees upon the occurrence of specified development events for their development projects. The Arizona Corporation Commission (“ACC”) requires us to record a portion of the funds we receive under ICFAs as contributions in aid of construction (“CIAC”), which are funds or property provided to a utility under the terms of a collection main extension agreement and/or service connection tariff, the value of which are not refundable. Amounts received as CIAC reduce our rate base once expended on utility plants.

The developer is not required to pay the bulk of the agreed-upon fees until a development receives platting approval. Accordingly, we cannot always accurately predict or control the timing of the collection of our fees. If a developer encounters difficulties, such as during a real estate market downturn, that result in a complete or partial abandonment of the development or a significant delay in its completion, we will have planned, built, and invested in infrastructure that will not be supported by development and will not generate either payments under the applicable ICFA or cash flows from providing services. As a result, our return on our investment and cash flow stream could be adversely affected.

In August 2013, we entered into a settlement agreement with ACC staff, the Residential Utility Consumers Office, the City of Maricopa, and the other parties to a rate case, which established the policy by which ICFA fees will be treated going forward. The settlement also prohibits us from entering into new ICFAs. In February 2014, the rate case proceedings were completed and the ACC issued Rate Decision No. 74364, approving the settlement agreement. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Recent Rate Case Activity,” included in Part II, Item 7 of this Form 10-K, for additional information.

New or stricter regulatory standards or other governmental actions could increase our regulatory compliance and operating costs, which could cause our profitability to suffer, particularly if we are unable to increase our rates to offset such costs.

In Arizona, water and wastewater utilities are subject to regulation by water, environmental, public utility, and health and safety regulators, and we are required to obtain environmental permits from governmental agencies in order to operate our facilities. Regulations relate to, among other things, standards and criteria for drinking water quality and for wastewater discharges, customer service and service delivery standards, waste disposal and raw groundwater abstraction limits, and rates and charges for our regulated services. There may be instances in the future when we are not in or cannot achieve compliance with new and evolving laws, regulations, and permits without incurring additional operating costs. For example, in 2006, the U.S. Environmental Protection Agency (“EPA”) implemented a new arsenic maximum contaminant level, which effectively required the installation and operation of costly arsenic treatment systems at many of our water production facilities.

Our costs of complying with current and future governmental laws and regulations could adversely affect our business or results of operations. If we fail to comply with these laws, regulations, or permits, we could be fined or otherwise sanctioned by regulators and our operations could be curtailed or shut down. We may also be exposed to product liability or breach of contract claims by third parties resulting from our noncompliance. These laws and regulations are complex and change frequently, and these changes may cause us to incur costs in connection with the remediation of actions that were lawful when they were taken. Failure by us to observe the conditions and comply with the requirements of permits and other applicable laws and regulations could result in delays, additional costs, fines, and other adverse consequences up to and including inability to proceed with development in our service areas.

We may incur higher compliance or remediation costs than expected in any particular period and may not be able to pass those increased costs along to our customers immediately through rate increases, or at all. This is because we must obtain regulatory approval to increase our rates, which can be time-consuming and costly and our requests for increases may not be approved in part, or in full.

We are required to test our water quality for certain parameters and potential contaminants on a regular basis. If the test results indicate that parameters or contaminants exceed allowable limits, we may be required either to commence treatment to remedy

the water quality or to develop an alternate water source. Either of these outcomes may be costly, and there can be no assurance that the regulatory authorities would approve rate increases to recover these additional compliance costs. In addition, by the time that test results are available, contaminated water may have been provided to customers, which may result in liability for us and damage our reputation.

In addition, governments or government agencies that regulate our operations may enact legislation or adopt new requirements that could have an adverse effect on our business, including:

- restricting ownership or investment;
- providing for the expropriation of our assets by the government through condemnation or similar proceedings;
- providing for changes to water and wastewater quality standards;
- requiring cancellation or renegotiation of, or unilateral changes to, agreements relating to our provision of water and wastewater services;
- changing regulatory or legislative emphasis on water conservation in comparison to other goals and initiatives;
- promoting an increase of competition among water companies within our designated service areas;
- requiring the provision of water or wastewater services at no charge or at reduced prices;
- restricting the ability to terminate services to customers whose accounts are in arrears;
- restricting the ability to sell assets or issue securities;
- adversely changing tax, legal, or regulatory requirements, including employment, property ownership, or general business regulations; changing environmental requirements and the imposition of additional requirements and costs on our operations; and including but not limited to changes adopted in response to regulatory measures to address global climate change;
- changes in the charges applied to raw water abstraction;
- changes in rate making policies; or
- restrictions relating to water use and supply, including restrictions on use, increased offsetting groundwater replenishment obligations, changes to the character of groundwater rights, and settlement of Native American claims.

Uncertainties in the interpretation and application of the 2017 Tax Cuts and Jobs Act could materially affect our tax obligations and effective tax rate.

Significant judgment is required in determining our provision for income taxes. Our calculation of the provision for income taxes is subject to our interpretation of applicable tax laws in the jurisdictions in which we file. In addition, our income tax returns are subject to periodic examination by the Internal Revenue Service and other taxing authorities.

The 2017 Tax Cuts and Jobs Act (the “TCJA”) was enacted on December 22, 2017, and significantly affected U.S. tax law by changing how the U.S. imposes income tax on corporations. The U.S. Department of Treasury has broad authority to issue regulations and interpretative guidance that may significantly impact how we will apply the law, which ultimately could impact our results of operations in the period issued.

The TCJA requires complex computations not previously provided in U.S. tax law. As such, the application of accounting guidance for such items is currently uncertain. Further, compliance with the TCJA and the accounting for such provisions require accumulation of information not previously required or regularly produced. As a result, we have provided a provisional estimate on the effect of the TCJA in our financial statements. As additional regulatory guidance is issued by the applicable taxing authorities, as accounting treatment is clarified, as we perform additional analysis on the application of the law, and as we refine estimates in calculating the effect, our final analysis, which will be recorded in the period completed, may be different from our current provisional amounts, which could materially affect our tax obligations and effective tax rate.

In addition, the ACC opened a docket to address the utility ratemaking implications of the TCJA. It is not clear what actions the ACC will ultimately take with regard to our regulated utilities. See “Management’s Discussion and Analysis of Results of Operations and Financial Condition - ACC Tax Docket” in Part II, Item 7 of this Form 10-K for more information on the ACC docket that addresses the utility ratemaking implications of the TCJA.

Changes to environmental and other regulation may require us to alter our existing treatment facilities or build additional facilities.

To comply with federal, state, and local environmental laws, our existing facilities may need to be altered or replaced. Altered and new facilities and other capital improvements must be constructed and operated in accordance with multiple requirements, including, in certain cases, an Aquifer Protection Permit issued by the Arizona Department of Environmental Quality, Arizona Pollution Discharge Elimination System permits from the Arizona Department of Environmental Quality, and an air quality permit from Maricopa or Pinal Counties. The provision of potable water is subject to, among others, the requirements of the federal Safe Drinking Water Act, and effluent from wastewater treatment facilities must comply with other requirements. Regulated contaminants and associated maximum contaminant levels may change over time, requiring us to alter or build additional treatment facilities.

Our ability to expand into new service areas and to expand current water and wastewater service depends on approval from regulatory agencies. Failure to obtain required regulatory approvals will adversely affect future growth.

In Arizona, the ACC is the regulatory authority that oversees the formation, expansion, and ongoing operations of water and wastewater utilities. The ACC has authority, among other things, to determine service areas for utility providers. In order for our owned utilities to provide water or wastewater service, they must obtain a CC&N for a service area before they can service that area. In addition, our owned utilities and/or the developments that we serve must demonstrate to the Arizona Department of Water Resources that there exists a 100-year water supply and obtain either a “Certificate of Assured Water Supply,” which is a certificate issued by the Arizona Department of Water Resources evidencing sufficient groundwater, surface water, or effluent of adequate quality will be continuously available to satisfy the water needs of the proposed use for at least one hundred years and which applies to a specific subdivision, or a Designation of Assured Water Supply, which applies to the utility’s entire service area. The designation area is coterminous with the CC&N. Further, our wastewater facilities require Arizona Department of Environmental Quality and/or EPA permits that regulate, among other things, the level of discharges from our facilities, the size of our facilities, and the location of our facilities. Any inability to obtain the necessary regulatory approvals, assured water supplies, or environmental permits would limit our ability to expand our water or wastewater service areas.

If we chose to expand to states other than Arizona, we may have difficulty acquiring the necessary approvals and permits or complying with environmental, health and safety, or quality standards of such states. See “—Doing business in jurisdictions other than Arizona may present unforeseen regulatory, legal, and operational challenges that could impede or delay our operations or adversely affect our profitability.”

Operational Factors

There is no guaranteed source of water.

Our ability to meet the existing and future water demands of our customers depends on an adequate supply of water. Regulatory restrictions on the use of groundwater and the development of groundwater wells, lack of available water rights, drought, overuse of local or regional sources of water, protection of threatened species or habitats, or other factors, including climate change, may limit the availability of ground or surface water.

As stated above, our primary source of water is pumping of groundwater from aquifers within service areas. In the event that our wells cannot meet customer demand, we can purchase water from surrounding municipalities, agencies, and other utilities. However, the cost of purchasing water is typically more expensive than producing it. Furthermore, these alternative sources may not always have an adequate supply to sell to us.

To date, we have been able to produce enough water to meet current customer requirements. However, no assurance can be given that we will be able to produce or purchase enough water to fully satisfy future customer demand. We can make no guarantee that we will always have access to an adequate supply of water that will meet all quality standards, or that the cost of water will not adversely affect our operating results.

If we are unable to access adequate water supplies, we may be unable to satisfy all customer demand, which could result in rationing. Rationing may have an adverse effect on cash flow from operations.

Water shortages may affect us in a variety of ways. For example, water shortages could:

- adversely affect water supply mix by causing us to rely on more expensive purchased water;
- adversely affect operating costs;
- increase the risk of contamination to water systems due to the inability to maintain sufficient pressure;

- increase capital expenditures for building pipelines to connect to alternative sources of supply, new wells to replace those that are no longer in service or are otherwise inadequate to meet the needs of customers, and reservoirs and other facilities to conserve or reclaim water; and
- result in regulatory authorities refusing to approve new service areas if an adequate water supply cannot be demonstrated and restrictions on new customer connections may be imposed in existing service areas if there is not sufficient water.

We may or may not be able to recover increased operating and construction costs as a result of water shortages on a timely basis, or at all, for our regulated systems through the rate setting process.

We rely on information technology systems to assist with the management of our business and customer relationships. A disruption of these systems could adversely affect our business and operations.

Our information technology systems and the information technology functions that are outsourced to the FATHOM™ business, which we previously owned, are an integral part of our business. For example, FATHOM™ systems allow us to read water meters remotely, identify high water usage, and identify water theft from disconnected meters. FATHOM™ systems also provide contracted services and back-office technologies and systems to bill our customers, provide customer service, manage certain financial records, and track assets and accounts receivable collections. A disruption of our information technology systems or the FATHOM™ systems could significantly limit our ability to manage and operate our business efficiently, which in turn could cause our business to suffer and cause our results of operations to be reduced.

Further, our information technology systems and the FATHOM™ systems are vulnerable to damage or interruption from:

- power loss, computer systems failures, and internet, telecommunications, or data network failures;
- operator negligence or improper operation by, or supervision of, employees;
- physical and electronic loss of customer data or security breaches, misappropriation, and similar events;
- computer viruses;
- intentional acts of vandalism and similar events; and
- fires, floods, earthquakes, and other natural disasters.

Damages or interruptions to our information technology systems or the FATHOM™ systems may result in physical and electronic loss of customer or financial data, security breaches, misappropriation, and similar events. These issues could prevent us from issuing billings timely, which could impact revenue, or could negatively impact the efficient operations of the business, resulting in additional costs. The lack of redundancy for some of our IT systems or the FATHOM™ systems, including billing systems, could exacerbate the impact of any of the foregoing events.

If future acquisitions do not achieve sufficient profitability relative to expenses and investment, our business and ability to finance our operations could be materially adversely affected.

A typical element of a utility growth strategy is the acquisition or development of other water and wastewater utilities. The potential negotiation of future acquisitions and development of new projects could require us to incur significant costs and expose us to significant risks, including:

- risks relating to the condition of assets acquired and exposure to residual liabilities of prior businesses;
- operating risks, including equipment, technology and supply problems, regulatory requirements, and approvals necessary for acquisitions;
- risks that potential acquisitions may require the disproportionate attention of our senior management, which could distract them from the management of our existing business;
- risks related to our ability to retain experienced personnel of the acquired company; and
- risks that certain acquisitions may require regulatory approvals, which could be refused or delayed and which could result in unforeseen regulatory expenses or unfavorable regulatory conditions.

These issues could have a material adverse effect on our business and our ability to finance our operations. The businesses and other assets we acquire in the future may not achieve sufficient revenue or profitability to justify our investment, and any difficulties we may encounter in the integration process could interfere with our operations and reduce operating margins. Acquisitions could also result in dilutive issuance of our equity securities, incurrence of debt and contingent liabilities, and fluctuations in quarterly results and expenses.

If we do not manage our anticipated growth effectively, we may not be able to develop or implement the infrastructure necessary to support our operations and could suffer a loss of profitability.

Since our formation in 2003, we have grown rapidly, with our total revenues increasing from \$4.9 million in 2004 to \$31.2 million in 2017 and total service connections increasing from 8,113 as of December 31, 2004 to 39,618 as of December 31, 2017. We have also expanded geographically, from 18 square miles of service areas in 2004 to 336 square miles as of December 31, 2017. Our growth has been driven principally by acquisitions and by organic growth resulting from increased development and service connections within our existing service areas.

Although we may not be able to achieve similar growth, or grow at all, in future periods, we expect to continue to significantly expand our facilities, infrastructure, marketing, testing, management, and administrative operations, as well as our financial and accounting controls. This expansion has placed, and will continue to place, strain on our management and administrative, operational, technical, and financial infrastructure. If management is unable to manage growth effectively, the quality of our services, our ability to attract and retain key personnel, and our business or prospects could be harmed significantly.

To manage growth effectively, we must:

- continue to expand our water management capacity;
- retain key management and augment our management team;
- continue to enhance our technology, operations, and financial and management systems;
- manage multiple relationships with our customers, regulators, suppliers, and other third parties; and
- expand, train, and manage our employee base.

We may not be able to manage effectively any expansion in one or more of these areas, and our failure to do so could harm our ability to maintain or increase revenues and operating results. The expenses incurred in pursuing growth could increase without a corresponding increase in our revenue base, which could decrease operating results and profit margin. In addition, future growth may require us to make significant capital expenditures or incur other significant expenses and may divert the attention of our personnel from our core business operations, any of which could affect our financial performance adversely.

The nature of our business exposes us to various liability claims, which may exceed the level of our insurance coverage and thereby not be reimbursed fully by insurance proceeds, or not be covered by our insurance at all, and may also make it difficult for us to obtain insurance coverage at affordable rates.

In recent years, societal factors have resulted in increased litigation and escalating monetary claims against industries and employers. Although the national insurance market currently provides insurance coverage at affordable premiums, there is no guarantee this will continue or that we will continue to be able to obtain coverage against catastrophic claims and losses. While we may self-insure for some risks in the future, should an uninsured or underinsured loss occur, we may be unable to meet our obligations as they become due.

The operation of our utilities is subject to the normal risks of occupancy as well as the additional risks of receiving, processing, treating, and disposing of water and waste materials. As a safeguard, we currently maintain general liability and workers' compensation insurance coverage, subject to deductibles at levels we believe are sufficient to cover future claims made during the respective policy periods. However, we may be exposed to multiple claims, including workers' compensation claims, that do not exceed our deductibles, and, as a result, we could incur significant out-of-pocket costs that could materially adversely affect our business, financial condition, and results of operations. In addition, the cost of insurance policies may increase significantly upon renewal of those policies as a result of general rate increases for the type of insurance we carry as well as our historical experience and experience in our industry. Our future claims may exceed the coverage level of our insurance, and insurance may not continue to be available on economically reasonable terms, or at all. If we are required to pay significantly higher premiums for insurance, are not able to maintain insurance coverage at affordable rates, or if we must pay amounts in excess of claims covered by our insurance, we could experience higher costs that could materially adversely affect our business, financial condition, and results of operations.

We are exposed to various risks relating to legal proceedings or claims that could materially adversely affect our operating results.

We are a party to lawsuits in the normal course of our business. Litigation in general can be expensive, lengthy, and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. Responding to lawsuits brought against us, or legal actions that we may initiate, can often be expensive and time-consuming. Unfavorable outcomes from these claims and/or lawsuits could materially adversely affect our business, results of operations, and financial condition, and we could incur substantial monetary liability and/or be required to change our business practices.

Operating costs, construction costs, and costs of providing services may rise faster than revenue.

The ability to increase rates over time is dependent upon approval of rate increases by utility regulators, which may be inclined, for political or other reasons, to limit rate increases. However, our costs are subject to market conditions and other factors, and may increase significantly. The second largest component of our operating costs after water production is made up of salaries and wages. These costs are affected by the local supply and demand for qualified labor. Other large components of our costs are general insurance, workers' compensation insurance, employee benefits, and health insurance costs. These costs may increase disproportionately to rate increases authorized by utility regulators and may have a material adverse effect on our financial condition and results of operations.

Increased operating expenses associated with the expansion of our business may negatively impact our operating income.

Increased operating expenses associated with any expansion of our business may negatively impact our income as we, among other things:

- seek to acquire new utilities and service areas;
- expand geographically in and outside of Arizona;
- make significant capital expenditures to support our ability to provide services in our existing service areas;
- fund development costs for our system and technology; and
- incur increased general and administrative expenses as we grow.

As a result of these factors, we may not sustain or increase our profitability on an ongoing basis.

Inadequate water and wastewater supplies could have a material adverse effect upon our ability to achieve the customer growth necessary to increase our revenues.

In many areas of Arizona (including certain areas that we service), water supplies are limited and, in some cases, current usage rates exceed sustainable levels for certain water resources. As discussed above, we currently rely predominantly (and are likely to continue to rely) on the pumping of groundwater and the generation and delivery of recycled water for non-potable uses to meet future demands in our service areas. At present, groundwater (and recycled water derived from groundwater) is the primary water supply available to us.

We do not currently anticipate any short-term concerns with physical, legal, or continuous availability issues in our service areas. Regardless, the supply of groundwater in Central Arizona, while considerable, is also ultimately finite, closely regulated, and geographically limited. In areas where we have not applied for a "Designation of Assured Water Supply," which is a decision and order issued by the director of the Arizona Department of Water Resources designating a private water company provider as having an adequate water supply, we have not performed hydrological studies or modeling to evaluate the amount of groundwater likely to be available to meet present and expected future demands. Insofar as we intend to rely on the pumping of groundwater and the generation and delivery of recycled water to meet future demands in our current service areas, our ability and/or the ability of developers inside of our service areas to meet regulatory requirements and to demonstrate assured and adequate water supplies is essential to the continued growth of our service connections and our capacity to supply water to our customers.

Insufficient availability of water or wastewater treatment capacity could materially and adversely affect our ability to provide for expected customer growth necessary to increase revenues. We continuously look for new sources of water to augment our reserves in our service areas, but have not yet obtained surface water rights. Our ability to obtain such rights may depend on factors beyond our control, such as the future availability of Colorado River water supplies. We also plan to construct facilities and obtain the necessary permits to recharge recycled water to stretch and augment our existing and planned future water supplies, but do not yet have this capability in all of our service areas. As a result, it is possible that, in the future, we will not be able to obtain sufficient water or water supplies to increase customer growth necessary to increase or even maintain our revenues.

We may have difficulty accomplishing our growth strategy within and outside of our current service areas. This would cause us to rely more heavily on regulatory rate increases to increase our revenues.

Our ability to expand our business, both within our current service areas and into new areas, involves significant risks, including, but not limited to:

- not receiving or maintaining necessary regulatory permits, licenses, or approvals;
- downturns in economic or population growth and development in our service areas;
- risks related to planning and commencing new operations, including inaccurate assessment of the demand for water, engineering and construction difficulties, and inability to begin operations as scheduled;
- droughts or water shortages that could increase water conservation efforts to a point that materially reduces revenue;
- regulatory restrictions or other factors that could adversely affect our access to sources of water supply;
- our potential inability to identify suitable acquisition opportunities or to form the relationships with developers and municipalities necessary to form strategic partnerships; and
- barriers to entry presented by existing water utilities in prospective service areas.

If we are unable to execute our growth strategy effectively, we will need to rely more heavily on regulatory rate increases to increase our revenue.

We may have difficulty recruiting and retaining qualified personnel, and due to the technical and specialized nature of our business, our profitability may suffer if we do not have the necessary workforce.

Our plants require some of our employees to be certified operators of record, a designation requiring specialized training and certification in water and wastewater systems. As workers with these qualifications retire in the industry, we may be unable to replace them readily in view of the relatively low number of younger workers that we believe are entering the workforce to pursue this line of work. Our operations require a variety of other technical skills and specialties in the areas of engineering, systems analysis, laboratory work, and equipment repair, and we may have difficulty recruiting and retaining personnel with these skills. If we cannot maintain an employee base with the skills necessary to conduct our operations, our efficiency, margins, and ability to expand our business could be adversely affected.

Any disruption or problem at our facilities could increase our expenses.

A natural disaster (such as an earthquake, fire, or flood) or an act of terrorism could cause substantial delays in our operations, damage or destroy our equipment or facilities, and cause us to incur additional expenses and lose revenue. The insurance we maintain against natural disasters may not be adequate to cover our losses in any particular case, which would require us to expend significant resources to replace any destroyed assets, thereby materially and adversely affecting our financial condition and prospects.

We face risks associated with the design, construction, and operation of our systems that may adversely affect our business and financial condition.

We are responsible for the design, construction, installation, and maintenance of our water treatment, reclamation, and distribution systems. We could be adversely affected by a failure to complete our construction projects on time or on budget, and a substantial delay in the progress of construction due to adverse weather, work stoppages, shortages of materials, non-issuances of permits, nonperformance of suppliers or contractors, or other factors could result in a material increase in the overall cost of such projects.

We cannot guarantee that our systems will operate as designed or be free from defects. The failure of our systems to operate properly could cause significant public harm. Any defects in our systems or significant reliability, quality, or performance problems with respect to our systems or services could have a number of negative effects on our profitability, results of operations, liquidity, and cash flows, including:

- loss of revenues;
- diversion of management and development resources and the attention of engineering personnel;
- significant customer relations problems;
- increased repair, support, and insurance expenses;
- adverse regulatory actions; and
- legal actions for damages by our customers, including but not limited to damages based on commercial losses and effects on human health.

Any failure of our network of water and wastewater pipes and water reservoirs could result in losses and damages that may affect our financial condition and reputation.

Our utilities distribute water and collect wastewater through an extensive network of pipes and store water in reservoirs located across our service areas. A failure of major pipes or reservoirs could result in injuries and property damage for which we may be liable. The failure of major pipes and reservoirs may also result in the need to shut down some facilities or parts of our network in order to conduct repairs. Any failures and shutdowns may limit our ability to supply water in sufficient quantities to customers and to meet the water and wastewater delivery requirements prescribed by applicable utility regulators, which would adversely affect our financial condition, results of operations, cash flow, liquidity, and reputation.

Risks associated with the collection, treatment, and disposal of wastewater and the operation of water utilities may impose significant costs that may not be covered by insurance, which could result in increased insurance premiums.

The wastewater collection, treatment, and disposal operations of our utilities are subject to substantial regulation and involve significant environmental risks. If collection or sewage systems fail, overflow, or do not operate properly, untreated wastewater or other contaminants could spill onto nearby properties or into nearby streams and rivers, potentially causing damage to persons or property, injury to the environment including aquatic life, and economic damages, which may not be recoverable in rates. This risk is most acute during periods of substantial rainfall or flooding, which are the main causes of sewer overflow and system failure. Liabilities resulting from such damage could adversely and materially affect our business, results of operations, and financial condition. Moreover, in the event that we are deemed liable for any damage caused by overflow, losses might not be covered by insurance policies, and such losses may make it difficult to secure insurance in the future at acceptable insurance premium rates. Similarly, any related business interruption or other losses might not be covered by insurance policies, which would also make it difficult for us to secure insurance in the future at acceptable insurance premium rates.

We may also incur liabilities under environmental laws and regulations requiring investigations and cleanup of environmental contamination at our properties or at off-site locations where there have been adverse environmental impacts. The discovery of previously unknown conditions, or the imposition of cleanup obligations in the future, could result in significant costs, and could adversely affect our financial condition, results of operations, cash flow, and liquidity. Such remediation losses may not be covered by insurance policies and may make it difficult for us to secure insurance in the future at acceptable insurance premium rates.

Contamination of the water supplied by us may result in disruption in our services, loss of credibility, lower demand for our services, and potential liability that could adversely affect our business and financial condition.

Our water supplies are subject to contamination, including contamination from compounds, chemicals in groundwater systems, pollution resulting from man-made sources (such as perchlorate and methyl tertiary butyl ether), and possible biological terrorist attacks. Contamination of water sources can lead to human death and illness, damage to natural resources and other parts of the environment, and cause other harms. Among other things, if we are found to be liable for consequences of water contamination arising out of human exposure to hazardous substances in our water supplies or other damage, we would be subject to civil or criminal enforcement actions, litigation, and other proceedings or clean up obligations. Further, our insurance policies may not apply or be sufficient to cover the costs of these claims, which could be significant.

Cleaning up water sources can be very expensive and if we are required to do so, it could have a material and adverse effect on our business, operating results, and financial condition. In the event that our water supply is contaminated, we may have to interrupt or stop the use of that water supply until we are able to treat the water or to substitute the supply of water from another water source, including, in some cases, through the purchase of water from a supplier. We may incur significant costs in order to warn consumers and to treat the contaminated source through expansion of current treatment facilities or development of new treatment methods. Using a new water source is generally associated with increased costs compared to an existing water source and, as indicated above, purchasing water is typically more expensive than obtaining the water from other means. If we are unable to treat or substitute our water supply in a cost-effective manner, our financial condition, results of operations, cash flow, liquidity, and reputation may be adversely affected. We may not be able to recover costs associated with treating contaminated water or developing new sources of supply through the rate setting process or through insurance.

We depend on an adequate supply of electricity and chemicals for the delivery of our water, and an interruption in the supply of these inputs or increases in their prices could adversely affect our results of operations.

We rely on purchased electrical power to operate the wells and pumps that are needed in order to supply potable and recycled water to our customers. An extended interruption in power supply that we cannot remediate through the use of backup generators could adversely affect our ability to continue these operations. Electrical power, which represented approximately 6.4% of our total operating expenses in fiscal year 2017, is a significant and potentially volatile operating expense. Electrical power costs are

beyond our control and can increase unpredictably in substantial amounts. Under these circumstances, our cash flows between our general rate case filings and our earnings may be adversely affected until the ACC has authorized a rate increase.

In addition, we require bulk supplies of chemicals for water and wastewater treatment, and if we were to suffer an interruption of supply that we cannot replace quickly, we might not be able to perform these functions adequately. Some chemicals are available from a single source or a limited number of sources. There is no assurance that these suppliers will continue to produce the chemicals in the quantities and quality and at the times they are needed. Moreover, the replacement of any of these suppliers could lead to significant delays and increase in our costs. Chemical costs represented approximately 1.7% of our total operating expenses in fiscal year 2017.

We are subject to environmental risks that may subject us to clean-up costs or litigation that could adversely affect our business, operating results, financial condition, and prospects.

Under various federal and state environmental laws, regulations, ordinances, and other requirements, a current or previous owner or operator of real property or a facility may be liable for the costs of removal, remediation, or containment of hazardous or toxic substances on, under, in, or released from such property. These liabilities are not limited to a potential effect on our water supply and include, but are not limited to, liabilities associated with air, soil, or groundwater contamination at any real estate or facilities we own or operate, including liabilities assumed in an acquisition of another utility. Environmental laws often impose liability regardless of whether the owner or operator knew of or was responsible for the presence of the hazardous or toxic substances. Although we currently conduct environmental screening assessments on new properties that we propose to acquire or use to identify significant sources of contaminants on surrounding properties, these assessments are not comprehensive, nor have they been conducted for all of the property owned or used by us. As a result, hazardous or toxic substances may exist at properties owned or used by us. If hazardous or toxic substances are discovered at real property or facilities owned or used by us (including a landfill owned by another party that is used by us for disposal of hazardous substances), we could incur significant remediation costs, liability exposure, or litigation expenses that could adversely affect our profitability, results of operations, liquidity, and cash flows.

We are subject to industrial risks that could adversely affect our results of operations.

The operations of our water and wastewater treatment plants involve physical, chemical, and biological processes and the use of pumps, generators, and other industrial equipment. As a result, our operations are subject to various industrial risks, including chemical spills, discharges or releases of toxic or hazardous substances or gases, effects resulting from confined operating spaces, fires, explosions, mechanical failures, storage tank leaks, and electric shock. These risks can result in personal injury, loss of life, catastrophic damage to or destruction of property and equipment or environmental damage, and related legal proceedings, including those commenced by regulators, neighbors, or others. They may also result in an unanticipated interruption or suspension of our operations and the imposition of liability. The loss or shutdown over an extended period of operations at any of our treatment facilities or any losses relating to these risks could have a material adverse impact on our profitability, results of operations, liquidity, and cash flows.

Market and Financial Factors

Our operations of regulated utilities are currently located exclusively in the state of Arizona, and more specifically approximately 98.8% of our active service connections are within a single municipality, which increases the impact of local conditions on our results of operations.

The customers of our regulated utilities are currently located exclusively in the state of Arizona and 98.8% of our active service connections are located in the City of Maricopa, Arizona. As a result, we cannot diversify or mitigate the risks presented by local regulatory, economic, political, demographic, and weather conditions in this area. An adverse change in any of these conditions would therefore affect our profitability, results of operations, liquidity, and cash flows more significantly than if our utilities also operated in other geographic areas.

Our existing indebtedness could affect our business adversely and limit our ability to plan for or respond to growth opportunities, and we may be unable to generate sufficient cash flow to satisfy our liquidity needs.

As of December 31, 2017, we had total indebtedness of \$115.1 million. In addition, we may incur substantial additional indebtedness in the future. Our indebtedness could have important consequences, including:

- limiting our ability to obtain future additional financing we may need to fund future working capital, capital expenditures, acquisitions, or other corporate requirements; and

- limiting, by the financial and other restrictive covenants in our debt agreements, our ability to borrow additional funds and to pay dividends.

Our ability to incur significant future indebtedness will depend in part on our ability to generate cash flow. This ability is affected by general economic, financial, competitive, legislative, regulatory, and other factors that are beyond our control. If our business does not generate sufficient cash flow from operations or if we are unable to borrow money or otherwise generate funds sufficient to enable us to fund our liquidity needs, we may be unable to plan for or respond to growth opportunities, which could adversely affect our operating results and business prospects.

We do not control when and where a developer may request service within our service areas, and if this occurs outside the location and capacity of existing infrastructure, it may require significantly more capital expenditures than currently anticipated.

If a developer has an ICFA, and/or once a developer has entered into a service agreement with our utility subsidiary and the property being developed has been included within a service area, we have the obligation to serve under the terms of those agreements and existing regulations. Although we have built substantial modern infrastructure within these utilities in areas where development is currently occurring, there is the potential that a developer may request service in another location within the service area. Extending/expanding the existing infrastructure to provide service may result in the need to make additional, currently unplanned, capital improvements and there is no guarantee that we may recover our costs timely. As a result, our return on our investment and cash flow stream could be adversely affected.

Foreclosure rates in our service areas, as well as other factors affecting real estate development, could affect the growth of our regulated customer base or result in a decline in our revenue.

A slowdown or severe downturn in the housing market could have an adverse effect on our operating results and financial condition. During periods of economic distress, there may be an increase in home foreclosures and vacancies. For example, during the economic downturn beginning in 2008, our utilities experienced an increase in the number of vacant homes, reaching a peak of 4,020 vacant connections as of February 28, 2009, approximately 11.9% of our total connections at the time. Accordingly, in the event of an economic downturn, we may experience a material reduction in revenues. Although the U.S. economy and housing market continue to perform well, we cannot predict the overall trajectory of the market. Our growth depends significantly on increased residential and commercial development in our service areas, and if developers or builders are unable to complete additional residential and commercial projects, our revenue may decline.

Our water and wastewater systems are subject to condemnation by governmental authorities, which may result in the receipt of less than the fair market value of our assets and a loss of revenue from our operations.

Municipalities and other governmental subdivisions have historically been involved in the provision of water and wastewater services, and efforts may arise from time to time to convert some or all of our assets to public ownership and operation. Arizona law provides for the acquisition of public utility property by governmental agencies through their power of eminent domain, also known as condemnation. Should a municipality or other governmental subdivision seek to acquire some or all of our assets through eminent domain, we would likely resist the acquisition.

Contesting an exercise of condemnation through eminent domain may result in costly legal proceedings and may divert the attention of our management from the operation of our business. Moreover, our efforts to resist any such condemnation may not be successful.

If a municipality or other governmental subdivision succeeds in acquiring some or all of our assets through eminent domain, there is a risk that we will not receive adequate compensation for such assets and that we will incur significant one-time charges. Condemnation also results in a loss of revenue from the operations of the affected utility.

The assets of our former utility subsidiaries, Cave Creek Water Co. and Valencia Water Company, were acquired from us by municipalities pursuant to condemnation proceedings, and our other utility subsidiaries could be subjects of such proceedings in the future.

We face competition for new service areas and acquisition targets.

We face competition from other water and wastewater utilities for new service areas and with respect to acquisitions of smaller utilities. These competitors consist primarily of municipalities and investor-owned utilities seeking expansion opportunities. Some of our competitors are larger than we are and have more resources and access to capital than we do. If we are unable to compete effectively for new service areas and acquisitions of existing utilities, our ability to increase our rate base and revenue could be adversely affected.

Our growth depends significantly on increased residential and commercial development in our service areas, and if developers or builders are unable to complete additional residential and commercial projects, our revenue may not increase.

The growth of our customer base depends almost entirely on the success of developers in developing residential and commercial properties within our Certificate of Convenience and Necessity (“CC&N”) areas. A CC&N is a permit issued by the ACC allowing a public service corporation to serve a specified area, and preventing other public service corporations from offering the same services within the specified area, which we refer to as “service areas.” Real estate development is a cyclical industry and the growth rate of development, especially residential development, since 2006, both nationally and in Arizona has been below historical rates. The sale of, for instance, single family residences is affected by a number of national and regional economic factors, including:

- interest rates and general levels of economic output;
- levels of activity in the local real estate market;
- the state of domestic credit markets, mortgage standards, and availability of credit;
- competition from other builders and other projects in the area and other states;
- federal programs to assist home purchasers;
- costs and availability of labor and materials;
- government regulations affecting land development, homebuilding, and mortgage financing;
- availability of financing for development and for home purchasers;
- changes in the income tax treatment of real property ownership;
- unexpected increases in development costs;
- increased commute times and fuel costs that may adversely affect the desirability of outlying suburbs;
- availability of, among other things, other utilities, adequate transportation, and school facilities; and
- environmental problems with such land.

While many developers presently hold necessary zoning approvals, land development within our service areas could also be affected by changes in governmental policies, including, but not limited to, governmental policies to restrict or control development. This may include, for example, actions by the local school districts to restrict admissions to local schools because of inadequate classroom space or, because of other problems, such as failure by local municipalities to approve plats for the development. An increase in current residential foreclosure rates or a deep or prolonged slowdown of the development process and the related absorption rate within the various developments in our service areas because of any or all of the foregoing could materially and adversely affect growth of our customer base and the generation of revenue.

Many national builders and developers in our service areas own or control substantial amounts of the developable land in these areas. There can be no assurance that these builders and developers have the financial capability to continue and complete their developments.

We will need additional capital to grow our business, and additional financing may not be available to us on favorable terms when required, or at all.

Adequate funds to support our growth may not be available when needed or on terms acceptable to us. We may need to raise additional funds to support more rapid expansion, improve our facilities and infrastructure, develop new and enhanced technologies, or respond to evolving regulatory standards. We may experience difficulty in raising the necessary capital due to volatility in the capital markets or increases in the cost of infrastructure finance. Increasingly stringent bond rating standards could make it more difficult for us to finance our growth by issuing tax-exempt bonds as we have in the past. In addition, we require regulatory approval from the ACC for some means of raising capital, such as issuance of debt by our regulated utilities, and approval may be denied or delayed. If adequate funds are not available or are not available on acceptable terms, we may not be able to take advantage of expansion opportunities, make the capital expenditures necessary to support our growth, or otherwise execute our strategic plan.

Doing business in jurisdictions other than Arizona may present unforeseen regulatory, legal, and operational challenges that could impede or delay our operations or adversely affect our profitability.

We may decide to pursue growth opportunities in states other than Arizona. Other states may present substantially different regulatory frameworks, and we may have difficulty acquiring the necessary approvals and permits or complying with environmental, health and safety, or quality standards. In addition, it may become more costly or difficult for us to comply with a multitude of standards and requirements across multiple states.

Other states may also expose us to new legal precedents, condemnation risks, and liability concerns based on state legislation or case law.

Our cost structure in other states may be significantly different than our current cost structure due to regional differences. For example, our cost structure may be significantly impacted by differences in labor and energy costs in other markets and the significant portion of overall production costs that they represent.

Our utilities business is subject to seasonal fluctuations and other weather-related conditions, such as droughts, which could adversely affect the supply of and demand for our services and our results of operations.

We depend on an adequate water supply to meet the present and future needs of our customers. Whether we have an adequate water supply depends upon a variety of factors, including underground water supply from which groundwater is pumped, the rate at which it is recharged by rainfall and snowpack, and changes in the amount of water used by our customers. In particular, the arid western U.S. region, which includes our present and potential service areas, has been required to deal with general conditions of water scarcity exacerbated by extended periods of drought.

Drought conditions could interfere with our sources of water supply and could adversely affect our ability to supply water in sufficient quantities to our existing and future customers. For example, our utilities have acted in the past as interim operators for several smaller troubled water systems, at the request of the ACC. In one such instance, the onsite well, which was the single source of water, ran dry due to aquifer decline. As a result, we were forced to haul water to the system for several years at a considerable cost. Any future interruption to our water supply or restrictions on water usage during drought conditions or other legal limitations on water use could result in decreased customer billing and lower revenues or higher expenses that we would not be able to recoup without prior regulatory approval for a rate increase, which may not be granted. These conditions could also lead to increases in capital expenditures needed to build infrastructure to secure alternative water sources. Furthermore, customers may use less water even after a drought has ended because of conservation patterns developed during the drought. Population growth could also decline under drought conditions as individuals and businesses move out of the area or elect not to relocate there. Lower water use for any reason could lead to lower revenue.

Demand for water is seasonal and varies with temperature and rainfall levels. If temperatures during the typically warmer months are cooler than normal, or if there is more rainfall than normal, the demand for our water may decrease, which would adversely affect our profitability, results of operations, liquidity, and cash flows. Consequently, the results of operations for one quarter are not necessarily indicative of results for future quarters or the full year.

We are subject to adverse publicity and reputational risks, which make us vulnerable to negative customer perception and could lead to increased regulatory oversight or other sanctions.

Water and wastewater utilities, including Palo Verde and Santa Cruz, have large customer bases and as a result are exposed to public criticism regarding, among other things, the reliability of their water and wastewater services, the quality of water provided, the timeliness and accuracy of bills that are provided for such services, and the quality of customer service. Adverse publicity and negative customer sentiment may render regulators and government officials less likely to view us in a favorable light, and may cause us to be susceptible to less favorable regulatory outcomes, as well as increased regulatory oversight, lower rates, and more stringent regulatory requirements. Unfavorable regulatory outcomes may include the enactment of more stringent laws and regulations governing our operations, as well as fines, penalties or other sanctions or requirements. The imposition of any of the foregoing could have a material adverse impact on our business, financial condition, results of operations and cash flows.

If the general public perceives recycled water to be unsafe, we will have difficulty executing our business plan and could face a loss of revenue.

Our Total Water Management model emphasizes the maximum use of recycled water for non-potable purposes. To implement this model, we cultivate relationships with developers, municipalities, and members of the communities we serve and focus on educating them regarding the benefits and safety of recycled water. If the recycled water supplied to customers is contaminated, either as a result of terrorism, system failure, pipeline, or other causes, public perception regarding the safety of recycled water would likely

suffer, regardless of whether we are at fault and potentially even if the contaminated water was supplied by another person. For example, if groundwater contamination occurs as a result of discharge of “gray water” (e.g., used sink or laundry water) into the aquifer, the public could confuse that with recycled water and attribute environmental harm to our system. Public perception of an unsafe water supply would harm our business, particularly with respect to our ability to implement water recycling as a key element of our business strategy.

Risks Related to the Ownership of Our Common Stock

The concentration of our stock ownership with our officers, directors, certain stockholders, and their affiliates will limit your ability to influence corporate matters.

Our directors, executive officers, and stockholders holding more than 5% of our capital stock and their affiliates beneficially own, in the aggregate, approximately 59% of our outstanding common stock, including 49% held by our director, William S. Levine. As a result, these stockholders are able to exercise significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, such as a merger or other sale of us or our assets. This concentration of ownership could limit your ability to influence corporate matters and may have the effect of delaying or preventing a third party from acquiring control over us. There can be no assurance that their interests will not conflict with the interests of our other stockholders.

Our common stock may be volatile or may decline regardless of our operating performance, and you may not be able to resell your shares at or above your purchase price.

The market price for our common stock is likely to be volatile, in part because our shares recently began trading publicly. Many factors, which are outside our control, may cause the market price of our common stock to fluctuate significantly, including those described elsewhere in this “Risk Factors” section, as well as the following:

- our operating and financial performance and prospects;
- our quarterly or annual earnings or those of other companies in our industry compared to market expectations;
- conditions that impact demand for our services;
- future announcements concerning our business or our competitors’ businesses;
- the public’s reaction to our press releases, other public announcements, and filings with the SEC;
- the size of our public float;
- coverage by or changes in financial estimates by investment analysts or failure to meet their expectations;
- the market’s reaction to our reduced disclosure as a result of being an “emerging growth company” under the Jumpstart Our Business Startups Act (the “JOBS Act”);
- market and industry perception of our success, or lack thereof, in pursuing our growth strategy;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- changes in laws or regulations which adversely affect our industry or us;
- changes in accounting standards, policies, guidance, interpretations, or principles;
- changes in senior management or key personnel;
- issuances, exchanges, or sales, or expected issuances, exchanges, or sales of our capital stock;
- changes in our dividend policy;
- adverse resolution of new or pending litigation against us; and
- changes in general market, economic, and political conditions in the U.S., and global economies or financial markets, including those resulting from natural disasters, terrorist attacks, acts of war, and responses to such events.

In addition, stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies in our industry. In the past, stockholders have instituted securities class action litigation following periods of market volatility. If we were involved in securities litigation, we could incur substantial costs and our resources and the attention of management could be diverted from our business.

We incur costs as a result of being a public company in the U.S.

As a public company in the U.S., we incur significant legal, accounting, insurance, and other expenses, including costs associated with U.S. public company reporting requirements. The expenses incurred by U.S. public companies generally for reporting and corporate governance purposes have been increasing. We expect these rules and regulations to increase our legal and financial compliance costs and to make some activities more time-consuming and costly. These laws and regulations could also make it more difficult or costly for us to obtain certain types of insurance, including director and officer liability insurance, and we may be forced to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. Furthermore, if we are unable to satisfy our obligations as a public company, we could be subject to delisting of our common stock, fines, sanctions and other regulatory action, and potentially civil litigation.

Substantial future sales of our common stock, or the perception in the public markets that these sales may occur, may depress our stock price.

Sales of substantial amounts of our common stock in the public market, or the perception that these sales could occur, could adversely affect the price of our common stock and could impair our ability to raise capital through the sale of additional shares.

We have also filed a registration statement registering under the Securities Act of 1933, as amended (the “Securities Act”), the shares of our common stock reserved for issuance in respect of stock options and other incentive awards granted to our officers and certain of our employees. If these officers or employees cause a large number of securities to be sold in the public market, such sales could also reduce the trading price of our common stock and impede our ability to raise future capital.

If our operating and financial performance in any given period does not meet the guidance that we provide to the public or the expectations of investment analysts, our stock price may decline.

We may provide public guidance on our expected operating and financial results for future periods. Any such guidance will be comprised of forward-looking statements subject to the risks and uncertainties described in this Form 10-K and in our other public filings and public statements. Whether or not we provide guidance, investment analysts may publish their estimates of our future financial performance. Our actual results may not always be in line with or exceed any guidance we have provided or the expectations of investment analysts, especially in times of economic uncertainty. If, in the future, our operating or financial results for a particular period do not meet any guidance we provide or the expectations of investment analysts or if we or investment analysts reduce estimates of our performance for future periods, the market price of our common stock may decline.

If investment analysts cease to publish research or reports about our business or if they publish negative evaluations of our common stock, the price of our common stock could decline.

The trading market for our common stock will rely in part on the research and reports that investment analysts publish about us or our business. However, if no or few analysts commence coverage of the Company, the trading price of our stock would likely decrease. Even if we do obtain such analyst coverage, if one or more of the analysts covering our business downgrade their evaluations of our stock, the price of our common stock could decline. If one or more of these analysts cease to cover our common stock, we could lose visibility in the market for our stock, which in turn could cause our common stock price to decline.

Our failure to achieve and maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act as a public company could have a material adverse effect on our business and share price.

We have to comply with Section 404(a) of the Sarbanes-Oxley Act. Section 404(a) of the Sarbanes-Oxley Act requires annual management assessments of the effectiveness of our internal control over financial reporting. Additionally, once we are no longer an emerging growth company, as defined by the JOBS Act, our independent registered public accounting firm will be required pursuant to Section 404(b) of the Sarbanes-Oxley Act to attest to the effectiveness of our internal control over financial reporting on an annual basis. The rules governing the standards that must be met for our management to assess our internal control over financial reporting are complex and require significant documentation, testing, and possible remediation.

Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles. We may encounter problems or delays for any requested improvements and receiving a favorable attestation in connection with the attestation to be provided by our independent registered public accounting firm after we cease to be an emerging growth company. If our independent registered public accounting firm is unable to provide an unqualified attestation report on our internal controls after we cease to be an emerging growth company, investors could lose confidence in our financial information and the price of our common stock could decline.

Additionally, the existence of any material weakness or significant deficiency would require management to devote significant time and incur significant expense to remediate any such material weakness or significant deficiency and management may not be able to remediate any such material weakness or significant deficiency in a timely manner. The existence of any material weakness in our internal control over financial reporting could also result in errors in our financial statements that could require us to restate our financial statements, cause us to fail to meet our reporting obligations, and cause stockholders to lose confidence in our reported financial information, all of which could materially and adversely affect our business and share price.

We cannot assure you that we will pay dividends on our common stock, and our indebtedness could limit our ability to pay dividends on our common stock.

We currently intend to continue to pay a regular monthly dividend on our common stock of \$0.023625 per share (\$0.2835 per share annually), or an aggregate of approximately \$5.6 million on an annual basis. However, our future dividend policy is subject to our compliance with applicable law, and depends on, among other things, our results of operations, financial condition, level of indebtedness, capital requirements, contractual restrictions, restrictions in our debt agreements and in any preferred stock we may issue in the future, business prospects, and other factors that our board of directors may deem relevant. Dividend payments are not mandatory or guaranteed; there can be no assurance that we will continue to pay a dividend in the future.

Taking advantage of the reduced disclosure requirements applicable to emerging growth companies may make our common stock less attractive to investors.

We are an “emerging growth company,” as defined in Section 2(a) of the Securities Act, as modified by the JOBS Act. As such, we are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies including, but not limited to, (i) not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act; (ii) reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements; and (iii) exemptions from the requirements of holding a non-binding advisory vote on executive compensation and of shareholder approval of any golden parachute payments not previously approved. We have elected to adopt these reduced disclosure requirements. We cannot predict if investors will find our common stock less attractive as a result of our taking advantage of these exemptions and as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

In addition, Section 107 of the JOBS Act also provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We are choosing to take advantage of this extended transition provision. See “—Risks Related to the Ownership of Our Common Stock—Our election to take advantage of the JOBS Act extended accounting transition period may make our financial statements more difficult to compare to other public companies.”

We could remain an emerging growth company through 2021 or until the earliest of (i) the last day of the first fiscal year in which our annual gross revenues exceed \$1.07 billion; (ii) the date that we become a “large accelerated filer” as defined in Rule 12b-2 under the Exchange Act, which would occur if the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the last business day of our most recently completed second fiscal quarter; and (iii) the date on which we have issued more than \$1 billion in non-convertible debt securities during the preceding three-year period.

Our election to take advantage of the JOBS Act extended accounting transition period may make our financial statements more difficult to compare to other public companies.

Pursuant to the JOBS Act, as an “emerging growth company,” we must make an election to opt in or opt out of the extended transition period for any new or revised accounting standards that may be issued by the Financial Accounting Standards Board (“FASB”). We have elected to opt in and take advantage of this extended transition provision. This means that, when a standard is issued or revised and it has different application dates for public or private companies, we can, for so long as we are an emerging growth company, adopt the timeline applicable for private companies. This may make comparison of our financial statements with any other public company that is not an emerging growth company (or an emerging growth company that has opted out of using the extended transition provision) difficult or impossible as a result of our use of different accounting standards.

Delaware law, certain provisions in our certificate of incorporation and bylaws, and regulations of the ACC may prevent efforts by our stockholders to change the direction or management of the Company.

We are a Delaware corporation, and the anti-takeover provisions of Delaware law impose various impediments to the ability of a third party to acquire control of us, even if a change of control would be beneficial to our existing stockholders. In addition, our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that may make the acquisition of our company more difficult, including, but not limited to, the following:

- only allowing our board of directors, Chairman of our board of directors, Chief Executive Officer, or President to call special meetings of our stockholders;
- setting forth specific procedures regarding how our stockholders may present proposals or nominate directors for election at stockholder meetings;
- requiring advance notice and duration of ownership requirements for stockholder proposals;
- permitting our board of directors to issue preferred stock without stockholder approval; and
- limiting the rights of stockholders to amend our bylaws.

These provisions could discourage, delay, or prevent a transaction involving a change in control of our company. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors of your choosing and cause us to take other corporate actions you desire. In addition, because our board of directors is responsible for appointing the members of our management team, these provisions could in turn affect any attempt by our stockholders to replace current members of our management team.

Additionally, the ACC must determine that certain types of transactions will not impair our financial status, prevent us from attracting capital at fair and reasonable terms, or impair our ability to provide safe, reasonable, and adequate service. Pursuant to this regulatory mandate, the ACC may impose conditions that could discourage, delay, or prevent a transaction involving a change in control of our company.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The following table lists the properties that we own or lease:

Nature of Property	Location	Operated By	Owned or Leased
Corporate Offices	Phoenix, Arizona	Global Water Resources, Inc.	Leased
Wastewater Treatment Plant	Maricopa, Arizona	Global Water - Palo Verde Utilities Company, LLC	Owned
Global Water Center - Regional Office	Maricopa, Arizona	Global Water - Palo Verde Utilities Company, LLC	Owned
Wastewater Utility Plant	8 Lift Stations - Maricopa, Arizona	Global Water - Palo Verde Utilities Company, LLC	Owned
Water Utility Plant	16 Well Sites - Maricopa, Arizona	Global Water - Santa Cruz Water Company, LLC	Owned
Water Utility Plant	5 Water Distribution Sites - Maricopa, Arizona	Global Water - Santa Cruz Water Company, LLC	Owned
Water Utility Plant	9 sites - Western Maricopa County, Arizona	Water Utility of Greater Tonopah, LLC	Owned
Water Utility Plant	4 sites - Northern Maricopa County, Arizona	Water Utility of Northern Scottsdale, LLC	Owned
Water Utility Plant	Western Maricopa County, Arizona	Eagletail Water Company, L.C.	Owned

We believe that our existing properties are adequate to meet our current needs.

ITEM 3. LEGAL PROCEEDINGS

In the ordinary course of business, we may, from time to time, be subject to various pending and threatened lawsuits in which claims for monetary damages are asserted. To our knowledge, we are not involved in any legal proceeding which is expected to have a material effect on us.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock is listed on the NASDAQ Global Select Market ("NASDAQ") under the symbol "GWRS". Our common stock began trading on the NASDAQ on April 28, 2016. There was no public market for GWRS common stock prior to April 28, 2016.

The following table sets forth, for the quarterly periods indicated, the high and low sales price of our common stock as reported on NASDAQ from April 28, 2016 through December 31, 2017:

	Sales Price	
	High	Low
Fiscal 2017:		
1st Quarter	\$ 9.28	\$ 7.90
2nd Quarter	\$ 9.96	\$ 8.43
3rd Quarter	\$ 10.00	\$ 9.17
4th Quarter	\$ 10.00	\$ 9.00
Fiscal 2016:		
1st Quarter	\$ —	\$ —
2nd Quarter (from April 28, 2016)	\$ 8.97	\$ 6.23
3rd Quarter	\$ 9.18	\$ 7.36
4th Quarter	\$ 9.29	\$ 7.56

Shareholders

As of March 3, 2018, there were approximately 7 shareholders of record of our common stock. Because many shares of our common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these holders of record.

Dividends

For the year ended December 31, 2017, we paid cash dividends to holders of our common stock totaling \$5.4 million, which included: from January 2017 through May 2017, a monthly dividend of \$0.0225 per share; from June 2017 through November 2017, a monthly dividend of \$0.02306 per share; and a monthly dividend of \$0.023625 per share for December 2017.

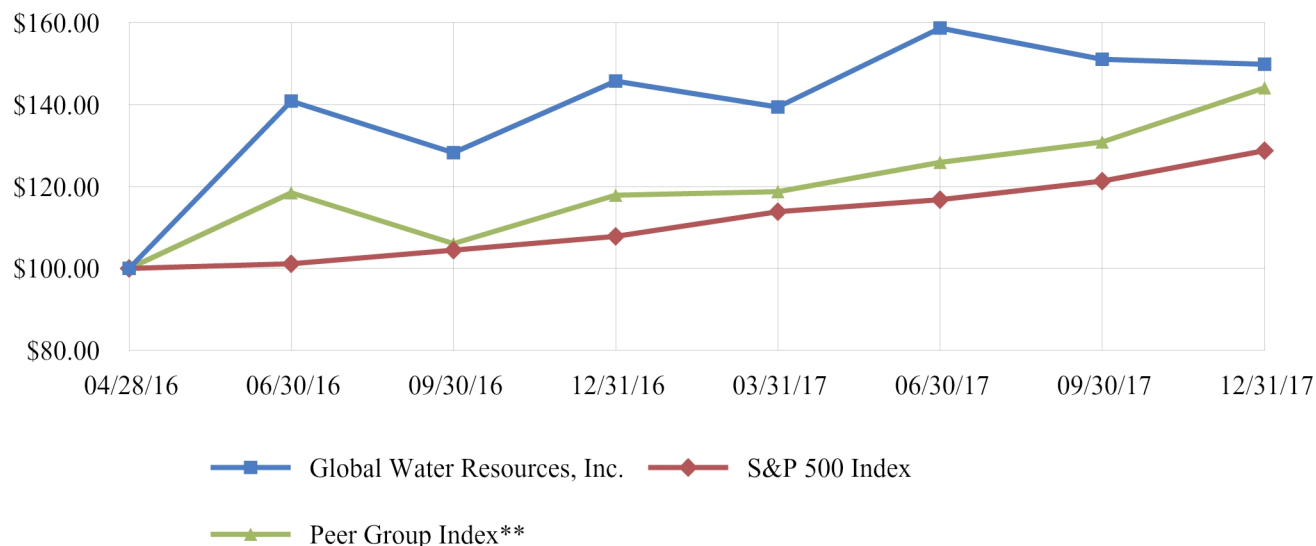
For the year ended December 31, 2016, we paid cash dividends to holders of our common stock totaling \$5.0 million, which included: from January 2016 through April 2016, a monthly dividend of CAD\$0.0283 per share; from May 2016 through June 2016, a monthly dividend of \$0.02 per share; from July 2016 through November 2016, a monthly dividend of \$0.022 per share; and a monthly dividend of \$0.0225 per share for December 2016.

We currently intend to continue to pay a regular monthly dividend of \$0.023625 per share (\$0.2835 per share annually). However, our future dividend policy is subject to our compliance with applicable law, and depending on, among other things, our results of operations, financial condition, level of indebtedness, capital requirements, contractual restrictions, restrictions in our debt agreements and in any preferred stock we may issue in the future, business prospects, and other factors that our board of directors may deem relevant. See "Management's Discussion and Analysis of Results of Operations and Financial Condition – Liquidity and Capital Resources" in Part II, Item 7 of this Form 10-K for a discussion of provisions of our senior secured notes that limit the payment of dividends.

Performance Graph

The following graph compares the relative performance of our common stock, the S&P 500 Index, and our Peer Group Index. This graph covers the period from April 28, 2016 (the first day GWRS common stock began trading on the NASDAQ) through December 31, 2017. The graph assumes that \$100 was invested on April 28, 2016 in the common stock of GWRS, the S&P 500 Index, and our Peer Group Index, and also assumes reinvestment of dividends. The stock price performance on the following graph is not necessarily indicative of future stock price performance.

COMPARISION OF 20 MONTH CUMILATIVE TOTAL RETURN*



* \$100 invested on April 28, 2016 in stock or index, including reinvestment of dividends. Fiscal year ending December 31.

** Peer group includes American States Water Company, American Water Works, Aqua America, Inc., Artesian Resources Corp., California Water, Connecticut Water Service, Inc., Middlesex Water Company, and York Water Co.

	4/28/2016	6/30/2016	9/30/2016	12/31/2016	3/31/2017	6/30/2017	9/30/2017	12/31/2017
Global Water Resources, Inc.	\$ 100.00	\$ 140.84	\$ 128.26	\$ 145.78	\$ 139.44	\$ 158.75	\$ 151.12	\$ 149.91
S&P 500 Index	\$ 100.00	\$ 101.11	\$ 104.45	\$ 107.85	\$ 113.82	\$ 116.75	\$ 121.37	\$ 128.80
Peer Group Index**	\$ 100.00	\$ 118.46	\$ 106.04	\$ 117.88	\$ 118.74	\$ 125.88	\$ 130.86	\$ 144.10

Issuer Purchases of Equity Securities

None.

ITEM 6. SELECTED FINANCIAL DATA

The following table presents selected consolidated financial data, which should be read in conjunction with our consolidated financial statements and related notes and Management's Discussion and Analysis of Financial Condition and Results of Operations included in Part II, Item 7 in this Form 10-K. The table presents the consolidated statements of operations and cash flow data for the years ended December 31, 2017, 2016, and 2015 and the consolidated balance sheet data at December 31, 2017 and 2016, which are derived from our audited consolidated financial statements included elsewhere in this Form 10-K. The table also presents the consolidated statements of operations and cash flow data for the year ended December 31, 2014 and the consolidated balance sheet data at December 31, 2015 and 2014, which were derived from our audited consolidated financial statements that are not included in this Form 10-K.

As the condemnation of Valencia Water Company, Inc. ("Valencia") was completed on July 14, 2015 and the sale of Willow Valley Water Company, Inc. ("Willow Valley") was completed on May 9, 2016, the Company's consolidated balance sheet, consolidated statements of operations, cash flow data, and operating metrics included Valencia and Willow Valley through the respective closing dates.

The following amounts are in thousands, except per share data and operating metrics:

	Year Ended December 31,			
	2017	2016	2015	2014
Consolidated Balance Sheet Data:				
ASSETS:				
Net property, plant, and equipment	\$ 213,459	\$ 200,489	\$ 194,152	\$ 240,424
Current assets	\$ 9,665	\$ 24,740	\$ 18,715	\$ 12,293
Other assets	\$ 15,444	\$ 13,590	\$ 22,875	\$ 52,162
Total Assets	\$ 238,568	\$ 238,819	\$ 235,742	\$ 304,879
LIABILITIES:				
Current liabilities	\$ 8,976	\$ 10,901	\$ 10,663	\$ 13,630
Long-term debt and capital leases	\$ 114,363	\$ 114,317	\$ 102,417	\$ 124,769
Noncurrent liabilities	\$ 100,369	\$ 98,612	\$ 102,599	\$ 138,800
Total Liabilities	\$ 223,708	\$ 223,830	\$ 215,679	\$ 277,199
SHAREHOLDERS' EQUITY	\$ 14,860	\$ 14,989	\$ 20,063	\$ 27,680
Total Liabilities and Shareholders' Equity	\$ 238,568	\$ 238,819	\$ 235,742	\$ 304,879
Consolidated Statements of Operations and Cash Flow Data:				
Revenues	\$ 31,208	\$ 29,799	\$ 31,956	\$ 32,559
Operating expenses	\$ 23,864	\$ 23,987	\$ 25,429	\$ (22,232)
Operating income	\$ 7,344	\$ 5,812	\$ 6,527	\$ 54,791
Total other income (expense)	\$ (3,394)	\$ (9,611)	\$ 35,459	\$ (6,855)
Income (loss) before income taxes	\$ 3,950	\$ (3,799)	\$ 41,986	\$ 47,936
Income tax benefit (expense)	\$ 601	\$ 1,287	\$ (20,623)	\$ 16,995
Net income (loss)	\$ 4,551	\$ (2,512)	\$ 21,363	\$ 64,931
Earnings (loss) per common share:				
Basic	\$ 0.23	\$ (0.13)	\$ 1.17	\$ 3.54
Diluted	\$ 0.23	\$ (0.13)	\$ 1.17	\$ 3.54
Net cash provided by operating activities	\$ 11,156	\$ 1,895	\$ 4,245	\$ 11,646
Cash dividends paid	\$ 5,399	\$ 5,036	\$ 27,607	\$ 3,454
Dividends declared per common share	\$ 0.28	\$ 0.26	\$ 1.43	\$ 0.20
Capital expenditures	\$ 20,885	\$ 8,588	\$ 3,355	\$ 1,655
Operating Metrics:				
Active water connections	19,851	19,013	19,964	26,188
Active wastewater connections	19,146	18,374	17,820	17,380

The balance sheets as of December 31, 2015 and 2014 have been adjusted to reflect the impact of ASU 2015-03, *Interest—Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs*, which required debt issuance costs be presented as a direct deduction from the carrying amount of the associated debt liability. As such, debt issuance costs of \$2.2 million and \$2.7 million have been reclassified from other assets to noncurrent liabilities for the years ended December 31, 2015 and 2014, respectively.

The balance sheet as of December 31, 2016 and the income statement for the year ended December 31, 2016 have been adjusted to reflect an immaterial correction of an error. See Footnote 1 - Description of Business, Basis of Presentation, Corporate Transactions, Significant Accounting Policies, and Recent Accounting Pronouncements, included in Part II, Item 8 of this Form 10-K, for additional information.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following management's discussion and analysis of financial condition and results of operations ("MD&A") should be read in conjunction with the consolidated financial statements and accompanying notes included in Part II, Item 8 of this Form 10-K.

Basis of Presentation

The financial statements of Global Water Resources, Inc. have been prepared in accordance with United States ("U.S.") generally accepted accounting principles ("U.S. GAAP") and, except where otherwise indicated, are presented in U.S. dollars and references to "\$", "US\$", and "dollars" are to U.S. dollars.

Overview

We are a water resource management company that owns, operates, and manages water, wastewater, and recycled water utilities in strategically located communities, principally in metropolitan Phoenix, Arizona. We seek to deploy our integrated approach, which we refer to as "Total Water Management," a term we use to mean managing the entire water cycle by owning and operating the water, wastewater, and recycled water utilities within the same geographic areas in order to both conserve water and maximize its total economic and social value. We use Total Water Management to promote sustainable communities in areas where we expect growth to outpace the existing potable water supply. Our model focuses on the broad issues of water supply and scarcity and applies principles of water conservation through water reclamation and reuse. Our basic premise is that the world's water supply is limited and yet can be stretched significantly through effective planning, the use of recycled water, and by providing individuals and communities resources that promote wise water usage practices.

Business Outlook

2016 and 2017 continued the trend of positive growth in new connections and re-establishing service on existing previously vacant homes. According to the 2010 U.S. Census Data, the Phoenix metropolitan statistical area ("MSA") had a population of 4.2 million and is the 14th largest MSA in the U.S., an increase of 29% over the 3.3 million people reported in the 2000 Census. Metropolitan Phoenix continues to grow due to its low-cost housing, excellent weather, large and growing universities, a diverse employment base, and low taxes. The Employment and Population Statistics Department of the State of Arizona predicts that Phoenix Metro will have a population of 4.9 million people by 2020 and 6.8 million by 2040. During the twelve months ended December 31, 2017, Arizona's employment rate improved by 1.7%, ranking the state in the top 14 nationally for job growth.

Also, according to the W.P. Carey School of Business Greater Phoenix Blue Chip Real Estate Consensus Panel, most sectors of real estate are expected to experience improved occupancy and growth. For Maricopa County and Pinal County combined, the W.P. Carey School of Business, using U.S. Census data, reported that single family housing permits were approximately 18,456 units for 2016.

For 2017, single family dwelling permits were up 12% to 19,863 permits in Maricopa and Pinal Counties combined according to the Home Builders Association of Central Arizona. The forecasts by the Greater Phoenix Blue Chip Real Estate Consensus Panel for 2018 and 2019 remain positive at approximately 24,000 and 27,000 single family dwelling permits, respectively. From there, we believe growth in the region could steadily return towards its normal historical rate of greater than 30,000 single family dwelling permits.

We believe that our utilities and service areas are directly in the anticipated path of growth primarily in the metropolitan Phoenix area. Market data indicates that our service areas currently incorporate a large portion of the final platted lots, partially finished lots, and finished lots in metropolitan Phoenix. Management believes that we are well-positioned to benefit from the near-term growth in metropolitan Phoenix due to the availability of lots and existing infrastructure in place within our services areas.

Factors Affecting our Results of Operations

Our financial condition and results of operations are influenced by a variety of industry-wide factors, including but not limited to:

- population and community growth;
- economic and environmental utility regulation;

- economic environment;
- the need for infrastructure investment;
- production and treatment costs;
- weather and seasonality; and
- access to and quality of water supply.

We are subject to economic regulation by the state regulator, the Arizona Corporation Commission (“ACC”). The U.S. federal and state governments also regulate environmental, health and safety, and water quality matters. We continue to execute on our strategy to optimize and focus the Company in order to provide greater value to our customers and shareholders by aiming to deliver predictable financial results, making prudent capital investments, and focusing our efforts on earning an appropriate rate of return on our investments.

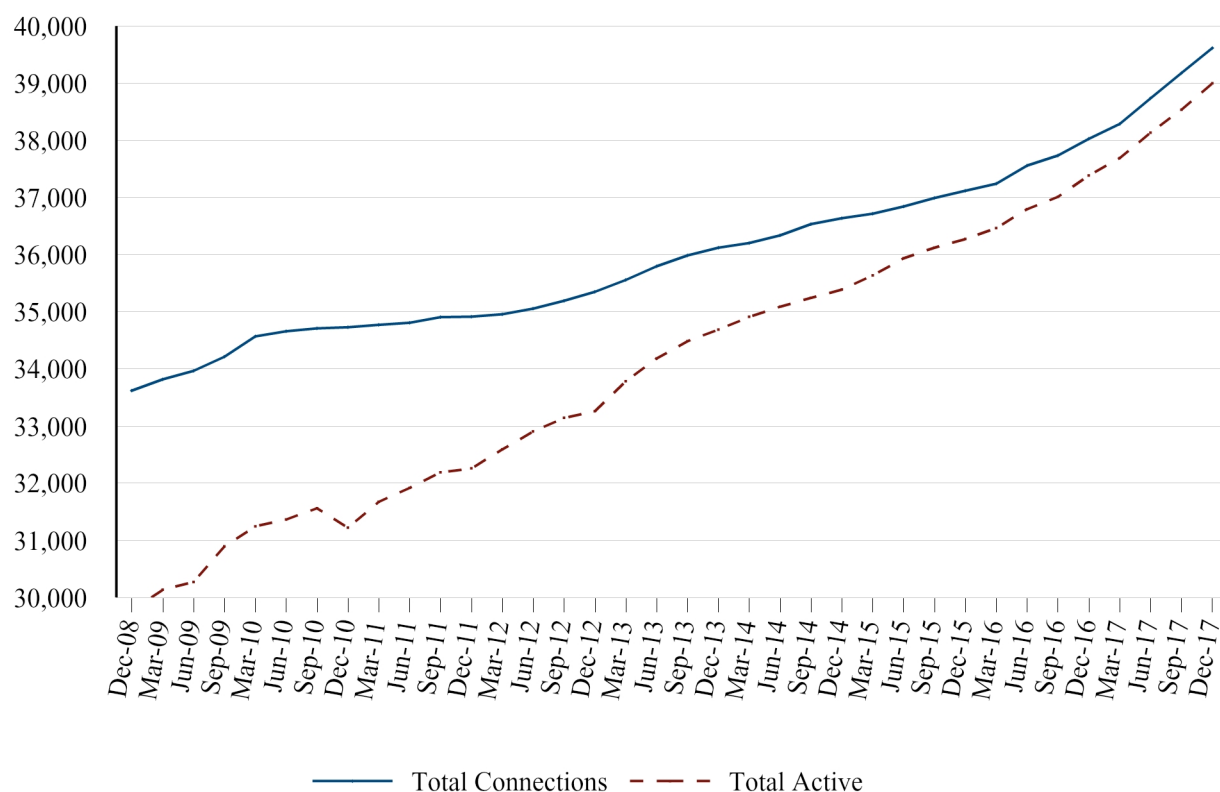
Population and Community Growth

Population and community growth in the metropolitan Phoenix area served by our utilities have a direct impact on our earnings. An increase or decrease in our active service connections will affect our revenues and variable expenses in a corresponding manner. Our total service connections, including both active service connections and connections to vacant homes, increased 1,592 connections, or 4.2%, from a total of 38,026 as of December 31, 2016 to 39,618 as of December 31, 2017. This increase is due primarily to the positive growth in new connections.

As of December 31, 2017, we have 38,997 active service connections compared to 37,387 active service connections as of December 31, 2016, an increase of 1,610, or 4.3%. As with the increase in total service connections, the increase is due primarily to the growth in new connections. Approximately 98.8% of the 38,997 active service connections are serviced by our Global Water - Santa Cruz Water Company, LLC (“Santa Cruz”) and Global Water - Palo Verde Utilities Company, LLC (“Palo Verde”) utilities as of December 31, 2017.

The graph below presents the historical change in active and total connections for our ongoing operations, adjusting for the July 2015 condemnation of the assets and operations of Valencia Water Company (“Valencia”) and the May 2016 sale of Willow Valley.

Total Active vs. Total Connections



During the economic downturn beginning in 2008, our utilities experienced an increase in the number of vacant homes, reaching a peak of 4,020 vacant connections as of February 28, 2009, approximately 11.2% of our total connections at the time; however, the negative trend began to reverse thereafter with the number of vacant homes decreasing to 621 or 1.6% of total connections as of December 31, 2017.

Economic and Environmental Utility Regulation

We are subject to extensive regulation of our rates by the ACC, which is charged with establishing rates based on the provision of reliable service at a reasonable cost while also providing an opportunity to earn a fair rate of return on rate base for investors of utilities. The ACC uses a historical test year to evaluate whether the plant in service is used and useful, to assess whether costs were prudently incurred, and to set “just and reasonable” rates. Rate base is typically the depreciated original cost of the plant in service (net of contributions in aid of construction (“CIAC”) and advances in aid of construction (“AIAC”) which are funds or property provided to a utility under the terms of a main extension agreement, the value of which may be refundable), that has been determined to have been “prudently invested” and “used and useful”, although the reconstruction cost of the utility plant may also be considered in determining the rate base. The ACC also decides on an applicable capital structure based on actual or hypothetical analyses. The ACC determines a “rate of return” on that rate base, which includes the approved capital structure and the actual cost of debt and a fair and reasonable cost of equity based on the ACC’s judgment. The overall revenue requirement for rate making purposes is established by multiplying the rate of return by the rate base and adding “prudently” incurred operating expenses for the test year, depreciation, and any applicable pro forma adjustments.

To ensure an optimal combination of access to water and water conservation balanced with a fair rate of return for investors, our water utility operating revenue is based on two components: a fixed fee and a consumption or volumetric fee. For our water utilities, the fixed fee, or “basic service charge,” provides access to water for residential usage and has generally been set at a level to produce 50% of total revenue. The volumetric fee is based on the total volume of water supplied to a given customer after the minimum number of gallons, if any, covered by the basic service charge, multiplied by a price per gallon set by a tariff approved

by the ACC. A discount to the volumetric rate applies for customers that use less than an amount specified by the ACC. For all investor-owned water utilities, the ACC requires the establishment of inverted tier conservation oriented rates, meaning that the price of water increases as consumption increases. For wastewater utilities, wastewater collection, and treatment can be based on volumetric or fixed fees. Our wastewater utility services are billed based solely on a fixed fee, determined by the size of the water meter installed. Recycled water is sold on a volumetric basis with no fixed fee component.

We are required to file rate cases with the ACC to obtain approval for a change in rates. Rate cases and other rate-related proceedings can take a year or more to complete. As a result, there is frequently a delay, or regulatory lag, between the time of a capital investment or incurrence of an operating expense increase and when those costs are reflected in rates. In normal conditions, it would not be uncommon to see us file for a rate increase every three years based on year one being the test year, year two being the rate case filing year, and year three being the rate case award year. However, based on our settlement with the ACC and extended new rate phase-in period, we will not be initiating the next rate case on this timeline. Moving forward, we will continue to analyze all factors that drive the requirement for increased revenue, including our rate of investment and recurring expenses, and determine the appropriate test year for a future rate case. See “—Recent Rate Case Activity” for additional information.

Our water and wastewater operations are also subject to extensive United States federal, state, and local laws and regulations governing the protection of the environment, health and safety, the quality of the water we deliver to our customers, water allocation rights, and the manner in which we collect, treat, and discharge wastewater. We are also required to obtain various environmental permits from regulatory agencies for our operations. The ACC also sets conditions and standards for the water and wastewater services we deliver. We incur substantial costs associated with compliance with environmental, health and safety, and water quality regulation.

Environmental, health and safety, and water quality regulations are complex and change frequently, and they have tended to become more stringent over time. As newer or stricter standards are introduced, they could increase our operating expenses. We would generally expect to recover expenses associated with compliance for environmental and health and safety standards through rate increases, but this recovery may be affected by regulatory lag.

Economic Environment

The growth of our customer base depends almost entirely on the success of developers in developing residential and commercial properties within our service areas. Real estate development is a cyclical industry and the growth rate of development, especially residential development, since 2006, both nationally and in Arizona has been and continues to be below historical rates. In addition, development in our service areas is contingent upon construction or acquisition of major public improvements, such as arterial streets, drainage facilities, telephone and electrical facilities, recreational facilities, street lighting, and local in-tract improvements (e.g., site grading). Many of these improvements are built by municipalities with public financing, and municipal resources and access to capital may not be sufficient to support development in areas of rapid population growth. For additional information and risks associated with the economic environment, see “Risk Factors” in Part I, Item 1A of this Form 10-K.

Infrastructure Investment

Capital expenditures for infrastructure investment are a component of the rate base on which our regulated utility subsidiaries are allowed to earn an equity return. Capital expenditures for infrastructure provide a basis for earnings growth by expanding our “used and useful” rate base, which is a component of its permitted return on investment and revenue requirement. We are generally able to recover a rate of return on these capital expenditures (return on equity and debt), together with debt service and certain operating costs, through the rates we charge.

We have made significant capital investments in our territories within the last fourteen years, and because the infrastructure is new, we do not expect comparable capital investments to be required in the near term, either for growth or to maintain the existing infrastructure. Nevertheless, we have an established capital improvement plan to make targeted capital investments to repair and replace existing infrastructure as needed, address operating redundancy requirements, and improve our overall financial performance, by lowering expenses and increasing revenue. Additionally, to reduce our deferred tax liability of approximately \$19.4 million resulting from the gain on the condemnation of the operations and assets of Valencia, we have identified certain currently planned investments within our capital improvement plan that we determined will qualify under the Internal Revenue Code §1033 re-investment criteria pursuant to a favorable Private Letter Ruling with the Internal Revenue Service. See “—Recent Events—Private Letter Ruling” for additional information.

Production and Treatment Costs

Our water and wastewater services require significant production resources and therefore result in significant production costs. Although we are permitted to recover these costs through the rates we charge, regulatory lag can decrease our margins and earnings if production costs or other operating expenses increase significantly before we are able to recover them through increased rates. Our most significant costs include labor, chemicals used to treat water and wastewater, and power used to operate pumps and other equipment. Power and chemical costs can be volatile. However, we employ a variety of technologies and methodologies to minimize costs and maximize operational efficiencies. Additionally, with our Total Water Management approach, whereby we maximize the direct beneficial reuse of recycled water, we can realize significant treatment costs and power savings because smaller volumes of water are required for potable use. Many utilities require that all water be treated to potable standards irrespective of use. Total Water Management focuses on the right water for the right use. Potable water is needed for consumption and recycled water is acceptable for non-potable uses such as irrigation and toilet flushing. Non-potable water does not need to be treated for commonly occurring and regulated constituents such as arsenic, or for other current or future human consumption health-based contaminants.

Weather and Seasonality

Our ability to meet the existing and future water demands of our customers depends on an adequate supply of water. Drought, overuse of sources of water, the protection of threatened species or habitats, or other factors may limit the availability of ground and surface water. Also, customer usage of water and recycled water is affected by weather conditions, particularly during the summer. Our water systems generally experience higher demand in the summer due to the warmer temperatures and increased usage by customers for irrigation and other outdoor uses. However, summer weather that is cooler or wetter than average generally suppresses customer water demand and can have a downward effect on our operating revenue and operating income. Conversely, when weather conditions are extremely dry, our business may be affected by government-issued drought-related warnings and/or water usage restrictions that would artificially lower customer demand and reduce our operating revenue. For additional information and risks associated with weather and seasonality, see “Risk Factors,” included in Item 1A of this Form 10-K. The limited geographic diversity of our service areas makes the results of our operations more sensitive to the effect of local weather extremes. The second and third quarters of the year are generally those in which water services revenue and wastewater services revenue are highest. Accordingly, interim results should not be considered representative of the results of a full year.

Access to and Quality of Water Supply

In many areas of Arizona (including certain areas that we service), water supplies are limited and, in some cases, current usage rates exceed sustainable levels for certain water resources. We currently rely predominantly (and are likely to continue to rely) on the pumping of groundwater and the generation and delivery of recycled water for non-potable uses to meet future demands in our service areas. At present, groundwater (and recycled water derived from groundwater) is the primary water supply available to us. In addition, regulatory restrictions on the use of groundwater and the development of groundwater wells, lack of available water rights, drought, overuse of local or regional sources of water, protection of threatened species or habitats, or other factors, including climate change, may limit the availability of ground or surface water. For additional information and risks associated with the access to and quality of water supply, see “Risk Factors,” included in Item 1A of this Form 10-K.

Recent Rate Case Activity

On July 9, 2012, we filed rate applications with the ACC to adjust the revenue requirements for seven utilities. In August 2013, we entered into a settlement agreement with the ACC staff, the Residential Utility Consumers Office, the City of Maricopa, and other parties to the rate case. The settlement required approval by the ACC before it could take effect. In February 2014, the rate case proceedings were completed and the ACC issued Rate Decision No. 74364, approving the settlement agreement. The collective rate increase included a 9.5% return on common equity which contributed to a 15% increase over revenue in 2011.

For our utilities, adjusting for the condemnation of the operations and assets of Valencia and the sale of Willow Valley, the settlement provided for a collective aggregate revenue requirement increase of \$3.6 million based on 2011 test year service connections, phased-in over time, with the first increase in January 2015 as follows (in thousands):

	Incremental	Cumulative
2015	\$ 1,083	\$ 1,083
2016	887	1,970
2017	335	2,305
2018	335	2,640
2019	335	2,975
2020	335	3,310
2021	335	3,645

Whereas this phase-in of additional revenues was determined using a 2011 test year, to the extent that the number of active service connections has increased and continues to increase from 2011 levels, the additional revenues may be greater than the amounts set forth above. On the other hand, if active connections decrease or we experience declining usage per customer, we may not realize all of the anticipated revenues.

From 2003 to 2008, we entered into approximately 183 infrastructure coordination and financing agreements (“ICFAs”) with developers and landowners covering approximately 275 square miles. Under these agreements, we have a contractual obligation to the developers and landowners to ensure that amongst other things, physical capacity exists through our regulated utilities for water and wastewater to the landowner/developer when needed. We receive fees from the landowner/developer for undertaking these obligations that typically are a negotiated amount per planned equivalent dwelling unit for the specified development or parcel of land. Payments are generally due to us from the landowner/developer based on progress of the development, with a portion due upon signing of the agreement, a portion due upon completion of certain milestones and the final payment due upon final plat approval or sale of the subdivision. The payments are non-refundable. Our investment can be considerable, as we may phase-in the construction of facilities in accordance with a regional master plan, as opposed to a single development.

Prior to January 1, 2010, we accounted for funds received under ICFAs as revenue once the obligations specified in the ICFA were met. As these arrangements are with developers and not with the end water or wastewater customer, the timing of revenue recognition coincided with the completion of our performance obligations under the agreement with the developer and with our ability to provide fitted capacity for water and wastewater service to the applicable development or parcel through our regulated subsidiaries.

The 2010 Regulatory Rate Decision No. 71878 established new rates for the recovery of reasonable costs incurred by the utilities and a return on invested capital. In determining the new annual revenue requirement, the ACC imputed a reduction to rate base for all amounts related to ICFA funds collected by us that the ACC deemed to be CIAC for rate making purposes. As a result of the decision by the ACC, we changed our accounting policy for the accounting of ICFA funds. Effective January 1, 2010, we recorded ICFA funds received as CIAC. Thereafter, the ICFA-related CIAC was amortized as a reduction of depreciation expense over the estimated depreciable life of the utility plant at the related utilities.

With the issuance of Rate Decision No. 74364, in February 2014, the ACC again changed how ICFA funds would be characterized and accounted for going forward. Most notably, the ACC changed the rate treatment of ICFA funds, and ICFA funds already received would no longer be deemed CIAC for rate making purposes. In conjunction with Rate Decision No. 74364, we eliminated the CIAC liability and reversed the associated regulatory liability brought about by the 2010 ruling. ICFA funds already received or which had become due prior to the date of Rate Decision No. 74364 were accounted for in accordance with our ICFA revenue recognition policy that had been in place prior to the 2010 Regulatory Rate Decision, wherein the funds received are recognized as revenue once the obligations specified in the ICFA were met. Rate Decision No. 74364 prescribes that of the ICFA funds which come due and are paid subsequent to December 31, 2013, 70% of the ICFA funds will be recorded in the associated utility subsidiary as a hook-up fee (“HUF”) liability, with the remaining 30% to be recorded as deferred revenue, until such time that the HUF tariff is fully funded, after which the remaining funds will be recorded as deferred revenue in accordance with our ICFA revenue recognition policy. A HUF tariff, specifying the dollar value of a HUF for each utility, was approved by the ACC as part of Rate Decision No. 74364. We are responsible for assuring the full HUF value is paid from ICFA proceeds, and recorded in its full amount by predetermined milestones in Rate Decision No. 74364, even if it results in recording more or less than 30% of the ICFA fee as deferred revenue.

We now account for the portion of future payments received under these agreements allocated to HUF liability as CIAC. However, from the regulator’s perspective, HUFs do not impact rate base until the related funds are expended. These funds are segregated in a separate bank account and used to construct plant assets. The HUF liability is to be relieved once the funds are used for the

construction of plant. For facilities required under a hook-up fee or ICFA, we must first use the HUF funds received, after which we may use debt or equity financing for the remainder of construction. The deferred revenue portion of these fees is recognized as revenue once the obligations specified within the applicable ICFA are met, including construction of sufficient operating capacity to serve the customers for which revenue was deferred.

We have agreed not to enter into any new ICFAs, and instead will utilize HUF tariffs, which have become an acceptable industry practice in Arizona. As part of the settlement, a HUF tariff was established for each utility. Existing ICFAs will remain in place, with 70% of future ICFA payments to be recorded as HUFs until the HUF liability is fully funded. The HUF liability is relieved as funds are expended to construct plant, at which time a corresponding amount is recorded to CIAC. The portion of ICFA proceeds not recorded as HUF will be recorded as revenue or deferred revenue, in accordance with our ICFA revenue recognition policy.

In addition to ICFAs, we have various line extension agreements with developers and builders, whereby funds, water line extensions or wastewater line extensions are provided to us by the developers and are considered refundable advances for construction. These AIACs are subject to refund by us to the developers through annual payments that are computed as a percentage of the total annual gross revenue earned from customers connected to utility services constructed under the agreement over a specified period. Upon the expiration of the agreements' refunding period, the remaining balance of the AIAC becomes nonrefundable and at that time is considered CIAC. CIAC are amortized as a reduction of depreciation expense over the estimated remaining life of the related utility plant. For rate-making purposes, a utility plant funded by AIAC and CIAC is excluded from rate base. The taxability of AIAC and CIAC was changed with the enactment of the TCJA. Previously, the majority of AIAC and CIAC that we collected were not taxable. However, with the enactment of the TCJA, they will be taxable going forward. The scope, timing and effect of the regulatory treatment of AIAC and CIAC under the TCJA are not known at this time.

Recent Events

Reorganization Transaction

On January 19, 2016, GWR Global Water Resources Corp. ("GWRC") announced that it agreed to pursue a reorganization transaction with the Company that resulted in GWRC merging with and into the Company (the "Reorganization Transaction"). The Reorganization Transaction closed on May 3, 2016. GWRC was organized in 2010 to acquire shares of the Company, and held an approximate 47.8% interest prior to the merger. The Reorganization Transaction was part of the Company's overall plan to simplify its corporate structure by eliminating one level of holding company ownership, refinance its outstanding tax-exempt bonds on more favorable terms (as described below), improve liquidity for shareholders over the medium to long-term and have a single governing jurisdiction in the U.S., where all of the assets, operations, and employees of the business are located. As a result of the merger, GWRC ceased to exist as a British Columbia corporation and the Company, governed by the corporate laws of the State of Delaware, is the surviving entity.

Debt Refinancing

With the completion of the initial public offering of shares of common stock of the Company in the United States ("U.S. IPO"), the Company had the right to redeem all of its outstanding tax-exempt bonds at a price of 103% of the principal amount, plus interest accrued at the redemption date. Following completion of the U.S. IPO, the Company entered into a note purchase agreement (the "Note Purchase Agreement") to issue two series of senior secured notes with total principal balance of \$115.0 million. On June 24, 2016, the Company closed the Note Purchase Agreement transaction, which proceeds were primarily used to pay down the outstanding \$106.7 million in tax-exempt bonds at 103%. For additional information, see "—Liquidity and Capital Resources —Senior Secured Notes."

Stipulated Condemnation of the Operations and Assets of Valencia

On July 14, 2015, the Company closed the stipulated condemnation to transfer the operations and assets of Valencia to the City of Buckeye. Terms of the condemnation were agreed upon through a settlement agreement and stipulated final judgment of condemnation wherein the City of Buckeye acquired all the operations and assets of Valencia and assumed operation of the utility upon close. The City of Buckeye paid the Company \$55.0 million at close, plus an additional \$108,000 in working capital adjustments. The City of Buckeye is obligated to pay the Company a growth premium equal to \$3,000 for each new water meter installed within Valencia's prior service areas in the City of Buckeye, for a 20-year period ending December 31, 2034, subject to a maximum payout of \$45.0 million over the term of the agreement.

Sale of Willow Valley

On March 23, 2015, the Company reached an agreement to sell the operations and assets of Willow Valley to EPCOR Water Arizona Inc. ("EPCOR"). Pursuant to the terms of the agreement, EPCOR purchased all the operations, assets, and rights used by Willow Valley to operate the utility system for \$2.3 million. The transaction was approved by the ACC on March 10, 2016, and closed on May 9, 2016.

Sale of Loop 303 Contracts

In September 2013, we entered into an agreement to sell certain wastewater facilities main extension agreements and offsite water management agreements for the contemplated Loop 303 service area, along with their related rights and obligations (which we refer to collectively as the "Loop 303 Contracts"), relating to the 7,000-acre territory within a portion of the western planning area of the City of Glendale, Arizona known as the "Loop 303 Corridor." Pursuant to the agreement, we sold the Loop 303 Contracts to EPCOR for total proceeds of approximately \$4.1 million (\$3.1 million of which has been received as of December 31, 2017), which will be paid to us over a multi-year period. Receipt of the remaining proceeds will occur and be recorded as additional income over time as certain milestones are met between EPCOR and the developers/landowners of the Loop 303 Corridor. As part of the consideration, we agreed to complete certain engineering work required in the offsite water management agreements, which we completed in 2013, thereby satisfying our remaining obligations relating to the Loop 303 Contracts. In April 2015, we received proceeds of approximately \$296,000 related to the sale of the Loop 303 Contracts. As of December 31, 2017, proceeds of \$1.0 million remain outstanding, and when received will be recorded as additional income over time as certain milestones are met between EPCOR and the developers/landowners.

Sonoran Acquisition Liability

On March 17, 2016, the Company entered into an agreement with Sonoran Utility Services, LLC ("Sonoran") to amend certain provisions of the purchase and sale agreement related to the acquisition of Sonoran's assets on June 15, 2005. The amended agreement allowed the Company to reduce its original \$3.8 million acquisition liability due to Sonoran in 2018 to \$2.8 million, through a settlement agreement executed subsequent to the Note Purchase Agreement. Upon settlement of the Sonoran acquisition liability in June 2016, the Company recorded a gain of \$954,000 in other income.

Private Letter Ruling

On June 2, 2016, the Company received a Private Letter Ruling from the Internal Revenue Service that, for purposes of deferring the approximately \$19.4 million gain realized from the condemnation of the operations and assets of Valencia, determined that the assets converted upon the condemnation of such assets could be replaced through certain reclamation facility improvements contemplated by the Company under Internal Revenue Code §1033 as property similar or related in service or use. In June 2016, the Company converted all operating subsidiaries from corporations to limited liability companies to take full advantage of the benefits of such ruling.

Pursuant to Internal Revenue Code §1033, the Company would have been able to defer the gain on condemnation through the end of 2017. On April 18, 2017, the Company filed a request for a one-year extension to defer the gain to the end of 2018, which the IRS approved on August 8, 2017. Following the approval of the extension, the Company has slightly modified the timing of certain planned investments within its capital improvement plan in accordance with Internal Revenue Code §1033. Accordingly, the Company substantially completed these investments in 2017, with the remaining improvements to be completed in early 2018. As a result of the Private Letter Ruling, the Company increased capital expenditures in 2017 as compared to recent years, and expects corresponding reductions to occur in 2018, 2019, and beyond. As of December 31, 2017, our deferred tax liability relating to the condemnation was approximately \$7.2 million.

Acquisition of Eagletail Water Company

On May 15, 2017, the Company acquired Eagletail Water Company ("Eagletail") for approximately \$80,000. At the time of acquisition, Eagletail, a small water utility located west of metropolitan Phoenix, added approximately 55 active water connections and eight square miles of approved service area to Global Water's existing regional service footprint.

ACC Tax Docket

On December 20, 2017, the ACC opened a docket to address the utility ratemaking implication of the Federal Tax Cut and Jobs Act (the "TCJA"). Numerous companies, including GWRI's regulated utilities, filed comments on or before January 22, 2018. The ACC subsequently held a workshop regarding the tax issue on January 31, 2018, and then discussed and approved an order on February 6, 2018. The order requires all utilities in Arizona to "apply regulatory accounting treatment which, includes the use of regulatory assets and regulatory liabilities, to address all impacts from the enactment of the TCJA." The order also orders

specified utilities on “Attachment A” to make one of the following three types of filings by April 7, 2018, “1) file an application for a tax expense adjuster mechanism, 2) file an intent to file a rate case within 90 days, or 3) any such other application to address rate making implications of the TCJA”. All of our currently operating regulated utilities are listed on Attachment A (with the exception of Eagletail). We are evaluating our options regarding our April 7 filing. The proposals we make on or before April 7 will then be reviewed by the ACC and the ACC will issue an order approving, modifying, or rejecting the proposals. It is not clear what actions the ACC will ultimately take with regard to our regulated utilities.

Segment Reporting

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing operating performance. In consideration of the Financial Accounting Standards Board’s Accounting Standards Codification 280, *Segment Reporting*, we are not organized around specific products and services, geographic regions, or regulatory environments. We currently operate in one geographic region within the State of Arizona, wherein each operating utility operates within the same regulatory environment.

While we report revenue, disaggregated by service type, on the face of our statement of operations, we do not manage the business based on any performance measure at the individual revenue stream level. We do not have any customers that contribute more than 10% to our revenues or revenue streams. Additionally, the chief operating decision maker uses consolidated financial information to evaluate our performance, which is the same basis on which he communicates our results and performance to our board of directors. It is upon this consolidated basis from which he bases all significant decisions regarding the allocation of our resources on a consolidated level. Based on the information described above and in accordance with the applicable literature, management has concluded that we are currently organized and operated as one operating and reportable segment.

Comparison of Results of Operations for the Years Ended December 31, 2017 and 2016

The following table summarizes our results of operations for the years ended December 31, 2017 and 2016 (in thousands):

	For the Year Ended December 31,	
	2017	2016
Revenues	\$ 31,208	\$ 29,799
Operating expenses	23,864	23,987
Operating income	7,344	5,812
Total other expense	(3,394)	(9,611)
Income (loss) before income taxes	3,950	(3,799)
Income tax (expense) benefit	601	1,287
Net income (loss)	\$ 4,551	\$ (2,512)
Basic earnings (losses) per common share	\$ 0.23	\$ (0.13)
Diluted earnings (losses) per common share	\$ 0.23	\$ (0.13)

Revenues – The following table summarizes our revenues for the years ended December 31, 2017 and 2016 (in thousands).

	For the Year Ended December 31,	
	2017	2016
Water services	\$ 14,367	\$ 13,978
Wastewater and recycled water services	16,765	15,740
Unregulated revenues	76	81
Total revenues	\$ 31,208	\$ 29,799

Total revenues increased \$1.4 million, or 4.7%, for the year ended December 31, 2017 compared with the year ended December 31, 2016. The operations of Willow Valley contributed revenue of \$306,000 for the year ended December 31, 2016 compared to no revenue for the year ended December 31, 2017. The revenue for the remaining operating utilities increased \$1.7 million, or 5.8%, to \$31.2 million for the year ended December 31, 2017 compared to \$29.5 million for the year ended December 31, 2016.

The increase in revenue for the remaining operating utilities reflects the increase in rates related to Rate Decision No. 74364 in February 2014 combined with a 4.3% increase in active service connections, coupled with an increase in consumption during the year ended December 31, 2017 compared to the year ended December 31, 2016.

Water Services – Water services revenue increased \$389,000, or 2.8%, to \$14.4 million for the year ended December 31, 2017 compared to \$14.0 million for the year ended December 31, 2016. The operations of Willow Valley contributed \$306,000 for the year ended December 31, 2016 compared to no revenue for the year ended December 31, 2017. The water services revenue for the remaining operating utilities increased \$695,000, or 5.1%, for the year ended December 31, 2017 compared to the year ended December 31, 2016.

Water services revenue based on consumption increased \$136,000, or 2.2%, to \$6.4 million for the year ended December 31, 2017 compared to \$6.2 million for the year ended December 31, 2016. The operations of Willow Valley contributed \$67,000 for the year ended December 31, 2016 compared to no revenue for the year ended December 31, 2017. Consumption revenue for the remaining operating utilities increased \$203,000, or 3.3%, to \$6.4 million for the year ended December 31, 2017 compared to \$6.2 million for the year ended December 31, 2016. The increase in consumption revenue for the remaining utilities is primarily driven by an increase in consumption combined with an increase in rates for the year ended December 31, 2017 compared to the year ended December 31, 2016.

Active water connections increased 4.4% to 19,851 as of December 31, 2017 from 19,013 as of December 31, 2016 primarily due to the positive growth in new connections.

Water consumption increased 3.3% to 2.3 billion gallons for the year ended December 31, 2017, compared to 2.2 billion gallons for the year ended December 31, 2016. However, adjusting for the sale of Willow Valley, which operations accounted for 17 million gallons of consumption for the year ended December 31, 2016, water consumption for the remaining operating utilities increased 4.1% to 2.3 billion gallons. The increase in consumption at the remaining operating utilities is primarily attributed to an increase in irrigation, residential, and golf course consumption, which was partially offset by a decrease in commercial consumption for the year ended December 31, 2017 compared to the year ended December 31, 2016. The increase in irrigation and residential consumption is driven by an increase in active connections combined with an increase in average temperature.

Water services revenue, excluding miscellaneous charges associated with the basic service charge, increased \$112,000, or 1.5%, to \$7.6 million for the year ended December 31, 2017 compared to \$7.5 million for the year ended December 31, 2016. The operations of Willow Valley contributed revenue of \$235,000, for the year ended December 31, 2016 compared to no revenue for the year ended December 31, 2017. The remaining utilities' basic water services revenue increased \$347,000, or 4.8%, for the year ended December 31, 2017 compared to the year ended December 31, 2016. This increase resulted from an increase in active service connections for the remaining operating utilities, combined with an increase in rates related to Rate Decision No. 74364.

Wastewater and Recycled Water Services – Wastewater and recycled water services revenue increased \$1.0 million, or 6.5%, for the year ended December 31, 2017 compared to the year ended December 31, 2016. The increase in wastewater and recycled water services revenue is primarily driven by a \$902,000 increase in wastewater services revenue combined with a \$123,000 increase in recycled water services revenue for the year ended December 31, 2017 compared to the year ended December 31, 2016. The increase in wastewater services revenue reflects the increase in rates related to Rate Decision No. 74364, as well as the increase in active wastewater connections, which increased 4.2% to 19,146 as of December 31, 2017 from 18,374 as of December 31, 2016.

Recycled water services revenue, which is based on the number of gallons delivered, increased \$123,000, or 17.7%, to \$816,000 for the year ended December 31, 2017 compared to \$693,000 for the year ended December 31, 2016. The increase in recycled water services revenue is primarily related to the increase in recycled water consumption coupled with an increase in recycled water rates. The volume of recycled water delivered increased 63 million gallons, or 9.9%, to 699 million gallons for the year ended December 31, 2017 compared to 635 million gallons for the year ended December 31, 2016. Recycled water rates increased 11.5% per Rate Decision No. 74364 compared to 2016.

Operating Expenses – The following table summarizes our operating expenses for the years ended December 31, 2017 and 2016 (in thousands):

	For the Year Ended December 31,	
	2017	2016
Operations and maintenance	\$ 6,087	\$ 6,188
Operations and maintenance - related party	1,462	1,853
General and administrative	9,407	9,667
Depreciation	6,908	6,279
Total operating expenses	<u>\$ 23,864</u>	<u>\$ 23,987</u>

Operations and Maintenance – Operations and maintenance costs, consisting of personnel costs, production costs (primarily chemicals and purchased electrical power), maintenance costs, and property tax, decreased \$101,000, or 1.6%, for the year ended December 31, 2017 compared to the year ended December 31, 2016.

Property tax expense increased \$162,000, or 8.9%, to \$2.0 million for the year ended December 31, 2017 compared to \$1.8 million for the year ended December 31, 2016. Property taxes are calculated using a centrally valued property calculation, which derives property values based upon three-year historical average revenues. As revenues increase, we expect property taxes to also increase.

Chemical and supply expenses decreased \$143,000, or 26.4%, to \$398,000 for the year ended December 31, 2017 compared to \$541,000 the year ended December 31, 2016. The decrease is primarily driven by a reduction in chemical utilization for the year ended December 31, 2017 compared to the year ended December 31, 2016, as additional chemicals were required in 2016 to ensure optimal operation of the wastewater facility in readiness for the inception of the Palo Verde wastewater recycling facility expansion project, which is underway.

Repairs and maintenance expense decreased \$66,000, or 26.2%, to \$186,000 for the year ended December 31, 2017 compared to \$252,000 for the year ended December 31, 2016. The decrease in repair and maintenance expense is primarily attributed to work performed as part of the accelerated capital expenditure plan. See “– Recent Events – Private Letter Ruling” for additional information. The addition of assets added through the plan has reduced the repair and maintenance requirements.

Total personnel expenses decreased \$40,000, or 2.3%, to \$1.7 million for the year ended December 31, 2017 compared to \$1.7 million for the year ended December 31, 2016, primarily due to a decrease in personnel related to the sale of Willow Valley, which operations represented \$60,000 of personnel expense for the year ended December 31, 2016 compared to zero expense for the year ended December 31, 2017. Total personnel costs for the remaining operating utilities increased \$20,000, or 1.2%, for the year ended December 31, 2017 compared to the year ended December 31, 2016. The increase in personnel expenses for the remaining utilities was primarily driven by an increase in medical insurance expense, which increased \$21,000 for the year ended December 31, 2017 compared to the year ended December 31, 2016.

Operations and Maintenance – Related Party – Operations and maintenance related party expenses are for service fees paid to FATHOM™ with respect to billing, customer service, and other support provided to our regulated utilities. Service fees paid to FATHOM™ decreased \$391,000, or 21.1%, to \$1.5 million for the year ended December 31, 2017 compared to \$1.9 million for the year ended December 31, 2016. FATHOM™ service fees partially decreased as a result of the sale of Willow Valley, which operations represented \$60,000 of such expenses for the year ended December 31, 2016 compared to zero expense for the year ended December 31, 2017. FATHOM™ service fees for the remaining operating utilities decreased \$331,000, or 18.5%, for the year ended December 31, 2017 compared to the year ended December 31, 2016. The decrease in service fees for the remaining operating utilities was driven by the renegotiation of the FATHOM™ service contract in November 2016, wherein the monthly rate per water connection decreased \$1.55, or 19.9%, from \$7.79 per month to \$6.24 per month beginning in January 2017.

General and Administrative – General and administrative costs include the day-to-day expenses of office operations, personnel costs, legal and other professional fees, insurance, rent, and regulatory fees. These costs decreased \$260,000, or 2.7%, for the year ended December 31, 2017 compared to the year ended December 31, 2016.

Deferred compensation expense decreased \$477,000, or 26.5%, to \$1.3 million for the year ended December 31, 2017 compared to \$1.8 million for the year ended December 31, 2016. The decrease was primarily related to the lower increase in the carrying value of our equity awards due to the change in stock price, which increased \$0.26 for the year ended December 31, 2017 compared to an increase of \$3.60 for the year ended December 31, 2016. The effect of the change in carrying value was partially offset by the vesting of the 2017 stock option grant for the year ended December 31, 2017.

Board compensation expense decreased \$112,000, or 12.9%, to \$754,000 for the year ended December 31, 2017 compared to \$866,000 for the year ended December 31, 2016. The decrease is related to the unrealized gains on the deferred phantom units

("DPU's"), due to a lower increase in stock price for the year ended December 31, 2017 compared to the year ended December 31, 2016. This decrease was partially offset by increases in stock option expense associated with the 2016 option grant.

Personnel related costs increased \$109,000, or 3.9%, to \$2.9 million for the year ended December 31, 2017 compared to \$2.8 million for the year ended December 31, 2016. The increase was driven by an increase in salaries coupled with an increase in medical expenses for the year ended December 31, 2017 compared to the year ended December 31, 2016. The increase in salaries expense was primarily related to personnel changes due to becoming a U.S. public company.

Public company expenses increased \$132,000, or 163.0%, to \$213,000 for the year ended December 31, 2017 compared to \$81,000 for the year ended December 31, 2016 due to becoming a U.S. public company in May 2016, with the year ended December 31, 2017 containing a full 12 months of expenses compared to eight months in 2016. Public company expenses were historically recorded at GWRC. Public company expenses primarily consist of listing fees, filing fees, and transfer agent expenses.

Franchise taxes increased \$82,000, or 68.9%, to \$200,000 for the year ended December 31, 2017 compared to \$118,000 for the year ended December 31, 2016. The increase in franchise taxes is associated with GWRI (a Delaware corporation) becoming a U.S. public company which requires that we pay \$200,000 in Delaware franchise tax each year, of which a pro rata amount of eight months was paid in 2016, compared to a full year in 2017.

Other Expense – Other expense totaled \$3.4 million for the year ended December 31, 2017 compared to other expense of \$9.6 million for the year ended December 31, 2016. The decrease of \$6.2 million in other expense was primarily driven by a \$6.7 million decrease in interest expense, associated with the June 2016 debt refinancing, combined with a \$219,000 change in Other – related party income, associated with our investment in FATHOM™, which were partially offset by a decrease in other income of \$744,000, primarily related to the gain on the settlement of the Sonoran purchase liability recognized in the year ended December 31, 2016.

Interest expense decreased \$6.7 million, or 56.8%, to \$5.1 million for the year ended December 31, 2017 compared to \$11.9 million for the year ended December 31, 2016. Interest expense decreased due to the June 2016 debt refinancing. As part of the refinancing, we paid \$3.2 million in prepayment penalties and wrote off the remaining \$2.2 million in capitalized loan fees related to the retired bonds during the year ended December 31, 2016. Additionally, interest expense was further reduced by approximately \$865,000 due to reduced interest rates on the new notes.

Other – related party income increased \$219,000 to income of \$234,000 for the year ended December 31, 2017 compared to income of \$15,000 for the year ended December 31, 2016. Other related party income includes royalty income based upon a percentage of certain FATHOM™ recurring revenue combined with the equity method gains and losses associated with our equity method investment in FATHOM™. The change in other related party income was primarily driven by a \$243,000 gain from the revaluation of our ownership interest in FATHOM™ in connection with FATHOM™'s financing transaction in March 2017 (See Note 5 – "Equity Method Investment" to the condensed consolidated financial statements in Part II, Item 8 of this report) combined with a reduction of our share of FATHOM™ operating losses for the year ended December 31, 2017 compared to December 31, 2016.

Other income decreased \$744,000 to \$1.5 million for the year ended December 31, 2017 compared to \$2.2 million for the year ended December 31, 2016. The decrease in other income is primarily related to the \$954,000 gain on the settlement of the Sonoran purchase liability recognized in the year ended December 31, 2016. Partially offsetting the decrease was an increase in the Valencia earnout of \$240,000 to \$1.4 million for the year ended December 31, 2017 compared to \$1.2 million for the year ended December 31, 2016. The Valencia earnout consists of \$3,000 for each new water meter installed within Valencia's prior service areas. This increase was primarily driven by accelerated growth in our former service territory. Other income was also affected by a \$54,000 loss we recorded for the sale of Willow Valley for the year ended December 31, 2016.

Income Tax (Expense) Benefit – Income tax benefit of \$0.6 million was recorded for the year ended December 31, 2017 compared to an income tax benefit of \$1.3 million for the year ended December 31, 2016. The income tax benefit recorded is primarily related to the recording of the impacts of the TCJA, partially offset by the expense incurred due to pre-tax net income for the year ended December 31, 2017.

Net Income (Loss) – Our net income totaled \$4.6 million for the year ended December 31, 2017 compared to a net loss of \$2.5 million for the year ended December 31, 2016. The \$7.1 million increase for the year ended December 31, 2017 compared to the year ended December 31, 2016 is primarily attributed to the \$6.7 million reduction of interest expense, a \$1.5 million operating income increase, a \$240,000 increase in the Valencia earnout, a \$204,000 change of our equity method investment, and a \$0.7 million change in income taxes. Additionally, net income for the year ended December 31, 2016 included a \$954,000 gain on the settlement of the Sonoran purchase liability.

Comparison of Results of Operations for the Years Ended December 31, 2016 and 2015

The following table summarizes our results of operations for the years ended December 31, 2016 and 2015 (in thousands):

	For the Year Ended December 31,	
	2016	2015
Revenues	\$ 29,799	\$ 31,956
Operating expenses	23,987	25,429
Operating income	5,812	6,527
Total other expense	(9,611)	35,459
Income (loss) before income taxes	(3,799)	41,986
Income tax (expense) benefit	1,287	(20,623)
Net income (loss)	\$ (2,512)	\$ 21,363
Basic earnings (losses) per common share	\$ (0.13)	\$ 1.17
Diluted earnings (losses) per common share	\$ (0.13)	\$ 1.17

Revenues – The following table summarizes our revenues for the years ended December 31, 2016 and 2015 (in thousands).

	For the Year Ended December 31,	
	2016	2015
Water services	\$ 13,978	\$ 16,320
Wastewater and recycled water services	15,740	15,020
Unregulated revenues	81	616
Total revenues	\$ 29,799	\$ 31,956

Total revenues decreased \$2.2 million, or 6.7%, for the year ended December 31, 2016 compared with the year ended December 31, 2015. The decrease in revenues was primarily related to the condemnation of the operations and assets of Valencia which occurred in July 2015 and the sale of Willow Valley in May of 2016, which together contributed revenue of \$4.0 million for the year ended December 31, 2015 and \$306,000 for the year ended December 31, 2016. The decrease related to the condemnation of Valencia and the sale of Willow Valley was partially offset by an increase in revenue for the remaining operating utilities, which increased \$1.6 million, or 5.7%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. The increase in revenue for the remaining operating utilities reflects the increase in rates related to Rate Decision No. 74364 in February 2014 combined with a 3.1% increase in active service connections (adjusted for the condemnation of the operations and assets of Valencia and the sale of Willow Valley) combined with an increase in consumption during the year ended December 31, 2016 compared to year ended December 31, 2015. This increase was partially offset by a \$535,000 reduction in unregulated revenue.

Water Services – Water services revenues decreased \$2.3 million, or 14.4%, to \$14.0 million for the year ended December 31, 2016 compared to \$16.3 million for the year ended December 31, 2015. The decrease is primarily due to the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which contributed \$4.0 million for the year ended December 31, 2015 and \$306,000 for the year ended December 31, 2016. The decrease in water services revenue was partially offset by an increase in water services revenue for the remaining operating utilities of \$1.4 million, or 11.4%, for the year ended December 31, 2016 compared to the year ended December 31, 2015.

Water services revenue based on consumption decreased \$452,000, or 6.8%, to \$6.2 million for the year ended December 31, 2016 compared to \$6.7 million for the year ended December 31, 2015. The decrease in revenue was primarily driven by the condemnation of the assets and operations of Valencia and the sale of Willow Valley, which contributed \$1.7 million for the year ended December 31, 2015 and \$67,000 for the year ended December 31, 2016. The decrease in water service revenue related to the condemnation of Valencia and sale of Willow Valley was partially offset by an increase water service revenue for the remaining operating utilities, which increased \$1.2 million, or 23.0%, to \$6.2 million for the year ended December 31, 2016 compared to \$5.0 million for the year ended December 31, 2015. The increase in water service revenue for the remaining operating

utilities is related to the onset of new rates in 2016 combined with an increase in active water connections and an increase in consumption compared to 2015.

Active water connections decreased 4.8% to 19,013 as of December 31, 2016 from 19,964 as of December 31, 2015 primarily as the result of the sale of Willow Valley. However, after adjusting to remove the active water service connections of Willow Valley, active connections increased 3.0% to 19,013 as of December 31, 2016 from 18,452 as of December 31, 2015.

Water consumption decreased 7.8% to 2.2 billion gallons for the year ended December 31, 2016 from 2.4 billion gallons for the year ended December 31, 2015. The decrease in water consumption was primarily driven by the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which consumed 467 million gallons for the year ended December 31, 2015 and 17 million gallons for the year ended December 31, 2016. The water consumption for the remaining operating utilities increased 13.9% to 2.2 billion gallons for the year ended December 31, 2016 compared to 1.9 billion gallons for the year ended December 31, 2015. The increase in consumption can be attributed to the increase in active connections (in each case adjusting for the condemnation of the operations and assets of Valencia and the sale of Willow Valley) combined with an increase in average temperature and a decrease in precipitation for the year ended December 31, 2016 compared to the year ended December 31, 2015.

Water services revenue associated with the basic service charge decreased \$1.8 million, or 19.0%, to \$7.5 million for the year ended December 31, 2016 compared to \$9.2 million for the year ended December 31, 2015. The decrease in basic water service revenue is primarily driven by the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which contributed \$2.2 million for the year ended December 31, 2015 and \$235,000 for the year ended December 31, 2016. The decrease was partially offset by an increase in basic revenues for the remaining operating utilities, which increased \$203,000, or 2.9%, to \$7.2 million for the year ended December 31, 2016 compared to \$7.0 million for the year ended December 31, 2015, reflecting growth in total active connections as well as an increase in rates due to Rate Decision No. 74364.

Wastewater and Recycled Water Services – Wastewater and recycled water services revenues increased \$720,000, or 4.8%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. The increase reflects the increase in rates related to Rate Decision No. 74364 as well as the increase of active wastewater connections, which increased 3.1% to 18,374 as of December 31, 2016 from 17,820 as of December 31, 2015.

Recycled water revenue, which is based on the number of gallons delivered, increased \$183,000, or 35.9%, to \$693,000 for the year ended December 31, 2016 compared to \$510,000 for the year ended December 31, 2015. The recycled water revenue increase is a function of an increase in rates and volume delivered. Recycled water rates increased 30% per Rate Decision No. 74364 compared to 2015. The volume of recycled water delivered decreased approximately 3 million gallons, or 0.5%, to 635 million gallons for the year ended December 31, 2016 from 639 million gallons for the year ended December 31, 2015.

Operating Expenses – The following table summarizes our operating expenses for the years ended December 31, 2016 and 2015 (in thousands):

	For the Year Ended December 31,	
	2016	2015
Operations and maintenance	\$ 6,188	\$ 7,080
Operations and maintenance - related party	1,853	2,179
General and administrative	9,667	7,957
Depreciation	6,279	8,213
Total operating expenses	<u>\$ 23,987</u>	<u>\$ 25,429</u>

Operations and Maintenance – Operations and maintenance costs decreased \$892,000, or 12.6%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. The decrease in operations and maintenance costs was primarily driven by the condemnation of the assets and operations of Valencia and the sale of Willow Valley.

Total personnel costs decreased \$386,000, or 18.4%, for the year ended December 31, 2016 compared to the year ended December 31, 2015, primarily due to a decrease in personnel related to the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which contributed \$534,000 for the year ended December 31, 2015 and \$60,000 for the year ended December 31, 2016. This decrease in personnel expenses was partially offset by an increase of \$88,000, or 5.7%, in personnel expenses of the remaining operating utilities for the year ended December 31, 2016 compared to the year ended December 31, 2015. Personnel expense for the remaining operating utilities increased due to an increase in salary and wages related to certain organizational changes for the year ended December 31, 2016 compared to the year ended December 31, 2015.

Utilities and power expense decreased \$92,000, or 5.8%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. Utilities and power expense decreased as a result of the condemnation of the operations and assets of Valencia and sale of Willow Valley, which contributed \$222,000 for the year ended December 31, 2015 and \$12,000 for the year ended December 31, 2016. The decrease in utilities expense was partially offset by an increase in the utility expense of the remaining operating utilities, which increased \$117,000, or 8.6%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. The increase in utilities expense is primarily related to an increase in consumption.

Property taxes decreased \$272,000, or 13.0%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. Property taxes primarily decreased due to the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which contributed \$210,000 for the year ended December 31, 2015 and zero for the year ended December 31, 2016. Property tax expense decreased for the remaining operating utilities by \$61,000, or 3.3%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. Property taxes for the remaining utilities decreased as a result of a change in property tax assessment in 2016 compared to 2015. Property taxes for the year ended December 31, 2015 did not change significantly when compared to the year ended December 31, 2014.

Operations and Maintenance – Related Party – Operations and maintenance related party expenses are for service fees paid to FATHOM™ with respect to billing, customer service and other support provided to our regulated utilities. Service fees paid to FATHOM™ decreased \$326,000, or 15.0%, to \$1.9 million for the year ended December 31, 2016 compared to \$2.2 million for the year ended December 31, 2015. FATHOM™ service fees primarily decreased as a result of the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which contributed \$475,000 in expenses for the year ended December 31, 2015 and \$60,000 for the year ended December 31, 2016. This decrease was partially offset by an increase in service fees for the remaining operating utilities, which increased \$89,000, or 5.2%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. FATHOM™ service fees for the remaining operating utilities increased in relation to an increase in their active water connections combined with a consumer price index increase in the monthly charge pursuant to the services contract.

General and Administrative – General and administrative costs include the day-to-day expenses of office operation, personnel costs, legal and other professional fees, insurance, rent, and regulatory fees. These costs increased \$2.3 million, or 28.3%, to \$10.2 million for the year ended December 31, 2016 compared to \$8.0 million for the year ended December 31, 2015. General and administrative costs decreased \$852,000, or 9.7%, during the year ended December 31, 2015 compared to the year ended December 31, 2014.

Personnel related costs decreased \$670,000, or 19.6%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. The 2016 decrease was driven by a non-recurring bonus of \$591,000 paid in relation to closing of the condemnation of the operations and assets of Valencia in 2015. Excluding the non-recurring bonus, personnel related costs decreased \$79,000, or 2.3%, primarily due to a decrease in medical expenses for the year ended December 31, 2016 compared to the year ended December 31, 2015.

Deferred compensation costs increased \$1.1 million, or 158.7% for the year ended December 31, 2016 compared to the year ended December 31, 2015. Deferred compensation increased as a result of the change in our stock price, which increased \$3.60 for the year ended December 31, 2016 compared to a U.S. Dollar adjusted stock price increase of \$0.97 for the year ended December 31, 2015, combined with the continued vesting of outstanding phantom stock units ("PSUs") and stock appreciation rights ("SARs"). PSUs and SARs derive their value from the value of one outstanding share of stock. Deferred compensation is recorded upon the vesting of these awards. Outstanding vested units are revalued periodically based upon the change in unit price as derived from the change in stock price.

City of Maricopa memorandum of understanding fees increased \$316,000 or 57.8%, to \$863,000 for the year ended December 31, 2016 compared to \$547,000 for the year ended December 31, 2015. Previously, we agreed to offset the cash payments associated with the license fees through December 31, 2015 with miscellaneous utility related services provided by us to the City of Maricopa. Beginning in January 2016, we began paying the City of Maricopa for the license fees calculated at 3% of revenues of Palo Verde and Santa Cruz. City of Maricopa memorandum of understanding fees for the year ended December 31, 2015 did not change significantly when compared to the year ended December 31, 2014.

Professional fees, which include legal and accounting costs, increased \$49,000, or 3.6%, for the year ended December 31, 2016 compared to the year ended December 31, 2015. Professional fees increased primarily as a result of a \$214,000 increase in legal expenses associated with being a U.S. publicly traded company, which expenses were historically recorded at GWRC, combined with an increase associated with the Private Letter Ruling. These increases were partially offset by a \$165,000 decrease in accounting and other services, which decreased as part of a reduction in expenses related to audit and tax services combined with a reduction in certain other consulting arrangements.

Board compensation costs increased \$1.0 million, or 259.2% for the year ended December 31, 2016 compared to the year ended December 31, 2015. The increase in board compensation is primarily related to \$649,000 in stock option expense associated with the 2016 option grant for the year ended December 31, 2016 compared to zero for the year ended December 31, 2015. Additionally, board compensation expense increased as a result of the change in stock price, which increased \$3.60 for the year ended December 31, 2016 compared to the U.S. Dollar adjusted increase of \$0.97 for the year ended December 31, 2015, combined with an increase in the number of deferred phantom units DPUs outstanding as of December 31, 2016 compared to December 31, 2015.

Miscellaneous expenses increased \$210,000 or 85.4% for the year ended December 31, 2016 compared to the year ended December 31, 2015. This increase is primarily related to an increase in the taxes and fees associated with the completion of the U.S. IPO and our status as a U.S. publicly traded company, of which a portion of these expenses were historically recorded at GWRC.

Depreciation – Depreciation expense decreased by \$1.9 million, or 23.5%, to \$6.3 million for the year ended December 31, 2016. This decrease is primarily related to the condemnation of the operations and assets of Valencia and the sale of Willow Valley, which recorded depreciation of approximately \$63,000 for the year ended December 31, 2016 and \$1.4 million for the year ended December 31, 2015 in addition to certain assets reaching the end of their useful lives and, therefore, having been fully depreciated.

Other Income (Expense) – Other expense totaled a net \$9.6 million for the year ended December 31, 2016 compared to net other income of \$35.5 million for the year ended December 31, 2015. The change in other expense is primarily driven by the \$43.0 million gain associated with the condemnation of the operations and assets of Valencia recorded in 2015 combined with a \$3.6 million increase in interest expense in 2016. The increase in net expense in 2016 was partially offset by a \$1.5 million increase in other income.

Interest expense increased 43.0% to \$11.9 million for the year ended December 31, 2016 compared to \$8.3 million for the year ended December 31, 2015. Interest expense increased due to the refinancing of debt that was completed in June of 2016. As part of the refinancing, we paid \$3.2 million in prepayment penalties and wrote off the remaining \$2.2 million in capitalized loan fees related to the retired bonds. These increases were partially offset by lower interest rate expense in the second half of 2016 related to the refinancing of our bonds in June 2016.

Other income increased to \$2.2 million for the year ended December 31, 2016 compared to income of \$767,000 for the year ended December 31, 2015. The increase in other income was primarily attributed to a \$954,000 gain on the settlement of the Sonoran purchase liability. The Sonoran liability was originally due in June 2018, however, by accelerating the payoff of the liability, we were able to reduce the original liability of \$3.8 million to \$2.8 million. Additionally, other income includes approximately \$1.2 million related to the Valencia earn out for the year ended December 31, 2016 compared to \$624,000 for the year ended December 31, 2015, wherein we receive \$3,000 for each new meter installed in the Valencia service area. These gains were partially offset by a \$54,000 loss on sale of Willow Valley in May of 2016 combined with a reduction in other income related to the 2015 gain of \$296,000 on proceeds received in relation to the sale of Loop 303 Contracts.

Income Tax (Expense) Benefit – An income tax benefit of \$1.5 million was recorded for the year ended December 31, 2016 compared to income tax expense of \$20.6 million for the year ended December 31, 2015. The income tax benefit is related to our current period losses.

Net Loss – Our net loss totaled \$2.9 million for the year ended December 31, 2016 compared to a net income of \$21.4 million for the year ended December 31, 2015. The \$24.2 million decrease for the year ended December 31, 2016 compared to the year ended December 31, 2015 is primarily attributed to the \$43.0 million gain on the condemnation of operations and assets of Valencia, net of a \$20.2 million tax liability for the year ended December 31, 2015. Additionally, interest expense increased \$3.6 million and deferred compensation and board compensation increased \$2.1 million. Interest expense increased due to the expenses associated with our debt refinancing. Deferred compensation increased primarily due to an increase in stock price, combined with option grants to members of the board. The amounts were partially offset by an income tax benefit of \$1.5 million related to our current period losses.

Outstanding Share Data

As of March 9, 2018, there were 19,631,266 shares of our common stock outstanding and options to acquire an additional 740,000 shares of our common stock outstanding.

Liquidity and Capital Resources

Our capital resources are provided by internally generated cash flows from operations as well as debt and equity financing. Additionally, our regulated utility subsidiaries receive advances and contributions from customers, home builders, and real estate developers to partially fund construction necessary to extend service to new areas. We use our capital resources to:

- fund operating costs;
- fund capital requirements, including construction expenditures;
- pay dividends;
- make debt and interest payments; and
- invest in new and existing ventures.

Our utility subsidiaries operate in rate-regulated environments in which the amount of new investment recovery may be limited. Such recovery will take place over an extended period of time because recovery through rate increases is subject to regulatory lag.

As of December 31, 2017, we have no notable near-term cash expenditure or debt obligations. While specific facts and circumstances could change, we believe that we have sufficient cash on hand and will be able to generate sufficient cash flows to meet our operating cash flow requirements and capital expenditure plan as well as remain in compliance with our debt covenants for at least the next twelve months.

In March 2014, we initiated a dividend program to declare and pay a monthly dividend. On November 9, 2017, we announced a monthly dividend increase from \$0.02306 per share (\$0.27672 per share annually) to \$0.023625 per share (\$0.2835 per share annually). Although we expect monthly dividends will be declared and paid for the foreseeable future, the declaration of any dividends is at the discretion of our board of directors and is subject to legal requirements and debt service ratio covenant requirements (see “—Senior Secured notes”).

Cash from Operating Activities

Cash flows provided by operating activities are used for operating needs and to meet capital expenditure requirements. Our future cash flows from operating activities will be affected by economic utility regulation, infrastructure investment, growth in service connections, customer usage of water, compliance with environmental health and safety standards, production costs, weather, and seasonality.

For the year ended December 31, 2017, our net cash provided by operating activities totaled \$11.2 million compared to \$1.9 million for the year ended December 31, 2016. The \$9.3 million change in cash from operating activities is primarily driven by the increase in operating income for the year ended December 31, 2017 compared to the year ended December 31, 2016 coupled with a decrease in interest expense due to the June 2016 debt refinancing, decrease in payments made relating to accounts payable and other current liabilities, and increase in deferred income tax expense.

For the year ended December 31, 2016, our net cash provided by operating activities totaled \$1.9 million compared to \$4.2 million for the year ended December 31, 2015. The \$2.4 million change in cash from operating activities is primarily driven by an increase in net losses for the year ended December 31, 2016 compared to the year ended December 31, 2015. This loss was primarily driven by the \$3.2 million prepayment penalty on the retirement of our tax exempt bonds.

Cash Used In Investing Activities

Our net cash used in investing activities totaled \$21.0 million for the year ended December 31, 2017 compared to \$6.2 million for the year ended December 31, 2016. The \$14.8 million change in cash used in investing activities was primarily driven by an increase in capital expenditures of \$12.3 million for the year ended December 31, 2017 compared to the year ended December 31, 2016. In addition, cash provided by investing activities for the year ended December 31, 2016 included \$2.3 million in cash proceeds from the sale of Willow Valley.

Our net cash used in investing activities totaled \$6.2 million for the year ended December 31, 2016 compared to \$52.0 million cash provided by investing activities for the year ended December 31, 2015. The \$58.1 million change was primarily driven by \$55.1 million in proceeds received in relation to the condemnation of the operations and assets of Valencia in 2015. In addition, capital expenditures increased \$5.2 million to \$8.6 million for the year ended December 31, 2016 compared to \$3.4 million for the year ended December 31, 2015. These capital expenditures for the year ended December 31, 2016 were partially offset by the \$2.3 million in cash proceeds from the sale of Willow Valley.

We continue to invest capital prudently in our existing, core service areas where we are able to deploy our Total Water Management model as service connections grow. This includes any required maintenance capital expenditures and the construction of new water and wastewater treatment and delivery facilities. Capital expenditures increased in 2017 as compared to recent years as a result of our decision to accelerate certain capital expenditures within our capital improvement plan related to the Private Letter Ruling (see “—Recent Events—Private Letter Ruling”). Our projected capital expenditures and other investments are subject to periodic review and revision to reflect changes in economic conditions and other factors.

Cash Used In Financing Activities

Our net cash used in financing activities totaled \$5.4 million for the year ended December 31, 2017, a \$18.7 million change as compared to the \$13.3 million in cash provided by financing activities for the year ended December 31, 2016. This change was primarily driven by the refinancing of tax exempt bonds in 2016, wherein we repaid \$106.7 million in tax exempt bonds with \$115.0 million in proceeds from our two series of senior secured notes, combined with the release of \$8.8 million in bond reserves associated with the refinancing. Additionally, we generated \$5.6 million in net proceeds from our U.S. IPO. Proceeds for the year ended December 31, 2016 were partially offset by the \$2.8 million payment to settle our Sonoran acquisition liability.

Our net cash provided by financing activities totaled \$13.3 million for the year ended December 31, 2016, a \$64.5 million change as compared to the \$51.3 million in cash used in financing activities for the year ended December 31, 2015. This change was primarily driven by the refinancing of tax exempt bonds, wherein we repaid \$106.7 million in tax exempt bonds with \$115.0 million in proceeds from our two series of senior secured notes, combined with the release of \$8.8 million in bond reserves associated with the refinancing. Additionally, we generated \$5.5 million in net proceeds from our recently completed U.S. IPO. Proceeds received for the year ended December 31, 2016 were partially offset by the \$2.8 million payment to settle our Sonoran acquisition liability, combined with \$5.0 million in dividends paid. Cash used in financing activities for the year ended December 31, 2015 was primarily driven by \$27.6 million in dividends paid and \$21.7 million in loan repayments of which \$21.3 million was associated with the retirement of the MidFirst loan.

Senior Secured Notes

On June 24, 2016, we issued two series of senior secured notes with a total principal balance of \$115.0 million at a blended interest rate of 4.55%. Series A carries a principal balance of \$28.8 million and bears an interest rate of 4.38% over a twelve-year term, with the principal payment due on June 15, 2028. Series B carries a principal balance of \$86.3 million and bears an interest rate of 4.58% over a 20-year term. Series B is interest only for the first five years, with \$1.9 million principal payments paid semiannually thereafter. The proceeds of the senior secured notes were primarily used to refinance the existing long-term tax exempt bonds, pursuant to an early redemption option at 103%, plus accrued interest, as a result of the U.S. IPO.

The senior secured notes require the Company maintain a debt service coverage ratio of consolidated EBITDA to consolidated debt service of at least 1.10 to 1.00. Consolidated EBITDA is calculated as net income plus depreciation, taxes, interest and other non-cash charges net of non-cash income. Consolidated debt service is calculated as interest expense, principal payments, and dividend or stock repurchases. The senior secured notes also contain a provision limiting the payment of dividends if the Company falls below a debt service ratio of 1.25. However, for the quarter ending June 30, 2021 through the quarter ending March 31, 2024, the ratio drops to 1.20. As of December 31, 2017, the Company was in compliance with its financial debt covenants.

Insurance Coverage

We carry various property, casualty, and financial insurance policies with limits, deductibles, and exclusions consistent with industry standards. However, insurance coverage may not be adequate or available to cover unanticipated losses or claims. We are self-insured to the extent that losses are within the policy deductible or exceed the amount of insurance maintained. Such losses could have a material adverse effect on our short-term and long-term financial condition and the results of operations and cash flows.

Critical Accounting Policies, Judgments, and Estimates

The application of critical accounting policies is particularly important to our financial condition and results of operations and provides a framework for management to make significant estimates, assumptions, and other judgments. Additionally, our financial condition, results of operations, and cash flow are impacted by the methods, assumptions, and estimates used in the application of critical accounting policies. Although our management believes that these estimates, assumptions, and other judgments are appropriate, they relate to matters that are inherently uncertain and that may change in subsequent periods. Accordingly, changes in the estimates, assumptions, and other judgments applied to these accounting policies could have a significant impact on our financial condition and results of operations as reflected in our financial statements.

Income Taxes

Estimation of income taxes includes an evaluation of the recoverability of deferred tax assets based on an assessment of the Company's ability to utilize the underlying future tax deductions against future taxable income before they expire. The Company's assessment is based upon existing tax laws and estimates of future taxable income. If the assessment of the Company's ability to utilize the underlying future tax deductions changes, the Company would be required to recognize fewer of the tax deductions as assets, which would increase the income tax expense in the period in which the determination is made. Additionally, an evaluation of the recoverability of deferred tax gains is based on an assessment of the Company's ability to fully utilize the deferred tax gain before its expires. The Company's assessment is based upon the ability to acquire qualifying properties. If the assessment of the Company's ability to fully utilize the deferred tax gain changes, the Company would be required to recognize income tax expense in the period in which the deferred tax gain expires.

Recent Accounting Pronouncements

A discussion of recently adopted accounting pronouncements is included footnote 1 to the consolidated financial statements contained in Part II, Item 8 of this annual report on Form 10-K and is incorporated herein by reference.

Jumpstart Our Business Startups Act (the "JOBS Act") Accounting Election and Other Matters

We are an "emerging growth company," as defined in the JOBS Act. Under the JOBS Act, emerging growth companies can elect to delay adopting new or revised accounting standards issued subsequent to the enactment of the JOBS Act until such time as those standards apply to private companies. We chose to take advantage of this extended transition provision. See "Risk Factors—Risks Related to Ownership of Our Common Stock—Our election to take advantage of the JOBS Act extended accounting transition period may make our financial statements more difficult to compare to other public companies" and "Risk Factors—Risks Related to the Ownership of Our Common Stock—Taking advantage of the reduced disclosure requirements applicable to emerging growth companies may make our common stock less attractive to investors" included in Part I, Item 1A of this Form 10-K, for additional information.

The Company historically accounted for stock appreciation rights ("SARs") as liability compensatory awards under ASC 710, Compensation – General, valued using the intrinsic value method, as permitted by ASC 718, Compensation – Stock Compensation ("ASC 718"), for nonpublic entities. Upon becoming a public company, as defined in ASC 718, in the second quarter of 2016, the Company was required to change its methodology for valuing the SARs. While the SARs will continue to be remeasured at each quarterly reporting date, the SARs are required to be accounted for prospectively at fair value using a fair value pricing model, such as Black-Scholes. The Company recorded the impact of the change in valuation methods as a cumulative effect of a change in accounting principle, as permitted by ASC 250, Accounting Changes and Error Corrections. The effect of the change increased the SAR liability by \$103,000 which was the difference in compensation cost measured using the intrinsic value method and the fair value method. An offsetting change to accumulated deficit in the consolidated balance sheet was recorded with the revaluation, net of \$38,000 in taxes. Any future changes in fair value will be recorded as compensation expense in the consolidated statement of operations.

Off Balance Sheet Arrangements

As of December 31, 2017 and 2016, we did not have any off-balance sheet arrangements.

Contractual Obligations

The following table summarizes our contractual cash obligations as of December 31, 2017 (in thousands):

	Total	Payments Due By Period			
		Less than 1 Year	1 - 3 Years	3 - 5 Years	More than 5 Years
Long term debt obligations	\$ 115,064	\$ 8	\$ 18	\$ 5,757	\$ 109,281
Interest on long-term debt ⁽²⁾	67,217	5,212	10,422	10,288	41,295
Operating lease obligations	225	124	60	41	—
FATHOM™ purchase obligations ⁽³⁾	717	717	—	—	—
Total ⁽¹⁾	\$ 183,223	\$ 6,061	\$ 10,500	\$ 16,086	\$ 150,576

- (1) In addition to these obligations, the Company pays annual refunds on advances in aid of construction over a specific period of time based on operating revenues generated from developer-installed infrastructure. The refund amounts are considered an investment in

infrastructure and eligible for inclusion in future rate base. These refund amounts are not included in the above table because the refund amounts and timing are dependent upon several variables, including new customer connections, customer consumption levels, and future rate increases, which cannot be accurately estimated. Portions of these refund amounts are payable annually over the next two decades, and amounts not paid by the contract expiration dates become nonrefundable and are transferred to contributions in aid of construction.

- (2) Interest on the long-term debt is based on the fixed rates of the Company's senior secured notes.
- (3) The Company entered into an agreement with FATHOM™ to replace a majority of its meter infrastructure in 2017, this project was completed in 2017, the final amount to be paid is reflective of finalizing contractual terms of the agreement. See Note 7 – “Transactions with Related Parties” of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for additional information.

Item 7A. QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk associated with changes in commodity prices, equity prices, and interest rates. The Company uses fixed-rate long-term debt to reduce the risk from interest rate fluctuations. Although the Company's long-term debt is based on fixed rates, changes in interest rates could impact the fair market value of the Company's long-term debt. As of December 31, 2017, the fair market value of the Company's long-term debt was \$115.7 million. For additional information about the Company's long-term debt, see Note 9 – “Debt” of the Notes to the Condensed Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K.

Other than interest-related risks, the Company believes the risks associated with price increases for chemicals, electricity, and other commodities are mitigated by the Company's ability over the long-term to recover its costs through rate increases to its customers, though such recovery is subject to regulatory lag.